

Market review of UK-EEA
consumer cross-border
interchange fees

Stakeholder submissions
on draft terms of
reference (MR22/2.1)

October 2022

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Names of individuals and information that may indirectly identify individuals have been redacted.

American Express



**American Express: Response to PSR's market
review of cross-border interchange fees – draft
terms of reference**

02 August 2022

[REDACTED]

[REDACTED]

A. Introduction

American Express welcomes the opportunity to provide feedback on the Payment Systems Regulator’s (PSR) draft terms of reference for a review of Visa’s and Mastercard’s cross-border interchange fees.

As the PSR is aware, unlike Visa and Mastercard, American Express operates a proprietary closed loop three party scheme in the UK, [REDACTED]

[REDACTED]

American Express supports the fair, reasonable and proportionate approach taken by the PSR to tailoring regulatory intervention in its recent provisional decision on remedies in the card-acquiring market review. While the current consultation on terms of reference for the market review into cross-border interchange fees is only in the early stages of the PSR’s work in this area, as the PSR develops its findings and once it reaches the point of considering potential remedies, we respectfully request the PSR to remain mindful of the potential risk that ambiguous or broad-brush regulatory intervention may give rise to unintended consequences for smaller three party schemes such as American Express and to continue to ensure a proportionate approach is taken. To avoid such outcomes, American Express would welcome the opportunity for ongoing dialogue with the PSR as an industry stakeholder throughout the course of the market review.

B. American Express response to the PSR’s consultation questions

As a general comment, American Express notes that the concept of market definition has a specific meaning for the purposes of competition law. While we recognise that the PSR has specific powers to conduct market reviews and has not defined the relevant “market(s)” for the purpose of this review, it may be helpful to clarify that UK-EEA consumer cross-border interchange fees are not a “market” as such. Rather we consider the relevant market is at least all card payments in the UK.

Q1: Do you agree with the proposed scope of the market review? If not, please explain:

- **how the proposed scope should be altered**
- **why you think the proposed scope should be altered in this way**

Please include any evidence you think is relevant to your response.

American Express agrees that the focus of the market review should be on UK-EEA cross-border interchange fees in the Visa and Mastercard payment systems. Our observations on this are set out below.

- a) **American Express operates a three party scheme** [REDACTED]

[REDACTED]

The draft terms of reference propose to “focus only on IFs which were covered by the caps imposed by the EU IFR prior to the UK’s withdrawal from the EU. That is, IFs applicable within 4PS to consumer and debit and credit transactions within the EEA.”

We welcome and agree with this approach to the scope of the PSR’s review, [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

- b) American Express’ model does not give rise to the antitrust concerns that have been examined in the context of Visa and Mastercard worldwide nor was American Express subject to the European Commission antitrust investigation that led to the provision of commitments by Visa and Mastercard to cap inter-regional interchange fees.

Four party schemes such as Visa and Mastercard operate with a network of PSPs performing the card issuing and/or the merchant acquiring function under licence by the schemes. The four party schemes and their PSPs rely on multilateral interchange fees to enable transactions to take place between independent PSPs. These PSPs are typically retail banks that use their client network to offer the card payment service to the retail banks account holders and merchant customers, as well as prospective customers.

Visa and Mastercard have historically set interchange fees based on a multilateral pricing agreement that sits at the heart of the model and which has been deemed anticompetitive, due to the collective pricing mechanism involved.¹ This mechanism has attracted antitrust scrutiny and criticism across the world and Europe, both at EU and national (including UK) levels. As the PSR describes in its draft terms of reference, the caps applicable since 2019 on Visa and Mastercard transactions made using a card issued outside the EEA at a merchant located in the EEA result from commitments given to resolve two such antitrust investigations by the European Commission.

The following statement summarises the concerns identified by the European Commission:

¹ Including by the UK Supreme Court and European Court of Justice. See: *Sainsbury’s Supermarkets Ltd (Respondent) v Visa Europe Services LLC and others (Appellants); Sainsbury’s Supermarkets Ltd and others (Respondents) v Mastercard Incorporated and others (Appellants)* [2020] UKSC 24 (17 June 2020) and *MasterCard Inc v European Commission* (Case C-382/12 P) [2014] 5 CMLR 23, which upheld the European Commission decisions in Cases COMP/34.579 - *MasterCard*, COMP/36.518 - *EuroCommerce*, and COMP/38.580 - *Commercial Cards*.

“The Statement of Objections ... alleges that MasterCard's interchange fees for transactions in the EU using MasterCard cards issued in other regions of the world breach European antitrust rules by setting an artificially high minimum price for processing these transactions.”²

Essentially, the concerns with multilateral interchange fees (paid by card acquirers and received by card issuers) were that they:

- (i) result from a collective pricing agreement between the PSPs and the four party schemes involved; and
- (ii) are non-negotiable for the merchants to whom these fees are passed on when paying for acquiring services provided by the four party scheme card acquirers, due to the dominance of Visa and Mastercard.

It is important to recognise that American Express operates a fundamentally different model to Visa and Mastercard. Consequently, American Express was neither a subject of these European Commission investigations nor a party to the commitments. [REDACTED]

[REDACTED]

c) [REDACTED]

d) Visa and Mastercard are the dominant duopoly: As the PSR notes in its draft terms of reference for its market review into scheme and processing fees, Visa and Mastercard accounted for 99% of card transactions in the UK by value and volume in 2021.

e) American Express is a small competitor [REDACTED] The PSR's data shows that American Express accounts for only a small share of card payments and as such is always a choice, not a 'must have', for consumers and merchants in the UK. As a result, American Express faces strong competitive constraints from the dominant four party card schemes, [REDACTED] Customers (cardholders and merchants) will only choose to use or accept a discretionary network like American Express if they see a benefit in doing so. [REDACTED]

[REDACTED]

Q2: Do you agree with our proposed approach? If not, please explain:

- how the proposed approach should be altered
- why you think the proposed approach should be altered in this way

² https://ec.europa.eu/commission/presscorner/detail/en/IP_15_5323

Please include any evidence you think is relevant to your response.

American Express broadly agrees with the PSR's approach to the market review. That said, we note that, unlike in the market review for scheme and processing fees, the PSR does not expressly propose to consider whether there are factors that mean that Visa and Mastercard have market power and face weak constraints in setting unregulated cross-border interchange fees.

Instead, the PSR proposes to understand the rationale for Visa and Mastercard's prices increases by examining the *"reasons provided by the card scheme operators and the considerations that Visa and Mastercard took into account, including strategic, competition and regulatory aspects"*.

Any examination of Visa and Mastercard's rationale for increasing cross-border fees should have regard to the dominant position enjoyed by these four party schemes and the impact that such market power has on their ability and incentives to increase prices. We therefore suggest that the PSR considers including this as part of the scope of the review.

Q3: Do you have views on the potential concerns we propose to investigate (set out in para 2.5 – potential harm to competition, innovation or service users)?

Are there other concerns with cross-border interchange fees that we should be considering?

Please include any evidence you think is relevant to your response.

As a small competitor to Visa and Mastercard, American Express welcomes the PSR's proposal to investigate concerns regarding the potential harm to competition and innovation (as well as service users) in its market review in line with its statutory objectives. Given the vast scale that Visa and Mastercard have, even a small increase in fees can have a huge impact on much smaller competitors, who do not have the same resources available for investments in innovation to ensure they can remain competitive. It is therefore critical the PSR clarifies how the income from such fees is utilised, to ensure this is not simply further entrenching the dominant position of these schemes.

British Airways

PSR Market review of UK-EEA consumer cross-border interchange fees

British Airways Response

Consultation questions

Question 1

- Do you agree with the proposed scope of the market review?

A. We have no objection with the proposed scope.

Question 2

- Do you agree with our proposed approach?

A. We have no objection with the proposed approach.

Question 3

- Do you have views on the potential concerns we propose to investigate (set out

in para 2.5)?

- A. British Airways have experienced increased cost, and therefore have become less competitive, due to its high volume of cross border payments between UK and EU and the increased costs imposed by Visa and Mastercard post Brexit. The majority of these resulted from customers with a EU issued card, which were processed in the UK, using merchant head office location. To mitigate these fees, the majority of EU payments were to be processed domestically. This involved change with the acquirer.
- B. British Airways has proactively reduced these costs, however the main restriction on mitigation activities to the cross border fees is the scheme rules that merchants must route payments via either a.) head office location or b.) the market in which a payment takes place (point of sale). This means that where the two are the same, for example UK merchant, UK point of sale, but EU issued card used **no mitigation can be taken**. For BA, this represents [REDACTED] of all cross border sales in UK/EU.

- Are there other concerns with cross-border interchange fees that we should

be considering?

- A. While BA has enacted a mitigation strategy this has involved complexity and incurred costs to implement, the application of interchange fee caps to cross-border transactions would remove the need to do this for both larger and smaller merchants (who may not be able to implement such changes). The overall impact of these fee increases on cross-border transactions is to make UK merchants less competitive compared to overseas and European merchants who will not incur these costs nor require the resource to mitigate them.

British Retail Consortium

BRC CONSULTATION RESPONSE – PSR MARKET REVIEW ON CARD FEES

ABOUT THE BRC

The BRC's purpose is to make a positive difference to the retail industry and the customers it serves, today and in the future.

Retail is an exciting, dynamic and diverse industry which is going through a period of profound change. Technology is transforming how people shop; costs are increasing; and growth in consumer spending is slow.

The BRC is committed to ensuring the industry thrives through this period of transformation. We tell the story of retail, work with our members to drive positive change and use our expertise and influence to create an economic and policy environment that enables retail businesses to thrive and consumers to benefit. Our membership comprises over 5,000 businesses delivering £180bn of retail sales and employing over one and half million employees.

Overview

The BRC welcomes the PSR's consultations on the market reviews of scheme and interchange fees.

Our most recent data shows that cards account for 67% of retail transactions, and 80% of retailers' cost of collection, with the value of card payments in 2020 totalling £326.2bn (BRC Payments Survey). It is therefore crucial to the retail industry that card fees are fair and competitive, and the BRC is very encouraged to see the PSR acting on this finally.

We firmly believe that interchange fees should be abolished, and other fees should be brought into regulation, as we have been advocating for many years.

Interchange fees

The BRC first formally complained to the European Commission in 1992 that [REDACTED] interchange fees unlawfully restrict competition and the annual BRC Payments Survey (formerly Costs of Collection Survey) began spotlighting excessive card costs in 1999.

Interchange Fee Regulation (IFR), introduced across the EU in 2015 after a generation of pressure from UK & European business, promised to "cut the cost of payments substantially for merchants, especially SMEs and that in turn should lead to a fall in consumer prices". In practice, it only regulates some interchange fees, and no card scheme fees.

In 2020, a UK Supreme Court ruling confirmed that [REDACTED] interchange fees are unlawful, yet these fees continue to be allowed by the PSR.

Following the UK's departure from the European Union, interchange fees have increased hugely for retailers. There have been new opportunities for anti-competitive behaviour and abuse of the card schemes dominant market position. UK-EEA multilateral interchange fees for card-not-present transactions have increased fivefold, from 0.2% to 1.15% for debit and 0.3% to 1.5% for credit, and there has been no evidence or reasoning to explain the dramatic rise in fees. CMSPI, the payments advisory firm, estimates that these changes to interchange have added £30.8 million in annual costs to UK retailers, at a time of soaring inflation (particularly as these rates are expressed in percentage terms) and coinciding with increased online and international expenditure following the COVID-19 pandemic.

PSR's proposed scope and approach – interchange fees

The BRC agrees with the proposed scope and approach of the market reviews. It is important to look at both debit and credit card fees and the rationale behind the sudden and sharp increase in costs. We are pleased to see that this is being treated as a priority by the PSR.

Within the scope of the market reviews, we also see it as important that the PSR considers other anti-competitive behaviours and, more widely, whether competition is working effectively in this market, and/or whether there are any issues for innovation and fintech firms caused by the dominant market position of the card schemes.

Whilst we agree with the approach outlined, the tangible aspects are somewhat vague, as we understand that this may change depending on the outcome of each stage.

It would be helpful to have an indication of proposed timings. As we have seen already, these fees have increased fivefold in a short period of time, and we believe a temporary intervention is likely to be required during the time period that the PSR is working on the market reviews. We are concerned that if the timeframes are too lengthy, the impact on the retail industry could be very harmful.

Whilst we understand the limitation that this particular market review is to look at cross-border interchange fees following the abuse of the regulatory loophole, we would welcome a broader examination of interchange fees and whether these are fit for purpose within the UK landscape. Many countries have abolished domestic interchange fees, including The Netherlands, Denmark and Canada, and in a market where card issuers generate sufficient income from other sources, it seems evident that interchange fees are no longer necessary in such a mature card market as the UK. This would be in line with the Supreme Court ruling of 2020 whereby the court declared interchange fees as unlawful.

CMSPI

About CMSPI

CMSPI is a technology-driven, global payments advisory firm focused on fostering improved productivity and innovation in the payment industry. CMSPI uses its data-driven insights and strategies to support hundreds of clients across the globe in making more informed business decisions.

This consultation response was constructed by CMSPI's market-leading '*Insights Team*', which is made up of economists, data and statistical experts, and experienced payments professionals. We have structured our response to reflect the key areas of the consultation document in which CMSPI can offer unique insights.

CMSPI Response to the Payment Systems Regulator's Market Review of Cross-Border Interchange Fees

Interchange Fee Regulation (IFR) provided an important step in enhancing market transparency with regards to multilateral interchange fees by capping the level of interchange the card schemes could charge for domestic and intra-regional consumer card transactions across the European Economic Area (EEA) (which at the time included the UK).¹ Following Britain's exit from the European Union (EU), the IFR ceased to apply to transactions between the UK and the EEA.²

CMSPI therefore strongly welcomes the PSR's further review of cross-border interchange rates. This is especially important as, following the implementation of the IFR, there were a number of UK court cases in relation to the competitiveness of multilateral interchange fees (MIFs) under UK and European competition law. In June 2020, those cases culminated in a judgment from the UK Supreme Court in which the Court ruled that MIFs were a restriction on competition under Article 101(1) TFEU and UK competition law. In seeking to address this element of the card payments market, merchants' interests are closely aligned with the PSR's goals of promoting competition and innovation within payments.

As outlined in the consultation document, this review aims to investigate the following areas:

¹ See the EY Study on the Application of the Interchange Fee Regulation, which finds that up to 72% of merchant cost savings are passed on to consumers. Available at:

<https://ec.europa.eu/competition/publications/reports/kd0120161enn.pdf>

² <https://www.supremecourt.uk/cases/docs/uksc-2018-0154-judgment.pdf>



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1. Increases to the below fees following the UK's exit of the EU:
 - o "Inbound IFs" - cross-border interchange rates on transactions with merchants in the EEA accepting a card issued in the UK.
 - o "Outbound IFs" - cross-border interchange rates on transactions with UK merchants accepting a card issued in the EEA.
2. Whether major card schemes' ability to increase these cross-border interchange fees is indicative of the market functioning sub-optimally.

