

# Undercard



# Bout

American Express prepares for 12 rounds with the DOJ

*Andrew Deichler*

American Express is lacing up its gloves and preparing to do battle with a fairly formidable opponent: the U.S. Department of Justice.

In an attempt to crack down on credit card companies that it feels hold too much of a monopoly on the industry, the DOJ filed an antitrust lawsuit against the three largest networks—Visa, MasterCard and American Express—for prohibiting merchants from

offering discounts, rewards and information about credit cards to consumers. Such rules increase costs for consumers and merchants, the DOJ said.

Visa and MasterCard, which control about 70 percent of the market, reached a settlement with the DOJ immediately after the suit was filed. If approved by the U.S. District Court for the Eastern District of New York, Visa and MasterCard would be obligated to allow merchants to participate in the previously barred activities. Connecticut, Iowa, Maryland, Michigan, Missouri, Ohio and Texas also joined in the motion.

American Express, however, has vowed to fight.

### Opening bell

“We have no intention of settling this case and will vigorously defend ourselves and the rights of our cardmembers in court,” said Kenneth I. Chenault, Chairman and CEO, in a letter to AmEx employees.

Chenault went on to say that the rules AmEx has in place keep their members from being “inconvenienced” by retailers at the point of sale, such as being persuaded to use other credit cards that cost less for merchants to accept.

On October 8, Chenault wrote an op-ed in *The Washington Post*, claiming that the lawsuit “does nothing for consumers,” and would result in “less competition, not more.”

According to Chenault, AmEx developed its

Could the Justice Department’s antitrust lawsuit create a monopoly, rather than avoid one?

current practices about 25 years ago in response to attempts by Visa and MasterCard to limit competition in the market. “In fact, earlier this decade, the Justice Department successfully sued Visa and MasterCard for operating as an illegal cartel,” he wrote.

AmEx contends that changing its policies with merchants could theoretically hurt its business by steering customers toward its toughest competitors. The

majority of AmEx customers also carry a Visa or MasterCard product, but not the other way around, Chenault noted. His logic: It would be easier to steer AmEx customers to use their Visa or MasterCard via discounts than to convince users of the other two cards to buy an AmEx product.

“There is some truth that it could give Visa and MasterCard an advantage,” said Anand Goel, CEO of Optimized Payments Consulting. “When you look at the three major card types—or four if you count Discover—AmEx is the most expensive on average, and makes a great portion of its revenue through charges to merchants.”

Goel feels that AmEx could benefit from challenging the lawsuit, even if it ultimately loses, because it would continue to receive higher interchange fees from merchants while the litigation is pending. This is considerable because the legal case could possibly take years to resolve itself.

### Counterpunch

AmEx insists that it does not have market power in the way that Visa and MasterCard do. Although no merchants are “forced” to accept any credit card, the majority of merchants do accept Visa and MasterCard because with so many users, not accepting the two top credit cards would result in poor business.

But this is not as much of a Rocky Balboa and Apollo Creed situation as it might appear. It is true that

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Visa and MasterCard have control over the vast majority of the credit market. Like Goel mentioned, AmEx charges merchants more than either Visa or MasterCard. But does the company have market share?

“Amex has significant market share,” Goel said. “The idea that it doesn’t... I don’t think that holds a lot of weight.”

The DOJ’s statement illustrated last year’s credit charges. Visa users came in at the highest, with charges of \$764.2 billion. But AmEx users charged \$419.8 billion, only about \$50 billion less than the \$476.9 billion that MasterCard users charged. The February 2010 issue of The Nilson Report listed total charge volume for 2009 at \$1.761 trillion, which puts Amex at 23.8 percent, Visa at 43.4 percent, MasterCard at 27.1 percent.

Additionally, credit card networks collect \$35 billion in fees from merchants annually, with AmEx

charging the most. Lifting some of the restrictions could benefit both merchants and consumers.

“From a merchant’s perspective, AmEx could be more competitive with their pricing,” Goel said.

### No decision

But would such benefits truly affect the market? Chenault wrote that while lifting the restrictions might result in some customers receiving discounts, it likely will not lead to overall lower prices for consumers. Merchants, he believes, are unlikely to drop prices because nothing in the lawsuit requires it. Chenault also mentioned that while merchants already have the ability to offer discounts and incentives to customers paying with cash, checks or debit cards, very few actually do.

“When dominant parties gain even more market share, no one will be able to negotiate freely or fairly with them, Chenault said. “The inevitable result would be higher costs for merchants and less value for consumers.”

But according to U.S. Attorney General Eric Holder, the lawsuit sends a “clear message” to credit card companies that the DOJ does not tolerate anticompetitive practices. “We want to put more money in consumers’ pockets, and by eliminating credit card companies’ anticompetitive rules, we will accomplish that,” he said.

Outside parties are a bit more neutral. David Bellinger, CTP, AFP’s Payments Director, said how much of a “win” the settlement is for merchants remains to be seen.

“What I will be looking for is how much the settlement sets up merchants to influence the interchange pricing set by the networks. That’s the key—

getting to a competitive balance,” said Bellinger. “If merchants are unable to generate a competitive effect similar to what they experience with all of the other services and prices treasury practitioners negotiate with banks, then the settlement will have only a marginal impact.”

The statement from the Justice Department and experiences from actions in other countries indicate that “the only change likely to produce a significant impact is the merchants’ ability to provide discounts for specific cards or networks,” Bellinger noted. But merchants could run into difficulty when attempting to implement new strategies at the point of sale. “Still, merchants were very successful at steering consumers to PIN debit, so they may now have some success with credit cards as well,” he said.

Goel agreed that lifting the regulations on retailers would not likely have a significant impact on the market, or even on AmEx. The majority of smaller, mom-and-pop retailers do not even accept the card, while the largest retailers are more prone to avoid steering altogether because they do not want to disrupt their customers. Goel noted that mid-sized retailers are the group that is most likely to take advantage of the changes, but even then, a major impact is doubtful.

“It’s probably not significant to AmEx’s bottom line,” Goel said. “Overall, there’s not enough volume where they would notice a difference. But part of it could be perception... AmEx doesn’t want to create an image that Visa and MasterCard are preferable.”