NOTE FILE C/0911/17 SERVIRED/SYSTEM 4B/EURO 6000

I. INTRODUCTION

The Council of the CNMC has authorized in the first phase with commitments the merger of SR2, SOCIEDAD DE MEDIOS DE PAGO, S.A., SISTEMA 4B, S.L. and EURO 6000, S.A., management companies for domestic card payment systems in Spain: Servired, System 4B and Euro 6000 (jointly, "SMP"), by means of the termination of the legal personality of said companies and their universal succession by a new entity, which will bring together the functions and services provided by the SMP.[1]

The new company will not be under the exclusive or joint control of any of its partners, as there is no stable majority in the decision-making process, its main shareholders being: BANCO SANTANDER, BBVA, CAIXABANK, BANKIA and BANCO SABADELL. The relationships between all the shareholders, the principles of action of the new system and other elements that must govern its operation are included in the Shareholders' Agreement.[2]

The operation analysed shows effects in the market for card payment systems, in which the SMPs are active.

The payment systems constitute the rules that govern card-based payment transactions, including network services provided to payment service providers, members of the system (card issuers and/or purchasers of payment transactions) to make these possible (rules about authorization, clearing and settlement of transaction processes). Furthermore, the systems are usually the holders and suppliers of the payment applications that allow payments to be made, as well as the payment brands that allow the identification and acceptance of card-based payment operations.

However, in the case of SMPs, these are not full payment systems because they lack their own payment applications and payment brands, having reached individual or collective agreements with VISA and MASTERCARD to use the payment applications of these international systems, of which they are also members[3] with which they carry out domestic payment transactions.[4] In this sense, the SMPs are technologically dependent on said international systems, developing their activity in the domestic sphere of payment operations performed with Visa and MasterCard cards in Spain.

In this context, in addition to the merger of the three SMPs into one, which will continue to provide its current functions, the Shareholders' Agreement foresees that the

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[1] Prior to the concentration operation, segregation occurred in these companies for all activities not directly related to the management of the card payment system.

[2] The Shareholders' Agreement establishes a mechanism to adjust the participation of shareholders based on their respective participation in the company's volume of activity.

[3] In the case of some entities, such membership occurs with the character of a member or principal (or independent) user and in the case of others with the member or associated user, sponsored by another principal member (or by collective members, in traditional terminology).

[4] All the universal payment cards used in domestic operations in Spain assigned to the SMPs are Visa or MasterCard cards and are identified with one of these brands, which is the one that guarantees their interoperability with any acceptance devices (payment terminals or ATMs) also assigned to Visa or MasterCard (or, as usual, to both), in addition to the SMP brand to which the issuer belongs (*co-branding* cards). Both the cards and the acceptance devices in the field of SMPs are also based on Visa or MasterCard's technical and functional specifications.

resulting entity will face the necessary investments to develop its own payment application, in order to offer a domestic payment system with full functions in competition with other payment systems, including international systems.

Therefore, with the merger would **disappear one of the peculiarities of the Spanish card payment sector, given that in the countries of the European Union the most usual thing is that there is a single SMP, with a payment application of its own, in which all financial entities that intermediate card payments are integrated**.

On the other hand, the financial entities that are shareholders of the SMPs also participate in the capital of the two main processing entities in Spain (REDSYS and CECABANK).

Therefore, there is strong vertical integration in the card payment services sector, as financial entities are the main issuers of cards and acquirers of payment transactions, demanding payment and processing system services, required for the execution of a payment transaction, to the three SMPs and the two main processors present in Spain respectively, of which they are principal shareholders.

For the proper valuation of the concentration, the CNMC required necessary information from third parties, attaching the proposal of commitments of the parties, so that they could also assess their suitability to resolve the possible obstacles to the maintenance of effective competition that may be derived from the operation.

II. ASSESSMENT and COMMITMENTS

The merger of the SMPs will strengthen the implicit vertical integration of the entire value chain of card payment transactions in Spain. In any case, it should be noted that this implicit vertical integration was already very significant prior to the concentration operation and is limited, in the sense that, with the exception of SYSTEM 4B, no financial entity controls individually or jointly any SMP or processor in Spain.

The operation has horizontal effects in the market for the provision of card payment systems services to domestic operations carried out with cards in Spain ("card payment systems service market"), in which they operate. The merger has also vertical effects in the markets for the issuance of payment cards (issuance market) and the acquisition of card payment transactions (acquisition market) in Spain, in which the financial entities (shareholders of the SMP and the merged entity) operate.

In addition, the transaction could have an effect on the processing market for card payment transactions in Spain (processing market), where the shareholders of the SMPs are also the shareholders of the main processors in Spain (REDSYS and CECABANK).

II.1. Effects on the market of the provision of services of card payment systems in Spain

The merger of the three SMPs will mean the creation of a single system that provides card payment system services to domestic operations carried out by practically all payment service providers established in Spain.

This is a market that shows important barriers to entry derived from significant economies of scale and networks that the system of the resulting entity will enjoy, which is difficult to replicate by third parties, so it does not seem that there is or will be a real alternative to the entity resulting from the merger in the provision of said services in Spain.