In our response, we summarise CMSPI's analysis of UK interchange fee increases, as well as positions expressed by some of the UK's largest merchants. With the combination of client data insights and merchant interviews, our response spans over 15% of the UK retail payment acceptance market (by value of transactions), with representation across various industries including grocery, restaurants, apparel, petrol, and electronics.

1. Increases to Cross-Border Interchange Fees

The following points are submitted in response to **Question 3: Do you have views on the potential concerns we propose to investigate?**

Reclassification

Since 2015, interchange levels within the UK and EU have been governed by the IFR, which sets an upper bound on interchange fees for certain transactions.³ However, the IFR covers only domestic and intra-regional⁴ transactions, with inter-regional interchange fees covered by separate commitments secured with the global card schemes in 2019.⁵ With these agreements having been made prior to the UK's exit of the EU, there are currently no legislative caps on inter-regional interchange fees on EEA-issued cards used to carry out transactions with UK merchants.⁶

Prior to the UK's exit of the EU, EEA-UK card transactions were classified as intra-regional, and the IFR interchange caps of 0.2% for consumer debit and 0.3% for consumer credit were therefore in force. In October 2021 and April 2022, respectively, Visa and Mastercard

³ https://ec.europa.eu/commission/presscorner/detail/en/MEMO_13_719

⁴ Intra-regional refers to transactions where the card was issued within the same geographical region as the merchant is domiciled – for example, where both are within the EEA.

⁵ Commitments made individually by Visa

https://ec.europa.eu/competition/antitrust/cases/dec_docs/39398/39398_14155_4.pdf and Mastercard

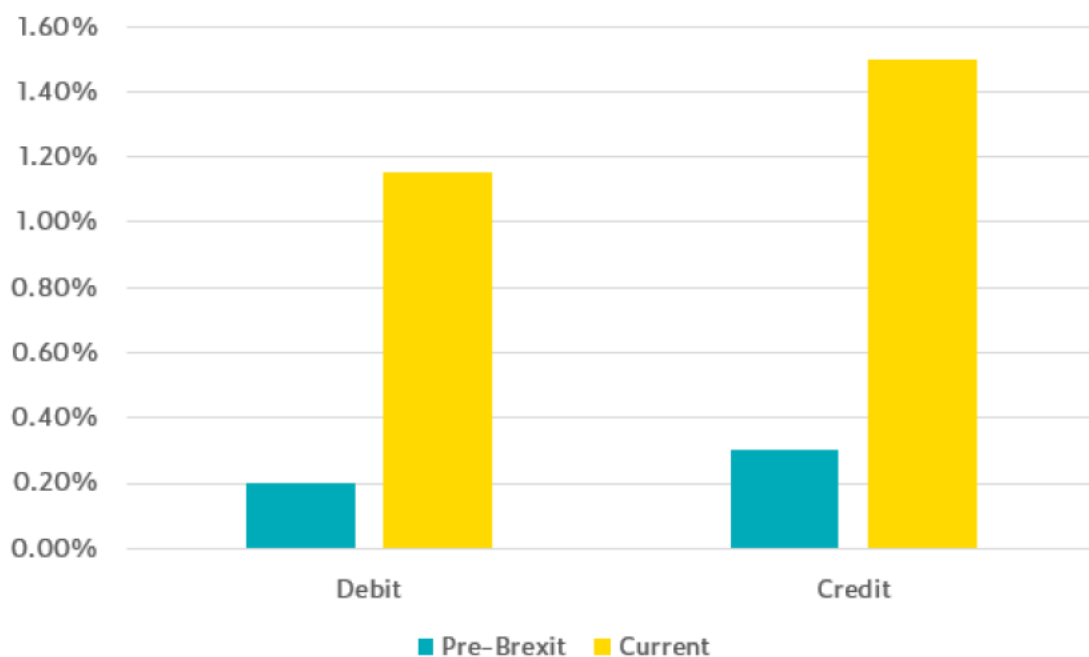
https://ec.europa.eu/competition/antitrust/cases/dec_docs/40049/40049_4173_3.pdf

⁶ <https://www.psr.org.uk/media/0gfaxvbc/psr-mr22-2-1-cross-border-interchange-fees-draft-tors-jun-2022.pdf>

reclassified interchange on these transactions as inter-regional, resulting in significant fee increases for UK merchants.⁷

As noted in the consultation document, following reclassification, interchange for UK merchants on Card Not Present transactions with EEA-issued consumer cards (“outbound IFs”) increased fivefold for Card Not Present transactions, with consumer debit increasing to 1.15% and consumer credit rising to 1.5% (Figure 1), while caps on Card Present transactions remained at IFR levels. These CNP fees are in line with interchange levels agreed for UK cards used in the EEA (“inbound IFs”), although there is at present no agreement specifically limiting outbound interchange to this level.

It is unclear if this fee increase is supported by increased costs to card schemes for processing cross-border payments between the UK and EEA post-Brexit, with the UK’s Parliamentary Treasury Committee recently writing to the international schemes to request a justification for the change.⁸



⁷ <https://www.bloomberg.com/news/articles/2022-07-14/mps-demand-answers-from-visa-and-mastercard-over-post-brexit-card-fees-hike>

⁸ <https://committees.parliament.uk/committee/158/treasury-committee/news/172071/treasury-committee-quizz-visa-and-mastercard-on-card-fee-increases/>

Figure 1. Comparison of current outbound interchange fees against pre-reclassification rates. Source: CMSPI interpretation of acquirer communications

Cost to UK Merchants

Visa and Mastercard's fivefold increase to fees on transactions previously regulated by the IFR has resulted in significant cost increases for UK merchants of all sizes. CMSPI estimates that increases to interchange rates within the proposed scope of this review, as named above, have added £30.8 million in annual costs to UK merchants, at a time when retailers are already struggling with inflation and as online volumes continue to rise post-pandemic.⁹

Merchants globally have raised concerns that inflation can also exacerbate rising costs caused initially by fee increases, as interchange is generally charged as a percentage of transaction value, resulting in fees increasing automatically in line with prices – to which the rising cost of card fees also contributes.¹⁰

In addition, these increases to cross-border fees have coincided with post-Covid-19 recovery for international commerce in the UK due to rising international travel, as a result of which international transactions are now more prevalent for UK retailers.¹¹ Furthermore, the UK has seen a continuing growth of ecommerce following the major increase to online spending catalysed by Covid-19 lockdown restrictions.¹² The combination of these additional factors is likely to have further contributed to increasing total interchange costs faced by UK merchants.

2. The Impact of UK-EEA Reclassifications

The following evidence is submitted in response to **Question 3: Are there other concerns with cross-border interchange fees that we should be considering?**

Whilst increases to consumer credit and debit rates present a significant cost increase to UK merchants, there are also several further ramifications of both regional reclassification and additional unregulated fee increases not within the scope of this review which CMSPI and its partner merchants would like to bring to the PSR's attention.

⁹ CMSPI estimates and analysis

¹⁰ <https://nrf.com/blog/swipe-fees-drive-inflation-and-consumers-ultimately-pay-price>

¹¹ <https://www.ons.gov.uk/peoplepopulationandcommunity/leisureandtourism/bulletins/overseastravelandtourism/april2022provisionalresults>

¹² <https://www.ons.gov.uk/businessindustryandtrade/retailindustry/timeseries/j4mc/drsi>

Fee Changes Due to Regional Reclassification

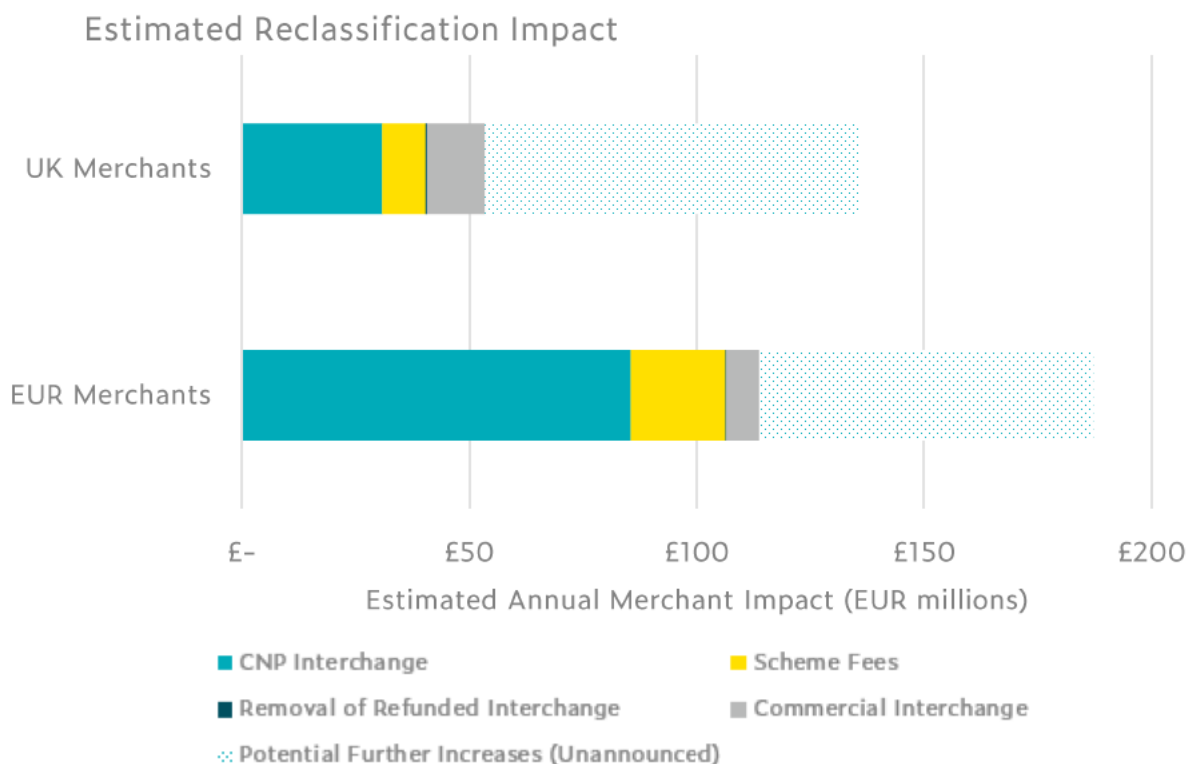


Figure 2. Total estimated combined cost impact for UK merchants due to cross-border fee changes. Source: CMSPI estimates and analysis based on CMSPI interpretation of acquirer communications.

CMSPI estimates that the combined total cost of post-Brexit fee changes due to regional reclassification for UK merchants currently stands at over £60 million for UK merchants.¹³

In addition to the approximately £30.8 million in increases to interchange fees by both major international card schemes evidenced above, this figure also includes interchange reclassifications on commercial cards, which is estimated to have resulted in a £12.7 million annual cost increase to UK merchants.¹⁴ It also includes Visa's removal of refunded interchange following a transaction refund on consumer transactions between the UK and EEA.

¹³ CMSPI estimates and analysis

¹⁴ Ibid.

Finally, regional reclassification of interchange fees may have wider effects should it be extended further to scheme fees. While Visa has brought some of its scheme fees in line with inter-regional rates, the full suite of UK-EEA scheme fees has yet to be fully raised to average inter-regional levels. By comparing intra-regional and inter-regional scheme fees in the UK, CMSPI estimates that if all scheme fees between the UK and EEA reached their inter-regional average, then the total aggregate impact of reclassification could reach over £135 million annually.¹⁵ Visa's current scheme fee reclassifications also impact Card Present transactions, increasing the proportion of merchants affected by the recent set of fee changes.

3. Additional Scope Considerations

The PSR's review of cross-border costs and interchange brings with it the opportunity to address additional concerns for merchants which are currently outside the scope of the PSR's review but which are related to its core investigative points around cross-border interchange fees.

The following two additional points for consideration relate to **Question 3: Are there other concerns with cross-border interchange fees that we should be considering?**

¹⁵ Ibid.

Further Interchange Fee Changes

Interchange fees on commercial cards, which were not covered by IFR, have continued to increase since 2015, but faced a further change in April 2022 (Figure 2).

April 2022 UK Interchange Changes

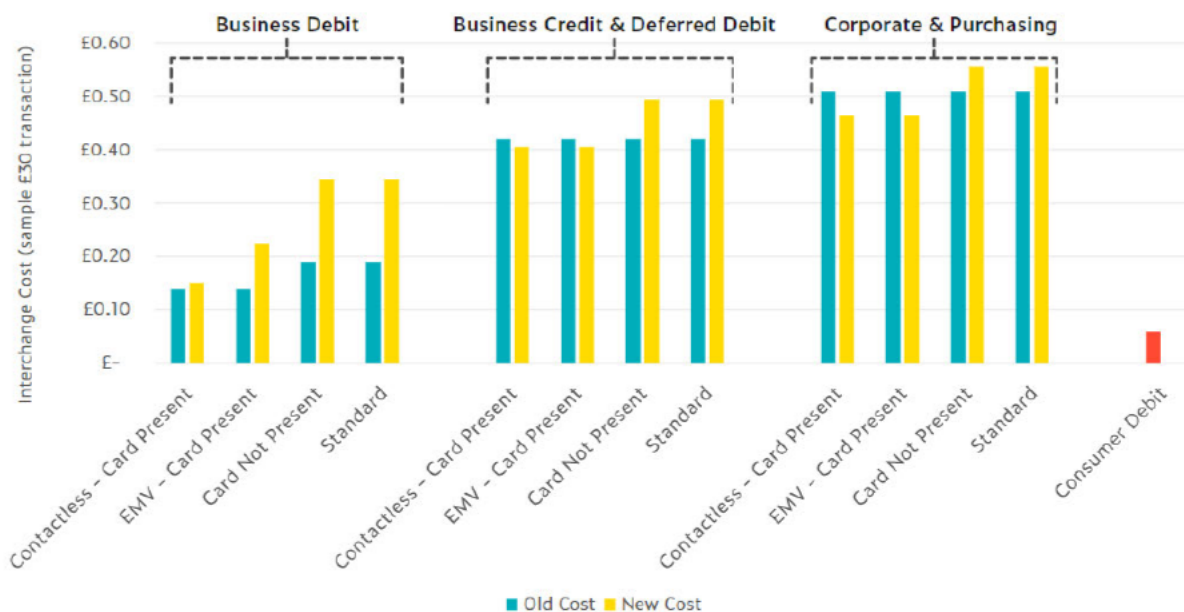


Figure 3. Changes to Visa commercial interchange fees for UK merchants in April 2022 for a sample 30 GBP transaction. Source: CMSPI estimates and analysis based on CMSPI interpretation of acquirer communications.

Current commercial interchange in the UK can be significantly higher than consumer interchange. The differential is illustrated in Figure 3, which shows the estimated effect of a set of commercial fee changes from Visa in April 2022 on a sample transaction, compared to the regulated consumer debit rate of 0.2%.

