Payment Systems Regulator

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

Final report

December 2024

MR22/2.7

Contents

1 Executive summary

Introduction

1.1 Debit and credit card payments are critical to the smooth running of the UK economy. They enable people to pay for their purchases and UK merchants to accept payments for goods and services. They are a well-established method for consumers to make payments in person and online.

1.2 Every time someone makes a Mastercard or Visa card payment, the merchant acquirer pays an interchange fee (IF) to the card issuer.

1.3 An important use of debit and credit card payments is for international transactions, that is, transactions where the payer and the recipient are based in separate countries. Such transactions are typically referred to as cross-border transactions and the IFs are called cross-border IFs.

Why we have carried out a market review

1.4 Before the UK's withdrawal from the EU, IFs for UK-EEA (European Economic Area) transactions counted as intra-EEA transactions. From December 2015 until the end of the transition period following the UK's withdrawal from the EU, these IFs were subject to caps under the EU Interchange Fee Regulation (EU IFR). A single set of caps applied for card-present (CP) and card-not-present (CNP) transactions. These caps were 0.2% of the value of the transaction for consumer debit cards (including prepaid cards) and 0.3% for consumer credit cards.

1.5 From January 2021, the EU IFR no longer applied to UK-EEA cross-border transactions. Following this, Mastercard and Visa increased the IFs for UK-EEA CNP transactions using consumer debit and credit cards fivefold – from 0.2% and 0.3% to 1.15% and 1.5% respectively. Visa increased the IFs for consumer debit and credit CNP transactions for EEA cards at UK merchants (UK-EEA CNP outbound IFs, or simply 'outbound IFs') in October 2021. Mastercard followed suit and increased the same IFs in April 2022.

1.6 Market reviews, in line with our competition, innovation and service-user objectives, are one of the principal ways in which the PSR investigates the market for payment systems, or the markets for services provided by payment systems, to see how well they are working for service users (those who use, or are likely to use, services provided by payment systems). IFs represent a cost to UK merchants. Many stakeholders, including UK merchants and acquirers, have raised concerns about Visa and Mastercard's increases. Historically, high IF levels have resulted from weak competition in the market. In light of these concerns and this history, we have conducted a market review into UK-EEA consumer IFs using our powers under the Financial Services (Banking Reform) Act 2013 (FSBRA).

1.7 The main objectives of this review were to understand:

- the rationale for and impact of increases in UK-EEA CNP IFs
- whether the increases in UK-EEA CNP IFs are an indication that aspects of the market are not working well for all service users, including organisations that accept cards and their customers

- what, if any, regulatory intervention is appropriate to ensure, in particular, that we meet our service-user objective.

1.8 We published our interim report in December 2023 and received responses to our interim report consultation from a range of stakeholders. This final report includes our final conclusions on whether the market is working well.

1.9 We are publishing this final report alongside a consultation on our approach to a price cap remedy. We have taken into account, responded and engaged with written responses to our interim report and any other additional representations that stakeholders made after the consultation closed. We also based our conclusions on information and evidence received in previous phases of this review.

Our findings

1.10 Effective competition supports good outcomes in payments markets, such as low prices, high service quality and continued innovation. However, we found that in increasing UK-EEA CNP outbound IFs, Mastercard and Visa were not subject to effective competitive constraints on the acquiring side of the network. As a result, the two card schemes have raised the outbound IFs higher than they would have done if competitive constraints were effective.

1.11 In summary, our findings are:

- Mastercard and Visa could and did **increase outbound IFs without needing to have regard to the potentially detrimental consequences for service users, namely organisations that accept cards and their customers** who receive and make payments and ultimately pay the increased IFs. This is because:
  - merchants and acquirers are unable to respond to increased IFs in such a way as to exert competitive constraints on Mastercard and Visa
  - increased IFs are in the interest of the issuers and, hence, the schemes themselves. Mastercard and Visa have a commercial incentive to raise IFs, since they compete with each other to attract issuers. The increased IFs provide more revenues for these banks to issue cards from their respective schemes.
- The schemes submitted that the IF levels that applied to UK-EEA CNP transactions when the UK was part of the EU and prior to the increases were inadequate, since they had been based on a flawed methodology (the one used to set the EU IFR IF levels). However, **the schemes were not able to show that they undertook any specific assessment** when deciding to increase the outbound IFs. Nor have they shown that they had any regard to the **interests of organisations that accept cards and their customers** (and not only to the interests of issuers and their own interests) in setting the higher level.
- By setting IF levels at the rates charged for transactions between the EEA and the rest of the world, Mastercard and Visa adopted levels that the European Commission had set in another context and for different circumstances – that is, for cards issued in non-EEA countries and used at EEA merchants at a time when the UK was in the EEA. In doing so, **the schemes based their levels on benchmarks that are not relevant to the UK-EEA context** (specifically, on means of payments funded via non-SEPA (Single Euro Payments Area) bank transfers even though both the UK and the EEA are part of SEPA). These benchmarks are also more expensive than benchmarks in the UK-EEA context (specifically, means of payments funded via **SEPA** bank transfers).

- An analysis of alternative payment methods, based on the data and to a large extent the methodology put forward to us by Visa, provides further evidence that the current levels of IFs are unduly high.
- We have also not seen any positive evidence that the outbound IF increases contributed to improving the quality and efficiency of payments in CNP transactions which would not have occurred without such higher prices. In particular we have seen no evidence that issuers used their increased incomes to fund service improvements (fraud, quality, efficiency or savings) that provided benefits to users on the acquiring side. As a consequence, we consider that Mastercard and Visa set the outbound IFs unduly high.
- Besides the political shift and deregulation of outbound IFs following the UK's withdrawal from the EU, we have found no compelling explanation of other factors, or change in circumstances, which prompted the change in IF levels. **Deregulation created an opportunity to raise the outbound IFs and the schemes seized it**.
- **The increases are costing service users approximately** [✂] **£150 million to £200 million per year** though we have seen no evidence that they generated any corresponding benefits for them. We have taken in the round the available evidence summarised above and described in this report.

1.12 We conclude that the increases to the current levels result from aspects of the market that are not working well, that they are contrary to UK service users' interests and that the situation requires regulatory intervention.

1.13 On the grounds of administrative priority, we have decided to close our review of IFs for consumer debit and credit CNP transactions for UK cards at EEA merchants (UK-EEA CNP inbound IFs, or simply 'inbound IFs').

Actions we are taking

1.14 We have considered potential remedies to address or at least mitigate the harm that outbound IFs are causing end-users. We have looked at all the evidence in the round and considered alternative forms of remedy. We conclude that restricting the maximum level of outbound IFs by introducing a price cap is the only effective form of remedy open to us.

1.15 We recognise that a price cap would not address the underlying cause of the harm we have identified – the lack of effective competition on the acquiring side. However, we have concluded that alternative actions related to UK-EEA CNP transactions – that did not cap directly the outbound IFs – would result in a continuous unnecessary cost to UK merchants and their customers, while such a price cap remedy would materially mitigate its adverse impacts.

Next steps

1.16 Alongside this final report, we are launching a consultation setting out our provisional views on a phased approach to implementing a price cap remedy on outbound IFs and, should we conclude a phased approach is appropriate, on the appropriate level for a stage 1 price cap.

1.17 This remedies consultation is open until 7 February 2025. We then plan to issue a decision on our approach to implementing a price cap in due course.

1.18 As detailed in our remedies consultation at paragraph 7.7, regardless of whether we ultimately decide a two-staged approach to a price cap is appropriate or not, we are progressing with our work on developing a longer-term (or stage 2) remedy. We intend to consult on the methodology for determining the appropriate level for outbound IFs during early 2025 and the outcome of that consultation will inform our next steps thereafter.

2 Introduction

This review considers Mastercard and Visa's increases to UK-EEA consumer CNP interchange fees (outbound IFs), for credit and debit CNP transactions.

In this report, we present our findings on why the increases to outbound IFs are not in the interests of UK merchants and their customers, and why intervention is warranted. This report also outlines why we consider it appropriate to close the review of IFs that apply to CNP payments made by UK consumers to EEA merchants (inbound IFs).

The aim of our review

2.1 Our aim in this review was, in summary, to:

- assess whether there are markets which are not working well for UK merchants and their customers that could explain why Mastercard and Visa increased the consumer debit and credit CNP IFs for UK-EEA CNP transactions (outbound IFs)
- identify any possible actions to remedy or mitigate any problems we found.[1]

2.2 We have considered these issues in accordance with our legal framework, including our general duties,[2] objectives[3] and regulatory principles.[4]

Background

2.3 Cards are the most popular non-cash method by which consumers make retail payments across the UK and the EEA, both domestically and internationally. Such popularity is due to a combination of increasing digitisation, the growing use of contactless payments, mobile and online banking, the presence of strong network effects that push both merchants and consumers to adopt card solutions, and, more recently, the lockdown restrictions imposed during the COVID-19 pandemic. To illustrate this:

- Recent data from UK Finance shows that, in 2023, debit and credit cards accounted for 61% of total payment volumes in the UK. UK Finance predicts that cards will account for 66% of all payments in the UK by 2033.[5]
- The data suggests that card usage is experiencing an upward trend: past figures from UK Finance show that in 2022 debit and credit cards accounted for 59% of total volumes, as opposed to the most recent 61% share mentioned above.[6]

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1 For further information on the scope of our work refer to: MR22/2.2, *Market review of UK-EEA consumer cross-border interchange fees: Final terms of reference* (October 2022).

2 FSBRA, section 49

3 FSBRA, sections 49(2), and 50–52

4 FSBRA, section 53

5 UK Finance, *UK payment markets 2024* (July 2024), page 9.

6 UK Finance, *UK payment markets 2024* (July 2024), page 9.

- Data from the British Retail Consortium (BRC) (a trade association for UK retail businesses) shows that, in 2023, consumer credit and debit cards accounted for 86% of the total value of retail transactions in the UK, and 76% of the total number of retail transactions.[7]
- In 2022 and 2023, Mastercard and Visa together accounted for around 99% of all payments made with debit and credit cards issued in the UK, both in terms of volume and value.[8]
- Data from the European Central Bank (ECB) show that, in 2023, card payments accounted for 54% of the total number of non-cash transactions in the Eurozone.[9]
- In 2022, in the Eurozone, card payments represented 51% of all online payments in terms of volume and 47% in terms of value.[10]

2.4 Many merchants, large and small, operate cross-border in the UK and EEA. Merchants and their customers need cross-border payment solutions to transact. Cards represent the most commonly used payment instrument for making UK-EEA online purchases. Mastercard and Visa are the cards most often used.

2.5 In 2022, 3.6% of all card transactions at UK merchants were UK-EEA cross-border card transactions.[11]

2.6 The role played by Mastercard and Visa in this space is important – the vast majority of EEA-issued cards, including co-badged ones, are either from Mastercard or from Visa and cross-border acceptance of EEA co-badged cards relies almost entirely on these international card schemes.[12] In addition, EEA issuers, in particular banks, are increasingly issuing cards that only come from these two international card schemes rather than national card schemes.[13]

2.7 The decline in the number of national card schemes in EEA countries (from 22 in 2013 to 17 in 2018) means that international card schemes are growing in the national markets as well as the European cross-border card market.[14]

2.8 The Single Payment Euro Area (SEPA) was launched by the EU in 2008, after the implementation of the first Payment Services Directive (PSD), with the purpose of enabling quick and secure cross-border bank transfers between the EU member States. As of 2023, countries within SEPA are the 27 Member States of the EU, Iceland, Lichtenstein, Norway (which with the EU member states form the EEA), Andorra, Monaco, San Marino, Switzerland, the UK and the Vatican City.[15] As a member state of the EU, the UK became

7 BRC, *Payments survey 2024*, pages 7 and 8.

8 UK Finance, *UK payment statistics 2023*, tab 8.1 and 8.2, and UK Finance, *UK payment statistics 2024*, tab 8.1 and 8.2.

9 ECB, *Payments statistics: First half of 2023*.

10 ECB, *Study on the payment attitudes of consumers in the euro area* (2022) – Chart 9.

11 PSR analysis of data on transaction values submitted by acquirers through the section 81 notice, and by Mastercard, Visa and American Express.

12 European Commission, *Study on the application of Interchange Fee Regulation* (2020), page 64.

13 ECB, *Card payments in Europe – current landscape and future prospects* (2019).

14 ECB, *Card payments in Europe – current landscape and future prospects* (2019).

15 See the ECB's website at https://www.ecb.europa.eu/paym/integration/retail/sepa/html/index.en.html (accessed 25 November 2024) and the European Payments Council's website at https://www.europeanpaymentscouncil.eu/about-sepa (accessed 25 November 2024).

part of SEPA since its foundation. After the leaving the EU in January 2021, the UK retained its SEPA membership.[16]

Issues this market review addresses

2.9 In 2021 and 2022, since the removal of previously applicable caps, Mastercard and Visa increased their IF levels for UK-EEA CNP transactions fivefold – from 0.2% to 1.15% for consumer debit cards and from 0.3% to 1.5% for consumer credit cards.

2.10 As outlined in our interim report, several UK businesses raised concerns with us about how the increases to outbound IFs have affected them. Every time a consumer uses an EEA-issued Mastercard or Visa debit or credit card for online transactions within the UK, an outbound IF is paid to the EEA issuer by the UK acquirer or other licensed payment service provider (PSP) that a merchant is contracted with to provide card-acquiring services. The acquirer may recover that cost as part of the merchant service charges (MSC) that it levies, so that IFs represent a cost to the merchant who accepted the card payment. In turn, a merchant may then pass part of this cost on to consumers.

2.11 To inform our understanding of whether Mastercard's and Visa's UK-EEA CNP payments are working well for UK merchants and, ultimately, for consumers, as part of our review, we examined specific issues, including:

- Key features relevant to understanding how the markets function – we have, for example, assessed the factors that may influence and constrain how Mastercard and Visa set cross-border IFs, including:
  - possible acquirers' and merchants' responses to an increase in outbound IFs
  - alternatives available to UK acquirers and merchants and whether Mastercard and Visa-branded cards have a must-take status for merchants.[17]
- The potential drivers of decisions by Mastercard and Visa to increase their fees – this includes competition, strategic and regulatory aspects.
- Information provided by Mastercard and Visa on the IF increases, including information provided to the Treasury Select Committee (TSC).[18]
- The potential effect of the increases in outbound IFs on UK merchants and their customers.

