

MARKET INVESTIGATION REFERENCE OF STORE CARDS

As you will know, on 18 March 2004 the OFT referred the provision of store card credit services to retailers and the provision of consumer credit through store cards to the Competition Commission for investigation.

The Competition Commission has requested a variation to the terms of reference, so that retailer network cards, for example Duet (issued by Creation Financial Services Ltd) and Style (issued by Style Financial Services Ltd), which have the essential characteristics of a store card, are included within the scope of the reference. It has also requested that the terms of reference be varied to include the provision of insurance products associated with store cards.

Network cards

A network card, while carrying the brand of a particular retailer, is also accepted as a means of payment by other retailers in the network which may not be part of the same corporate group or trade under a common name. Many retailers within a given network may have their brand on a network card. The card issuer's brand may also appear on the cards. While the presence of the store card network may provide some additional benefits to both the retailer and the customer, in other respects the cards are similar to store cards limited to a single retailer. As with the cards of individual stores, settlement of payments for network card transactions are made through a three-party settlement system, linking the customer, retailer and card provider. The network cards confer similar benefits on users and raise similar issues for investigation by the CC e.g. concerning the transparency of charges, the levels of interest charged, and the ease of comparison of those charges and benefits with charges for using conventional four-party credit cards such as VISA.

The network cards identified above are issued by some of the main store card providers identified by the OFT in its report (*Store cards*, March 2004, OFT 706, paragraph 4.75) and are subject to similar switching costs and incumbency advantages as apply to the supply of store card credit services to individual retailers. Furthermore, if any remedies were considered appropriate, then an inability of the Competition Commission to apply remedies to these sorts of network cards would be likely to cause distortions in the supply of store card credit services and in the supply of consumer credit through store cards.

Proposed variation

The OFT is therefore minded to vary the terms of reference. It proposes to modify the definition of 'store card' in the terms of reference to include such cards, by including 'retailers who belong to a store card network' and providing a definition of 'store card network'.

Insurance services

The Competition Commission believes that it is able to address certain aspects of the provision of insurance products associated with store cards, but wishes to be sure that it would have the ability to remedy any adverse effects arising from the provision of such insurance should it be considered appropriate to do so.

There are several forms of insurance sold with store cards. They are payment protection insurance, which is often sold together with price protection and purchase protection insurance, and card protection insurance, covering lost and stolen cards. Payment protection insurance covers repayments on the card if the customer is unable to work due to accident, sickness or unemployment. Price protection insurance applies to any price reductions which may occur within a given period following purchase. Purchase protection insurance covers the customer against loss, theft or damage of goods purchased using the card.

Store card credit services

The Competition Commission has evidence that most store card contracts between the provider and the retailer include the provision of insurance products within the same contract, and that store card providers see the provision of such insurance as an integral part of the store card offer and include the income streams from insurance sales when estimating the costs, revenues and profitability of their store card services.

Consumer credit through store cards

Consumers do not usually get the choice of payment protection insurance without purchase protection or price protection insurance and one premium is charged for the insurance package. This single premium is based on the store card balance outstanding at the accounting date and is payable regardless of whether the cardholder pays off the balance within the interest free period. If the balance is not paid within the interest free period then a further premium will be charged at the next accounting date based on the outstanding balance, that is, the insurance premium payable is related to the credit provided.

The effect of this is that some consumers may continue to pay for parts of the insurance package that they no longer either require or are entitled to receive. This is because price and purchase protection only last for a set period, e.g. 90 days, but a consumer, who makes no further purchases but continues to revolve existing credit,

may continue to pay for these elements after they have elapsed. Such a consumer receives no additional benefit resulting from these continuing payments, even if the cover has not lapsed.

While the relationship between premia for price and protection insurance and outstanding balance is in itself a cause for concern, it also helps make it more difficult for consumers to assess the costs and benefits of using store cards to finance purchases.

Such difficulties are features which may prevent, restrict, or distort competition between store cards and possible substitutes.

There also appear to be barriers to entry in the provision of payment, price and purchase protection insurance in relation to store cards, as only the credit provider and possibly the retailer have information on the card's balance each month. Thus other providers have much less opportunity to sell these insurance services. The store card provider therefore has a significant advantage which restricts competition to supply insurance services associated with store cards.

Furthermore, since revenues from insurance sales are taken into account by providers when assessing the overall profitability of store card operations, the OFT suspects that these revenues will be a factor taken into account when setting the level of interest rates on store card borrowing.

Proposed variation

The OFT is therefore minded to vary the terms of reference. It proposes first to refer expressly to insurance services provided explicitly in connection with the provision of store cards and of consumer credit through store cards, and secondly to clarify the position as regards store card credit services provided to retailers.

A copy of the original terms of reference and of the proposed variation to the terms of reference is enclosed.

I would be grateful if, should you have any comment on the proposed variation, you would provide them by Monday 31 January 2005.