Cross-Border Acquiring Rules

Scheme rules currently state that regions are assigned based on the presence of the merchant in a given geography, rather than their acquirer or payments processor. These rules differ slightly depending on the payment channel used: for CP transactions, the merchant must have physical stores in that country, whereas for CNP transactions the merchant must have an entity established in the given country.¹⁶ Merchants have raised

¹⁶ <https://usa.visa.com/content/dam/VCOM/global/support-legal/documents/providing-proper-location-of-merchant-business.pdf>

concerns that these rules could limit competition in the market for cross-border acquiring, and may be a further element to bring into scope when looking to address cross-border card fees.

4. Limitations and Scope of Review

CMSPI welcomes the actions of the PSR to maintain and encourage effective competition within the UK card market and, in particular, in relation to cross-border interchange. However, CMSPI also puts forward the following points regarding the scope of the PSR's review into cross-border interchange fees following discussion with our merchant community.

The following two additional points for consideration relate to **Question 1: Do you agree with the proposed scope of the market review?**

Commercial Interchange Fees

As evidenced in Section 2 of this response, interchange fees for commercial transactions can be significantly higher than those for consumer transactions in the UK.

This additional area of consideration, which is not in scope of this review as a result of commercial fees remaining unregulated under IFR, could enable the PSR to take action on concerns over competition in commercial card interchange fees. In response to Question 1 of the PSR's consultation, some in CMSPI's merchant community have expressed concern that inaction on commercial interchange fees could allow for continuously rising costs and signal a lack of competition in this space.

Refunded Interchange Fees

As evidenced in Section 2 of this response, UK merchants no longer receive interchange fee refunds on refunded Visa consumer transactions between the UK and EEA (since October 2021).

While the impact of these changes is not estimated to have been as significant as other changes discussed in this consultation response, in part because only one of the two global schemes has thus far chosen to make these changes, merchants have expressed concerns that these changes are a further indication of the necessity of bringing UK-EEA transactions in line with pre-Brexit requirements.

CMSPI would therefore put forward on behalf of its merchant community that this review should include interchange refunds within its scope.

The following further point for consideration relates to **Question 2: Do you agree with our proposed approach?**



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Necessity of Legislation

Finally, CMSPI's merchants have expressed concern over whether a public consultation on outbound MIFs should have been necessary. While CMSPI welcomes this consultation and the PSR's review of cross-border interchange, there is no confirmation that the protections on cross-border interchange already in place prior to Brexit were intended to be discarded. In addition, there is significant legal evidence on the anti-competitive nature of interchange, in particular following the Supreme Court's determination on that issue in June 2020, stating that "MIFs charged to AAM in the relevant period were contrary to article 101(1) [of the TFEU] (and the equivalent provisions of UK and Irish competition law)."¹⁷

Merchants have therefore expressed concern that to require a full public consultation process for issues of law relating to protections not fully enshrined in UK law following withdrawal from the EU may set a precedent, significantly increasing time expense for both the PSR – and other regulatory bodies – as well as the wider merchant community.

Summary













			VISA	MASTERCARD	ESTIMATED ANNUAL UK MERCHANT IMPACT
 CNP INTERCHANGE	 UK Merchants		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<div style="background-color: #f06292; border-radius: 10px; padding: 5px; text-align: center; color: white;"> €34.65 MILLION </div>
	 EU Merchants		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	
 COMMERCIAL INTERCHANGE	 UK Merchants		<input checked="" type="checkbox"/>	<input type="checkbox"/>	<div style="background-color: #00bcd4; border-radius: 10px; padding: 5px; text-align: center; color: white;"> €14.31 MILLION </div>
	 EU Merchants		<input checked="" type="checkbox"/>	<input type="checkbox"/>	
 SCHEME FEES	 UK Merchants		<input checked="" type="checkbox"/>	<input type="checkbox"/>	<div style="background-color: #ffeb3b; border-radius: 10px; padding: 5px; text-align: center; color: white;"> €10.72 MILLION </div>
	 EU Merchants		<input checked="" type="checkbox"/>	<input type="checkbox"/>	
 CONSUMER INTERCHANGE REFUNDS REMOVED	 UK Merchants		<input checked="" type="checkbox"/>	<input type="checkbox"/>	<div style="background-color: #00695c; border-radius: 10px; padding: 5px; text-align: center; color: white;"> €0.33 MILLION </div>
	 EU Merchants		<input checked="" type="checkbox"/>	<input type="checkbox"/>	

Figure 4. Summary of changes to UK card fees (and estimated annual impact to UK merchants in EUR) following regional reclassification of EEA-UK transactions. Source:

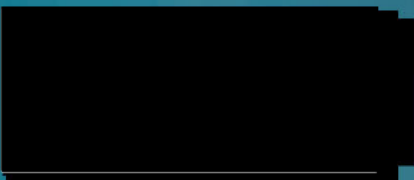
¹⁷ <https://www.supremecourt.uk/cases/docs/uksc-2018-0154-judgment.pdf>, p.83

CMSPI estimates based on interpretation of acquirer communications. Note: Scheme fee increases shown are partial and do not represent full reclassification.

CMSPI welcomes the PSR's review into cross-border interchange fees following post-Brexit regional reclassifications, particularly in combination with its review into UK scheme and processing fees and taking into account previous legal decisions by the Supreme Court on the anti-competitive nature of interchange. CMSPI estimates that UK merchants have seen an annual cost increase of £60 million as a result of changes to Card Not Present consumer fees, commercial fees, scheme fees, and the removal of interchange refunds between the UK and EEA (Figure 4). As several of these factors are currently out of the proposed scope of the PSR's investigation, CMSPI puts forward that the investigation scope be expanded in order to fully consider the broader effects of these changes on the UK merchant community, and therefore to best enable the PSR to understand how to encourage effective competition within the UK card payments industry.



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Coadec



COADEC RESPONSE

MR22/2.1: Market review of UK-EEA consumer cross-border interchange fees

About Coadec:

The Coalition for a Digital Economy (Coadec) is the policy voice of tech startups and scaleups in the UK. Since 2010, Coadec has worked to engage on behalf of tech startups in public policy debates in the UK across a range of priority issues for startups including access to finance, immigration and skills, and technology regulation.

General comments on the PSR consultation paper

Coadec greatly welcomes the PSR's market review of UK-EEA consumer cross-border interchange fees.

The PSR explains that it wants to understand the rationale behind the – fivefold – increases in interchange fee (IF)¹ rates for Visa and Mastercard's consumer debit and credit UK-EEA card-not-present (CNP) transactions since the UK's withdrawal from the EU, as well as the impact of these increases.² In particular, the PSR asks whether the card scheme operators' ability to increase these fees is an indication that the market(s) or aspects of market(s) is not working well.³

In our view, Mastercard and Visa's ability to increase these fees is unmistakable evidence that the market is not working well – and the PSR must intervene.

The PSR has already said in response to the House of Commons Treasury Select Committee that it has not seen any cost justification for Mastercard and Visa's interchange fee increases.⁴

Hence, absent such cost justification, we see only three possible explanations for the interchange fee increases:

- (1) Mastercard and Visa agreeing with each other⁵ to increase their UK-EEA cross-border interchange fees, at the same time and by the same amount – this would of course be a serious breach of UK competition law; or
- (2) Mastercard and Visa increasing their UK-EEA cross-border interchange fees independently of each other, but nevertheless each representing a "*decision of an*

¹ Also called "*multilateral interchange fee*" (MIF).

² PSR Consultation paper: Market review of UK-EEA consumer cross-border interchange fees: An update and draft terms of reference (MR22/2.1), June 2022 (**PSR Cross-border interchange consultation**), para. 1.18.

³ PSR Cross-border interchange consultation, para. 2.1.

⁴ Letter from Chris Hemsley, PSR Managing Director, to Rt Hon Mel Stride MP, Chair, Treasury Select Committee, 17 December 2021, answer to Q1.

⁵ Or otherwise coordinating.



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associations of undertakings” (i.e. of Mastercard and Visa’s issuers respectively, given issuers’ common interest in higher interchange fees) – this would also be a breach of competition law; or

- (3) Mastercard and Visa are each exercising an abuse of a dominant market position, of setting excessive and/or unfair prices, i.e. by raising prices so significantly without apparent constraint. This would also be a breach of competition law.

In our view, the most likely explanation for the interchange fee increases is a combination of (2) and (3).

The PSR has responsibility for enforcing UK competition law – primarily the Competition Act 1998 (**CA98**) – in relation to payment systems.⁶

The PSR also of course has regulatory duties – under the Financial Services (Banking Reform) Act 2013 (**FSBRA**). In our view, those regulatory duties also require the PSR to act in response to Mastercard and Visa’s dramatic interchange fee increases.

We explain each of these in turn.

(1) Mastercard and Visa’s UK-EEA cross-border interchange fee increases is potentially the result of a price-fixing agreement between Mastercard and Visa

The card schemes’ dramatic increases in their UK-EEA consumer cross-border interchange fees in 2021 could have been the result of a direct agreement between Mastercard and Visa to raise those prices. This is also more likely given the quick succession of Mastercard and Visa’s UK-EEA interchange announcements – Mastercard’s at the end of 2020 and Visa’s March 2021, with both increases effective from October 2021⁷ – and identical levels of interchange fee increases.

This first explanation assumes, however, that in the absence of such (illegal) price-fixing, there would be a competitive constraint on the level of interchange fees, such that the payment scheme that set a higher interchange fee might suffer a loss of business (e.g. a loss of acquirers and/or merchants to the scheme that set a lower interchange fee).

In reality, however, Mastercard and Visa do not compete with each other to attract and/or retain acquirers and/or merchants on the level of interchange fee, either UK-EEA cross-border or any interchange fees,

On the contrary, competition in payment card markets and other similar “*multi-sided markets*” is characterised by what the European Commission has called “*reverse competition*”,

⁶ Concurrently with the Competition & Markets Authority (**CMA**).

⁷ See Consultation paper, footnote 8.



namely, where Mastercard and Visa actually compete with each to increase the level of interchange fees, in order to attract and/or retain card issuers and cardholders, namely:

“IFs are subject to reverse competition meaning that competition between card schemes to attract card issuers (banks) leads to ever higher interchange fees (and consequently, MSCs). IFs are basically revenues offered to banks by card schemes in exchange for issuing their cards rather than the cards of the competitors. Therefore, an increase in MIFs offered by one card scheme leads banks to issue the cards of this particular scheme.”⁸

“In the context of card payments, reverse competition means that card schemes compete with each other by offering higher MIF revenues to banks that issue their cards. This results in higher fees for card payments in general, which are passed on merchants and, ultimately, consumers (rather than lower fees which would be the case under normal competition). As a result there is a welfare loss for merchants and consumers and a restricted market entry for new players, as ever increasing levels of MIFs are considered as a minimum threshold by banks that issue cards.”⁹

The Commission provided multiple case studies (and analysis) of such reverse competition.

Accordingly, in our view Mastercard and Visa’s dramatic increases in their UK-EEA consumer cross-border interchange fees is an unambiguous example of such reverse competition.

Such reverse competition of course does not vindicate Mastercard and Visa’s interchange fee increases. On the contrary, it shows why such price increases are likely to harm consumers¹⁰ and competition, are also likely to be unlawful, and also why it is less likely that there is an explicit “price fixing” agreement explanation for the fee rises.

(2) Mastercard and Visa’s UK-EEA interchange fee increases are the result of likely unlawful anti-competitive agreements between Mastercard and Visa card issuers respectively

UK and EU regulators and courts have now found repeatedly that the setting of payment card interchange fees is the result of anti-competitive agreements between Mastercard and Visa’s respective issuers.

⁸ European Commission Staff Working Document: Impact Assessment accompanying the Commission’s proposal for the EU Interchange Fee Regulation, SWD(2013) 288 final (**IFR Impact Assessment**), Volume 1/2, page 19.

⁹ IFR Impact Assessment, Volume 1/2, page 86.

¹⁰ I.e. both merchants and end-consumers.



Moreover, the European Commission, and the EU's and UK's highest courts, have specifically found that UK-EEA cross-border interchange fees “violate [EU and UK competition] rules on restrictive business practices”.¹¹

There is no plausible reason why the UK's withdrawal from the EU should change these legal findings.

In particular, the courts and regulators have repeatedly found that decisions on the level and structure of intra-EEA interchange fees¹² are decisions of “associations of undertakings” – namely, decisions of associations of Mastercard and Visa issuers within the meaning of Article 101(1) Treaty on the Functioning of the European Union (TFEU) (and also Section 2 CA98). This is essentially because issuers “share a common interest as regards the MIF because it yields guaranteed revenues for their issuing business”.¹³ This conclusion is also irrespective of Mastercard's or Visa's successive changes of structure from membership associations to public companies.¹⁴

The European Commission, and UK and EU Courts, have also repeatedly found that the Mastercard and Visa have failed to show that their intra-EEA MIFs (or any MIFs) meet (any of) the cumulative conditions required for exemption under Article 101(3) TFEU, in particular:

- i. the existence of “objective efficiencies” resulting from the MIFs;
- ii. that all customer groups in a payment card system – i.e. cardholders and merchants – must receive a “fair share of the benefits” that result from the MIFs; and
- iii. that the MIFs are “indispensable” to achieving these benefits.¹⁵

Furthermore, in the European Commission's most recent MIF decisions (in 2019) concerning Mastercard and Visa's EEA-to-rest-of-World inter-regional MIFs¹⁶, its “preliminary conclusion” was that Mastercard's and Visa's inter-regional MIFs infringed Article 101 TFEU.¹⁷ This was because the Commission found that Mastercard and Visa's inter-regional

¹¹ European Commission press release: Antitrust: Commission prohibits MasterCard's intra-EEA Multilateral Interchange Fees (IP/07/1959), 2007. See also summary at *Sainsburys v MasterCard; Asda, Argos, and Morrisons v MasterCard; and Sainsbury's v Visa* UK Court of Appeal [2018] EWCA 1536 (Civ) para. 12-36.

¹² I.e. of which UK-EEA interchange fees were previously.

¹³ European Commission Mastercard Decision, para. 3.

¹⁴ See European Commission Decision 2007 Case COMP/34.579, COMP/36.518 and COMP/38.510 (**European Commission Mastercard Decision 2007**), para. 3; and also *Dune v Mastercard and Dune v Visa* [2021] CAT 35, para. 90-103.

¹⁵ For example, see European Commission Mastercard Decision, para. 5-12, and also all subsequent EU and UK MIF decision judgments.

¹⁶ European Commission Decisions of 29 April 2019 Case AT.40049 – Mastercard II (**European Commission 2019 Mastercard Inter-Regional MIF Decision**) and Case AT.39398 – Visa MIF (**European Commission 2019 Visa Inter-Regional MIF Decision**), concerning inter-regional MIFs applicable to merchants located in the EEA with consumer debit and credit cards issued outside of the EEA.

¹⁷ European Commission 2019 Mastercard Inter-Regional MIF Decision, para. 2; and European Commission 2019 Visa Inter-Regional MIF Decision, para. 3.