In this sense, operators such as Visa and MasterCard that provide such services, although marginally and, generally, linked to payment service providers that have a significant volume of international transactions, do not have sufficient economies of scale and network in the domestic market to create an alternative system, at least right away.[5]

However, it should be kept in mind that the pre-existing competition between the SMPs is quite limited, due to the lack of or reduced mobility of banking entities between systems (which has been limited to that associated with concentrations in the banking sector) and implicit vertical integration existing between card issuers/procurers, payment systems and processors.

In any case, given the absence of a real alternative to the provision of such services to domestic operations carried out in Spain, at least in the short term, there are certain **risks** that the resulting entity will be used by its main shareholders to limit competition in the card payment sector. In particular, the main shareholders could have the capacity and incentives to:

a. hinder or delay access to the system for new members, when these may represent a significant competitive threat for their innovative business models, etc.

b. use the commercial policies of the system as an instrument to influence, control and limit the competitive capacity of their members, especially the smallest members associated with EURO 6000, which operated in a system adapted to their needs, and could also hinder the development of innovative initiatives for card payments that are not aligned with their own interests, as in the case of cashback[6] that exist in nearby countries.[7]

c. apply measures that directly or indirectly limit or condition the freedom of their members to issue cards or make payment purchases outside of the system.

Given the aforementioned, there must be certain guarantees that ensure the neutrality of the new operator with respect to any of its members (whether shareholders or not) and its freedom to select the systems and payment applications to be used in each payment instrument or acceptance device put on the market and the operations performed with them, as well as regarding the services they can offer to meet the needs of their customers (card holders and businesses).

For these purposes, the parties have presented a series of **commitments** in relation to:

1- System access

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[5] They are, nevertheless, important international operators with great competitive capacity that, potentially, could be able to create an alternative system, establishing lower prices and demanding less guarantees to their members, through cross-subsidies with the rest of their activities in Spain or internationally.

[6] That allows the end user to obtain cash through their purchases in a commercial establishment, without having to go to an ATM.

[7] In fact, it is very important to bear in mind that until now the SMPs in Spain have not developed these cashback solutions, and the only operator that has put them on the market, ING (through the Twyp Cash service), has not been able to use the infrastructure or the rules of the SMP, which has clearly increased this operator's costs.

The commitments indicate that all payment service providers that comply with the requirements established in the applicable regulations and whose participation is accepted by the resulting entity, can be a member of the system, taking into account criteria of objectivity, non-discrimination and proportionality. These requirements will not limit access beyond what is necessary to prevent specific settlement risks, operational risks and business risks to guarantee the operational and financial stability of the system.

The proposal for commitments anticipates that the decision regarding acceptance or denial of access to new members must be adopted within a maximum period of two months from the formal request of the interested entity, which will be accompanied by the documents that justify their legal authorization to act as payment service provider.

The proposal for commitments includes an additional guarantee for those requesting entities to which the system has denied access, in a motivated and duly justified way through the establishment of an arbitration mechanism before the CNMC, which will decide on the controversy, committing the company itself to comply with the final arbitration resolutions adopted by the CNMC in this regard.

The access fees of new members in the system will be charged in line with the usual average amounts in the European Union's card payment systems, and the amount cannot be such that it acts as a deterrent or constitutes an unjustified obstacle to accessing the system.

2- Core services to be provided by the system:

a) The notifiers agree that the company's core services will not be mandatory with respect to the operations that have not been assigned to the company's payment system.

b) They also guarantee that only essential services are supported by all members (related to the minimum standards approved by the BCE) and that for the rest, which can be considered as a backbone but only in relation to certain activities, a system of remuneration is established, guaranteeing the correct charge of the costs linked to the provision of said services, in other words, to be supported by the operations in which internal payment applications or optional services are used.

3- Optional services to be provided by the system[8]

a) The optional services that are established will be accessible to all members that request them and must be invoiced separately to users who contract them, establishing a system of remuneration that guarantees the correct billing of costs related to their provision, including a proportion of the common costs, according to the common resources used.

b) On behalf of an easy access to these services, all its members will be informed about every statement issued by the Board of Directors in relation to each optional service, the start-up of new services and the conditions for their provision. This

[8] The system will provide optional services to members requesting it, considering as such those services related to the settlement and compensation of payment transactions within the system and whose provision is feasible without disturbing the operation thereof and that are requested by one or more member entities.

duty should be carried out by the system in order to provide transparency to the procedure.

c) The proposal of commitments includes the procedure that members of the system must follow to request the provision of an optional service:

- The Board of Directors of the resulting entity will approve or deny, on a reasoned basis, the provision of said service within a maximum period of three months from the formal presentation of the request.
- In the event of approval, the Board of Directors will set the term foreseen as necessary for its effective implementation, without prejudice to any revisions that may arise.
- An additional guarantee includes an arbitration procedure before the CNMC regarding disputes that may arise between the new entity and the requesting members of an optional service, whose service has been denied.[9] The company will be obliged to submit the arbitrations ordered by the applicant companies and to comply with the final arbitration decisions that may be adopted by the CNMC in relation to these claims.

