

# Chapter 1

## Summary & Conclusions

### 1.1 Summary and conclusions

The Betalingsservice direct debit service is one of the most well-known payment solutions in Denmark. Betalingsservice was launched in 1974 by PBS (now Nets) and is currently used by 95 percent of all Danish households. In 2012, around 16,500 companies, public authorities and associations (e.g. creditors) carried out 195 million transactions via Betalingsservice.

In general terms, the form of payment, which Betalingsservice comprises, is called a "direct debit", with the payment initiated by the creditor. Direct debits are often particularly useful for payments with an ongoing agreement between customer and creditor. In comparison to other direct debit solutions, such as automatic card payment, Betalingsservice has a number of advantages, and Betalingsservice is the most widely used direct debit product in Denmark.

New payment solutions are being developed, including mobile payment solutions such as Mobile Pay. These solutions, however, are of limited use for customers with recurring payments in an ongoing contract, and it is the authority's assessment that the current competitive pressure on Betalingsservice from these solutions is limited. Thus, Betalingsservice has a strong market position, and Nets is therefore the central provider of direct debit in Denmark.

With Nets' role as the central provider of direct debit, the great proliferation of Betalingsservice and the product's strong position, it is appropriate to conduct a competition analysis of Betalingsservice, including taking a closer look at Nets' earnings and costs as well as the role of banks in connection with Betalingsservice. To ensure that the benefits of Betalingsservice accrue as far as possible to businesses and, ultimately, their customers, it is essential that there are no irregularities in the system. It is thus important that the market should offer the products, which customers want at the lowest possible price.

The key findings of the analysis are presented in Box 1.1.

#### Box 1.1

#### Main conclusions

- » **Betalingsservice is the most widely used direct debit product in Denmark.** Betalingsservice is used by 95 percent of Danish households, and Nets, through Betalingsservice, is the central provider of direct debit in Denmark.
- » **Betalingsservice's operating margin is significantly higher than the average profit margin in the private urban trade sector.** Since 2009, Betalingsservice's operating margin has been [more than twice as high as] the average profit margin in the private urban trade sector. In 2012, the EBIT margin was [10-30] percent.
- » **Nets' earnings from direct debit are increasing.** In the period 2003-2012, Nets [more than doubled] its profit before tax from Betalingsservice, and in that same period profit before tax per transaction increased by [100-200] percent. In 2012, profit before tax was DKK [150-350] million. Nets increased earnings per transaction in the period 2003-2012, while the number of transactions has increased by approximately 40 percent.
- » **The price per Betalingsservice transaction has not dropped despite an increasing number of transactions.** The average payment to Nets per Betalingsservice transaction was somewhat constant in the period 2003-2012 and was DKK [4.32-6] in 2012.

During the same period, the number of transactions increased by 40 percent, while the actual cost per transaction dropped by [10-30] percent. Thus, Nets has economies of scale associated with the handling of Betalingservice. However, the cost reduction did not result in lower prices.

- » **Nets' payment to banks represents the largest single cost associated with Betalingservice and is continuing to rise.** The payment increased by more than [40-60] percent from 2003 to 2012 and by [0-20] percent from 2009 to 2012 when adjusted for inflation. Costs resulting from the payment to the banks are [significantly higher than] the second-largest cost item associated with Betalingservice.
- » **Nets' model for payment to banks has not reduced the cost of Betalingservice.** Following the Authority's analysis of Betalingservice in 2011, Nets changed its structure for remunerating the banks. Nets' revised structure for remunerating the banks did not result in a lower average payment to the banks. On the contrary, the payment to the banks per transaction continued to rise in the period 2011-2012. Forthwith, the payment to the banks will be based on own cost studies.

Nets considers various data about the earnings and costs associated with Betalingservice to be confidential. This data is either omitted entirely or replaced by intervals or descriptive words inserted in brackets [].