MIFs constituted “a decision of an association of undertakings that had as its object and effect an appreciable restriction of competition in the market for acquiring card payments within the EEA”¹⁸, in particular, that inter-regional MIFs amounted to “horizontal price fixing”, which is “by its very nature harmful to competition”.¹⁹

The Commission noted also “the lack of competition between Visa and MasterCard in the acquiring market” and that the Mastercard and Visa “Honour All Cards Rule[s]” which means that “a merchant, which accepts ‘ordinary’ Visa cards [...] cannot refuse payments that carry a higher interchange fee, for example because the card [...] is inter-regional and therefore carries a higher MIF”. Last, the Commission found that the inter-regional MIFs were capable of appreciably affecting trade between EEA Member States and did not appear to meet the requirements for exemption under Article 101(3) the MIFs.

All such findings are directly applicable to the UK-EEA cross-border MIFs, or more so.

Mastercard and Visa nevertheless proposed “Commitments” to cap their inter-regional MIFs at 0.2% for debit card present (CP) transactions, 0.3% for credit card CP transactions, 1.15% for debit card card-not-present (CNP) transactions, and 1.50% for credit card CNP transactions (**the Mastercard and Visa Inter-regional MIF Commitments**), which the Commission accepted.

Our understanding is that Mastercard and Visa’s UK-EEA inbound MIFs are subject to those EU Commitments.²⁰ Hence, Mastercard and Visa have evidently decided to increase their UK inbound CNP MIFs to the levels set in these Commitments – and also to increase their UK-EEA outbound CNP MIFs to the same levels.

While this does not make such interchange fee increases lawful, we agree with the Commission’s preliminary conclusion that Mastercard’s and Visa’s inter-regional MIFs infringed Article 101 TFEU and are “by their very nature harmful to competition”.

Hence, whether classified as (former) EEA-MIFs or as UK-EEA inter-regional MIFs, in our view, Mastercard’s and Visa’s UK inter-regional consumer card MIFs are the result of unlawful anti-competitive price-fixing agreements between Mastercard and Visa card issuers – and Mastercard and Visa should therefore repeal the interchange fee increases.

(3) Mastercard’s and Visa’s increases in their UK-EEA interchange fees represent excessive and/or unfair pricing abuses

¹⁸ European Commission 2019 Visa Inter-Regional MIF Decision, para. 32.

¹⁹ European Commission 2019 Visa Inter-Regional MIF Decision, para. 34.

²⁰ As UK-EEA inbound MIFs means MIFs applicable to merchants in the EEA with consumer cards issued in the UK, i.e. now outside of the EEA.



The PSR notes that, since the UK's withdrawal from the EU, Mastercard and Visa have increased the IF rates for UK-EEA consumer CNP transactions by a factor of five, i.e. from 0.2% to 1.15% for debit cards (a factor of 5.75, or 475%) and from 0.3% to 1.5% for credit cards (a factor of 5.00, or 400%).

Moreover, in combination with the Mastercard and Visa scheme and processing fee increases, the cost to merchants of UK-EEA CNP transactions has increased by a factor of up to 11 (or 1,000%).²¹

Such price increases are not merely evidence that the market is not working well. On the contrary, such price increases are evidence of likely excessive and/or unfair pricing, in abuse of dominant market positions, contrary to Article 102 TFEU and Chapter II CA98.

For example, by comparison, the Competition & Markets Authority (**CMA**) has recently fined pharmaceuticals company, Advanz, £100 million, after finding that Advanz had charged "*excessive and unfair prices*" for supplying a pharmaceutical product²², following Advanz having "*inflated*" its prices by 1,110% between 2009 and 2017.²³ In particular, the CMA found that Advanz had "*abused its dominant position in breach of the prohibition imposed by [...] the 'Chapter II prohibition' of the Competition Act 1998 [...], by charging excessive and unfair prices*".²⁴

The CMA has also recently accused pharmaceutical firms Pfizer and Flynn of similar "*illegal pricing*", for abusing their dominant positions to "*overcharge the NHS*" for vital anti-epilepsy drugs, following price increases of "*between 780% and 1,600%*" over a four-year period.²⁵ The CMA has also recently fined other pharmaceuticals firms £260 million for similar pricing abuses.²⁶

In each of these cases, the CMA found (and/or provisionally found) that each of these firms:

- i. have dominant market positions; and
- ii. abused their dominant positions, in breach of the Chapter II prohibition CA98, by charging excessive and unfair prices – on the basis pricing increases of between around 800% and 1,600% over four- to eight-year periods.

²¹ Since 2015, Visa's scheme and processing fees for UK-EEA consumer debit and credit card CNP transactions have increased from 0.01% to 1.16%, hence the total of Visa's UK-EEA consumer debit CNP interchange fee plus scheme and processing fees has increased from 0.21% to 2.31%, i.e. by a factor of 11, or 1,000%.

²² Liothyronine tablets, a thyroid drug.

²³ CMA Press release: CMA fines pharma firm over pricing of crucial thyroid drug, 29 July 2021.

²⁴ Decision of the Competition and Markets Authority: Excessive and unfair pricing with respect to the supply of liothyronine tablets in the UK, Case 50395, 2021, para. 1.4.

²⁵ See CMA Press release: CMA accuses pharma firms of illegal pricing, 5 August 2021, concerning suspected unfair pricing of phenytoin sodium capsules by pharmaceuticals firms Auden Mckenzie and Actavis UK.

²⁶ See CMA Press release: CMA finds drug companies overcharged NHS, 15 July 2021, concerning excessively high prices of hydrocortisone tablets.



In comparison, Mastercard and Visa's UK-EEA cross-border interchange fee (and scheme and processing fee) prices have increased between 400% and 1,000% in less than just one year.

Hence, in our view, Mastercard and Visa's UK-EEA cross-border interchange fee increases represent similar excessive and unfair pricing abuses of their respective dominant market positions.

Mastercard and Visa have dominant (or moreover parallel monopoly) market positions in the supply of acquirers and in turn to merchants, essentially because Mastercard and Visa do not compete for either acquirers or merchants. For example, the European Commission said in its most recent MIF decisions that "*The Commission's preliminary view [is] that merchants' lack of countervailing bargaining power might be due to several factors, in particular the must-take nature of Mastercard cards [and must-take nature of Visa cards...] and the [resulting] lack of competition between Mastercard and Visa [for acquirers and merchants].*"²⁷

Our view that Mastercard and Visa have such dominant monopoly positions is consistent with past regulatory decisions²⁸ and also with the European Commission's current review of the EU market definition²⁹, especially concerning market definition in "*multi-sided markets*", such as payment card systems.³⁰

(4) Mastercard and Visa's UK-EEA interchange fee increases are incompatible with the PSR's statutory competition objective, in particular, of ensuring efficient interchange fee pricing

The PSR is carrying out its market review under Part 5 of the Financial Services (Banking Reform) Act 2013 (**FSBRA**) ("*Regulation of payment systems*").

FSBRA also defines the PSR's general duties, namely, "*to advance one or more of its payment systems objectives*": the competition objective, the innovation objective, and the

²⁷ European Commission 2019 Mastercard Inter-Regional MIF Decision, para. 36; and European Commission 2019 Visa Inter-Regional MIF Decision, para. 37.

²⁸ European Commission Mastercard Decision 2007 found that "*The Commission [...] retains as [the] relevant product market [...] the market for acquiring payment card transactions [but...] It can be left open [...] whether acquiring for Mastercard products is a product market on its own [separate from Visa]*" (para. 307).

²⁹ See European Commission Staff Working Document Evaluation of the Commission Notice on the definition of relevant market for the purposes of Community competition law, SWD(2021) 199 final.

³⁰ In particular, the Commission's expert advisers to the Commission's review (Professors J.-U. Franck and M. Peitz) highlight that multi-sided platforms are likely to act as monopolists on the "*multi-homing*" side of the market, i.e. where users (such as acquirers and merchants) "*must take*" all platforms (i.e. to Mastercard and Visa), in contrast to the "*single-homing*" side of the market, where users (such as issuers and cardholders) have the option to choose between platforms.



service-user objective.³¹ Of these, the competition objective requires the PSR to “*promote effective competition in the market for payment systems, and the markets for services provided by payment systems*”, including between different operators of payment systems (**PSOs**), and between different payment service providers (**PSPs**). In doing so, the PSR may have regard to “*the level and structure of fees, charges or other costs associated with participation in payment systems*”.³²

What this means should of course be with reference to the Government’s stated intentions in enacting FSBRA and establishing the PSR, in which the Government said that:

“4.14 [...*Designated PSOs, such as Mastercard and Visa*] will be required through statute to adhere to principles on:

- *Efficient and transparent pricing;*
- *Non-discriminatory access;*
- *Good governance;*
- *Maintaining and developing the payment system; and*
- *Co-operation.*

4.16 *On efficient and transparent pricing, the requirement will be that prices are set at the appropriate level to benefit current and future end-users of the payment system. [Payment system operators] will be required to ensure that their pricing structures are transparent to their users, and that they are derived through a fair and transparent methodology. [...Each PSO] will, when requested, present its pricing methodology to the regulator, who will then review it and require amendments as appropriate. Where the regulator is not satisfied that the [PSO] is using an acceptable pricing methodology, and having given it sufficient opportunity to remedy the situation, the regulator will have the power to intervene to directly set prices for (1) direct access to a payment system [e.g. scheme and processing fees], [...] (3) interchange fees.”*

It is evident though that Mastercard and Visa have not derived their UK-EEA cross border interchange fees through “*a fair and transparent methodology*” at all, nor presented such a methodology to the PSR for review. Accordingly, it is highly unlikely that such interchange fees “*at the appropriate level to benefit current and future end-users of the payment system*”.³³ On the contrary, such interchange fees are likely to harm end-users, especially merchants, as well as cardholders.

The PSR must therefore intervene – as the Government said it should do – to set Mastercard and Visa’s UK-EEA cross-border interchange fees directly, using the powers given to the PSR for this purpose.³⁴

³¹ Section 49.

³² Section 50.

³³ Which is essentially the same test as required under Article 101(3) TFEU.

³⁴ Namely, to vary agreements relating to payment system fees and charges, FSBRA Section 57.



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In particular, the PSR should order that Mastercard and Visa reverse their UK-EEA cross-border interchange fee increases, at least until such time that the schemes are able to demonstrate that such increases are compatible with both competition law and the PSR's statutory objectives.



Response to consultation questions

Scope

Question 1

- ***Do you agree with the proposed scope of the market review? If not, please explain:***
 - ***how the proposed scope should be altered; and***
 - ***why you think the proposed scope should be altered in this way.***
- ***Please include any evidence you think is relevant to your response.***

We agree with the PSR's proposed scope of the market review, namely, to focus on EU-EEA cross-border debit and credit consumer card interchange fees in the Mastercard and Visa card payment system, i.e. the interchange fees that Mastercard and Visa have decided to increase following the UK's withdrawal from the UK.

We also agree on prioritising "outbound" interchange fees (i.e. interchange fees on transactions using EEA-issued cards to make payments to a merchant located in the UK), as these are the interchange fees paid by UK merchants.

We note though that "inbound" interchange fees (on transactions using a UK-issued card to make payments to merchants based in the EEA) are still harmful to UK consumers, as these may increase the prices paid by UK consumers at EEA merchants, especially where such EEA merchants have now chosen to surcharge UK-issued cards.

We are concerned though that the PSR should not disregard other interchange fees that also now fall outside the UK Interchange Fee Regulation (**UK IFR**), namely:

- cross-border interchange fees between the UK and the rest of the World; and
- commercial card interchange fees.

Under the Commitments made by Mastercard and Visa to the EU, EEA merchants benefited from reductions in cross-border interchange fees between the EEA and the rest of the World. UK merchants would have also benefited from such Commitments had the UK remained in the EU.

Hence, in addition to the increases in Mastercard and Visa's UK-EEA cross-border interchange fees, the UK's withdrawal from the EU has also meant a failure to secure reductions in UK-to-rest-of-the-World interchange fees, leading to a double whammy for UK merchants.

In our view, the PSR should therefore bring such UK-to-rest-of-the-World cross-border interchange fees into the scope of the review.



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We also note that commercial card interchange fees, which are currently unregulated by either the UK IFR, EU IFR, or any relevant card scheme Commitments, are generally much greater still even than Mastercard and Visa's new UK-EEA cross-border interchange fees, namely, of up to 2.5%. Such interchange fees impose a substantial cost on merchants (and their customers), especially those merchants with a high share of commercial card transactions, such as wholesale (i.e. business-to-business) and travel sector merchants.

In our review, the PSR should consider a separate review of commercial card interchange fees, as part of its wider card fees work.



The PSR's proposed approach

Question 2

- ***Do you agree with our proposed approach? If not, please explain:***
 - ***how the proposed scope should be altered; and***
 - ***why you think the proposed scope should be altered in this way.***
- ***Please include any evidence you think is relevant to your response.***

The PSR says that it wants to understand the impact of and rationale for the rises in IF levels for UK-EEA consumer debit and credit CNP transactions. The PSR is rightly concerned that Visa and Mastercard's ability to increase these fees is an indication that the market(s) or aspects of market(s) is not working well for users, including in the form of higher prices paid by UK merchants and consumers.

We agree that the PSR should examine the potential drivers and justifications for the increases in these IFs since the UK's withdrawal from the EU, including the reasons given by the card scheme operators, and the impact of the IF increases on competition, innovation, and service users.

As we have set out above, we consider that the interchange fee increases are contrary to UK competition law, and to the PSR's statutory objectives, and that the PSR must therefore intervene, to ensure that Mastercard and Visa repeal the IF increases.



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Question 3

- ***Do you have views on the potential concerns we propose to investigate (set out in para 2.5)?***
- ***Are there other concerns with cross-border interchange fees that we should be considering?***
- ***Please include any evidence you think is relevant to your response.***

We have set out our concerns about Mastercard and Visa's UK-EEA (and also other) cross-border interchange fees at the outset of our response above (and also in response to Question 1).

HSBC

HSBC UK Bank plc

PAYMENT SYSTEMS REGULATOR

Market Review of UK-EEA Consumer Cross-Border Interchange Fees

RESPONSE TO CONSULTATION

01AUG2022

COVER SUBMISSION

HSBC UK Bank plc ('HSBC UK') welcomes the opportunity to respond to the Payment Systems Regulator's consultation on the draft Terms of Reference for the market review of UK-EEA Consumer Cross-Border Interchange Fees.

As a major card issuer in the UK that uses both VISA and MasterCard payment systems across our debit and credit card portfolios, we support the PSR's review of the interchange fees applicable to consumer card transactions between the UK and EEA (UK-EEA) within these card payment systems. Whilst we do not have a merchant acquiring business, it is important for all parties in the market that such fees are functioning in line with the PSR's statutory competition, innovation and service-user objectives to avoid adverse outcomes, either directly or indirectly.