II.2. Effects on the markets for issuance, acquisition and processing of card payments in Spain

In principle, the operation could encourage competition in the issuance and acquisition markets in Spain, as payment service providers and end users will have greater alternatives in card products, payment applications and acceptance brands, thanks to the new developments that the resulting entity plans to make, which will result in improvements in the quality and conditions of the services provided.

The increase in competitive pressure could be higher in the acquisition market, as merchants will have the ability to pre-select the payment application included in their acceptance devices, which will increase their negotiating power with financial entities at the time of purchase, establish the conditions under which they provide acquisition services (lower discount rates, premiums, etc.).

However, the operation generates certain risks:

1. **Risk of hindering the selection of alternative payment applications**

The resulting entity can become an instrument to influence the behaviour of its members in the issuance and acquisition markets, especially in relation to the selection of payment applications to be used in each transaction. Some responses to the market test indicate that there is a high risk that alternative applications to the new system will be discriminated entirely or, at least, with respect to domestic operations.

These risks are lower in the card issuance market in Spain, given that Visa or MasterCard payment applications are very relevant for end users in order to be able to make international transactions , either physically or in online purchases.

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[9] Controversies regarding the implementation of the service or the correlation of the fees applied to the provision of an optional service with the costs corresponding to its implementation and operation may also be submitted to the arbitration decision of the CNMC.

In contrast, in the Spanish card payment acquisition market, these risks may be higher. Especially in relation to cards with two pre-installed applications, since the system's shareholders may have the capacity and incentives to use their control of the market acquisition of card payments in Spain to hinder the capacity and incentives of merchants to autonomously use their pre-selection regulatory rights for the benefit of rival payment applications.

In this context, the **commitments**:

a) Guarantee the freedom of the member entities, through:

- The possibility of ascribing to the company's payment system all or some of its card payment products or acceptance products and the operations performed with them.
- Costs arising from the operation of the company's own payment applications will be borne solely by the member entities in whose payment transactions such applications were used[10].

b) They guarantee the freedom of choice on the part of the payment payer, through:

- The commitment that the issuing entities may incorporate in their cards their own payment applications along with those of one or another payment system (*cobadging)*.
- the obligation for member entities to implement in their acceptance devices (POS and ATMs) the appropriate technical procedures so that the ordering parties can make the final effective decision on the payment application used in the operation[11].

c) They expressly guarantee the freedom of the beneficiaries (shops) who have pre-installed a payment application in their POS, to change this pre-selection at any time, immediately and without any cost to them.

2. Risk of coordination in the markets for the issuance and acquisition of card payments

On the other hand, the activity of the merged firm could generate **coordination** risks for competitive behaviour of the banking entities that are members of the system in the markets for issuance and acquisition of card payments in Spain. This is because the implicit vertical integration is reinforced and could be a possible development of a payment application within the entity, which can increase the capacity and incentives of the members of the new system to coordinate. This coordination could take place or be facilitated because of hypothetical exchanges of sensitive commercial information between members of the system.

In this regard, this Competition Directorate understands that mechanisms should be established to prevent flows of sensitive commercial information between the

[10] To this end, a complementary fee shall be established for the use of the company's payment applications, which shall include the proportional part of the common services used, in proportion to the volume of activity of the members in terms of payment transactions in which said applications have been used. This is without prejudice to the application to all members in the first year of activity of the company for an extraordinary fixed fee aimed at funding the necessary investments for the availability of the aforementioned applications.

[11] In the terms established in Article 8.6 of Regulation (EU) 2015/751

members of the system and between their payment applications and those of third parties.

To avoid this, the **commitments** include a series of mechanisms to prevent the flow of sensitive information. In particular, the company will establish in the scope of all its services a system of information sealing that ensures that the disaggregated information on the activity of each of the member entities is not disseminated to the rest or to their representatives in the company's administrative bodies or management. In addition, the commitments foresee that managers and personnel of the company having access to sensitive commercial information will be independent of any of said entities and they will sign a confidentiality agreement with the company.

3. Exclusion risk in the payment processing market

The market for card payment processing in Spain, is especially sensitive in Spain, since in practice there are only two entities capable of performing these functions. As a result, after the operation there is a risk that CECABANK will see its activity reduced, as long as its scale is very limited and its activity has traditionally been associated with the Euro 6000 card payment system, which will disappear as an independent entity after the merger.

The **commitments** guarantee that the member entities will have full freedom to select the processing entity that will provide them with services of this nature, which may be different from that of other member entities or from whom, where appropriate, provides services to the entity system manager. In this regard, the system will not impose discriminatory or non-objective conditions between said entities, which in any case must meet interoperability requirements.[12]

The commitments will last for five years from the day following the registration of the merger deed in the Mercantile Registry, although this period may be extended for three more years. Information reporting obligations to the CNMC are included to guarantee adequate monitoring of the commitments made.

[12] Established in Article 7.5 of EU Regulation 2015/751.