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The Hungarian Competition Office investigation into the use of ‘cash substitutes’

In Hungary, the country’s Competition Office has begun an investigation into the use of so-called ‘cash substitutes’ such as mobile payments and cards for the making of payments, with the main goal of such investigation appearing to be to explore the conditions applicable between traditional credit institutions and retailers. Dr Szabolcs Mestyán and John Fenemore of Lakatos, Köves and Partners discuss this investigation in the context of regulatory and policy developments surrounding payment infrastructure in Hungary, and analyse why the Hungarian Government is paying particular attention to the retail payments sector.

On 20 January 2017 the Hungarian Competition Office (Gazdasági Versenyhivatal) launched[1] a targeted inspection in the field of payments via ‘cash substitutes[2]’ (e.g. cards, mobile phone payments). Whilst ‘cash substitutes’ cover a broad range of payment mechanisms - and according to the Hungarian Competition Office’s order dated 20 January 2017 more innovative methods of payment will also be explored in the course of the inspection - the primary goal of the inspection seems to be the analysis of conditions applicable between traditional credit institutions and retailers.

The launch of the inspection was preceded by a study which concluded that small retailers face more adverse conditions from banks compared to their larger counterparts, a phenomenon that has been ‘known’ to market players for many years. Given this, what lies behind the timing of the inspection?

The Hungarian Government, and in particular the Ministry of National Economy, has been committed in recent years to facilitating a reduction in the number of cash payments (which add the greatest costs to a transaction) and to promoting the wider use of alternative payment methods. The inspection of the Hungarian Competition Office and the measures taken by the Ministry of National Economy are seemingly independent but it is no coincidence that the inspection was launched only a month after the Ministry of Economy issued its ministerial decree[3] on subsidising the acquisition by businesses of the necessary infrastructure (in particular POS terminals) required to be able to accept payments by bank cards. The number of POS terminals (and thus the number of businesses accepting card payments) has increased gradually over the past decade, but such increase has been modest from year to year. In turn, the Hungarian Government expects a larger increase by the end of 2017 as a result of the subsidies introduced by the ministerial decree.

Among the few conditions of granting the subsidy the ministerial decree sets one that is interesting from the perspective of the inspection of the Hungarian Competition Office: the retailer is eligible for the subsidy only if the commission of the bank (the provider of the POS terminal) does not exceed 1% of the gross payments made by payment cards on a monthly basis. It is assumed that such commissions currently range from between 3-5% and therefore a suspicion has emerged among market players that one of the implied goals of the inspection

1. Order of the Hungarian Competition Office dated 20 January 2017.
2. Defined under Act CCXXXVII of 2013 on credit institutions and financial undertakings.
3. Decree 47/2016 (XII.6) of the Ministry of National Economy on the subsidy for increasing the number of terminals required for the acceptance of payment cards.

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by the Hungarian Competition Office is the reduction of these commission rates.

In any case, should the Hungarian Competition Office raise concerns in connection with the different costs, commissions and possibly rates quoted for retailers of different sizes, assuming that such intention will or already exist(s), it will be a difficult exercise to prove its detrimental effect on competition or on the fair operation of the market. Given the proposed timeline of the inspection, which is only planned to be completed by around the end of the second quarter of 2018, the Hungarian Competition Office seems to be aware of this. The difficulty is due not only to the issues the authority would normally expect to encounter when exploring new areas, but also to the fact that the inspection relates to a highly regulated area where, in addition to conventional considerations, pricing is also influenced by the large number of compliance and risk taking (exposure limit) rules imposed on financial institutions. Although granting infrastructure and settling payments does not create a lender-debtor relationship between the bank and the retailer *per se*, the risks for the banks are similar in these transactions to those in respect of an overdraft. The risks of non-payment by a small business are usually higher than those in respect of a large business. It follows that as with a loan, where conditions are often softer and individually negotiated in respect of a large corporation, the conditions of providing payment services are also softer for such larger corporations due to the long-term (usually even global or multi-jurisdictional) relationship, sound liquidity history, and risk and collateral profile of these larger retailers. However, even if one sets aside the regulatory and risk related considerations, it may still appear somewhat justified when a bank argues that installing a hundred or more POS terminals with a retailer client is obviously cheaper (per terminal) than the installation of only one.

At this point one faces the general and widespread phenomenon that large players in any market usually operate at significantly lower costs than their smaller counterparts simply because they, due to their size, are able to benefit from economies of scale. This is an advantage that forces small businesses either to leave the market, to operate with lesser profit margins or to offer goods and services at a higher price. The catch-22 nature of this is far from new in a region where decades-long attempts to favour small and medium sized businesses has resulted in only very modest achievements.

Nevertheless, the policy of favouring small businesses backed by the central goal of reducing the number of cash payments may well justify the Hungarian Government's close scrutiny of the retail payment services industry in Hungary. In fact, from the Government's perspective it is high time for such an approach and one might wonder why this has not been in focus in previous years. Whether or not there is an implied intention to rearrange the market or attack current established participants is a question for the future. Current sentiments are that the 'battle' between the Hungarian banking sector and the Hungarian Government is over and thus banks are not preparing for or expecting hostility in connection with the inspection. One could even hope that if the Government achieves its goal and payment card acceptance becomes widespread, the banks will naturally also benefit from such a change even with lower commissions. On the other hand, the Hungarian Competition Office does indeed need to take a thorough view of the market and consider the results of its inspection accordingly. If a constructive discussion could be had during the next 16 months between banks, the Hungarian Competition Office and the retailers, and if during that period the initiatives of the Hungarian Government to subsidise the installation of POS terminals at small businesses pave the way for a larger market by the time the inspection closes, it could easily become unnecessary to conclude the process with sanctions against particular participants. The press release of the Hungarian Competition Office on the launch of the inspection itself emphasises that the inspection does not mean that a formal sanctioning procedure will automatically follow. This also gives rise to optimism that the Hungarian Competition Office will be open for constructive discussion and that this process provides room to reshape the market (to the extent necessary) for all stakeholders' benefit.