As previously communicated to the PSR, HSBC UK has not been directly involved in card-acquiring in the UK for the last decade. As a result, our comments below primarily relate to our Debit and Credit card issuing business using Mastercard and Visa.

Scope

1. **Do you agree with the proposed scope of the market review? If not, please explain:**

- **How the proposed scope should be altered?**
- **Why you think the proposed scope should be altered in this way?**

Please include any evidence you think is relevant to your response.

1.1 HSBC UK supports the proposed scope of the market review.

1.2 We recognise the purpose of the market review to understand the rationale for the reported increases in cross-border UK-EEA interchange fees following the UK's withdrawal from the EU and the consequent removal of the caps imposed by the EU Interchange Fee Regulation.

1.3 We agree it is appropriate that outbound interchange fees are prioritised in the review.

Our Proposed Approach

2. **Do you agree with our proposed approach? If not, please explain:**

- **Why you think the proposed approach should be altered in this way?**

Please include any evidence you think is relevant to your response.

2.1 HSBC UK supports the proposed approach to the market review.

2.2 The card schemes set the interchange fee and we agree that the PSR will need to explore with them the economic, commercial or other reasons for the increases in outbound and inbound interchange fees between UK-EEA.

2.3 The approach proposed to look at the impact and rationale for the increase in interchange fee levels for UK-EEA consumer debit and credit is well defined with the focus on outbound interchange fees.

3. **Do you have views on the potential concerns we propose to investigate (set out in para 2.5)?**

Are there other concerns with cross-border interchange fees that we should be considering?

Please include any evidence you think is relevant to your response.

3.1 HSBC UK has no additional comments.

Global Pay

**GPUK LLP RESPONSE TO THE PAYMENT SYSTEMS REGULATOR'S CONSULTATION ON
DRAFT TERMS OF REFERENCE IN THE MARKET REVIEW OF UK-EEA CONSUMER CROSS-
BORDER INTERCHANGE FEES**

1. **Executive Summary**

- 1.1 This response is prepared on behalf of GPUK LLP trading as Global Payments ("GPUK").
- 1.2 GPUK welcomes the opportunity to respond to the Payment Systems Regulator's ("PSR") consultation on the draft terms of reference in the PSR's market review of UK-EEA consumer cross-border interchange fees ("**Consultation**" and "**Review**").
- 1.3 GPUK is supportive of the PSR carrying out the Review.
- 1.4 GPUK would encourage the PSR to continue to consult with the full range of stakeholders within the payments ecosystem as it progresses with the Review.

2. **Consultation Questions**

Question 1: Do you agree with the proposed scope of the market review? If not, please explain how the proposed scope should be altered and why you think the proposed scope should be altered in this way.

- 2.1 Yes, GPUK agrees with the PSR's scope of the review.

Question 2: Do you agree with our proposed approach to the market review? If not, please explain how the proposed approach should be altered and why you think the proposed approach should be altered in this way.

- 2.2 Yes, GPUK agrees with the PSR's scope of the review.

Question 3: Do you have views on the potential concerns we propose to investigate? Are there other concerns with cross-border interchange fees that we should be considering?

- 2.3 GPUK agrees with the proposed approach.

Harcus Parker

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29 July 2022

Cross-border interchange fees market review team
Payment Systems Regulator
12 Endeavour Square
London E20 1JN

BY EMAIL: cardfees@psr.org.uk

Dear Sirs,

PSR Consultation: Market review of UK-EEA consumer cross-border interchange fees/An update and draft terms of reference June 2022

We write in response to your consultation: [PSR MR22/2.1 Market review of UK-EU consumer cross-border interchange fees draft terms of reference](#), to share our views on the Draft Terms of Reference.

We do not disclose any sensitive or confidential information.

We act for Commercial and Interregional Card Claims I Limited and Commercial and Interregional Card Claims II Limited. On 6th June 2022, these companies filed four applications for Collective Proceedings Orders in the Competition Appeal Tribunal. In these applications, the claimants allege that Mastercard and Visa have infringed competition law through the setting of multilateral interchange fees on commercial cards, and on consumer cards used inter-regionally. In the litigation, the claimants seek damages for the losses they have suffered. Beyond the litigation and for the longer term, they seek the abolition of harmful interchange fees. Your consultation engages this latter objective.

In answer to your question 1 – whether we agree with the proposed scope of the market review - we comment as follows:-

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- We support the PSR's proposed investigation into inbound and outbound UK-EEA interchange fees in the Mastercard and Visa payment systems, covering both debit and credit consumer cards.

In answer to both your question 1 and your question 3 (other concerns with cross-border interchange fees):-

- We note your statement in paragraph 2.5 that, “[w]e expect our thinking to develop over the course of the review, including the possibility that our concerns (regarding potential harm to competition, innovation or service-users) are amended, not pursued further or new ones added.” In our view, it is critical – at the outset of your market review - to define a scope that encompasses all reasonably-foreseeable issues. The current proposed scope, however, omits one critical change in the market which we believe has substantial effects on merchants, particularly in some sectors such as travel and hospitality. Since the UK left the EU, the UK is no longer within the scope of the Mastercard and Visa interregional commitments. That means that when a card issued in a country outside the EEA (and UK) is used in a transaction occurring in the UK, the applicable interchange fees would previously have been regulated by those commitments, but no longer. The result is that those interchange fees have also risen substantially. This is not captured in your current scope, but in view of its commercial importance and the fact that it is closely-related to your current scope, should be included.
- Commercial card interchange fees are far higher than domestic consumer card fees. We believe the PSR should – whether in this current market review or separately – investigate (and report publicly) whether this should be so. Commercial cards are commonly used, particularly in certain sectors of the economy, and those merchants accepting a lot of commercial card payments are consequently paying very much higher fees than those who do not, and it is not clear why.

As regards with your proposed approach in question 2, we comment on one underlying assumption you make:-



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- In paragraph 1.16, you state, “[a]s IFs [*Interchange Fees*] represent a cost to merchants of accepting card payments, they are likely to be passed on to some or all of their customers (at least in part).” This statement is not supported by any evidence, and prejudices the outcome of a fundamental issue in the interchange litigation before the Competition Appeal Tribunal. We note that in the only interchange case to have proceeded to trial in the UK, pass-on was considered, but not found. We therefore do not accept the contention, or the assumption, that any IFs have been passed on to customers. It is enough to found your investigation on the concerns of merchants about how IFs affect their businesses. Consequently, we disagree with the framing of the statement in paragraph 2.4: “including in the form of higher prices paid by UK merchants and consumers”; specifically, while overcharged interchange fees clearly affect UK merchants, it is not established that these cause consumers to pay higher prices.

We are happy to discuss these comments with the PSR and provide further information.

Harcus Parker

Yours faithfully

Harcus Parker Limited

Innovate Finance

MR 22/1.1 Market review of card scheme and processing fees

MR 22/2.1 Market review of UK-EEA consumer cross-border interchange fees

Innovate Finance response to the PSR consultations and terms of reference

About Innovate Finance

Innovate Finance is the independent industry body that represents and advances the global FinTech community in the UK. Innovate Finance's mission is to accelerate the UK's leading role in the financial services sector by directly supporting the next generation of technology-led innovators.

The UK FinTech sector encompasses businesses from seed-stage start-ups to global financial institutions, illustrating the change that is occurring across the financial services industry. Since its inception in the era following the Global Financial Crisis of 2008, FinTech has been synonymous with delivering transparency, innovation and inclusivity to financial services. As well as creating new businesses and new jobs, it has fundamentally changed the way in which consumers and businesses access finance.

Introduction and key points

Innovate Finance welcomes the opportunity to respond to the PSR's consultations on the draft terms of reference in relation to the proposed market reviews into scheme and processing fees and cross-border interchange fees.

In preparing this response, we have consulted with our FinTech start-up and scale-up members that span the issuer and acquirer sides of the discussion. Based on engagement with our members, it is clear that there is currently not a consensus on the best approaches to be taken by the PSR. However, all members are in agreement that these issues are of critical importance to industry, and there is a need to avoid unintended consequences for innovators in the market.

In light of the above, Innovate Finance would urge the PSR to engage further with the FinTech community. We would be happy to facilitate member roundtable discussions and / or wider engagement with the FinTech community.

[ENDS]

Lloyds Banking Group

LLOYDS
BANKING
GROUP



LLOYDS BANKING GROUP PLC

Market review of card scheme and processing fees

Market review of UK-EEA consumer cross-border interchange fees

Response to PSR's Consultation on its Draft Terms of Reference

2nd August 2022

[REDACTED]

Lloyds Banking Group Response

Lloyds Banking Group (LBG) welcomes the opportunity to respond to the Payment Systems Regulator's (PSR) consultation paper on the draft Terms of Reference for the Market Review of card scheme and processing fees and the Market Review of UK-EEA consumer cross-border interchange fees. The reviews as outlined in the consultation papers touch on critical issues, including cross-border card payment interchange, scheme fees and retail payments. These are areas that have been the subject of regulatory and legal scrutiny for many years, and in which there remains considerable uncertainty for stakeholders. These studies are therefore an opportunity for the PSR to resolve some of these issues and to provide the clarity and certainty required to support competition, innovation, and investment.

We would welcome working collaboratively with the PSR through these reviews to help with its understanding of how the markets operate in practice, and to provide constructive views as the analysis progresses.

Our position as one of the largest banks in the UK brings insight into the perspectives of a number of different groups who may be affected by the outcome of these reviews, including consumers and merchants. Previous market reviews have successfully involved stakeholders such as ourselves through roundtables, bi-lateral meetings and working and discussion papers, and we encourage the PSR to make the most of such tools again for these reviews.

We would like to note a few points that we hope the PSR will consider.

In terms of scheme & processing fees:

- The card schemes operated by Visa and Mastercard provide significant value to both our retail and merchant customer groups by facilitating a robust and easy to use payment network with well-known consumer protections. They have also enabled significant investment in features to protect customers and merchants such as Strong Customer Authentication, contactless payments, tokenisation, and other initiatives which are continuing to improve the payment experience of all participants. We hope the PSR will take this value into account as part of its assessment.
- We continue to work closely with Pay.UK and the PSR on the development of the New Payments Architecture (NPA), including on the key issue of promoting account-to-account payments through Open Banking. Given the PSR's stated expectation for competition between cards and the NPA, reviews of the two should not be approached in isolation. We believe the scheme and processing fees review needs to go hand-in-hand with this work on the NPA; to ensure consumer protections, encourage competition, and unlock account-to-account payments. We would welcome involvement in discussions regarding the use of further investment in Open Banking and the NPA. We would also highlight the letter we sent to Pay.UK in June, regarding its commitments to industry for the NPA, in which we reiterated our firm belief that a viable commercial fee arrangement is needed to enable a commercial and sustainable model which is competitive and supports future innovation.
- Our previous responses to both the card-acquiring market review and the proposed remedies noted that it is the complexity of scheme fees which we believe impacts the ability of acquirers to provide meaningful price comparisons for merchants. This review is an opportunity to address this issue, which is at the root of the PSR's concerns in the merchant card-acquiring review. The PSR should be clear that such complexity is within the scope of what it will explore.
- To gain a complete picture, we would suggest that the PSR may also want to include in the scope of its review so-called "non-compliance assessments" by the Schemes and the financial consequences associated with these. These can result in participants (such as acquirers) having to make significant additional payments to the schemes based on conduct of merchants and/or customers who may be impacted by rule changes imposed by the schemes.

And in terms of cross-border interchange:

- Continuing legal uncertainty created by unprecedented levels of litigation in the UK courts about the level of interchange (even when set within a regulated cap as is the case for domestic interchange) may deter investment and entry into the retail payments and banking markets and may result in erosion of customer or merchant benefits. It would be a missed opportunity if this review were not also used by the PSR to provide legal certainty over the level of interchange in the future (particularly for domestic transactions), ensuring card schemes remain on a commercial and sustainable footing and providing clarity for emerging alternatives such as NPA.

We welcome further discussion with the PSR on the terms of reference for these market reviews and the substance of the issues that these will address.

Mastercard

Mastercard response to *PSR 'Market review of card scheme and processing fees' and 'Market review of UK-EEA consumer cross-border interchange fees'* draft terms of reference

2 AUGUST 2022

Introduction

Mastercard is providing a joint response to the PSR's separate consultations on its draft terms of reference for its 'market review of card scheme and processing fees' (MR22/1.1) and its 'market review of UK-EEA consumer cross-border interchange fees' (MR22/2.1). Noting that the market reviews have a different focus, several of the issues which Mastercard wishes to highlight overlap both and so it makes sense to respond in this way.

Mastercard is pleased that the PSR recognises the importance and value of card payments in the UK. Card payments are highly valued as a means of payment by both consumers/businesses as payers and merchants as payees. They operate in an increasingly competitive retail payments market where users have many other choices of how to pay and be paid. They succeed because they combine speed and convenience, with very high levels of operational resilience, dispute resolution and consumer protection tools and an increasingly wide array of value-added services which enhance the overall payment experience.

But card payments are not ubiquitous. They are not always accepted and where they are accepted they are not always the preferred payment option, as merchants may steer customers to alternatives. In a diverse and dynamic payments market, different payment options may be more or less suited to different payment needs. For example, cards play a relatively small role in both person to person and business to business transactions. They are more suited to person to business transactions, but even for that purpose they may not be favoured by smaller merchants or those operating in sectors such as financial services or utilities or subscriptions where direct debit may be the merchant's preferred (or sometimes only) method of receiving payment. Card payments may play a greater role for deferred delivery payments, where consumer protection is of greatest value.

In undertaking these market reviews, the PSR will need to consider card payments within the wider payments market. As we outline in the remainder of this response, the PSR's proposed narrow focus on fees will not enable it to develop a full understanding of how well competition is functioning more broadly. Mastercard recognises the importance of fees in an overall assessment of a market and understands why the PSR may want to examine them. But an investigation of fees in isolation is likely to limit the PSR's ability to assess how well the market is delivering in the interests of its participants.

Overall Approach

As the PSR highlights, these market reviews (particularly the scheme and processing fees review) follow on from its card-acquiring market review, but it is notable that the PSR is taking a very different approach. That previous market review was broadly titled "*Market review into the supply of card-acquiring services*" and the PSR sought to investigate the functioning of the card-acquiring market generally, as outlined in the Terms of Reference which framed its approach to the market review in wide terms:-

- "*We are assessing whether the supply of card-acquiring services is working well for UK merchants, and ultimately consumers.*"
- "*We will consider how competition is working in the supply of card-acquiring services and whether there are aspects of the market(s) that adversely affect competition in the supply of those services.*"
- "*We will examine how competition in the supply of card-acquiring services operates.*"

In its approach, the PSR listed 11 areas which it would investigate including:-

- "*the nature and characteristics of card-acquiring services and developments in the supply of these services*"
- "*who provides card-acquiring services and how the supply of these services has developed historically*"
- "*how the supply of card-acquiring services may differ across broad types of merchants*"
- "*the scope for differentiation and innovation in the supply of card-acquiring services*"
- "*the quality of service that merchants receive from their provider of card-acquiring services*"

Of those 11 areas which the PSR listed for investigation, only one referred to the fees paid by merchants. The PSR made no pre-judgement that the level or type of fees charged by acquirers was a matter of concern. It was one factor or indicator to consider in assessing the overall functioning of the market. The PSR's final remedies also identify quality of service as an important factor in driving switching.