16 European Payments Council, *Brexit from 1 January 2021 onwards: Get ready for the end of the transition period* (July 2020).

17 A must-take card refers to a situation where merchants feel compelled to accept a given card even if it means incurring higher acceptance costs, because they are concerned that turning down such a card would impair their ability to attract customers. See: Jean-Charles Rochet and Jean Tirole, *Must-take cards: Merchant discounts and avoided costs*, Journal of the European Economic Association, Volume 9, Issue 3 (2011), pages 462 to 495.

18 Mastercard, *Letter to the Treasury Select Committee* (2 August 2022).
Visa, *Visa response to Treasury Select Committee on cross-border interchange* (August 2022).

2.12 In line with our terms of reference, this review focused on outbound IFs in the Mastercard and Visa card payment systems, as these are the IFs that recently increased materially in October 2021 (Visa) and April 2022 (Mastercard). These fees are paid by UK acquirers to EEA issuers.[19] We covered both debit and credit consumer cards.

2.13 Since the UK's withdrawal from the EU, Mastercard and Visa also increased inbound IFs, which are paid by EEA acquirers to UK issuers. These are currently subject to caps agreed between Mastercard and Visa and the European Commission.

2.14 In our interim report, we provisionally concluded that aspects of the markets are not working well and that intervention on outbound IFs may be appropriate. We also consulted on closing the review into inbound IFs on grounds of administrative priority.

2.15 The UK is not alone in looking, in recent years, at whether IFs are set appropriately. The European Commission set IFs for transactions within the EEA through the 2015 EU Interchange Fee Regulation (EU IFR), and accepted commitments setting caps for transactions between the EU and the rest of the world in 2019. In July 2024, the New Zealand Commerce Commission published a consultation paper on IFs[20], which sought views on issues around reducing domestic IFs. It also noted that 'cards issued in Australia and used in New Zealand can have higher IFs than cards issued from outside of the Asia-Pacific region and used in New Zealand (for example, the United Kingdom)'[21] and sought evidence related to these different fee levels. In 2021, the Reserve Bank of Australia concluded a review of retail payments regulation which included looking at IFs charged on foreign cards.[22] In October 2024, it published an Issues Paper seeking views on, amongst other things, capping IFs on foreign card transactions in Australia.[23]

What we have done to date

2.16 In the course of this market review, we took the following actions:

- In November 2021, we announced our market review of card fees.
- In January 2022, we sent Mastercard and Visa initial information requests. These requests informed the draft terms of reference for our market review into UK-EEA cross-border IFs.
- In June 2022, we published our draft terms of reference.
- In July 2022, we held roundtables and consulted on our draft terms of reference with stakeholders.

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19 MR22/2.2, *Market review of UK-EEA consumer cross-border interchange fees: Final terms of reference* (October 2022), page 7, paragraph 2.3. In this final report, as in our interim report, we use 'CNP outbound IFs' and 'outbound IFs' interchangeably to refer to UK-EEA consumer CNP outbound IFs; we use 'CNP inbound IFs' and 'inbound IFs' interchangeably to refer to UK-EEA consumer CNP inbound IFs./2.2, *Market review of UK-EEA consumer cross-border interchange fees: Final terms of reference* (October 2022), page 7, paragraph 2.3. In this final report, as in our interim report, we use 'CNP outbound IFs' and 'outbound IFs' interchangeably to refer to UK-EEA consumer CNP outbound IFs; we use 'CNP inbound IFs' and 'inbound IFs' interchangeably to refer to UK-EEA consumer CNP inbound IFs.

20 *Retail payment system: Costs to businesses and consumers of card payments in Aotearoa New Zealand: Consultation paper* (July 2024).

21 *Retail payment system*, paragraph 4.42.

22 *Review of retail payments regulation: Conclusions paper* (October 2021).

23 *Merchant card payment costs and surcharging: Issues paper* (October 2024), page 12.

- In October 2022, following feedback on our draft terms of reference, we published our final terms of reference.
- In December 2022, we published our working paper on our initial thinking on the impacts of cross-border IF increases.[24]
- In December 2023, following feedback on our final terms of reference, we published our interim report.

2.17 In preparing this final report, in addition to considering feedback in response to the interim report, we have engaged with stakeholders. This engagement took various forms, including information and document requests, voluntary questionnaires, roundtable discussions and bilateral meetings. The stakeholders who provided feedback and/or who we otherwise engaged with are listed below:

- the card scheme operators, Mastercard and Visa
- American Express
- two FinTech's
- two digital wallet providers
- a trade association representing EEA issuers, acquirers, and card scheme operators
- a trade association representing UK issuers and acquirers
- a trade association representing EEA acquirers
- a national trade association representing its country's financial service sector
- a European issuer trade association
- three national issuer trade associations in Europe
- seven Members of the European Parliament (MEPs) representing different countries
- 13 issuers, who collectively account for over 90% of UK card transactions by value[25]
- 19 card acquirers, who collectively account for over 90% of UK card transactions by value[26]
- four merchant representative bodies who together cover thousands of independent and major UK retailers from a broad range of sectors, one merchant trade association who represents retailers and wholesalers in Europe, and nine large merchants
- a hospitality and travel company
- three independent individuals

24 MR 22/2.4, *Market review of cross-border interchange fees: A discussion of the impact of the UK-EEA cross-border interchange fee increases: Working paper* (December 2022).

25 PSR analysis. [✂].

26 PSR analysis. [✂].

Links to our strategy

2.18 Our PSR Strategy states that, as a general principle, we will focus on whether our work is likely to deliver improved outcomes for end users, in the short or longer term. This is consistent with the approach other economic regulators use. It means we consider what effect our proposals may have on 'people and (non-payment) businesses' that need to make or receive payments.[27]

2.19 One of our strategic priorities, set out in our Strategy, is 'promoting competition between UK payment systems and the markets supported by them; [and] protecting users where that competition is not sufficient'. Work on this basis for cross-border IFs – and whether any shorter-term measures, such as a cap, might be appropriate until we develop and implement any longer-term measures to introduce more competition – was flagged in our strategy as one of the actions we were taking to meet our competition strategic priority.[28]

Who this affects

2.20 This final report will be of particular relevance to all participants of the designated payment systems operated by Mastercard and Visa:

- the scheme operators
- card issuers (especially EEA-based card issuers)
- card acquirers
- merchants (that is, organisations that accept card payments)

2.21 Other stakeholders that may be interested in this report include:

- industry groups and trade bodies
- firms based in Gibraltar, Jersey, Guernsey and the Isle of Man

Equality and diversity considerations

2.22 We have considered the equality and diversity issues that may arise from our current analysis, including the detriment we see and the remedies we are contemplating.

2.23 We do not consider that our proposed remedies would negatively affect any of the groups with protected characteristics under the Equality Act 2010.

2.24 We will continue to consider equality and diversity implications during the consultation period to our remedies consultation and as our thinking evolves. We will also revisit these considerations after we receive any relevant feedback.

27 *The PSR Strategy* (January 2022).

28 *Ensuring our strategy is fit for the future* (May 2024).

Our powers, objectives and approach

2.25 We have conducted our market review using our powers under Part 5 of the Financial Services (Banking Reform) Act 2013 (FSBRA). FSBRA gives us wide-ranging powers to take action, including the power to impose general and specific directions and requirements, if we consider it appropriate following our review.[29]

2.26 Any decision to exercise these powers is informed by our regulatory principles and objectives. FSBRA requires us to have regard to certain factors, including our regulatory principles, and in so far as is reasonably possible, to act in a way which advances one or more of our objectives when deciding whether to impose a general direction or requirements.[30,31] We will also have regard to our objectives and regulatory principles when deciding whether to impose specific directions or requirements in the context of a market review.

2.27 In order to assess whether it would be appropriate to intervene through directions or requirements in the context of a market review, we first consider how well markets for payment systems, or services provided by payment systems, are working in line with our objectives.[32] These are to:

- promote effective competition in the market for payment systems, and markets for services provided by payment systems in the interests of those who use, or are likely to use, payments systems (the 'competition objective').
- promote the development of, and innovation in, payment systems in the interests of those who use, or are likely to use, services provided by payment systems, with a view to improving the quality, efficiency and economy of payment systems (the 'innovation objective').
- ensure that payment systems are operated and developed in a way that takes account of, and promotes, the interests of those who use, or are likely to use, services provided by payment systems (the 'service-user objective').

2.28 We note in particular that pursuant to section 50 of FSBRA we may have regard to a range of considerations in assessing the effectiveness of competition in the relevant market, including:

a. the level and structure of fees, charges or other costs associated with participation in payment systems (subparagraph k)
b. the ease with which new entrants can enter the market (subparagraph l)

2.29 IFs are a tool that can be used by card network operators (in this instance Visa and Mastercard) to balance the costs of card payments to ensure that each side of the market (merchants via acquirers and cardholders via issuers) benefits sufficiently from using payment cards. When set at the right level, the IF ensures that it is in the joint intertest of the service users, that is, organisations that accept cards and their customers.

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29 FSBRA section 54 and section 55.

30 Namely, the importance of maintaining the stability of, and confidence in, the UK financial system, the importance of payment systems in relation to the performance of functions by the Bank of England in its capacity as monetary authority, and our regulatory principles in section 53 of FSBRA (section 49 (3) of FSBRA).

31 Our statutory objectives are set out in sections 50, 51 and 52 of FSBRA.

32 FSBRA sections 50 to 52.

2.30 In this market review we have therefore considered whether the increased levels in outbound IFs indicate that aspects of the markets are not working well by reference to our objectives. Specifically, we have considered whether the levels of the increased fees reflected effective competition conditions, supported innovation, and took account of and promoted the interests of users of the schemes' network on both sides market, in particular, UK service users (the organisations that accept cards and their customers who have faced those increases).

2.31 For this purpose, in this report we have therefore considered the following:

a. Nature of competition: whether the schemes face competitive constraints on either side of their network (Chapter 4); this is in particular relevant to assess the effectiveness of competition in ensuring that the current level of outbound IFs serve the interests of users; as noted in our terms of reference, we were concerned that Mastercard's and Visa's decision to increase these fees is the result of a lack of effective competitive constraints in the market and an indication that competition may not be working well in supporting our statutory competition, innovation or service-user objectives.

b. The levels of IFs for UK-EEA transactions: whether these IFs are unduly high (Chapter 5), that is, higher than the level(s) that would emerge if competition was working well, specifically if the schemes were facing competitive constraints on the acquiring side and had taken into account the interests of merchants and their customers in setting the level of fees. Within this context, we have also considered whether the increases may be justified on the basis that they had contributed to improving the quality and efficiency of payments in CNP transactions, for example by bringing innovation to the market which would not have occurred absent such higher prices.

c. Whether higher IFs are passed through from acquirers to merchants and their customers (Chapter 6).

2.32 As regards the assessment of the appropriateness of the UK-EEA IFs levels set out in Chapter 5, we note that other corridors have been capped by regulation as a result of findings by the European Commission that IFs in those corridors breached Article 101 TFEU (Treaty on the Functioning of the European Union). Specifically, these corridors which are currently regulated include domestic IFs (which are set by regulation at 0.2/0.3 in both the UK and intra-EEA since 2015 and retained following the UK's withdrawal from the EU[33]) and intra-regional EEA-RoW IFs (which are set at 1.15%/1.50% as a result of commitments given by Mastercard and Visa to the European Commission in 2019). We have noted that in setting both the 2015 and 2019 caps, the European Commission has had regard in particular to MIT- (merchant indifference test) type analysis - that is, an analysis based on merchant's acceptance of Mastercard and Visa cards and appropriate alternatives available to merchants for each type of transaction (that is, within EEA and outside the EEA). However, there is no established methodology for calculating appropriate levels for cross-border IFs, which means that pending the development of such a methodology, there are theoretical and empirical challenges in carrying out this type of analysis.

33 We note that the Financial Services and Markets Act 2023 provides powers to the Secretary of State to repeal this specific instrument of assimilated EU legislation, however no policy statement has been made by the Secretary of State about such repeal and potential new UK instrument or intervention to replace it as appropriate.

2.33 As such, we have sought to assess the appropriateness of the current levels of UK-EEA IFs, and whether these had been set at a level that served the interests of all users (in particular UK merchants and their customers) on the basis of a range of analysis and evidence. In doing so, we considered:

a. The stated rationale for the increase: We have spoken to the schemes, received written representations, and looked into internal documents from Mastercard and Visa that could shed some light on the rationale for the increases and the extent the interests of service users, that is, organisations that accept cards and their customers, had been taken into account.

b. **Comparison between current levels of UK-EEA IFs and other (regulated) IFs**: We have assessed how current levels compare to the regulated levels that applied to these transactions before the UK's withdrawal from the EU (by virtue of Regulation 2015/251)[34] and the IF levels that apply, pursuant to the 2019 Commitments, to all outbound IF levels for RoW-EEA transactions (that is mainly non-SEPA transactions)[35], taking into account the differences and similarities between transactions across each of these corridors and whether such differences and similarities might provide a rationale for the current levels of UK-EEA IFs. We note that IFs for CNP payments made in the UK with cards issued in the rest of the world have remained unchanged since the UK left the EU, and they are equal to 1.15/1.50%. We also note that cross-border IFs in jurisdictions other than the UK and the EEA are generally uncapped and they may be higher than 1.15%/1.50%.[36]

c. **Alternatives to Mastercard and Visa**: We have looked at the cost to merchants of using alternative payment methods available for UK-EEA transactions[37] (including a study provided by Visa on the cost to merchants of alternative payment methods).[38]

d. **Possible justification for the price increases**: specifically, we looked at factors which Mastercard, Visa and some issuers identified as relevant when setting outbound IF levels, in particular costs linked to **fraud levels and other issuer costs**[39] (including data provided by the schemes and by one European issuer). Within this context we have therefore assessed whether higher IFs were used by issuers to fund service improvements that provided benefits to users on the acquiring side (for example, investments in fraud prevention) and as such could provide a justification for the increases in the levels of UK-EEA IFs.

2.34 For the avoidance of doubt, we have not carried out an analysis under Chapter 2 of the Competition Act 1998 ("**CA98**") but rather we have considered whether, reacting as rational operators to incentives taking into account the competitive constraints (or lack thereof) on each side, schemes set the IFs at levels that do not take account the interest of service users, that is, organisations that accept cards and their customers, or support innovation.

