

MERCHANT ADVISORY NO. 2: NEW DEBIT RATES

Dear Merchant,

This law firm, Constantine & Partners, is lead counsel for United States merchants in the merchants' antitrust case against Visa and MasterCard. The official name of the case is the *Visa Check/MasterMoney Antitrust Litigation*.

Last month in a detailed "Merchant Advisory" I explained the progress of the case, the process for Court consideration of the Settlements reached with Visa and MasterCard and the Plan to allocate and distribute to merchants the billions of dollars which Visa and MasterCard agreed to pay merchants in settlement of this case. Most importantly, we also described merchants' newly won right to make a decision to continue accepting or to reject Visa and/or MasterCard signature debit transactions and/or credit transactions on or after January 1, 2004. That first Merchant Advisory as well as this "Merchant Advisory No. 2" is available on the following websites:

www.cpony.com (Constantine & Partners website)

www.nrf.com (National Retail Federation website)

www.fmi.org (Food Marketing Institute website)

www.imra.org (International Mass Retail Association website)

A copy of the two Merchant Advisories can also be obtained by calling 212-350-2799.

This second Merchant Advisory updates and supplements the previous Advisory and specifically provides information concerning new interchange rates for Visa and MasterCard signature debit that are scheduled to go into effect next year.

This week Visa announced signature debit (“Visa Check”) interchange rates scheduled to go into effect on January 31, 2004. MasterCard announced rates for its signature debit product (sometimes called “MasterMoney” or “Debit MasterCard”) which are scheduled to go into effect on April 2, 2004.

These new Visa and MasterCard debit interchange rates, which are ultimately paid by merchants as part of their merchant “discount” fees are set forth in seven detailed charts which are attached to this Advisory. Here, we will simply try to summarize the newly announced rates and again explain each merchant’s option to accept or reject Visa and/or MasterCard signature debit in light of the newly announced rates.

Visa

Three of the attached charts show and analyze the interchange rates which Visa has announced will be effective January 31, 2004. Until then, the rates Visa

was required to put into effect on August 1, 2003 under the Settlement will remain in effect.

Visa has set these January 31, 2004 rates at levels which are above the August 1, 2003 interim rates required by the Settlement and below the rates that Visa utilized prior to agreeing to settle the case on May 1, 2003. The attached charts compare the January 31, 2004 rates to the pre-settlement rates and to the August 1, 2003 interim rates required under the Settlement until Visa signature debit is untied from Visa credit and a merchant is free to reject signature debit, if it so chooses.

Although the charts provide detail on Visa's newly announced rates, the overall trend in these rates can be summarized. The January 31, 2004 rates, on average, are down 11% from pre-settlement levels, but up 26% from the rates Visa is required to utilize while acceptance of signature debit is still forced on a merchant. This forced acceptance ends on January 1, 2004. The new Visa rates are down 12% for a typical \$40 debit transaction from the pre-settlement levels, but up 23% from the August 1, 2003 rates. The new Visa rates are down 19% on a \$100 transaction from pre-settlement levels but up 4% from the August, 2003 interim rates.

The new Visa rates are "list" prices. Newspaper reports appearing in the

Wall Street Journal and other publications indicate that Visa and MasterCard are attempting to convince certain merchants to continue accepting signature debit after January 1, 2004 with offers of special lower rates and other monetary incentives.

In the past, Visa has changed announced rates prior to their effective date in response to individual merchant announcements that they would reject a specific payment product. Also in the past, Visa and MasterCard have altered announced rates prior to their effective date.

MasterCard

Three of the attached charts show and analyze the interchange rates which MasterCard has announced will be effective on April 2, 2004. The interim rates which went into effect under the Settlement on August 1, 2003 will be in effect until then. The April 2, 2004 MasterCard rates, on average, are very similar to the interim rates. In some cases they are slightly higher and in some cases slightly lower.

The overall trend in the MasterCard rates which are set forth in detail in the attachments can be summarized.

MasterCard's April 2, 2004 rates on average are down 32% from pre-settlement levels, but up 3% from the August 1, 2003 interim rates.

MasterCard's new rates on a typical \$40 transaction are down by 33% from pre-

settlement levels and down 1% from the interim rates. MasterCard's new rates on a \$100 transaction are down 30% from pre-settlement levels but up 11% from the interim rates.

A Comparison of Visa's New Rates with MasterCard's New Rates

The recent rate announcements are additional evidence of a growing rivalry between Visa and MasterCard, set in motion by your case. The Visa "Settlement Service Fee" and the MasterCard attempt to have that Visa fee declared illegal were other recent indications that the goal of getting Visa and MasterCard to compete with each other has been partially achieved.

The fact that this has led to downward (as opposed to upward) price competition is a good sign.

The first chart attached to this Advisory compares the new Visa and MasterCard debit rates. Please keep in mind that for the last decade or more, MasterCard's rates have been consistently higher than Visa's. That has now changed drastically.

Visa's new signature debit rates will be 26% higher than MasterCard's on average, (31 basis points higher) 23% higher on a \$40 transaction (27 basis points higher) and 4% higher on a \$100 transaction (five basis points higher).

MasterCard's new rates are much lower than Visa's.

In the face of these new rates, scheduled to go into effect on January 31, 2004 (Visa) and April 2, 2004 (MasterCard), each individual merchant has several options. Each merchant must individually decide what it will do given these options.

- A merchant can continue to accept Visa and MasterCard signature debit and pay merchant discount fees that reflect these new rates.
- A merchant can attempt to negotiate with either Visa or MasterCard for rates that are lower than those announced, as it has been publicly reported other merchants have.
- A merchant can upon 30 days advance written notice to its card transaction processor or acquirer, stop accepting Visa signature debit and/or MasterCard signature debit and/or Visa credit and/or MasterCard credit. A form for notifying the processor/acquirer of such a choice is attached. The merchant can also tell the processor/acquirer to block unwanted signature debit transactions without cost to the merchant.
- A merchant can continue to accept Visa and/or MasterCard signature debit, but attempt to steer or convince shoppers to use a different form of payment.
- To help a merchant to identify Visa and MasterCard signature debit

cards until the time that they have all been reissued with the word “Debit” on them,¹ a merchant can obtain from its processor/acquirer a listing of all debit Bank Identification Numbers (BINs) to allow the merchant to identify these debit cards electronically. A form which can be used by merchants to request these BINs is attached to this Advisory.

This Merchant Advisory No. 2 is not designed to suggest what a merchant’s decision should be. However, with this Advisory and the previous Merchant Advisory and the forms and charts attached, each merchant should have the information it needs to make its own choices, given the new rights merchants won in this case.

If you have questions about the mechanical aspect of making your decision or registering a decision to reject signature debit or credit or requesting merchant signage, or obtaining debit card BINs or directing your processor to block signature debit transactions, you are free to call us, the merchants’ lead counsel. We will not advise you about what your decision should be.

This will be an exciting time for merchants to be active participants in rapidly

¹ A process which will take place over a three year period under the Settlements.

evolving payment markets, which recently have shown signs of greater competition for the merchants' business.

Sincerely,

CONSTANTINE & PARTNERS

Lead counsel for the certified class of plaintiffs

www.cpony.com

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