By contrast, the current market reviews are titled "*Market review of card scheme and processing fees/ UK-EEA consumer cross-border interchange fees.*" Rather than investigating the competitive functioning of card products more broadly the PSR is proposing from the outset to focus only on the

fees charged. The PSR will recognise (as it did in the card-acquiring market review), that fees are just one element of the functioning of a market. In order to understand the effectiveness of competition, it is necessary to examine many other factors which were included as part of the card-acquiring market review such as innovation, quality of service, changes in products over time and varying usage by different merchants.

As we describe in further detail in response to the questions below, by focussing only on fees, the PSR may be unable to draw firm conclusions about how competition in the cards sector has developed generally and to understand the huge increase in added value to merchants, which those fees reflect.

Responses to questions on 'market review of card scheme and processing fees'

We provide responses to each of the PSR's questions below, but first wish to highlight an additional important issue which the Terms of Reference do not appear to address, namely the scheme and switch separation requirements contained in Article 7 of the Interchange Fee Regulation.

The purpose of the separation is to create two distinct markets – a market for scheme services and a market for switching services. The separation requirements ensure that Mastercard's commercial strategies and decisions for each are made entirely independently and specifically that there can be no bundling of commercial offerings between scheme and switch. The effect is that Mastercard's customers will make separate and independent decisions as to whether to purchase Mastercard scheme services and Mastercard switch services. Therefore, although Mastercard participates in both markets in the UK, the PSR will need to consider them separately in line with the objectives and obligations which Article 7 imposes. For each market, there will be quite different market players, competitive constraints and market dynamics to consider, as well alternative options. In its final Terms of Reference, the PSR will need to outline how it intends to manage the separation and independently consider competitive constraints in each.

Question 1

- **Do you agree with our description of scheme and processing fees? If not, please explain:**
 - **how our description should be altered and whether there are alternative approaches to categorising Mastercard and Visa scheme and processing fees**
 - **why you think the description should be altered in this way. For example, you may think it is important to distinguish between fees which are mandatory and those which are optional**

Mastercard is broadly content with the PSR's description of its fees, except that 'processing' fees should more accurately be described as 'switching' fees. Processing is different and a much broader function than switching. It is undertaken by independent payment processors and includes a wider range of activities including for example issuing and acquiring processing services. The functions of authorisation, clearing and settlement of card transactions are collectively referred to as switching.

As highlighted above, as the Interchange Fee Regulation requires a separation of scheme and switch fees, it is an important distinction for the PSR to be aware of as it undertakes the market reviews. Different parts of Mastercard set those fees independently and they are subject to different competitive constraints. That separation may also limit the PSR's ability to investigate and reach general conclusions about the fees paid by issuers/acquirers.

The wide variety of types of Mastercard fees reflects the range of products and services offered, which is extensive. The PSR will be aware from the card-acquiring market review that some fees relate directly to transactions, but some do not, whilst other fees are avoidable in certain situations. The PSR is therefore likely to need to consider what further sub-categorisation of fees may be required in order for it to manage its investigation. Mastercard welcomes the opportunity to assist and engage with the PSR in that process in order to ensure a mutual understanding of the approach being taken and how a logical framework can be developed.

Question 2

- **Do you agree with the proposed scope of the market review? If not, please explain:**
 - **how the proposed scope should be altered**
 - **why you think the proposed scope should be altered in this way**

Mastercard operates in an increasingly diverse competitive landscape. The PSR has not provided adequate justification for focussing only on Visa and Mastercard and excluding other providers of consumer to business payment services. In particular, excluding Amex (and other card schemes is incongruent with a review focused on fees (as the PSR proposes) as the fees charged by those other card schemes are generally amongst the highest in the market. It is overly simplistic to consider only total market share because schemes such as Amex have a much larger presence in specific important (and more profitable) sectors of the market such as cobrands (in which Amex is a market leader), premium consumer, commercial and cross-border/travel. By excluding Amex from the market review,

the PSR will be unable properly to investigate the competitive functioning of the market as a whole – and some of the most profitable parts of the cards sector and if (ultimately) any remedies do not apply to Amex, they will not benefit the category of merchants for which Amex acceptance is a critical part of their business.

Mastercard recognises the PSR is proposing to use 2014 as the starting point for its market review because that was the date chosen for the card-acquiring market review. However, that review began in 2018 and Mastercard believes that there is no logical reason to go back as far for the purposes of this market review, particularly because Mastercard understands that the PSR will be repeating its data collection process in any case and therefore will not be relying on the data which it previously collected. It is also important to note that the PSR chose 2014 for the card-acquiring market review specifically because it wanted to measure whether acquirers had passed on the interchange reductions of the IFR, but that 'before and after' analysis is not relevant for this market review. Indeed, the scheme and switch separation (also introduced by the IFR) is likely to add a further complication to the PSR's analysis and data collection. In any case, Mastercard believes that 8 years is an unnecessarily long period over which to conduct this market review and that 5 years would be more appropriate, because anything earlier is of very limited relevance to understanding the functioning of the market in 2022 and beyond.

More broadly, we have outlined above our concerns about the PSR limiting the scope of the market review only to fees, which is in stark contrast to the scope of the card-acquiring market review to "*examine the supply of card-acquiring services*" and everything associated with it. This narrow focus will inevitably limit the PSR's understanding of the market dynamics and risks findings being based an inadequate assessment of how the market functions. We address this risk further in response to question 3.

Question 3

- **Do you agree with our proposed approach to the market review? If not, please explain:**
 - **how the proposed approach should be altered**
 - **why you think the proposed approach should be altered in this way**

As a result of the narrow scope, Mastercard believes that the proposed approach risks giving the PSR a limited and distorted view of the market. In particular, by not examining the competitive functioning of the payments market more broadly, the PSR appears to view Mastercard (and Visa) in isolation and not recognise the wider competitive retail payments market in which they operate.

The factors mentioned in paragraphs 2.7 and 2.8 are addressed in question 5 below and so here we focus on the issues listed in paragraph 2.9, which the PSR proposes to investigate. As highlighted above, Mastercard believes that those 14 issues of 'potential concern' which the PSR proposes to examine are too narrowly defined. Whilst acknowledging that they follow from the PSR's proposed scope, a limited focus on fees will not allow the PSR properly to understand: the evolution of services provided and the value delivered by cards; the differences between alternative payment methods/why certain payments better suit certain needs; the evolving nature of retail payments; and the factors influencing the effectiveness of competition.

The PSR should adopt a broader outcomes-focussed view of the retail payments sector and Mastercard (and Visa's) role within it. It should consider levels of satisfaction of both payers and payees and how they compare with alternative payment methods. It should examine the value proposition of cards and how that also compares with alternative payment options and the correlation between the value proposition and the fees charged. It should investigate how and why certain payers and payees may prefer certain payment methods for certain types of payment, the correlation with fees, and availability of steering options which enable merchants to direct payers to their preferred payment method. It should explore the changing competitive landscape of retail payments in the UK, what it will mean for card payments in the future and who competitive constraints will involve.

Without this type of investigation and analysis, the PSR will be unable to understand the wider market in which cards operate and the impact which it has on fees charge both now and in the future.

Question 4

- **Are there specific types of scheme and processing fees we should focus our work on? Perhaps because the scheme and processing fees represent a large percentage of total network fee revenues or because they have changed substantially?**
- **Are there specific types of scheme and processing fees we should not focus our work on? Perhaps because the fees represent a small percentage of total network fee revenues or because they have not changed substantially?**
- **In your response, please explain:**
 - **which scheme and processing fees we should or should not focus on**
 - **why you think we should focus on these scheme and processing fees**

As highlighted above, Mastercard's customers pay wide-ranging and diverse sets of different fees, reflecting the breadth of services our customers adopt and value which those services deliver. Many of the fees are optional, even for those issuers and acquirers that have already chosen the Mastercard payment network, giving issuers and acquirers the choice as to whether to procure certain additional products/services from Mastercard, to develop their own capabilities, buy them elsewhere or not at all. Some fees reflect services which are in effect provided to merchants, whilst others are more directly to the benefit of issuers and acquirers. The size and focus of an issuer or acquirer's business means that certain services may be of greater or lesser value to them and they will pay fees accordingly.

Merchants are one step removed from Mastercard. Mastercard generally has no contractual relationship with merchants, who do not pay Mastercard's fees directly. Acquirers will often pass on Mastercard's fees to merchants (in addition to their own margin) and they will decide whether and how to do so. No merchant is obliged to accept Mastercard, but those who choose to do so make that choice having weighed the benefits which they receive against the costs which the acquirers charge.

No payment method is cost-free for merchants to accept and the increased acceptance of digital payments is in part due to merchants growing recognition of the comparably higher costs of accepting cash. Different payment methods will incur different types of costs, which include direct costs (fees), indirect costs and back-office costs. It will be important for the PSR to recognise that although card payment costs are more easily identifiable (as they are charged directly as fees), similar costs exist for account to account payments. Most obviously, banks will recover the costs of managing Faster Payment transactions indirectly from their customers in different ways meaning that those costs are spread (less transparently) across the population of users and are therefore likely to be subject to limited competitive constraint.

The PSR is correct to recognise that it will in some way need to focus its examination of fees on certain types or categories of fees. The available time and resources may not permit the PSR to examine every fee individually and so the PSR may wish to consider narrowing the range of fees which it examines. However it chooses to do so, the PSR must ensure it provides a fair view of all of the fees charged and the value associated with them. Again, if the focus is too narrow on particular categories or individual fees, the PSR will not be able to develop a sufficient understanding of the competitive market in which those fees are set, because Mastercard looks at the whole landscape.

Question 5

- **Do you have views on the potential factors that we propose to investigate (set out in paragraphs 2.7 and 2.8)?**
- **Are there other factors in relation to scheme and processing fees that we should be considering?**

We addressed the broader approach which Mastercard believes that the PSR should be taking in this market review in response to question 3. Here, we understand that the PSR is asking only about the particular factors which it will investigate in order to understand the level of competitive constraint which Mastercard experiences. We address each proposed factor in turn.

Firstly, the PSR's proposal to examine barriers to entry "*in setting up and running card payment systems*", suggests the PSR believes that the only form of competition which Mastercard and Visa may face is from alternative card schemes. Of course, the PSR will be aware from its own work that competition to card schemes is much wider and includes various forms of account to account payments, open banking, digital wallets, BNPL and others likely to emerge in the future such as stablecoins and person to person payment providers moving into person to business payments, as has been seen in several other markets. It is vital that the PSR take a broader view and recognises that there are non-card-based payment acceptance alternatives to Mastercard and Visa which exert increasingly competitive constraints on them.

Secondly, Mastercard welcomes the PSR's intention to investigate the varied alternative payment acceptance options available to merchants. As mentioned above, no merchant is obliged to accept Mastercard and those who do have different means of steering their customers to other options, if they wish to do so. The PSR's own evidence demonstrates that cards are the preferred payment method of many merchants, taking account of costs incurred and the benefits received. Nevertheless, in some sub-sectors, cards have a small market share compared with other payment methods such as cash, direct debit or account to account options.

Thirdly, the proposal to investigate the lack of fee transparency of card scheme fees for merchants is somewhat misconceived. As the PSR will be aware, it is acquirers (and issuers), not merchants, who pay Mastercard's fees. Any merchant concerns about lack of fee transparency can only relate to the acquirer fees which they pay, in respect of which Mastercard has no visibility (let alone control). Of course, the PSR investigated the issue of acquirer fee transparency in detail during the card-acquiring market review and is currently proposing remedies to address its concerns, but this cannot form any

basis for a conclusion that Mastercard (and Visa) have market power or face weak constraints. As for our range of scheme fees, these are available in full to our acquirers and they may in turn be communicated to merchants when the acquirer chooses to do so. The detail of each of Mastercard's individual fees will in many cases be more than is useful to a particular merchant, as our diverse and wide-ranging fee schedule reflects the range of different services adopted by some (but not all) of Mastercard's customers.

Fourthly, we welcome further engagement with the PSR about how Mastercard fees are charged to different customers. In simple terms, Mastercard does not differentiate its fees in this way and they apply on a non-discriminatory basis to all customers. The PSR will be aware from its card-acquiring market review that acquirers do differentiate in how they charge merchants, whilst issuers may recover their costs from their customers in many different ways.

Responses to questions on 'market review of UK-EEA consumer cross-border interchange fees'

Question 1

- **Do you agree with the proposed scope of the market review? If not, please explain:**
 - **how the proposed scope should be altered**
 - **why you think the proposed scope should be altered in this way**

Mastercard is satisfied with the scope of the review being limited to UK-EEA cross-border consumer interchange fees. We understand why the PSR is choosing to focus on outbound interchange fees being paid by UK merchants, but, as we describe further below, it is important to recognise the purpose of interchange and the benefits which it drives.

Whilst it may be a cost to acquirers/merchants, it is an important source of revenue for issuers to cover the costs which they incur in providing card payment services to their customers. Therefore, although the PSR may have no need to investigate the interchange fees which are paid by EEA merchants, it should be mindful that those same interchange fees are received by UK issuers and help fund the services which the PSR values in promoting the interests of UK consumers. Of course, the same occurs in reverse which will be important for the PSR to bear in mind as it investigates the interchange fees paid by UK merchants.

Therefore, although Mastercard has no comments on the scope (in terms of card and transaction type), we believe that it is important that the PSR looks beyond a simplistic view of the level of the fee, in order to understand what the fee is actually for and how it contributes the development of card payments more broadly.

Question 2

- **Do you agree with our proposed approach? If not, please explain:**
 - **how the proposed approach should be altered**
 - **why you think the proposed approach should be altered in this way**

Mastercard recognises that the PSR wants to understand the impact of interchange levels. Mastercard agrees with this approach, but it is important that the PSR undertakes the task comprehensively and does not look only at one side of the market.

Any investigation into interchange requires the PSR to examine the purpose and benefits of interchange. A cost to a merchant/acquirer generates a commensurate source of revenue, investment and cost recovery to the issuer. The PSR understands that Mastercard does not receive interchange and is therefore objective in determining the level at which it is set. Mastercard sets interchange fees at levels which fairly balance the interests of issuers and acquirers (and their respective customers) and the value which the card payment generates. As is well-recognised, that will differ according to many factors such as markets, transaction type and user type.

Mastercard welcomes the opportunity further to engage with the PSR about the vital role which interchange plays in the cards ecosystem, the benefits of setting the fees at a particular level and how it promotes positive benefits and value to all participants.

Question 3

- **Do you have views on the potential concerns we propose to investigate (set out in para 2.5)?**
- **Are there other concerns with cross-border interchange fees that we should be considering?**

These issues are largely addressed in response to question 2.