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34 See paragraphs 2.103, 2.109, 2.135, 2.138, and 2.155 to 2.158 in Annex 2.

35 See paragraphs 2.105, 2.110, 2.161 to 2.169, 2.172, and 2.175 to 2.179 in Annex 2.

36 For example, IFs for cross-border payments in New Zealand are currently uncapped and may be as high as 2.40% of the value of the transaction. For more information, see Table 4.1 of *Retail payment system: Costs to businesses and consumers of card payments in Aotearoa New Zealand: Consultation paper* (July 2024).

37 See paragraphs 2.102 to 2.116, 2.129, and 2.130 in Annex 2.

38 See Annex 3.

39 See paragraphs 2.4 to 2.27, 2.35 to 2.67, 2.74 to 2.93 in Annex 2.

3 Background

This chapter provides an overview of:

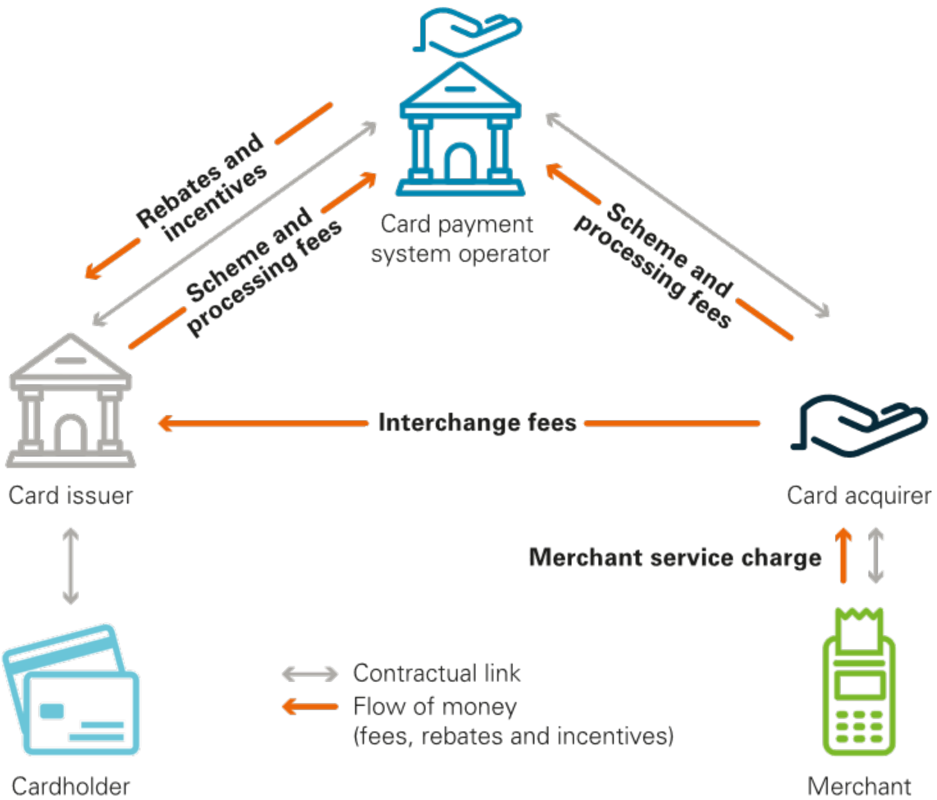
- what interchange fees (IFs) are, in the context of flows of money in four-party card schemes
- the regulation of IFs and the changes to IFs that led to this review
- the wider context relevant to this review, including competition law enforcement and litigation in relation to Mastercard and Visa's historic IFs

Four-party card schemes

Simplified overview

3.1 Mastercard and Visa operate what are known as four-party card payment systems or four-party card schemes.

Figure 1: Simplified structure of a four-party card payment system



3.2 Figure 1 sets out the main parties that make up the four-party model. These include the following groups:[40]

- **Merchants**: organisations that accept card payments.
- **Acquirers**: banks or other organisations licensed by card payment system operators to process debit and credit card payments on behalf of merchants.
- **Card payment system operators (such as Mastercard and** Visa**)**: organisations that manage the 'scheme rules' on card payments and set the terms on which issuers, acquirers, merchants, cardholders and other parties participate in the card payment system.
- **Issuers**: banks or other organisations licensed by card payment system operators to provide cards to cardholders. The issuer pays an acquirer the money a merchant is owed for a transaction and debits a cardholder's account. During the subsequent settlement process, the IF is transferred to the issuer.

3.3 Figure 1 also shows the main flow of fees between parties in a four-party card payment system, including:

- **Interchange fees (IFs)**, which acquirers pay to issuers each time a card is used to buy goods or services[41]; these per-transaction fees are usually a percentage of the transaction value but can vary depending on transaction and IF type
- **scheme and processing fees (S&P fees)**, which are set by Mastercard and Visa
- **rebates and incentives** which Mastercard and Visa pay to issuers (and occasionally to acquirers); as set out in our Market review of card scheme and processing fees interim report[42], in some instances incentives more than totally offset the fees charged to issuers
- **merchant service charge (MSC)**, which is the total amount merchants pay to acquirers for card-acquiring services; this comprises IFs, scheme and processing fees, and acquirer net revenue.

IFs

3.4 IFs are transaction fees paid by acquirers, on behalf of their merchants, to issuing banks and other issuers. IFs can vary by:

- the card product (debit or credit) used for the transaction
- the transaction environment – card present (CP) (such as in-store purchases where payment is made via chip and PIN or contactless method) or card not present (CNP) (which includes online purchases and phone orders).
- the category of card – consumer or commercial

40 Full definitions for each of these terms can be found in the Glossary (see annex 4 of this Report).

41 The IF is typically deducted from the transaction amount that is paid by the issuer to the acquirer. Acquirers then typically pass the IF on to merchants through the MSC, so it represents a cost to merchants for accepting card payments.

42 MR 22/1.9 *Market review of card scheme and processing fees: Interim report* (May 2024), pages 76 and 78, paragraphs 5.19 to 5.25.

- the region the card is issued in
- the region where the transaction takes place

3.5 Mastercard and Visa set the default multilateral IF level (MIF) that acquirers pay to issuers and, in turn, merchants pay through the MSC to their acquirers.[43] While issuers and acquirers can bilaterally negotiate lower IFs, this happens very rarely.

3.6 In their responses to a letter from the Treasury Select Committee (TSC) Mastercard and Visa said that IFs represent a mechanism to distribute the cost of the payment services across the two sides of the card scheme.

3.7 Mastercard said: 'Interchange is a small fee typically paid by card acquirers (the merchant/retailer's bank) to card issuers (cardholder's bank), to recognise the value delivered to merchants/retailers, governments and consumers by accepting electronic payments, the infrastructure required to make this possible and do so securely and the costs incurred in these respects'.[44]

3.8 Issuers can, should they choose, put the derived income towards operation and maintenance costs for their internal payment processor, increased security of transactions and any future development to make transactions faster, more convenient and secure.[45] Visa said: 'Interchange supports [issuers'] ability to issue and manage cards and digital credentials. It enables those players to fortify security against bad actors trying to steal information or commit fraud; 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'.[46]

Transaction and IF types

3.9 Card transactions where an issuer, an acquirer and the merchant point of sale location (the merchant location) are in the same country are typically defined as domestic transactions.[47] The IFs for these transactions are called domestic IFs.

3.10 Transactions where the card used for the purchase was issued in a country other than that of the merchant's location are typically referred to as cross-border transactions. These IFs are called cross-border IFs.

3.11 For the purposes of this market review, we distinguish between two types of UK-EEA cross-border transactions and related IFs.

- **Outbound IFs:** IFs for transactions using non-UK-issued cards to make payments to merchants located in the UK. For UK-EEA transactions, these IFs relate to payments made with EEA-issued cards at UK merchants. These fees are paid to EEA issuers and represent a cost to UK merchants.

43 Mastercard sets its default IF according to its rules (see rule 8.3*)* and webpage. Visa sets its IFs according to information contained on its website (see Frequently asked questions: What does it cost and how is this decided?).

44 Mastercard, *Letter to the Treasury Select Committee* (2 August 2022), page 4.

45 *Market review of cross-border interchange fees: A discussion of the impact of the UK-EEA cross-border interchange fee increases* (December 2022), pages 7 and 16, paragraphs 2.7 and 3.27.

46 Visa, *Visa response to Treasury Select Committee on cross-border interchange* (August 2022), page 1.

47 This is the UK Interchange Fee Regulation definition.

- **Inbound IFs:** IFs for transactions using UK-issued cards to make payments to merchants located outside the UK. For UK-EEA transactions, these IFs relate to payments made with UK-issued cards at EEA merchants. These fees are paid to UK issuers and represent a cost to EEA merchants.

Pricing of card-acquiring services

3.12 Card acquirers charge merchants for accepting credit and debit payment cards.

3.13 As set out in our recent card acquiring market review (CAMR) final report, acquirers tend to price card-acquiring services separately from card acceptance products and value-added services.[48] Merchants, depending on their size, have one or more of the following pricing options for card-acquiring services which are provided for in the contract between the merchant and the acquirer:[49]

- interchange fee plus (IC+) pricing, whereby for any given transaction an acquirer automatically passes through at cost the IF applicable to that transaction
- interchange fee plus plus (IC++) pricing, whereby for any given transaction an acquirer automatically passes through at cost the IF and other scheme fees applicable to that transaction[50]
- standard pricing, whereby for any given transaction an acquirer does not automatically pass through at cost the IF applicable to the transaction and the pricing option does not satisfy the criteria for fixed pricing
- fixed pricing, whereby a merchant pays a fixed, periodic fee for card-acquiring services, the amount of which does not depend on the volume or value of transactions it accepts or the characteristics of these transactions, within specified limits

3.14 By definition, in IC++ and IC+ pricing, acquirers automatically pass any IF charge on to merchants, so these are defined as 'pass-through' options.

3.15 Under the standard and fixed pricing options, acquirers do not automatically pass IFs on to merchants, but may choose to include the cost of IFs within the pricing arrangements. These pricing options are also known as 'blended' options because the individual cost components of the MSC (IFs, scheme and processing fees, and acquirer margin) are often aggregated. However, periodic renegotiation of contracts may result in the acquirer passing on increasing fees.

3.16 Figure 2 below breaks down UK-EEA CNP cross-border transactions at UK merchants in 2022 by pricing option. It shows that the majority (around 80%) of transactions, by value, were on pass-through pricing options (that is, IC++ and IC+). Standard and fixed pricing added up to about 20% of UK-EEA CNP cross-border transactions at UK merchants in 2022 by value.[51]

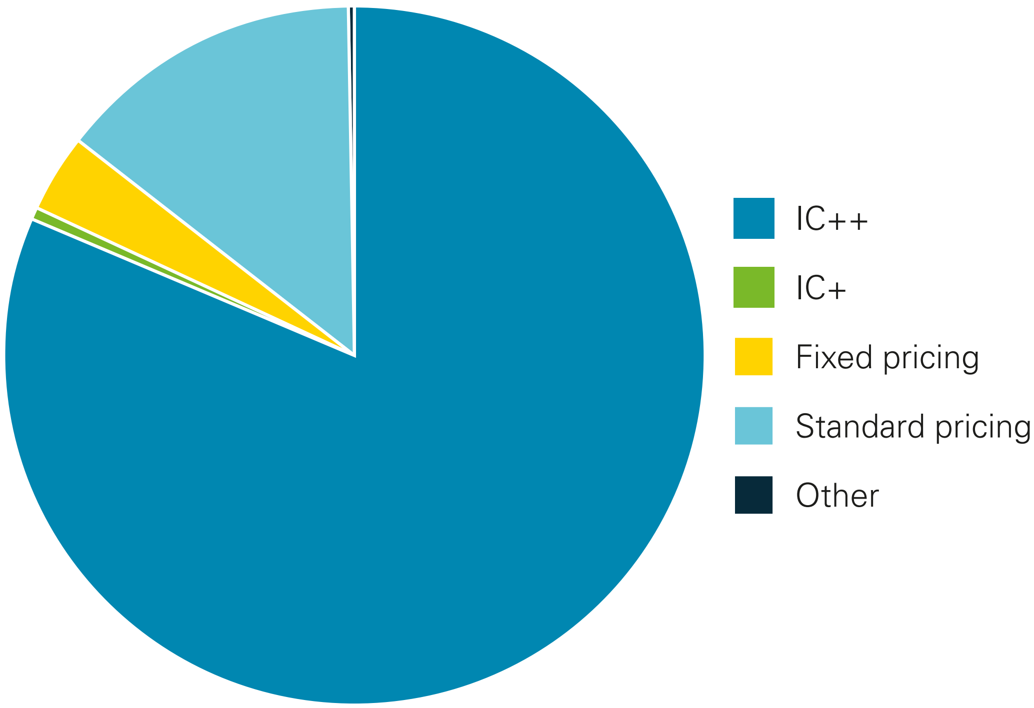
48 MR18/1.8, *Market review into card-acquiring services: Final report* (November 2021), page 31, paragraph 3.63.

49 MR18/1.8, *Market review into card-acquiring services: Final report* (November 2021), pages 31 to 33, paragraphs 3.63 to 3.71, and Annex 1.

50 At the time of the transaction, the acquirer may also pass-through other card scheme and processing fees that are not directly attributable to transactions.

51 PSR analysis based on 2022 data [✂].

Figure 2: Breakdown of UK-EEA CNP cross-border transactions by value at UK merchants in 2022 by pricing options



Source: PSR analysis of data from UK acquirers

3.17 We found in our CAMR final report that although IC++ pricing accounts for the largest proportion of transactions by value, the vast majority of merchants are not on IC++ contracts, with over 95% having standard pricing.[52] Merchants on IC++ pricing are typically the largest merchants, generally with an annual turnover above £50 million.[53]

Issuers

3.18 Issuers receive Mastercard's and Visa's UK-EEA CNP IFs. We asked UK issuers how they have used the additional income derived from the UK-EEA cross-border IF increases. All UK issuers asked said that they do not consider individual sources of card revenue, such as UK-EEA IF revenue, in making their decisions on rewards for cardholders or on investments (including in fraud prevention). They make decisions more holistically, at card portfolio level.[54]

52 MR18/1.8, *Market review into card-acquiring services: Final report* (November 2021), page 32, paragraph 3.64.

53 MR18/1.8, *Market review into card-acquiring services: Final report* (November 2021), page 7, paragraph 1.15 and *CICC (1441-1444) – Judgment (CPO Applications)* (8 June 2023), paragraph 86.