Nets has growing earnings from Betalingservice. From 2003 to 2012, Nets [more than doubled] its profits before tax from Betalingservice, and in 2012 it had profits before tax of DKK [150-350] million. During the same period, the number of transactions increased by about 40 percent. This means that Nets increased its earnings per direct debit transaction in a period when the number of transactions also increased. This has led to an operating margin of more than [10-30] percent, which is [significantly higher than] the average profit margin in the private urban trade sector.

The basis to Nets' earnings from Betalingservice is the price which creditors pay to Nets for using the product. Since 2007, the price of the basic Betalingservice service has been DKK 4.32. Besides the basic service, creditors make use of additional and supplementary services associated with Betalingservice. Thus, the average payment to Nets per transaction was DKK [4.32-6] in 2012. This is [0-20] percent lower than the level in 2003, when adjusted for inflation.

Nets' costs arising from Betalingservice can be divided into three categories: distribution costs; decentralised production, which represents the remuneration of the banks; and other costs. Since 2007, the total cost per transaction has been declining, and in 2012 it was DKK [2-6]. When the costs of Betalingservice are compared to those of direct debit products in other countries, Betalingservice have significantly higher costs. For example, the costs of Betalingservice are twice as high as the costs of the Norwegian direct debit product.

In the period 2003-2012, when the number of transactions increased by approximately 40 percent, the actual cost per transaction dropped by [10-30] percent, while the average price per transaction dropped by [0-20] percent. Thus, the lower costs did not result in lower pricing for Betalingservice.

Nets' remuneration of the banks, which represents decentralised production, is the largest cost item for Betalingservice. The cost resulting from remuneration of the banks is [significantly higher than] the second largest cost item for Betalingservice. The remuneration can be characterised as an interchange fee going from the creditor's provider to the customer's bank. Previously, in an EU regulation the Commission introduced a cap of 8.8 euro cents, corresponding to DKK 0.66, on interchange fees for direct debit products, and these fees may eventually be banned completely

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for both cross-border and domestic transactions. This regulation, however, applies only to direct debits in euros and thus has no impact on Betalingsservice. Parts of the regulation could apply to direct debits in Denmark if Denmark committed the Danish krone to the provisions of the regulation.

Remuneration of the banks increased by more than [40-60] percent in the period 2003-2012 and by [0-20] percent in the period 2009-2012, when adjusted for inflation. Following the Authority's analysis of Betalingsservice in 2011, Nets changed its structure for remunerating the banks. Nets' new structure for remunerating the banks has not led to a lower average remuneration to the banks. On the contrary, the payment to the banks per transaction increased steadily from 2011 to 2012. **Forthwith, the payment to the banks will be based on recurring reviews of the banks' costs.**

Betalingsservice is covered by the general provisions of the Danish Competition Act. Unlike some of the Nets Group's other products, such as the Dankort card and international debit cards, Betalingsservice is not regulated by the provisions of the Danish Payment Services Act on unfair prices and profit margins.

In its 2011 analysis, the Competition and Consumer Authority pointed out that Nets had high and rising earnings from Betalingsservice, and judged that the competitive pressure from alternative products was limited. Since then, Nets' earnings have increased further, just as the remuneration to the banks has increased, and Nets remains the key provider of direct debit in Denmark. In addition, Betalingsservice is still assessed to have a strong market position, while the number of alternative direct debit products is limited.

Stricter regulation of direct debit products might entail both advantages and disadvantages, and this analysis does not include an exhaustive assessment of these. For example, regulation of direct debit may well prevent continued growth in the earnings from Betalingsservice. Conversely, there would be a risk that the development of new and better direct debit solutions, including innovation in the market, could be hampered as a result of regulation.

On this basis, the Authority finds that further consideration might be given to examining the advantages and disadvantages of regulating direct debit products in Denmark, including whether regulation of the area could harm innovation in this market. Such an analysis might also include details of what a possible adjustment could look like.

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