The PSR appears to be pre-judging its analysis of interchange by referring to "*potential harm to competition, innovation or service-users*": the PSR should identify what harm they have in mind and

what evidence there is to already suggest that such harm is occurring. Mastercard is not aware of evidence of any harm of this kind, but does intend to present strong evidence to the PSR that setting interchange at the correct level does support each of the PSR's objectives as it: promotes competition (by providing a vital source of revenue to smaller, new entrant issuers); promotes innovation (by providing the revenue necessary for issuers to invest in card payment innovation); and promotes the interests of service-users (by increasing the availability, resilience, security, convenience and functionality of card payments). In addition, it also promotes efficiency by encouraging consumers to select payment methods that are low-cost to merchants, which is a key benefit of interchange.

As outlined above, any proper assessment of interchange must examine the impact on both sides of the market. The PSR must ensure that its approach and its focus is objective in that respect and does not view interchange fee simply as a cost which must be justified, but appreciates that there is also a benefit which should be recognised.

All queries in relation to this response should be to [REDACTED]
[REDACTED]

Payments Association



connecting the future

Market Review of UK-EEA consumer cross-border interchange fees

**PSR
June 2022**

Response from The Payments Association

Introduction

The Payments Association welcomes the opportunity to contribute to the PSR “*Market Review of UK-EEA consumer cross-border interchange fees*”.

The community’s response contained in this paper reflects views expressed by our members and industry experts recommended by them who have been interviewed and who are referenced below. As The Payment Association’s membership includes a wide range of companies from across the payments value chain, and diverse viewpoints across all job roles, this response cannot and does not claim to fully represent the views of all members.

We are grateful to the contributors to this response, which has been drafted by [REDACTED], our Head of Policy & Government Relations. We would also like to express our thanks to the PSR for their continued openness in these discussions. We hope it advances our collective efforts to ensure that the UK’s payments industry continues to be progressive, world-leading and secure, and effective at serving the needs of everyone who pays and gets paid.

With special thanks to:

- [REDACTED], Co funder and CEO, Weavr
- [REDACTED], Head of Product Pricing, Trust Payments
- [REDACTED], Principle Payments Consultant, ENDAVA
- [REDACTED], Director of Product – Card Payments, Modulr
- [REDACTED], Founder & CEO, StarLiX
- [REDACTED], Director of Relationship Management, Chargebacks911
- [REDACTED], Regulatory Change Manager, Modulr
- [REDACTED], Project Cross Border Lead, The Payments Association
- [REDACTED], Global Head of Card Business, Nium
- [REDACTED], Director, Payments Consultancy Ltd
- [REDACTED], CEO, Paynetics UK
- [REDACTED], Head of Payment Card Scheme Compliance, DECTA
- [REDACTED], Board Member & Head of Product Offering DECTA
- [REDACTED], UK General Manager, Paybl Ltd
- [REDACTED], Head of Europe and Global Head of Travel Payments, Nium
- [REDACTED], Director of Product, Modulr

Please note that this response does not reflect the views of Mastercard or Visa.

[REDACTED]
Director General
The Payments Association

Contents

The section numbering below corresponds to the numbering of the 'questions for respondents' in this paper.

1. Do you agree with the proposed scope of the market review?

Overall, we agree. However some diverging opinions have emerged:

- Some members think that the schemes have taken the interpretation that the UK is now in a different region, inconsistently applying cross-border charges for CNP transactions but not for CP ones. And they suggest this to be included in scope
- Other members suggest including inbound IFS, otherwise UK consumers may not be aware of where the e-commerce merchant is legally registered, and therefore face higher fees.

2. Do you agree with our proposed approach?

Largely, our members agree. However, some would appreciate the PSR reviewing transactions that are currently being charged as CNP when the customer is, in fact, present within the store. This is increasingly occurring with the growth of mobile and digital transactions applied in-store and it is stifling innovation and increases fees for merchants.

3. Do you have views on the potential concerns we propose to investigate (set out in para 2.5)?

The vast majority of our diverse membership cannot see any potential concern, mainly because interchange fees are set by the scheme but collected by the issuer, hence no concern can effectively arise. Nonetheless, some have questioned where the increase is going into the value chain, and would welcome more transparency in terms of why the increase and who ultimately benefits from it.

Are there other concerns with cross-border interchange fees that we should be considering?

Largely, our members broadly agree that more transparency is mandatory and seek clarification on the reasons behind the increase in interchange fee beyond Brexit. Further, they would encourage the PSR to also review the impact of marketing promotions and subsidies offered by the Visa / Mastercard network to certain merchants as a way of offsetting the impact of higher cross-border interchange fees.

About The Payments Association

The Payments Association (previously the Emerging Payments Association, or EPA) is a community for all companies in payments, whatever their size, capability, location or regulatory status. Its purpose is to empower the most influential community in payments, where the connections, collaboration and learning shape an industry that works for all. It works closely with industry stakeholders such as the Bank of England, the FCA, HM Treasury, the PSR, Pay.UK, UK Finance and Innovate Finance.

Through its comprehensive programme of activities and with guidance from an independent Advisory Board of leading payments CEOs, The Payments Association facilitates the connections and builds the bridges that join the ecosystem together and make it stronger. These activities include a programme of monthly digital and face-to-face events including an annual conference, PAY360, The PAY360 Awards dinner, CEO round tables and training activities. The Payments Association also runs six stakeholder working project groups covering financial inclusion, regulation, financial crime, cross-border payments, open banking and digital currencies. The volunteers in these groups represent the collective views of the industry and work together to ensure the big problems facing the industry are addressed effectively. The association also conducts original research which is made available to members and the authorities. These include monthly whitepapers, insightful interviews, and tips from the industry's most successful CEOs.

See www.thepaymentsassociation.org for more information. Contact [REDACTED] for assistance.

Revolut



Revolut

Revolut Ltd Response to the PSR's UK-EEA Consumer Cross Border Interchange Fee Consultation

Date: 29 July 2022

To: Cross-border interchange fees market review team (Payment Systems Regulator)

Question 1- Do you agree with the proposed scope of the market review? If not, please explain:

- how the proposed scope should be altered
- why you think the proposed scope should be altered in this way
- Please include any evidence you think is relevant to your response.

Partially. Revolut supports the scope as being consumer UK-EEA CNP card based transactions. However we have some recommendations for modifications of scope:

We understand why cross border interchange fees are to be reviewed following developments post-Brexit. While you note in the consultation document that Outbound IFs will be the 'priority', we would recommend narrowing the scope clearly to only target potential action on Outbound IFs. Only Outbound IFs are impacting UK merchants' cost of acceptance directly, and attempts to regulate Inbound IFs will require a more complicated assessment given it will require a review of acquiring markets and competition in a range of third countries, many of which have radically different payment ecosystems (e.g. EU markets with local national card schemes or instant payment schemes).


Question 2: Do you agree with our proposed approach? If not, please explain:

- how the proposed approach should be altered
- why you think the proposed approach should be altered in this way

Please include any evidence you think is relevant to your response.

We have no major concerns with the approach to understand the drivers, justifications and impact of the increases, though we would note there is considerable complexity in the real world impact on merchants due to other developments in scheme fees and CNP volumes post Covid. This impact varies greatly across merchant sizes and sectors, with some very large merchants having power to decide which card or non-card payment types to accept - and therefore impacting consumer adoption of alternative payment types. We believe the PSR will need to conduct detailed assessments in additional areas before any decisions could be made on potential interventions, such as:

- An assessment of Merchant Service Charges (MSC) in different circumstances for online payments post COVID, how they are charged, and the pricing which is offered to small businesses in particular

- 
- An assessment for different merchant categories and sizes of the total impact of the increased EEA cross border fees (to determine to what extent they represent a meaningful impact on the cost of acceptance of the majority of merchants whose transactions are primarily domestic)
 - A detailed cost benefit analysis to understand potential impacts on consumers of any reduction to current interchange rates
 - An assessment on the technical and commercial feasibility of using alternative non-interchange based payment methods for cross border transactions today (e.g. A2A)
 - An assessment on the risk of lower cross border interchange rates undermining issuers ability to fund transitions towards alternative non-interchange payment solutions for cross border transactions
 - A broad assessment of competition at the issuer, scheme and acquirer level to ensure remedies are targeted at the level where competition is lacking
 - Investigating whether competition has been limited in relation to Processing (Switching)
 - Increased costs for issuing banks as a result of Brexit

Question 3: Do you have views on the potential concerns we propose to investigate (set out in para 2.5)? Are there other concerns with cross-border interchange fees that we should be considering?

Please include any evidence you think is relevant to your response.

Overall, we believe both issuing and acquiring are very competitive markets in the UK, and further price interventions on inter-regional interchange are unwarranted and will create significant risks of unintended outcomes for consumers without any meaningful impact on the total cost of acceptance of the vast majority of merchants in the UK.

Interventions to reduce interchange fees, such as those introduced by the IFR, have historically primarily reduced acceptance costs for larger merchants¹, notably those on interchange plus pricing. However they have had much less impact on smaller merchants' cost of acceptance, and have been a contributing factor to the trend of reduced benefits or increased costs for consumers (which can negatively impact financial inclusion). Inter-regional interchange fees are likely to represent a very small subset of the total cost of acceptance of most UK merchants, making further price interventions there less impactful than alternative initiatives to boost broader competition in the UK retail payments market.

We believe rather than forcing lower interchange caps on a sub-set of global cross border interchange fees, the PSR should drive broader change by (i) boosting transparency on fees and enabling easier switching for smaller merchants and (ii) supporting the development of non-card solutions for domestic and international retail spending to increase choice and reduce costs. The PSR is already pursuing positive work in both these areas, but we would see opportunities to further enhance action - notably in simplifying Account to Account usage for cross border transactions and expanding the definition of Payment Accounts to enable Open Banking data aggregation to include merchant's acquiring data (as this will empower

¹ [PSR Card Acquiring Market Review](#)



merchants to better understand what they are being charged and encourage them to consider alternative payment solutions).

We would note that as account to account transactions mature, and stablecoins and Central Bank Digital Currencies emerge, the ability for any single participant within the card ecosystem to have market power will diminish significantly.

In conclusion, we would recommend that the focus remains on driving long term positive change in the UK payments market, and any short term action in relation to competition and pricing needs to be targeted very narrowly to solve problems without unintentionally impacting other parties (e.g. those at the issuing and acquiring level where competition and innovation is robust).

We thank the PSR for the open consultation and stand ready to support your efforts to increase competition and choice in the UK payments market.

Tesco

Office of Chris Hemsley, MD
Scheme and processing fees market review team
Cross-border interchange fees market review team
Payment Systems Regulator
12 Endeavour Square
London
E20 1JN
cardfees@psr.org.uk

1st August 2022

Dear Mr Hemsley

I am writing in response to the PSR Consultation papers 'MR22/1.1 Market review of card scheme and processing fees' and 'MR22/2.1 Market review of UK-EEA consumer cross-border interchange fees'. We welcome the reviews and as you are aware have been in discussions with the PSR over the last 3 years about our concerns with increasing card scheme and processing fees.

In 2019 we wrote to the PSR advising that since the Interchange fee regulation in late 2015 scheme fees have grown across the Tesco retail and wholesale business threefold with no evidence to show the benefits that these cost increases deliver to our business, our retail customers, or our business customers, who are all affected.

This trend in scheme fee increases has continued and we are now at fourfold our previous costs with no evidence to show the benefits. This is particularly difficult for businesses and consumers faced with cost-of-living challenges and we would ask the PSR for timelines for this review to be completed and consideration of imposing interim measures to cap fees during their investigation to mitigate further increases during this difficult consumer environment.

We would also like the PSR to consider widening the wording around the scheme fee review to include ALL fees charged by Visa and Mastercard for card processing that are passed through an acquirer to the merchant, including but not limited to scheme and processing fees. Ensuring a full review.

As a mainly domestic retailer the UK-EEA consumer cross-border interchange fees increase has not had a major impact on our business's although we do fully support the market review. We would ask the PSR to consider broadening the scope of the Interchange fee review to look at other costs that were not capped in the 2015 regulation, for example business/corporate cards.

In April 2022 Visa Business debit card transactions interchange fees increased from [REDACTED] (capped at [REDACTED] to between [REDACTED] and [REDACTED] per transaction. For our wholesale business Booker this increase has been estimated to cost the business a further [REDACTED] with no benefit to the Booker business but with a downstream impact onto our smaller business customers and then onto their retail customers.

We would welcome any direct consultation with the schemes to discuss proposed scheme or interchange fee changes using our experience as the largest retailer and a wholesaler across the UK but disappointingly this is not the current process.

If you would like to discuss any of the points in this letter, then please do not hesitate to contact me as we would be very happy to discuss this issue with you directly.

Yours Sincerely,

[REDACTED]

For and on behalf of
Tesco Stores Limited, Booker Group and One Stop Stores Limited

UK Finance

PSR consultations on:

- **Card scheme and processing fees market review**
- **UK-EEA consumer cross-border interchange fees**

UK Finance Response

Date: Tuesday 2 August 2022

UK Finance is the collective voice for the banking and finance industry.

Representing more than 300 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation.

INTRODUCTION

UK Finance represents a wide range of payment providers, including card schemes, acquirers and issuers; interbank payment providers; payment gateways; and third-party providers.

UK Finance is submitting a joint response to the two proposed market reviews' terms of reference – the first on card scheme and processing fees; and the second on cross-border interchange fees.

Primarily, this is because both market reviews require a detailed analysis of business models and fee structures of the Visa and Mastercard payment systems, as well as the broader payments market, and as a trade association we are not in a position to do so. Our response is therefore restricted to high-level commentary on the nature of the payments market, and to general considerations on the scope and approach of the market reviews.

UK Finance is unlikely to respond formally to the later stages of these market reviews for the same reasons, although as always, we stand willing to help the PSR in its considerations.

OVERARCHING COMMENTS

- The payment market in the UK is extremely competitive and evolving rapidly. Consumer choice in retail payments has increased in recent years, notably with the introduction of Open Banking and Buy-Now Pay-Later and more recently crypto payments, benefitting users by providing merchant choice in acceptance and improving efficiencies in payment provision. Competition therefore should be viewed not only within the existing card payment ecosystem, but also in the context of other payment developments. In order to maintain this competitive market and the associated benefits for consumers, regulators and policymakers should ensure all types of payment methods are able to compete in the same, fair, and even manner.
- Card payment systems are broadly recognised as a benchmark for other payment systems where similar sophisticated commercial model(s) are needed. Some members agree that the commercial underpinning of the four-party card payment ecosystem, including interchange and other fees that are exchanged between various participants, is intrinsic to its working well and enables benefits, such as reliability, responsiveness, innovation and protections to customers and retailers.