54 For more details on this, see paragraph 2.27 in Annex 2.

Regulation of interchange fees

UK Interchange Fee Regulation (IFR)

3.19 UK domestic IFs, for payments made at UK merchants using UK-issued cards, are regulated by the UK version of the EU IFR (UK IFR).[55] The UK IFR came into effect on 31 December 2020.

3.20 The UK IFR caps the level of IFs on both CP and CNP domestic consumer debit and credit card transactions at 0.2% and 0.3% of the value of the transaction respectively.

3.21 The PSR is the lead authority for monitoring and enforcing compliance with the UK IFR. The UK IFR does not apply to cross-border IFs for payments made at UK merchants using cards issued outside the UK.

EU Interchange Fee Regulation (EU IFR)

3.22 Until December 2020, the EU IFR applied to the UK. The EU IFR came into force in 2015.[56] It set business rules for card payments and introduced price caps on the IF levels for domestic transactions and for transactions across the different countries in the EEA (intra-regional IFs). These caps fixed the maximum level of IF payable by merchants when accepting certain card payments.

3.23 In putting the EU IFR in place, the European Commission aimed to address the problem of 'high and divergent' IFs in the EEA, while facilitating cross-border card payment services.[57] One concern was that high IFs were leading to higher final prices for goods and services at the expense of consumers. The price caps came into effect on 9 December 2015, and the majority of provisions relating to business rules were effective from 9 June 2016.

3.24 When the UK was part of the EU, the EU IFR provisions applied caps for IFs on UK domestic and UK-EEA card transactions at 0.2% of the value of consumer debit card transactions and 0.3% of the value of consumer credit card transactions. Since 31 December 2020, the UK IFR caps the level of domestic IFs within the UK.

The 2019 European Commission Commitments

3.25 In 2019, in response to the European Commission's competition law investigation into inter-regional IFs, Mastercard and Visa offered commitments to the European Commission to cap IFs on transactions involving non-EEA-issued cards and EEA merchants (the 2019 Commitments). These were accepted by the Commission.[58] The UK no longer being in the

55 The EU IFR is assimilated into UK Law by the Retained EU Law (Revocation and Reform) Act 2023 in accordance with the Financial Services and Markets Act 2023.

56 Official Journal of the European Union, *Regulation (EU) 2015/751 of the European Parliament and of the Council of 29 April 2015 on interchange fees for card-based payment transactions (Text with EEA relevance)* (April 2015).

57 Official Journal of the European Union, *Regulation (EU) 2015/751 of the European Parliament and of the Council of 29 April 2015 on interchange fees for card-based payment transactions (Text with EEA relevance)* (April 2015), paragraph 13.

58 European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision and 2019 Commitments; CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision and 2019 Commitments.

EEA[59], the 2019 Commitments apply to UK-issued cards when used for transactions at EEA merchants.

3.26 As a result of the 2019 Commitments, UK-EEA inbound CP IFs are subject to caps of 0.2% and 0.3% for debit and credit cards respectively. UK-EEA inbound CNP IFs are subject to higher caps of 1.15% and 1.5% for debit and credit cards respectively. These commitments were set to be in place until November 2024. On 5 July 2024, the European Commission noted the voluntary continuation by Visa and Mastercard of the caps for inter-regional IFs beyond November 2024.[60] The European Commission stated that, under the voluntary continuation, inter-regional IFs for debit and credit card transactions under these schemes will remain capped for another five years until November 2029.[61] The European Commission observed that 'Mastercard and Visa debit and credit cards are still "must-take" for EEA merchants [and that] in the absence of caps, merchants would face the risk of excessive IFs passed on to them through their Merchant Service Charges.'[62]

3.27 A key input to the setting of the levels in the 2019 Commitments was a merchant indifference test (MIT) on inter-regional transactions, both debit and credit, and CP and CNP. The MIT used different payment alternatives as comparators for CP and CNP transactions[63]:

- For inter-regional CP transactions, the comparator was cash.
- For inter-regional CNP transactions, the comparator was means of payments funded via bank transfers. These were bank transfers outside the Single Euro Payments Area (SEPA), since the relevant inter-regional transactions involved the EEA Contracting Parties (including the UK at the time) and other third parties that were outside the EEA and SEPA payment systems.

3.28 At the time, the UK was part of the EEA and SEPA. When the UK withdrew from the EU and the EEA, it stayed in SEPA. The SEPA region includes both EEA and non-EEA countries.[64] Non-EEA SEPA countries currently include Andorra, Monaco, San Marino, Switzerland and the Vatican City, alongside the UK. The European Payment Council (EPC) sets the participation criteria that countries need to meet to be deemed eligible for SEPA participation.[65]

59 'EEA' is defined in the 2019 Commitments as "those countries participating in the European Economic Area as of the Commencement Date or joining thereafter for the duration of each such country's participation in the EEA during the term of these Commitments".

60 European Commission Daily News 05/07/2024, - 'Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024'

61 European Commission Daily News 05/07/2024, - 'Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024'

62 European Commission Daily News 05/07/2024, - 'Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024'

63 See, for example, European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision, recitals 79 to 84.

64 European Payments Council, EPC list of Countries in the SEPA Schemes' Geographical Scope (2 January 2023).

65 These criteria include relationship with the EU, criteria to ensure a level playing field with other SEPA Scheme participants, legal and regulatory criteria, Market and Operational criteria and additional criteria to preserve the integrity of the SEPA Schemes.

3.29 Currently there are no caps on IFs for UK-EEA CNP cross-border transactions using EEA-issued cards at UK merchants (outbound IFs). The applicable caps for UK-EEA consumer CNP transactions are illustrated in Figure 3 and Table 1.

Figure 3: Caps for UK and EEA consumer CNP transactions

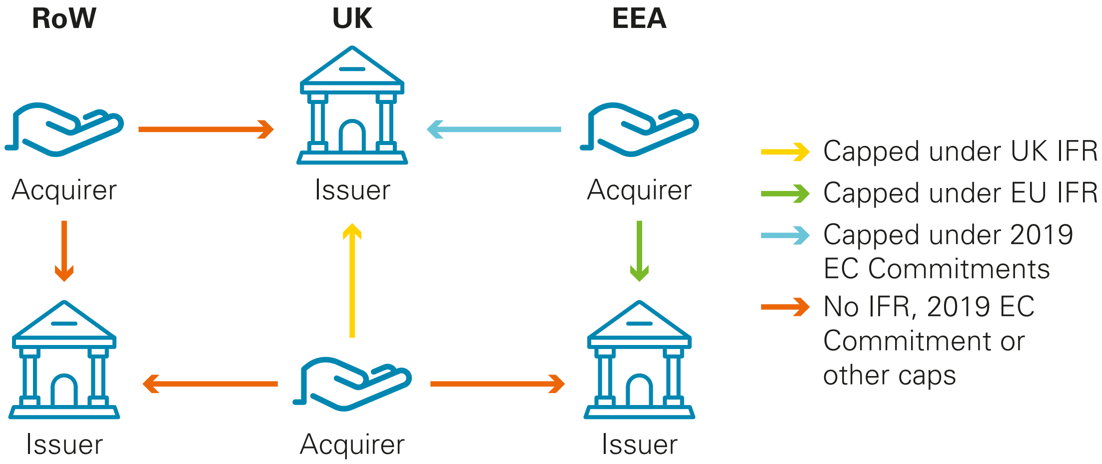


Table 1: Caps for UK and EEA consumer CNP transactions

Regions	Location of issuer	Location of merchant	IF levels pre-the UK's withdrawal from the EU	IF levels now	Are they capped?
UK domestic	UK	UK	0.2%/0.3%	0.2%/0.3%	Yes (UK IFR)
UK->EEA Inbound IF	UK	EEA	0.2%/0.3%	1.15%/1.5%	Yes (2019 Commitments)
EEA->UK Outbound IF	EEA	UK	0.2%/0.3%	1.15%/1.5%	No
EEA domestic	EEA	EEA	0.2%/0.3%	0.2%/0.3%	Yes (EU IFR)

Merchant indifference test

3.30 The merchant indifference test (MIT) is a methodology originally developed in economic literature and then further developed by the European Commission to set IF caps for cards.[66] It involves identifying a merchant's costs of accepting one or more suitable alternative payment method(s), for example, by surveying merchants and using that data to calculate a figure that can be used as a proxy for a competitive IF level.

66 Rochet, J.C. and Tirole, J, '[Must-take cards: merchant discounts and avoided costs](#)', *Journal of the European Economic Association* Volume 9, Issue 3 (2011), pages 462 to495.

3.31 The EU IFR caps are based on this methodology, as illustrated by the extract below:[67]

'The caps in this Regulation are based on the so-called "Merchant Indifference Test" developed in economic literature, which identifies the fee level a merchant would be willing to pay if the merchant were to compare the cost of the customer's use of a payment card with those of non-card (cash) payments (taking into account the fee for service paid to acquiring banks, i.e. the merchant service charge and the interchange fee). It thereby stimulates the use of efficient payment instruments through the promotion of those cards that provide higher transactional benefits, while at the same time preventing disproportionate merchant fees, which would impose hidden costs on other consumers….'

3.32 The 2019 European Commission Commitments are also based on an MIT calculation:[68]

'…taking into account the specificities of inter-regional transactions, the Commission conducted a market investigation requesting data from Visa, Mastercard, certain competitors and merchants. The MIT-compliant MIF caps were calculated by comparing the merchants' costs of accepting payments made by debit and credit cards to those of accepting payments made with alternative means of payment. The relevant alternative means of payment are composed of payment instruments which must not, and do not, include a MIF component.'

3.33 For inter-regional CNP transactions, payment methods that were identified as plausible payment alternatives for the purposes of the MIT were: 'means of payments funded via bank transfers (which are outside the domestic payment systems of the EEA Contracting Parties and the Single European Payment Area, SEPA; "non SEPA bank transfers")'.

Regulatory and legal scrutiny of IFs

3.34 This review is carried out in accordance with our legal framework, in particular our general duties[69], statutory objectives to promote competition, foster innovation and protect service users[70], that is, organisations that accept cards and their customers, and regulatory principles[71] as outlined in Chapter 2.

3.35 Payment cards in general, and IFs in particular, have received a considerable amount of regulatory attention, some of which provides relevant context for our review, principally the 2019 European Commission Commitment Decisions, the Supreme Court judgment in *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 (Sainsbury's SC) and the more recent Court of Appeal judgment in *Dune Group Ltd and others v Visa Europe Ltd and others; Dune Group Ltd and others v Mastercard Inc. and others* [2022] EWCA Civ 1278 (Dune CA). Whilst not considering these in detail, this report will refer to them as appropriate.

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67 Official Journal of the European Union, Regulation (EU) 2015/751 of the European Parliament and of the council of 29 April 2015 on interchange fees for card-based payment transactions (Text with EEA relevance), at recital 20.

68 European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision (section 7.2.1, page 15); CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision (section 7.2.1, page 14).

69 FSBRA, section 49

70 FSBRA, sections 49(2), and 50 - 52

71 FSBRA, section 53

3.36 In that regard, we note that it is established in EU and UK law that Mastercard's historic intra-EEA and domestic IFs infringed EU competition law. In 2007, the European Commission found that Mastercard IFs applicable within the European Economic Area (EEA MIFs) had been in breach of article 101(1) TFEU since 22 May 1992 and Mastercard had not provided sufficient proof that any of the first three article 101(3) exemption criteria were met (Mastercard EC).[72] This decision was upheld by the General Court (Mastercard GC)[73] and by the Court of Justice of the European Union (Mastercard CJEU)[74] and has become final within the meaning of section 58A of the Competition Act 1998. It establishes that Mastercard's historic intra-EEA IFs restricted competition, and that the card scheme had failed to demonstrate that these IFs were justified, taking into account any efficiencies created.

3.37 In Sainsbury's SC, the Supreme Court held that the 'essential factual basis upon which the Court of Justice held that there was a restriction on competition [in Mastercard CJEU] [was] mirrored' in the appeals before it. Specifically, it stated that '[t]hose facts include[d] that: (i) the MIF is determined by a collective agreement between undertakings; (ii) it has the effect of setting a minimum price floor for the MSC; (iii) the non-negotiable MIF element of the MSC is set by collective agreement rather than by competition; (iv) the counterfactual is no default MIF with settlement at par (that is, a prohibition on ex post pricing); (v) in the counterfactual there would ultimately be no bilaterally agreed IFs; and (vi) in the counterfactual the whole of the MSC would be determined by competition and the MSC would be lower.'[75]

3.38 The Supreme Court held that even had it not been bound by Mastercard CJEU, it would conclude that there was a restriction on competition in the consolidated appeals and therefore followed it:

'99. On the facts as found, the effect of the collective agreement to set the MIF is to fix a minimum price floor for the MSC. In the words of Mr Dryden, AAM's expert economist, it sets a "reservation price".

100. That minimum price is non-negotiable. It is immunised from competitive bargaining. Acquirers have no incentive to compete over that part of the price. It is a known common cost which acquirers know they can pass on in full and do so. Merchants have no ability to negotiate it down.

101. Whilst it is correct that higher prices resulting from a MIF do not in themselves mean there is a restriction on competition, it is different where such higher prices result from a collective agreement and are non-negotiable.

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72 European Commission, Commission Decision of 19 December 2007 (Case No COMP/34.579 Mastercard). No penalty was imposed as the decision had been notified to the European Commission. Mastercard appealed this decision to the General Court and in the meantime reduced its EEA IFs to zero.

73 MasterCard Inc v European Commission (Case T-111/08) [2012] 5 CMLR 5 (24 May 2012).

74 MasterCard Inc v European Commission (Case C-382/12 P) [2014] 5 CMLR 23 (11 September 2014).

75 Sainsbury's Supermarkets Limited v Mastercard Incorporated and others [2020] UKSC 24 (Sainsbury's SC); see also Sainsbury's Supermarkets Limited v Mastercard Incorporated and others [2018] EWCA Civ 1536 (Sainsbury's CA); and Sainsbury's Supermarkets Ltd v Mastercard Incorporated and others [2016] CAT 11 (Sainsbury's CAT). The Supreme Court remitted to the CAT for further determination issues of fair share and quantum, however the cases subsequently entered into a confidential settlement agreement bringing the litigation to an end.