PROCEDURAL COMMENTS

- For both reviews, the PSR should consider carefully the scope of the review and definitions around the relevant market, given the complex and dynamic nature of the sector.
- The PSR should also explain its rationale for the proposed time-period that will be considered in both reviews (i.e. from 2014 to the present day). The experience in the recent Card Acquiring Market Review (CAMR) has been that the amount of data provided over the five-year period was not well considered and quickly became obsolete given the rapid developments in the market. It does not seem proportionate to take an even longer period into account for these market reviews.
- We would also urge the PSR to undertake its economic and structural analysis with due regard to the differences between a retail payment ecosystem and, for instance, utility markets. The payments market has delivered positive outcomes for end users, including security, resilience, and innovation. The PSR should take account of these outcomes under its service user and innovation objectives, alongside its competition objective.
- As with the CAMR, we suggest the PSR should also undertake merchant surveys and market testing to help build a sufficient evidence base for these reviews.

Visa

Visa Europe's response to the Payment Systems Regulator's draft Terms of Reference for the market review of UK-EEA consumer cross-border interchange fees

5 August 2022

Executive summary

Visa Europe (referred to as 'Visa' in this document) is pleased to respond to the Payment Systems Regulator's (PSR) draft Terms of Reference on its upcoming market review of UK-EEA consumer cross-border interchange fees, published on 21 June 2022. We welcome further engagement with the PSR as it progresses its market review.

First, we set out some key context relating to Visa and interchange fees:

- **Visa takes its role as a global payments network extremely seriously.** Our success depends on merchants being able to confidently complete their sales and grow their businesses, and consumers being able to pay safely and securely. It is for this reason we constantly invest in the security and resilience of our network and in innovating our service offerings.
- **Visa does not earn revenue from interchange fees.** Interchange fees ensure there is a value transfer between the financial institutions who provide services to both consumers and merchants. Setting interchange fees is a complex business decision involving many individuals and a range of business considerations, including competitive dynamics, operational challenges and market developments. It underpins many of the card services which in the UK typically remain free to cardholders.
- **Competition in the UK payments sector is thriving and no more so than e-commerce payments.** There are an increasing number of ways to pay for goods and services, driven by consumer expectations, technological advances, open innovation and collaboration between organisations. From a consumer perspective, you can pay by card using a number of different globally located card schemes, move money account-to-account, use a digital wallet to make purchases, use a merchant payment programme and, increasingly, utilise buy-now-pay-later (BNPL) products.

In response to the consultation on the Terms of Reference for the PSR's market review of UK-EEA consumer cross-border interchange fees, we provide some overarching comments:

- **As a central part of the market review, we would encourage the PSR to build a picture of the relevant market in cross-border payments,** including the impact and implications of current and future competitor constraints, and innovation.
- **As part of this, the PSR should seek to understand the many different characteristics of cross-border e-commerce transactions;** including the merchant categories that tend to use them, their

higher risk of fraud, and the need for greater vigilance and investment by issuers to support security and how they are linked to the fees associated with these payment types.

- **The PSR should focus on the outcomes for end-users of payments systems, including safety, security, and reliability**, and the value that they derive from their use of payment systems for making cross-border payments. This should involve taking account of outcomes, positive and negative, for both consumers and merchants.

As we outline later in our response, Visa believes that there are three critical elements in a thriving payments system – security, innovation and value. These elements must be carefully balanced. Prioritising one over the others can have unintended consequences to the detriment of consumers and merchants and we urge the PSR to keep this in mind as it conducts its review.

We summarise the structure of our response below:

- In **Sections 1-4** of this response, we describe in more detail the efforts Visa makes to deliver positive outcomes for the consumers and merchants who rely so much on payments networks; we describe how competition is thriving in the UK payments sector and we set out the importance of interchange fees to all participants in the payments value chain.
- In **Section 5**, we respond to the PSR's questions posed in the draft Terms of Reference.

We look forward to working closely with the PSR during the market review process. We encourage the PSR to acknowledge the challenges of running a high-quality exercise and the impact its work has on market participants and the sector more widely.

1 Visa exists to enable individuals, businesses and economies to thrive

Visa strives to uplift everyone everywhere by being the best way to pay and be paid. For more than 60 years, we have invested heavily and continuously in our global network and operations. **We remain focused on delivering an innovative, reliable and secure transaction processing network, for merchants and consumers, no matter where they are in the world.** We enable transactions between 3.9 billion cards¹, 80m+ merchants² and 15,000 financial institutions³ in 200+ countries and territories.

In 2018, we completed the transition of Visa's UK operations to our global infrastructure, meaning that UK businesses and consumers benefit from the availability and reliability of our global network, which has successfully processed more than 99.999% of the transactions it has received over the last five years.

Visa's success depends on merchants being able to confidently complete their sales and grow their businesses, and consumers being able to pay safely and securely. Furthermore, **the Visa network levels the playing field between small and large merchants.** Every merchant that accepts Visa - irrespective of size, resource, or sophistication - can transact securely with billions of Visa cards across the globe and know that they will get paid because we stand behind every Visa transaction.

By tapping into our network, smaller e-commerce sites can benefit from Visa's world class security and fraud fighting tools so they can better compete with the big technology players. Similarly, every financial institution participating in the Visa system has access to the same payment products, processing capabilities, system resilience and availability, dispute tools and fraud fighting technologies as the largest financial institutions, enabling them to more confidently authorise transactions at merchants in other countries.

Visa is a supporter and champion of small businesses and delivers products, services and programmes to enable small businesses to reach more consumers and grow and thrive in the digital world. Building on Visa's support for the UK government initiative, The Great British High Street, Visa announced a global commitment in 2020 to digitally enabling 50 million small businesses, 8 million in Europe, including in the UK. We continue to use our network to help small businesses get online, receive digital payments and attract a wider customer base – all important components to help them prosper and grow.

2 Visa drives trust through stringent standards of safety, security and reliability

Fraud is a key area which continues to be a concern and a priority for consumers and merchants. Some fraud trends are worrying – including Authorised Push Payment ('APP') scams, where people and business are tricked into sending money using instant account-to-account payments to an account controlled by a fraudster.

¹ As of December 31, 2021.

² Data provided to Visa by acquiring institutions and other third parties as of September 30, 2021. Merchant locations reported excludes an additional estimate of 20 million small businesses that utilise payment facilitators as of September 30, 2021.

³ For the 12 months ended March 31, 2022.

In the UK, in 2021, £583 million was lost to APP scams (up 39% from 2020)⁴, overtaking card fraud losses for the first time.

Instant payments lack many of the fraud prevention capabilities and consumer protections that exist with card payments. Despite reports of fraudsters trying to take advantage of the pandemic, fraud rates on cards continue to fall. Incidents of fraud occur in less than 0.1% of transactions on our network, among the lowest of all payment forms.

Trust – which is based on safety, security and reliability – is the foundation of everything that Visa does. **We invest heavily and continuously in network security – more than any other part of our business.** Over the past five years alone, we have spent nearly £7 billion on reducing fraud and enhancing network security.

In addition to our secure data centres, we operate a series of integrated cyber command and intelligence hubs globally that handle 24/7 security monitoring, incident response and investigations, and threat intelligence. In 2021 alone, our fraud prevention capabilities helped stop over £19 billion in attempted fraudulent transactions for merchants and financial institutions.

Given the expansion in e-commerce since the start of the pandemic, we have increased our focus on securing online commerce through new products and services, innovation, and extensive investments in Artificial Intelligence (AI). Visa cardholders benefit from the greater effectiveness of our fraud controls on their cards, including receiving helpful real-time alerts from their financial institutions, when a suspicious transaction is spotted.

Globally, Visa cardholders can count on our zero liability protections on unauthorised or fraudulent transactions, ensuring that they do not have to pay for transactions they did not authorise. In the UK, credit cardholders have important legislative protections through Section 75 of the Consumer Credit Act. The Visa brand promise helps ensure that cardholders around the world continue to have confidence to pay for goods and services from UK merchants using both debit and credit cards.

In addition, we maintain well-established dispute resolution rules and processes to support our strong consumer protections. These were particularly valuable throughout the pandemic when consumers were often able to dispute charges or get refunds on purchases that did not work out as planned.

3 Competition in the payments sector is thriving

In the UK, the payments industry is characterised by a strong digital infrastructure, a sophisticated technology sector and a well-constructed regulatory environment, leading to a thriving and dynamic market landscape. Today, there are an increasing number of ways to pay for goods and services, driven by consumer expectations, technological advances, open innovation and collaboration between organisations.

From a consumer perspective, you can pay by card from a number of different globally located card schemes, move money account-to-account, use a digital wallet to make purchases, use a merchant

⁴ UK Finance Annual Fraud Report.

payment programme and, increasingly, utilise a buy-now-pay-later (BNPL) product. These services are delivered by banks, FinTechs, and global technology and e-commerce platforms – all providing consumers, merchants and businesses with increased choice.

The dynamic environment we see in payments is delivering new payment use cases, new business models, and greater frictionless commerce. **We believe this fast-moving and intense market competition provides important context when considering regulatory policy around payments.** There is a dynamic and ever-expanding range of payment options available for UK consumers and merchants today, and on the near-term horizon. We believe that each of these payment options should be able to compete freely on the basis of those three key elements - security, value and innovation.

4 Multi-party payment system and the importance of interchange fees

As noted above, interchange fees ensure that there is a value transfer between the financial institutions who provide services to both consumers and merchants. It underpins many of the card services which in the UK are typically free to cardholders.

When setting interchange fee levels, it's important to find value for everyone – encouraging merchants to accept card payments and encouraging consumers to use their cards.

An appropriate level of interchange fee enables merchants to reach a bigger customer base and offer the trust, speed, convenience and operational efficiencies associated with digital payments. They can take confidence in the reliability of the Visa network and reassurance that they will be paid once the purchase has completed, anywhere in the world.

For financial institutions, amongst other things, **interchange fees support their ability to issue cards and digital credentials that provide their customers with flexibility and choice in accessing a range of funds through debit, pre-paid and credit.** It contributes towards the provision of customer support teams to answer cardholder enquiries. It helps reimburse cardholders if a card is used fraudulently. And it supports innovation including the development of new products and services, making it easier for consumers to manage their financial lives safely and securely.

There is not a formulaic approach recognised by regulatory authorities for calculating interchange fees. The interchange fees Visa sets reflect a complex business decision involving many individuals and a range of business considerations.

Interchange fees also underpin innovation in the FinTech sector, which currently employs more than 80,000⁵ people in the UK alone. Here, interchange fees help new digital banks launch and thrive, which in turn provides greater competition in the sector and gives consumers access to even greater choice. As we have outlined, Visa believes that there are three critical elements in a thriving payments system – security, value and innovation. These elements must be carefully balanced. Prioritising one over the others can have unintended consequences to the detriment of consumers and merchants.

⁵ The Department of International Trade 2019.

5 Visa's responses to the consultation questions

5.1 Question 1: Do you agree with the proposed scope of the market review?

The PSR's consultation on its Terms of Reference states that:

We are conducting this market review because we want to understand the rationale for the increases in cross-border UK-EEA interchange fees and whether the card scheme operators' ability to increase these fees is an indication that the market(s) or aspects of market(s) is not working well.⁶

The relevant market that is under review is not clear from the consultation document. Rather, the PSR has proposed to focus the market review on the rationale surrounding a single set of historical changes to interchange fees.

In the PSR's Markets Guidance document⁷, it is stated that:

Market reviews and market studies are the principal ways in which we investigate the market for payment systems, or the markets for services provided by payment systems, to see how well they are working for service users (i.e., those who use, or are likely to use, services provided by payment systems). They are in line with our competition, innovation and service-user objectives. (Emphasis added)

In line with this description, Visa would encourage the PSR to build a picture of the relevant market including its dynamics (both current and future), the competitive constraints, innovation and end-user outcomes to help with its assessment of the review.

To provide context as to the scope of transactions covered by this review scope as stated within the Terms of Reference consultation, the changes made to interchange fees for card-not-present cross-border transactions did not impact the vast majority of transactions with UK merchants. Visa data shows that for UK merchants, there was no change to 98% of transactions.⁸

More specifically, Visa notes that the PSR proposes to cover both inbound and outbound interchange fees, with a priority on outbound interchange fees. While the priority is indicated to be outbound interchange fees, we would remind the PSR that the rates that apply to inbound interchange fees reflect the capped rates agreed with the European Commission, as part of a multi-year process which completed in October 2019⁹, when the UK was part of the European Union.

5.2 Question 2: Do you agree with the proposed approach of the market review

The PSR's consultation on its Terms of Reference states that the market review would look at the following issues:

⁶ Paragraph 2.1, Terms of Reference.

⁷ PSR (2015) Market Reviews, market studies and market investigation references.

⁸ Visa Net Data January – June 2022.

⁹ Applicable October 2019 – November 2024.

- *The potential drivers and justifications for the increases in these IFs since the UK's withdrawal from the EU. As part of this, we shall examine the reasons provided by the card scheme operators and the considerations that Visa and Mastercard took into account when assessing the opportunity to increase these fees, including strategic, competition and regulatory aspects.*
- *The impact of the increases in IFs for UK-EEA consumer debit and credit CNP transactions on competition, innovation and service users.¹⁰*

This approach is limited for the purposes of a market review exercise. It is apparent that the draft Terms of Reference are currently focused on understanding the rationale and impact of a single set of historical changes to cross-border interchange fees, as opposed to looking at the broad aspects of a market from all relevant perspectives.

Visa suggests that the PSR's approach should include the following:

- This PSR should seek to understand the competitive dynamics of cross-border payments, including both within the card payments value chain, as well as the competitive constraints that different end-to-end cross-border payment solutions exert on each other. This would take into account all providers of cross-border payment services, all of which are relevant when considering the competitive environment in which card payment schemes operate.
- The PSR should seek to understand the many different characteristics of cross-border e-commerce transactions; including the merchant categories that tend to use them, their higher risk of fraud, the need for greater vigilance and investment by issuers to support security, and how these characteristics are linked to the fees associated with these payment types.
- The PSR should focus on the outcomes for end-users of payments systems, including safety, security, and reliability, and the value that they derive from their use of payment systems for making cross-border payments. This should involve taking account of outcomes, positive and negative, for both consumers and merchants.
- The review should take a forward-looking view, reflecting the dynamic and fast-moving nature of cross-border payments innovation and of payments more generally. The PSR should also take into consideration the potential ways in which competitive dynamics and constraints on operators can develop in the future, including through entry by new competitors and through changes in the roles that existing operators play in value chains.
- The review should take a specific focus, as defined by the PSR, on how the market is operating in terms of the levels of competition, innovation and provision of service.

5.3 Question 3: Do you have any views on the potential concerns we propose to investigate? Are there other concerns with cross-border interchange that we should consider?

As explained above, our concerns relate to the limitations in the PSR's scope and approach to this market review. Visa recommends that the PSR uses this review to build a picture of the relevant market including its dynamics (both current and future), competitor constraints, innovation, and end-user outcomes to help with its assessment of the review.

¹⁰ Paragraph 2.6, Terms of Reference.

PUB REF: MR22/2.1 Submissions

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