102. Whilst it is also correct that settlement at par sets a floor, it is a floor which reflects the value of the transaction. Unlike the MIF, it involves no charge resulting from a collective agreement, still less a positive financial charge.

103. There is a clear contrast in terms of competition between the real world in which the MIF sets a minimum or reservation price for the MSC and the counterfactual world in which there is no MIF but settlement at par. In the former a significant portion of the MSC is immunised from competitive bargaining between acquirers and merchants owing to the collective agreement made. In the latter the whole of the MSC is open to competitive bargaining. In other words, instead of the MSC being to a large extent determined by a collective agreement it is fully determined by competition and is significantly lower.'[76]

3.39 The extension of the Commission's prohibition decision in Mastercard to the Visa scheme and its application to domestic intra-EEA IFs by the SC in Sainsbury's v Visa and Mastercard[77] underlines the extent to which the four-party scheme system operated by Mastercard and Visa is capable of operating contrary to competition law. As explained above, the setting of a minimum MIF within the four-party schemes operated by Mastercard and Visa amounts to a restriction of competition (involving an agreement on prices), which has the effect of immunising one part of the MSC from competition; the merchant being unable to negotiate with the acquirer the level of that part of the MSC. Accordingly, this prevents an element of the MSC being negotiated down, with the consequent effect of artificially increasing the MSC.

3.40 More recently, in Dune CA, the Court of Appeal upheld the Competition Appeal Tribunal's (CAT) determination that it could not extend Sainsbury's SC to deliver summary judgment in respect of domestic and intra-EEA IFs following the entry into effect of the IFR caps in 2015, or for inter-regional IFs in general. As regards the introduction of the IFRs, the CAT accepted that it was arguable that this could change the relevant counterfactual to be applied in determining whether the MIF had an effect on competition. As regards inter-regional IFs in general, the Court of Appeal accepted that it was arguable that the merchant's negotiating power in relation to the MSC may not be affected by the higher inter-regional IFs, such that they could not be said to have an 'appreciable' effect on competition and whether or not that was the case was a matter for evidence.[78] These issues required consideration at a full hearing before any such determination could be made.[79]

3.41 A substantive trial of these and other issues will take place as part of the Umbrella Interchange Fee litigation, pursuant to the Umbrella Proceedings Order given in July 2022 by the CAT pursuant to Practice Direction 2/2022 (PD2/2022).[80] PD2/22 sets out the procedural rules in place under which the designated 'Host Cases' (a large number of individual actions all claiming damages from Mastercard and/or Visa due to alleged breaches of competition law arising from IFs) are the subject of the Merchant Interchange Fee Umbrella Proceeding.

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76 Sainsbury's Supermarkets Limited v Mastercard Incorporated and others [2020] UKSC 24 (Sainsbury's SC);

77 Sainsbury's Supermarkets Limited v Mastercard Incorporated and others [2020] UKSC 24 (Sainsbury's SC).

78 Dune Group Limited and others v Visa and others [2022] EWCA Civ 1278 (Dune CA); Dune Group Limited and others v Mastercard and others [2022] CAT 14 (Dune CAT). §§56-58

79 Dune CAT. See also Commercial and Inter-regional card claims v Mastercard and others [2023] CAT 38, referring to Dune at paragraphs 94-97.

80 Practice Direction 2/22 (2 June 2022).

3.42 A hearing on Trial 1 on liability in relation to UK and Irish domestic MIFs took place in February and March 2024. At present, it is envisaged that there will be further hearings on the following issues:[81]

- Trial 2, to take place in October or November 2024, to deal with all issues relating to acquirer and merchant pass-on.
- Trial 3, to take place at a future unspecified date, to deal with all other issues including liability issues arising in relation to non-UK and non-Irish domestic MIFs.

3.43 At the present time, therefore, there has been no judgment reached on whether or not the IFs for cross-border transactions subsequent to the introduction of the EU IFR are or were compatible with UK competition law.[82]

3.44 As regards the 2019 Commitments, to the extent that the European Commission's market testing or analysis considered the position of the UK, it was: (i) as a member of the EEA, (ii) while the UK-EEA IFs were subject to the IFR, and (iii) as a country in which the IFs caps would apply. As a result of the drafting of those commitments, point (iii) above changed upon the UK's departure from the EU. In our view this does not, of itself, require or endorse an increase in UK-EEA IFs.[83] In those circumstances, even if one accepts that the UK's withdrawal from the EU had the effect going forward of transforming UK-EEA IFs into inter-regional IFs (or a category of inter-regional IFs), it does not follow that the 2019 Commitments are the appropriate way for IFs to be determined for those transactions. As such, it is difficult to see how the 2019 Commitments could be determinative to the appropriateness of Mastercard and Visa's UK-EEA CNP IF increases.

3.45 Table 2 below summarises the main relevant regulatory and legal precedents, and the IF levels considered.

Table 2: Summary of regulatory and legal precedents

Regulatory decision/action and judgments	IF level	Outcome
Visa (2002)[84]	Intra-EEA debit: €0.28 maximum Intra-EEA credit: 0.7% maximum Transparency obligations; differential IFs for CP and CNP transactions	Commitments accepted by the European Commission (2002 to 2007)

81 A hearing on pass on issues took place in May 2023. A detailed summary of the different trials is set out in the CAT's 2023 judgment in Case Nos: 1441-1444/7/7/22 Commercial and Interregional Card Claims I and II Ltd v Mastercard and Visa: Collective Proceedings Order (CPO) applications [2023] CAT 38, see paragraphs 20-25. The CPO applications were refused; in a subsequent order of 4 September 2023 sets out a timetable for filing revised applications by 15 December 2023, with a CPO certification hearing in April 2024.

82 It is possible that the proceedings currently before the CAT may ultimately settle and/or be subject to further appeals.

83 A fundamental point common to the EU IFR and the 2019 Commitments is that the IF caps set maximum levels but do not preclude IFs being set at a lower level or not set at all.

84 European Commission, *2002/914/EC: Commission decision of 24 July 2002 (Case No COMP/29.373 – Visa International – Multilateral Interchange Fee) (Text with EEA relevance) (notified under document number C(2002) 2698)*. The IFs related to Visa's EU region, which at the time included the EU Member States as well as Iceland, Liechtenstein, Norway, Turkey, Israel, Cyprus, Malta, and Switzerland (see paragraph 5).

Regulatory decision/action and judgments	IF level	Outcome
Mastercard – OFT (2005)[85] **Mastercard – CAT (2006)**[86]	UK domestic credit/charge cards (0.9% to 1.5%)	Notified agreement declared incompatible with UK/EU competition law Decision subsequently withdrawn on appeal
Mastercard I (2007)[87] **Judgments: Mastercard GC,**[88] **CJ**[89]	Intra-EEA debit: 0.4% of the transaction value increased by €0.05 and 1.05% increased by €0.05 Intra-EEA credit: between 0.8% and 1.2%	Prohibition decision[90] Upheld by the General Court and Court of Justice
Visa debit (2010)[91]	The decision: i) required Visa to reduce its weighted average EEA debit MIF to 0.2%; ii) recorded the allegation that the MIFs had both the object and effect of restricting competition; and iii) without making a finding on liability, and subject to compliance with the decision, held that the Commission would not take further action against Visa in relation to its EEA debit MIFs	Commitments accepted (2010 to 2015)
Visa credit (2014)[92]	0.3% (weighted average intra-EEA credit MIF), no increase to domestic credit MIFs and within two years intra-EEA credit MIF to apply	Commitments accepted (2014 to 2019); superseded by the EU IFR
EU IFR (2015)[93]	0.2%/0.3% (domestic and intra-EEA)	–

85 CA98/05/05, decision and press release (includes links to annexes to the decision).

86 Mastercard v OFT case page, see, in particular, Mastercard v OFT [2006] CAT 14.

87 Commission decision of 19 December 2007 (Case No COMP/34.579 Mastercard).

88 MasterCard Inc v European Commission (Case T-111/08) [2012] 5 CMLR 5 (24 May 2012).

89 MasterCard Inc v European Commission (Case C-382/12 P) [2014] 5 CMLR 23 (11 September 2014).

90 See paragraph 3.36. The European Commission found that the Mastercard EEA IFs applicable since 22 May 1992 had been in breach of Article 101(1), and Mastercard had not proved to the requisite standard that any of the first three Article 101(3) exemption criteria were met.

91 Case No COMP/39.398 – Visa Europe – Debit IFs, Commitments and Commitments decision (September 2010).

92 European Commission, Case No COMP/39.398 – Visa Europe – Credit IFs, Commitments and Commitments decision (February 2014). The Commitments also related to cross-border acquiring; see section 6.

93 Regulation (EU) 2015 / 751 of the European Parliament and Council. See paragraph 3.22 above.

Regulatory decision/action and judgments	IF level	Outcome
Cross-border acquiring (Mastercard)[94]	NA. Prior to the entry into force of the EU IFR, Mastercard's rules obliged acquiring banks to apply the IFs of the country where the retailer was located, preventing retailers in high-IF countries from benefiting from lower IFs offered by an acquiring bank located in another Member State	Mastercard fined €570 million (reduced by 10% for settlement) The infringement ended when Mastercard amended its rules in view of the entry into force of the EU IFR
2019 Commitments Decisions[95]	The decisions required each of Mastercard and Visa to reduce their inter-regional MIFs to 0.2%/0.3% (for CP debit and credit transactions) and 1.15%/1.5% (for CNP debit and credit transactions); These commitments were given to address competition concerns that the MIFs had both the object and effect of restricting competition, but no finding on liability was made.	2019 Commitments accepted, bringing to an end the European Commission's investigation in relation to Mastercard's and Visa's consumer credit and debit IFs (2019 to date)
Sainsbury's SC[96]	Intra-EEA and UK domestic	*Mastercard CJ* extended to the Visa scheme and to UK domestic IFs (pre-IFR)
UK IFR[97]	UK domestic, 0.2%/0.3% (consumer debit/credit)	–
Dune – CAT[98]	Intra-EEA and UK domestic pre-IFR Intra-EEA and UK domestic post-IFR, inter-regional, commercial, Italian domestic IFs	Summary judgment granted, relying on *Sainsbury's SC* *Mastercard I* and *Sainsbury's SC* distinguished; summary judgment denied – substantive hearing as part of the Umbrella Proceedings
Merricks v Mastercard Collective Proceedings – CAT[99]	UK IFs - consumer claimants (Mastercard only) The majority of claims relate to the period 1997 - 2009.	Issues of pass-on to be considered at the Merchant Interchange Fee Umbrella Proceedings hearings – see below

94 European Commission, Case AT.40049 – MasterCard II (22 January 2019) (Prohibition decision).
95 See paragraph 3.25 above.
96 See paragraph 3.37 above.
97 See paragraph 3.20 above.
98 See paragraph 3.40 above.
99 Case 1266/7/7/16 Walter Hugh Merricks CBE v Mastercard Incorporated and others.

Regulatory decision/action and judgments	IF level	Outcome
Merchant Interchange Fee Umbrella Proceedings – CAT[100]	EEA, domestic, inter-regional – merchant claimants	Hearings on the issues of pass-on commenced in November 2024 with further hearings to take place in March 2025
Commercial Card Claims – CAT [101]	UK commercial IFs for the period 2016 – 2022 – merchant claimants	Revised CPO applications approved.[102]

Increases in UK-EEA consumer CNP IFs

3.46 Following the UK's full exit from the EU in January 2021, the EU IFR no longer applied to transactions in the UK. The UK IFR applied only to wholly domestic transactions, that is, cards issued in the UK. Subsequently, Mastercard and Visa decided to increase IFs for consumer debit and credit CNP transactions involving UK issued cards at EEA merchants and EEA issued cards at UK merchants (consumer debit and credit) from 0.2% and 0.3% to 1.15% and 1.5%, respectively.

3.47 Mastercard and Visa announced and introduced changes to cross-border IFs as follows:

- At the end of 2020, Mastercard announced it would increase inbound IFs for consumer CNP transactions from 0.2% and 0.3% to 1.15% and 1.5% for debit and credit cards, respectively. These increases became effective in October 2021.
- In March 2021, Visa announced increases in both inbound and outbound IFs for consumer CNP transactions from 0.2% and 0.3% to 1.15% and 1.5% for debit and credit cards, which came into effect from October 2021.
- In the third quarter 2021, Mastercard announced it would increase outbound IFs for consumer CNP transactions from 0.2% and 0.3% to 1.15% and 1.5% for debit and credit cards, respectively. The increases became effective in April 2022.

3.48 For CP transactions using consumer debit and credit cards, inbound and outbound UK-EEA IFs have remained at the levels set under Mastercard and Visa's 2019 Commitments, (0.2% and 0.3%, respectively).

100 Case 1517/11/7/22. There are a large number of separate claims which form the CAT Umbrella Proceedings.

101 Cases 1441-1444/7/7/22. Commercial and Interregional Card Claims I Limited ("CICC I") v Mastercard Incorporated & Others, Commercial and Interregional Card Claims II Limited ("CICC II") v Mastercard Incorporated & Others, Commercial and Interregional Card Claims I Limited ("CICC I") v Visa Inc. & Others and Commercial and Interregional Card Claims II Limited ("CICC II") v Visa Inc. & Others.

102 See CAT judgment on revised CPO applications in Commercial and Interregional Card Claims collective proceedings actions against Mastercard and Visa [2024] CAT 39.

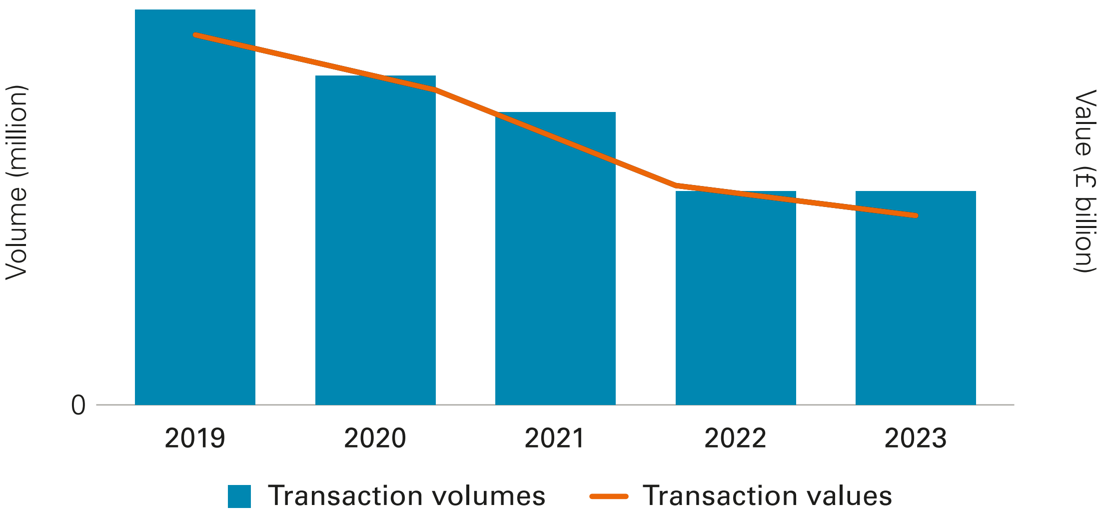
3.49 We note that the current UK-EEA CNP IF levels are aligned to the EEA-RoW caps set out in the 2019 commitments, which are reportedly lower than the IF levels charged for CNP transactions made between RoW countries (countries other than the UK and the EEA Member States). IF levels on RoW-RoW CNP transactions are generally uncapped: for example, IFs for cross-border payments between New Zealand and other RoW countries can be as high as 2.40% of the value of the transaction made.[103]

Quantification of the increases

3.50 We have gathered data from Mastercard and Visa to compute the scale of their increases in outbound IFs. The data covers the years 2019 to 2023.

3.51 Figure 4 shows CNP transaction volumes and values for 2019 to 2023 where the card used is issued in the EEA and the merchant is located in the UK, that is, UK-EEA debit and credit CNP transactions resulting in outbound IFs. A steady decline of transaction values can be seen between 2019 and 2021 (showing a total drop of 41%). A further, but significantly smaller decrease in transactions values took place between 2021 and 2023. The trend is different in the case of transaction volumes: after experiencing a sustained decline between 2019-2022 (a drop of approximately 46%), transaction volumes stabilised and show no significant change between 2022 and 2023.

Figure 4: EEA cards used at UK merchants, transaction volumes and values (2019 to 2023)



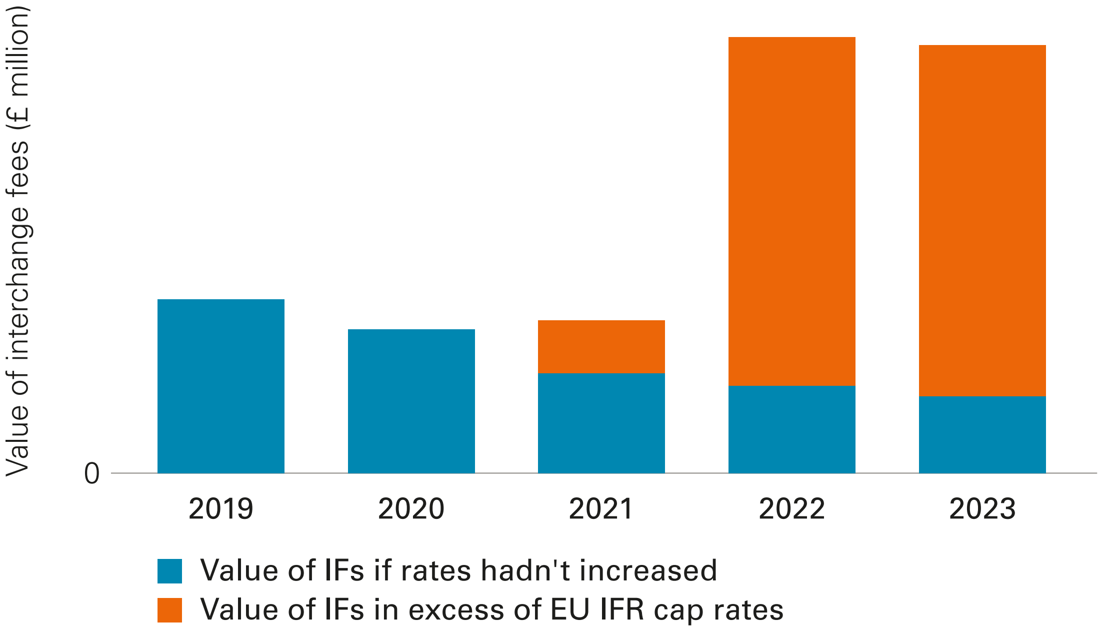
Source: PSR analysis of data from Mastercard and Visa (2024). [✂].

Note: the figures for transaction volumes and values take account of any relocation that has already happened (see Chapter 4); we have removed numerical values from the axis to avoid disclosing potentially sensitive information.

103 See Table 4.1 of Retail Payment System: costs to businesses and consumers of card payments in Aotearoa New Zealand: Consultation Paper: https://comcom.govt.nz/__data/assets/pdf_file/0031/359491/Retail-Payment-System-Costs-to-businesses-and-consumers-of-card-payments-in-Aotearoa-New-Zealand-Consultation-Paper-23-July-2024.pdf.

3.52 Figure 5 shows that outbound IFs have significantly increased since Visa and Mastercard raised their MIFs (in October 2021 and April 2022, respectively). The blue bars in the figure show what IFs would have been if MIFs had stayed at EU IFR levels (0.2% for debit cards and 0.3% for credit cards). The orange bars, from 2021 onwards, show the additional interchange revenue resulting from the outbound IF increases. The actual interchange generated by card transactions after the outbound IF increases can be obtained by summing up the blue and the orange bars. The data shows that, in 2022 and 2023, the extra interchange revenue amounted to between £150 to £200 million per year [✁].[104]

Figure 5: EEA cards used at UK merchants, outbound IFs (2019 to 2023)



Source: PSR analysis of data from Mastercard and Visa. [✁]

Note: the figures for outbound IFs take account of any relocation that has already happened (see Chapter 4); we have removed numerical values from the axis to avoid disclosing potentially sensitive information.

104 PSR analysis of data submitted by Mastercard and Visa [✁].

4 Nature of competition in four-party card schemes

Four-party card schemes like Mastercard and Visa are two-sided networks, serving users on both sides of the payment system they operate. Issuers and cardholders are on one side (the issuing side); acquirers, merchants (and their customers) are on the other (the acquiring side). Any decision Mastercard and Visa make on how much to charge the acquiring side for EEA consumer CNP transactions at UK merchants will depend on how far they face competitive constraints on this side.

This chapter sets out why we conclude that Mastercard and Visa were not subject to effective competitive constraints on the acquiring side when they decided to increase the UK-EEA consumer CNP interchange fees (outbound IFs), and the commercial incentives that they had to do so.

To inform our assessment, we considered the submissions and representations from Mastercard and Visa, and the information and feedback provided by various stakeholders on these specific issues.

Introduction

4.1 As explained in Chapter 3, four-party card schemes like Mastercard and Visa set the MIF, which is the default IF that applies in the absence of any other rate agreed between an issuer and an acquirer. In practice, such alternative agreements occur very rarely.[105]

4.2 Mastercard and Visa operate in two-sided markets, with issuers and cardholders on one side (the issuing side), and acquirers and merchants on the other side (the acquiring side).

4.3 The ability to set high IFs is constrained if there are effective competitive constraints on the acquiring side. That is, if the payment market was working well, acquirers and merchants would have sufficient bargaining power to renegotiate any increase in fees from the schemes. They would be able to steer their customers towards cheaper alternative payment methods, and, ultimately, they would be able to refuse accepting a card transaction without fear of losing the sale. However, the schemes' considerations change radically when competitive constraints on the acquiring side are not effective. That happens when:

- acquirers cannot practically refuse to offer card-acquiring services for a given card-brand
- merchants cannot practically refuse (or even discourage use of) the same card-brand, since doing so would almost certainly mean losing business

105 See paragraphs 3.5 in Chapter 3.

4.4 This is what we refer to below as 'lack of downward pressure on the acquiring side'. In that case, an increase in IFs will have limited to no impact on card acceptance. The card schemes can increase the IFs without having to worry about a possible reaction from acquirers and merchants.

4.5 In this scenario, schemes do not need to compete for acquirers and merchants. So, it will make sense for them to increase fees on the acquiring side to the hypothetical maximum level that acquirers and merchants will tolerate, that is, a level above which acquirers and merchants would find it more convenient to accept alternative payment methods instead of cards. At the same time, increasing IFs helps card schemes to secure issuers, by providing them with a sufficiently high stream of revenues to be willing to issue cards under those schemes. Increased IFs will represent an extra cost for merchants (including SMEs) and are likely to be partly reflected in retail prices to consumers.

Lack of downward pressure on outbound IFs

4.6 In four-party card schemes like Mastercard and Visa, an acquirer contracts directly with the scheme to be able to offer card acquiring services to merchants and acquire (carry out) card transactions on their behalf. The acquirer then contracts with merchants to offer these services to them. Accordingly, any competitive constraints on the ability of the scheme to increase IFs could potentially come from the actions that acquirers or merchants may take in response to IF levels set by the scheme.

4.7 Accordingly, in this chapter we consider:

- whether UK acquirers and/or merchants had any way of responding when the schemes increased the outbound IFs in October 2021 and April 2022
- whether such responses provided effective competitive constraints on Mastercard and Visa when setting the new outbound IF levels.[106]

4.8 For the reasons set out below, we found that the schemes do not face effective competitive constraints on the acquiring side and as a result there was very limited, if any, downward pressure on outbound IFs.

Lack of constraints from UK acquirer responses

4.9 As acquirers pay IFs to the issuer, our analysis of competitive constraints on Mastercard and Visa when deciding to increase the IF levels begins with acquirers and their potential responses.

4.10 The acquirers' customers are the merchants who use card-acquiring services as the means to receive payments for goods and services they sell. Acquirers offer the relevant payment services that their merchants need to receive payments. We found that virtually all UK acquirers offer card-acquiring services for both Mastercard and Visa. The acquirers confirmed that this is because UK merchants (especially retail merchants) must be able to accept both Mastercard and Visa to do business. As illustrated in more detail in Annex 1, in general, no merchant accepts one card scheme but not the other. In practice, all the acquirers we spoke

106 Competitive constraints refer to possible factors that can limit or influence firms' behaviour and pricing strategies, including existing and /or potential competition between providers and consumer choice.

to, who represent more than 90% of the UK market, confirmed that both they, and the merchants they serve, offer both Visa and Mastercard as payment systems. [107]

4.11 In Chapter 6, we performed some analysis of the impact of the outbound IF increases on UK acquirers, to establish how far they could respond to the increases, assuming they had the ability to do so.[108]

4.12 As discussed in more detail in Chapter 6, our analysis of UK acquirer data for 2022 shows that the financial impact of the outbound IF increases on UK acquirers was modest. This is because most of these fees were passed on to UK merchants. Approximately 95% of all the outbound IF increases were passed on to UK merchants either immediately (80%) or at some point (15%). Only around 5% of these increases were 'absorbed' by a small number of UK acquirers and never passed on to merchants.[109]

4.13 In response to our interim report, one of the schemes challenged our provisional finding that most IFs were passed on to the merchants. We are confident that pass-through from acquirers to merchants was significant and that, as explained below, this removed acquirer financial incentives to countervail the increases. The scheme's submission and our response are presented, respectively, in paragraphs 1.16 and 1.22 of Annex 1.

4.14 Near complete and rapid pass-through to merchants means that the outbound IF increases had very little direct financial effect on UK acquirers, limiting the acquirers' incentives to change their behaviour in response to such increases.[110]

4.15 As explained in more detail in Annex 1, changes in IFs apply equally to all the acquirers, so they did not provide an opportunity for one UK acquirer to undercut the others in terms of their offering to merchants.[111] Almost complete pass-through by acquirers to merchants indicates that merchants have little choice but to accept the increases. If acquirers thought that merchants had alternatives, they could be expected to have absorbed at least some of the IF increase, for fear of losing merchant customers to such an alternative.[112]

4.16 UK acquirers not only had little reason to try to change their behaviour in response to the fivefold outbound IF increases but also had no ability to do so. They had to continue to offer both Mastercard and Visa acceptance services to merchants since ceasing to provide those acquiring services would entail significant business losses.[113]

4.17 As we set out in more detail in Annex 1, acquirers told us they were and are very unlikely to leave either card scheme in response to the outbound IFs increases.[114] As already stated, not providing acquiring services to merchants would entail significant business losses for acquirers. Some acquirers and merchants summed this up as the 'must-take' status of the Mastercard and Visa cards to merchants.[115]

107 See paragraphs 1.8 to 1.10 in Annex 1.

108 See paragraphs 6.4 to 6.14 and 6.34 to 6.52 in Chapter 6.

109 PSR analysis of UK acquirer data for 2022. See paragraphs 6.6 to 6.12.

110 Changes in merchant behaviour could still affect acquirers by reducing transaction volumes, but (as we examine later in paragraphs 6.34 to 6.52) this potential change was also very constrained.

111 See paragraphs 1.18, 1.19 and 1.21 of Annex 1.

112 See paragraphs 1.11 to 1.15 in Annex 1.

113 See paragraphs 1.8 to 1.10 in Annex 1.

114 See paragraphs 1.8 to 1.11 in Annex 1.

115 See paragraphs 1.8 to 1.10, 1.18, 1.19 and 1.21 in Annex 1.

4.18 This is consistent with the fact that [✂].[116]

4.19 We conclude that UK acquirers' responses to the increase in outbound IFs did not and do not provide effective competitive constraints on outbound IFs increases; acquirers lack both the ability and the incentive to respond by, for example, finding alternatives to Mastercard and Visa's payment systems.

Potential constraints from merchant responses

4.20 Since, as described in more detail in Chapter 6, acquirers passed most of the outbound IF increases to merchants, our analysis of any competitive constraints faced by Mastercard and Visa then considered merchants and their potential responses.[117]

4.21 Sufficiently strong merchant responses could reduce volumes of transactions processed by Mastercard and Visa and would provide a competitive constraint on outbound IFs. We consider here how this might work in theory, and then whether in practice it does provide a competitive constraint.

4.22 When considering whether and how to respond to the outbound IF increases, merchants weigh the cost and any associated risks against the benefits in the form of savings they might achieve, including by avoiding the increased IFs.

4.23 In principle, a merchant might respond to higher UK-EEA outbound IFs for a card scheme by:

- declining to accept Mastercard and Visa cards for UK-EEA CNP transactions.
- reducing the volumes of transactions that incur outbound IFs.

4.24 If the response to the increases in outbound IFs is declining to accept cards (see paragraph 4.23, first bullet point), the competitive constraints are straightforward. Merchants declining Mastercard- and Visa-branded cards would have a clear financial impact. The schemes would take this into account when deciding whether and to what extent to raise the outbound IFs.

4.25 If, instead, the response is reducing transaction volumes (see paragraph 4.23, second bullet point), the competitive constraints exist if the following two conditions are satisfied:

- merchants reduce their exposure to the transactions associated with the IFs
- this reduction has the potential negatively to impact the schemes financially compared to likely market outcomes if there had been no outbound IF increases.

4.26 The following subsections consider the potential for UK merchants to:

- decline Mastercard and Visa cards in response to the outbound IF increases, significantly impacting the scheme revenues
- reduce the volumes of transactions that incur outbound IFs, financially impacting the schemes more than if they had not increased these fees.

116 See paragraph 1.7 and 1.13 in Annex 1.

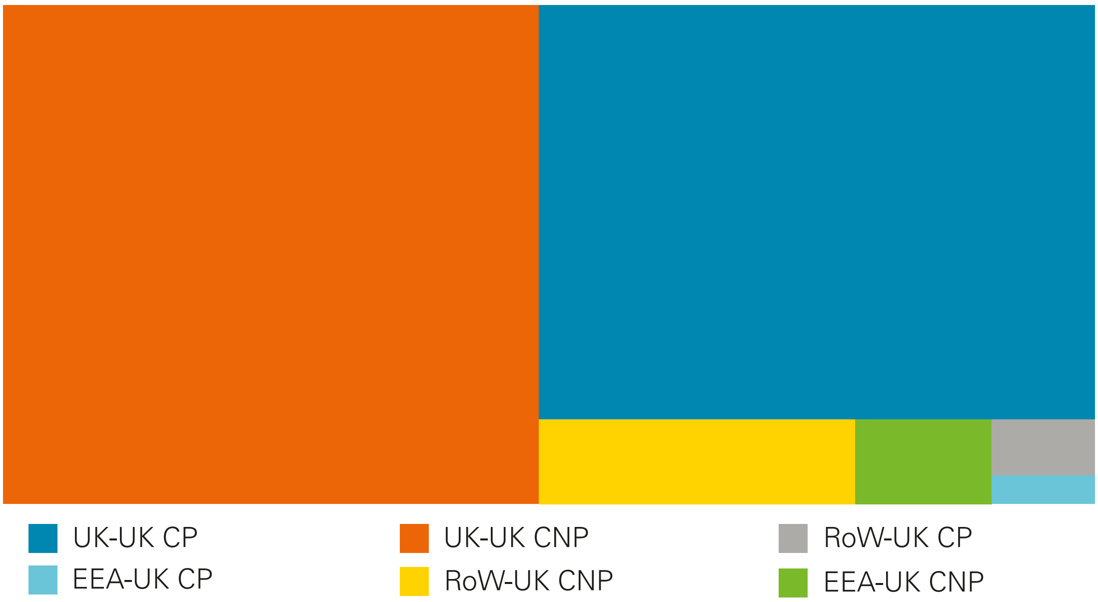
117 See paragraphs 6.34 to 6.50 in Chapter 6.

Declining card acceptance to avoid the increases

4.27 A merchant's decision to accept a particular card brand and product (such as Visa consumer debit) is based on the full 'basket' of transaction types that can be received via the card – domestic and cross-border, both CP and CNP. For most UK merchants, UK-EEA CNP transactions represent only a small proportion of transactions using a card brand and category. Of total card transactions at UK merchants, 3.6% are UK-EEA cross-border, 2.5% of the total are CNP UK-EEA cross-border; and around [✂] of the total are Mastercard and Visa CNP UK-EEA transactions – the transactions that generate the increased outbound IFs.[118]

4.28 Figure 6 shows, for Mastercard and Visa only, the shares of transaction values acquired in the UK, split between domestic transactions (UK-UK), transactions made with cards issued in the EEA (EEA-UK), and transactions made with cards issued in the rest of the world (RoW-UK). Additionally, transactions are divided into card-present (CP) and card-not-present (CNP). The graph reveals that CNP cross-border transactions with the EEA account for [✂] of total Mastercard and Visa transactions acquired in the UK. If we include CP transactions as well, this number increases to [✂].[119]

Figure 6: Shares of transaction values acquired in the UK in 2023, for Mastercard and Visa only, for UK domestic transactions (UK-UK), transactions made with cards issued in the EEA (EEA-UK), and transactions made with cards issued in the rest of the world (RoW-UK).



Source: PSR internal analysis of figures submitted by Mastercard and Visa (2023).

118 PSR internal analysis of data submitted by acquirers, Mastercard, Visa and American Express as part of the s81 notice (2023).

119 PSR internal analysis of data submitted by Mastercard and Visa (2023).

4.29 Mastercard's and Visa's scheme rules prevent UK merchants from accepting transactions with domestic IFs while refusing those from same-brand EEA-issued cards with the higher cross-border IFs. The Honour All Cards (HAC) rule states that merchants who accept the schemes' consumer debit or credit cards domestically cannot refuse to accept these cards in a cross-border context. In terms of issuer location, the HAC rule makes accepting a card brand an all-or-nothing decision, at least at a product level.[120]

4.30 In the UK, in 2023, 86% of all retail sales were card-based.[121] There is no national card scheme, and, in both 2022 and 2023, Mastercard and Visa accounted for around 99% of all transactions made with a card issued in the UK.[122] All merchants who responded to our review said they accept all Mastercard- and Visa-branded cards and have not considered declining any of them in the last five years.[123] Refusal of such cards would mean significant losses in sales, as customer would most likely buy instead from alternative merchants who continue to accept them.124 The fear of losing customers and their transactions means merchants typically accept cards even when these cost them more than alternative payment methods. There is no doubt that Mastercard and Visa are both currently 'must-take' payment methods for the vast majority of UK retailers.[125]

4.31 Given the above, and as explained in more detail in Annex 1[126], refusing to accept EEA-issued cards is likely to be inconceivable for any merchant with material domestic business. It would likely lead to a dramatic loss of domestic sales and of all the margins on these. Overall, these margins are likely to be far larger than the savings from avoiding outbound IF increases.[127]

4.32 For these reasons, it is highly unlikely that the typical UK merchant (with only [✂] of Mastercard and Visa CNP UK-EEA transactions out of all transactions[128]) would stop accepting either Mastercard- or Visa-branded cards in response to an increase in outbound IFs. This would be the case even if alternatives to these cards were readily available for UK-EEA cross-border transactions, which they are not (as we discuss later in this chapter when we talk about UK merchants potentially steering consumers towards alternative payment methods).

4.33 For some UK merchants (such as those operating in the travel industry), UK-EEA CNP transactions represent a much higher percentage of total transactions. So, a fivefold increase in outbound IFs will have a greater financial effect on them in terms of the overall IFs they pay (see also Chapter 6). If they changed their behaviour on card acceptance, that

120 See paragraphs 1.25 and 1.26 in Annex 1.

121 BRC, [Payments survey 2024](), pages 7 and 8. This statistic includes both in person (CP) and remote (CNP) transactions.

122 See UK Finance, *UK Payment Statistics 2023*, tab 8.1 and 8.2, and UK Finance, *UK Payment Statistics 2024*, tab 8.1 and 8.2. These are both in person (CP) and remote (CNP) transactions.

123 Stakeholder responses to PSR information requests dated 11 January 2023 and 18 July 2023. [✂].

124 This is because currently there are virtually no established alternatives to Visa and Mastercard in the UK. Moreover, even cardholders with multiple cards do not necessarily hold both Visa and Mastercard, and may use different cards (and the different accounts associated with them) for different purposes.

125 See also paragraphs 1.8 to 1.10 in Annex 1.

126 See paragraph 1.25, 1.26 and 1.31 in Annex 1.

127 See also paragraphs 1.29 to 1.30 in Annex 1.

128 See Figure 6.

could represent a constraint on Mastercard and Visa's ability to raise the outbound IFs. We observe, however, that:

a. As discussed in the next subsection (paragraphs 4.44 and 4.45), the small group of UK merchants with significant levels of UK-EEA CNP transactions have largely relocated to/set up operations in the EEA. Evidence from the schemes shows that the vast majority of such merchants did this following (and mainly, if not solely due to) the UK's withdrawal from the EU and before the announcement of the outbound IF increases.[129] Consequently those merchants have no reason to decline Mastercard and Visa cards (even assuming that was possible) in order to avoid or mitigate the impact of IF increases. It follows that, large merchants, those that typically relocated themselves and moved most of their EEA cross-border operations to the EU after the UK's withdrawal from it, do not act as a constraint on increases to outbound IFs.

b. Even those merchants with levels of Mastercard and Visa UK-EEA CNP transactions significantly above the UK average still tend to generate most of their business domestically. Given the ubiquity of Mastercard and Visa cards in the UK (see paragraph 4.30), they are unlikely to be able to decline these cards.

c. An individual merchant with very large volumes of UK-EEA trade and exceptionally strong bargaining power in relation to Mastercard and Visa might exercise some pressure over the card schemes to get a better deal. For example, in November 2021, Amazon told its customers it would stop accepting payments made with UK-issued Visa **credit** cards from 19 January 2022, blaming the 'high fees Visa charges for processing credit card transactions'.[130] However, on 17 January 2022, an '11th hour reprieve' was reported, with Amazon 'sending affected customers emails telling them they would be able to continue to use their Visa credit cards to pay for items, and for Amazon Prime'.[131] It was subsequently reported that 'Amazon had reached a global truce' with Visa.[132] Such bespoke deals appear to be exceptional, obtained by very few merchants with high bargaining (or countervailing) power. Such deals do not constrain outbound IFs as a whole. Even where merchants can exert such exceptional bargaining power, any discounts or benefits they achieve are for themselves only. Such deals do not generate benefits or any other positive spill-over for other merchants.

4.34 Responding to our interim report findings, Mastercard said that, if IFs are too high, merchants may choose not to accept Mastercard- and Visa-branded cards. The scheme stated that the fact that many PayPal transactions are not funded by international cards or are funded by international cards other than Visa and Mastercard indicates that merchants are provided with suitable alternatives to reduce the usage of cards.[133] We do not consider that to be the case. As explained in paragraphs 4.29 to 4.31 and in more detail in Annex 1, the HAC rule prevents merchants from refusing cards on the basis of an issuer's location, while the 'must-take' status of Mastercard and Visa cards makes it unrealistic for the vast majority of UK retailers to refuse them for all transactions.[134] The scheme's submissions

129 In the next subsection we also explain why merchant relocation did not have a negative financial impact on the schemes compared to a state of the world with no outbound IF increases and hence did not represent a competitive constraint on Mastercard and Visa.

130 The *Guardian*, Amazon to stop accepting UK-issued Visa credit cards (17 November 2021).

131 The *Guardian*, UK Amazon users can continue using Visa credit cards after dispute is settled (17 January 2022).

132 *Financial Times*, Amazon reaches 'global' truce with Visa on credit card fees (17 February 2022).

133 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂]

134 See paragraph 1.25, 1.26 and 1.31 in Annex 1.

and our responses on this are presented in Annex 1, respectively, in paragraphs 1.34 to 1.36 and in paragraphs 1.43 to 1.44.

4.35 Overall, given the near ubiquity of Mastercard and Visa in the UK, their 'must-take' status, and the HAC rules, the vast majority of merchants could not and cannot respond to the fivefold outbound IF increases by declining Mastercard- and Visa-branded cards. We know of no UK merchant who decided to decline to accept Mastercard or Visa as a result of the increase. Better deals that may be negotiated by a very small minority of extremely large merchants directly with the schemes do not protect the interests of the vast majority of merchants. Accordingly, changes in card acceptance did not and do not provide a credible and effective competitive constraint on outbound IFs.

Reducing volumes on which outbound IFs are levied

4.36 We also considered whether UK merchants, while continuing to accept these cards, were or may be able to reduce the volume of transactions subject to UK-EEA outbound IFs. We then considered whether such actions could financially affect the schemes (compared to a scenario where they did not increase their outbound IFs).

4.37 In principle, UK merchants have three ways to lower their exposure to the relevant transactions:

- cross-border acquiring
- merchant relocation
- steering EEA consumers towards alternative payment methods

Cross-border acquiring

4.38 In principle, an acquirer in one country could process transactions for a merchant located in a different country. To pay lower fees on cross-border transactions, in principle a UK merchant would be able to contract with an EEA-based acquirer to process its UK-EEA CNP transactions in the EEA rather than the UK. Such a transaction could be treated as a domestic or intra-regional EEA transaction. It would therefore fall under the EU IFR and incur an IF of 0.2% or 0.3% (for debit or credit, respectively) rather than 1.15% or 1.5% as a UK-EEA CNP transaction processed by a UK acquirer.

4.39 However, because the card scheme rules classify transactions according to the merchant's location, not the acquirer's or payment processor's, IFs are levied on the basis of the merchant location.[135] This is also explained in more detail in Annex 1.[136] The card schemes' rules also state that an acquirer cannot accept transactions from a merchant located outside the acquirer's country of domicile.[137,138]

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135 Mastercard sets its default IFs according to its rules (see rule 8.3) and webpage. Visa sets its IFs according to information contained on its website (see Frequently asked questions: What does it cost and how is this decided?).

136 See paragraphs 1.48, 1.49 and 1.54 in Annex 1.

137 *Mastercard rules* (4 June 2024), p. 39 (accessed 26/11/2024).

138 *Visa core rules and Visa product and service rules* (19 October 2024), page 101 (accessed 26/11/2024).

4.40 The scheme rules are also consistent with the definition of cross-border transaction in the EU IFR as one where either:

- the issuer and the acquirer are located in different Member States
- the issuer is located in a Member State different from the point of sale.[139,140]

4.41 There is consensus among stakeholders that cross-border acquiring is currently not possible, also because of scheme rules. Stakeholders' submissions and our response are presented in Annex 1.[141] We therefore conclude that cross-border acquiring did not and does not provide an effective competitive constraint on the outbound IF increases in question.

Merchant relocation

4.42 We considered whether UK merchants could avoid or mitigate the increases in outbound IFs by relocating part or all of the relevant transactions to an EEA country, where the lower intra-EEA IFs would apply.

4.43 Under the card scheme rules, which levy IFs according to the merchant location, merchants can relocate their transactions by establishing themselves in that other location and accepting payments there.[142] For example, a UK-located merchant selling online to consumers in France could establish a presence in the EEA and use an EEA-based acquirer to process these transactions. These transactions would constitute EEA domestic transactions and would be subject to the lower IFs capped under the EU IFR.

4.44 The evidence (see Annex 1) shows that whilst very large merchants established a presence in the EEA ('relocated') following the UK withdrawal from the EU, most UK merchants did not have this option.[143] This is not surprising, as relocation carries the financial and logistical burden of setting up a new legal entity responsible for the sales of

139 European Parliament and European Council, Regulation (EU) 2015/751 of the European Parliament and of the Council, Article 2, section 29.

140 It is also likely that an EEA acquirer would need to obtain FCA authorisation to offer services to UK merchants. Broadly, when a firm provides regulated payment services in the UK, as a regular occupation or business activity, and neither the firm nor their services fall within an exclusion or exemption, the firm must be authorised or registered by the FCA. It is a merchant acquirer's responsibility to consider whether their activities fall within the FCA's regulatory perimeter based on their specific circumstances, including where each part of their activity takes place. A firm that fails to do so risks committing a criminal offence under regulation 138 of the Payment Services Regulations 2017.

141 See paragraphs 1.48, 1.49, 1.51, 1.54 to 1.56 in Annex 1.

142 How Mastercard sets its default IFs is explained in its rules (see rule 8.3) and webpage. How Visa sets its default IFs is explained on its website (see 'Frequently asked questions, What does it cost and how is this decided ?').

143 See paragraphs 1.80 to 1.84 in Annex 1.

goods or services in that jurisdiction[144], requiring proof that it undertakes its business activities locally and complies with local tax and other regulations.[145]

4.45 For completeness, the evidence indicates that most if not all cases of relocation were not motivated by the outbound IF increases but by other factors (for example, the new customs regulations that have made it more difficult and time-consuming to ship goods between the UK and the EU), which meant that following the UK's withdrawal from the EU it made sense for merchants who had the opportunity to do so to move operations (and volumes) across the jurisdictions, so as to have both UK- and EEA-based operations.[146] Consistent with this, volumes for UK-EEA CNP cross-border transactions declined significantly after the withdrawal and before the outbound IF increases. Their levels have stabilised following those increases (Figure 4).

4.46 In addition, we note that UK merchant relocation to the EEA did not and does not imply a negative financial impact on the schemes compared to a scenario where Mastercard and Visa had not increased the outbound IFs (a no-increase scenario). Indeed, [✂]. The pre-assessment undertaken by [✂]. Internal documents from Mastercard show that [✂].[147] Internal documents from Visa show that, despite relocation, [✂].[148] Each of the schemes found it financially appropriate to raise the fees knowing that their most direct competitor could do so or had done so. This means that each scheme would have lost more financially from issuers migrating to its rival scheme in a scenario in which it had not matched the other scheme's IF increase than it might lose from merchant relocation due solely to the outbound IF increases and not to the UK's withdrawal from the EU.

4.47 The schemes and one issuer disagreed with our assessment of merchant relocation. In particular, one scheme submitted that merchants' ability and incentives to relocate are particularly strong for CNP transactions, as the 'branch' location may not need to provide customer service but solely process the transaction. We note, however, that Mastercard's and Visa's rules impose strict requirements for relocation, even in the case of e-commerce. Stakeholders' submissions and our response are presented in Annex 1, paragraphs 1.83 to 1.99.

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144 See paragraphs 1.83 and 1.84 in Annex 1.

145 *Mastercard rules* 5.5 states that the merchants' location for card-not-present transactions must meet the following criteria:

1. Merchant conducts business locally - By way of example and not limitation, a post office box address, the location at which a server is stored, the address of a warehouse having no business-related functions, the Uniform Resource Locator (URL) of a website, or address of the Merchant's law firm, vendor, or agent does not satisfy this requirement.
2. The Merchant holds permits to operate locally.
3. The Merchant complies with local tax laws and regulations.
4. The Merchant is subject to local consumer laws and courts.

Visa Merchant Data Standard Manual state that: a Merchant must use its principal place of business as the Merchant outlet location for card-absent transactions – that is the fixed location where the Merchant's executive officers direct, control, and coordinate the entity's strategy, operations, and activities).

146 See paragraphs 1.66, 1.72 and 1.75 in Annex 1.

147 See paragraph 1.69 in Annex 1. We note that the relevant internal document from Mastercard refers to the 'potential Mastercard revenue impact if UK merchants would fully localise their Cross-border volumes to a UK domestic entity', i.e., it refers to transactions from UK consumers at EEA merchants. However, we have no reason to believe that a similar conclusion would not also apply to transactions in the other direction, i.e., EEA consumers at UK merchants.

148 Visa, [✂].

4.48 We conclude that merchant relocation did not and does not provide an effective competitive constraint on the outbound IF increases in question.

4.49 For completeness, we agree that, as Visa noted, if relocation of UK merchants to the EEA were to regain momentum, the proportion of transactions impacted by the IF increases would fall.[149] If this were to happen, outbound IFs would increasingly fall only on small to medium enterprises (SMEs), which cannot use relocation to mitigate the impact of IF increases. The prospect of merchant relocation would not mitigate the impact suffered by SMEs (that is, it would not provide an effective competitive constraint) and actually would introduce (or exacerbate) a competitive gap between these and the larger merchants. There could then be a reduced volume of UK centred trade taking place, as a result of merchants trying to avoid the consequences of the schemes' increases in cross-border IFs. We note that this would be inconsistent with our regulatory principle of the desirability of sustainable growth in the UK economy in the medium or long term.[150]

Consumer steering towards alternative payment methods

4.50 Finally, UK merchants could steer EEA consumers towards alternative payment methods to lower their exposure to the relevant transactions. We have considered whether UK merchants could exert downward pressure on outbound IFs by encouraging EEA consumers to use alternative payment methods that are less costly to the merchant. For example, this could be done by:

- introducing card surcharges or offering discounts or bonuses for using an alternative payment method
- providing information on the fees facing a merchant and how they compare to alternative payment methods
- asking the consumer to choose an alternative payment method
- presenting website payment options in a way that nudges consumers to use alternative payment methods (for example, by making these methods more prominent).

4.51 The ability of a UK merchant to use any of these strategies depends on what alternative payment methods, if any, are available and acceptable to EEA consumers as well as to the merchant. To credibly exert downward pressure on outbound IFs, such alternatives must be available for remote purchases by EEA consumers and acceptable to UK merchants – which means that they will need to be freely available to consumers, understood and afford similar levels of service. It is important to note that it is the consumer who chooses the payment method from the options a merchant will accept. So, a merchant who wants a particular payment method to be used must successfully steer or nudge the consumer to choose it.

4.52 As explained in paragraph 4.22, when considering whether and how to respond to the increases, merchants will compare costs and benefits of potential action.

149 Visa, *Visa response to Treasury Select Committee on Cross-border Interchange*, page 5.

150 FSBRA, section 53(c)

4.53 For a UK merchant wanting to reduce its exposure to outbound IF increases, there are likely to be two key questions:

1. What alternative payment methods are available to an EEA consumer who wants to purchase goods and services from a UK merchant by remote payment?
2. What are the likely costs and risks of trying to steer potential consumers to use an alternative payment method and how do these compare to the savings that arise by using that alternative method, and specifically from avoiding the outbound IF increases?

4.54 Answers to the two questions above will ultimately determine merchants' ability to mitigate the impact of the increases in outbound IFs through consumer steering.

4.55 We note that, in addition to the marginal acceptance costs (per transaction), the costs of any alternative payment methods that the EEA consumers may be willing to use as an alternative include two further types of costs: 'adoption costs' and 'learning costs'. Adoption costs are those that the merchants incur to adopt a payment method and integrate it with their internal systems. Learning costs are incurred when adopting a payment method that is new to the merchant.

4.56 The risks include the chance that any steering attempt by the merchant will deter the consumer and result in them losing the transaction altogether.

<u>Available alternative payment options</u>

4.57 Stakeholders (see Annex 1) said that in addition to Mastercard and Visa, the following payment options are available to EEA consumers:[151]

- pass-through digital wallets such as Apple Pay and Google Pay[152]
- staged (or e-money) digital wallets such as PayPal, Revolut Pay and Skrill[153]
- 'buy now pay later' (BNPL) solutions ([✄])
- SEPA bank transfers
- payment solutions based on SEPA bank transfers – account-to-account (A2A) payment solutions, Open Banking (OB) payment solutions and any other payments funded via SEPA bank transfers[154]
- other international card schemes such as American Express and Diners Club

151 See paragraphs 1.110 to 1.127 and 1.135 to 1.145 in Annex 1.

152 With pass-through wallets, the customer initiates the transaction using the wallet as an interface, while the wallet forwards the payment information (stored as a token) to the merchant (or their acquirer). The wallet does not store any money and funding is required from a card or bank account. Google Pay and Apple Pay are examples of pass-through wallets.

153 E-money wallets can store money and are involved in the flow of funds. Generally, both the customer and merchant should hold an account at the respective wallet provider. The customer chooses to use a funding method or e-money stored on the wallet and the merchant receives the transaction value in its wallet. E-money wallets are also referred to as staged wallets as they separate the funding stage, in which the customer transfers funds into the wallet, from the payment stage, in which those funds are transferred to the merchant. PayPal is an example of e-money wallet.

154 Amazon Pay (funded by bank transfers, international), Bancomat Pay (Italy), Bizum (Spain), Blik (Poland), CurrencyFair (International), EPS (Austria), Giropay (Germany), iDeal (Netherlands), Multibanco (Portugal), PayByBank (Greece), PayPal (funded by bank transfers, international), Przelewy24 (Poland), Siirto (Finland), Sofort (International), Swish (Sweden), Trustly (International), Wise (International).

- domestic card schemes[155]

4.58 The next paragraphs explain the implications (including costs and risks) for merchants who wanted to respond to the outbound IFs by steering customers towards alternatives. However, it is worth clarifying the following points regarding potential alternatives to Mastercard and Visa for EEA consumer transactions at UK merchants (see Annex 1 for a more detailed overview of such payment methods).

4.59 **Apple Pay** and **Google Pay** currently simply provide an interface for card payments and, in the cross-border space, specifically for payments made using international cards such as Mastercard and Visa. So, they do not currently represent real alternatives to Mastercard and Visa.[156]

4.60 **PayPal Digital Wallet** reflects in its fees the full cost of Mastercard and Visa cards also when the wallets is funded by other means (see Chapter 5), including the UK-EEA CNP cross-border IFs.[157,158] As such, it did not and does not represent a real alternative.

4.61 **A BNPL provider** [✂] is [✂].[159,160]

4.62 **American Express** and **Diners Club** are typically more expensive than Mastercard- and Visa-branded cards, and have more limited penetration among EEA customers.[161] As such, they do not represent a valid alternative to avoid or mitigate the impact of outbound IF increases.

4.63 It follows that the only options that could in principle represent an alternative for UK merchants wanting to steer consumers away from Mastercard and Visa to avoid the increased outbound IFs are:[162]

- domestic card schemes operating in EEA countries
- payment solutions (often local) based on SEPA bank transfers (A2A/open banking payment solutions) that are less costly to the merchant

155 Bancomat (Italy), Bancotnact (Belgium), Carte Bancaires (France), KBC/CBC (Belgium), Dankort (Denmark).

156 See paragraphs 1.111 to 1.114, and 1.128 in Annex 1.

157 See paragraph 5.27 in Chapter 5.

158 See paragraphs 1.115, 1.128, 1.139, 1.143 and 1.179 in Annex 1.

159 See paragraph 5.26 in Chapter 5.

160 See paragraphs 1.116 to 1.117, 1.128, 1.143 and 1.179 in Annex 1.

161 For completeness we note that, despite being international card schemes, they are not particularly used by EEA consumers – particularly Diners Club. According to RBR data, there were around 16 million American Express cards and less than 2 million Diners Club cards in circulation in Europe (including non-EEA countries) in 2018. See RBR, Payment Cards Issuing and Acquiring Europe, International Card Schemes, Figure 2.2 and 3.2 (pp. 82 and 86).

162 Based on information gathered from acquirers and payment facilitators representing over 90% of the UK market, we found that currently the following payment method could be less costly to UK merchants (in terms of marginal acceptance costs) compared to Mastercard and Visa in the UK-EEA cross-border space: Bancontact (Belgium), Bancomatpay (Italy), Bizum (Spain), BLIK (Poland), ePay (Bulgaria), Giropay (Germany), iDeal (Netherlands), MyBank (Italy), Open Banking (multiple EEA countries), Paytrail (Finland), Przelewy24 (Poland), SEPA Direct Debit (multiple EEA countries), Swish (Sweden), SEPA (multiple EEA countries), Skrill (international) Sofort (multiple EEA countries), Trustly (multiple EEA countries), Vipps (Denmark, Finland and Norway).

- E-money or staged digital wallets such as Revolut Pay and Skrill[163]
- SEPA bank transfers (i.e., 'naked' SEPA bank transfers)[164]

Likely costs and risks

4.64 As stated above (paragraph 4.44) only very large merchants or merchants with significant EEA volumes were able to relocate to the EU following the UK withdrawal from the EU, while most UK merchants did not have this option. Thus, merchants affected by cross-border IF increases are smaller merchants and merchants with limited EEA volumes that did not relocate. In considering the potential costs they would incur in steering EEA consumers to use alternative payment methods (to avoid the outbound IF increase), we recognise that these merchants have a relatively low number of cross-border transactions from the EEA, potentially spread across a number of EEA countries.

4.65 In gauging the effectiveness and risks of steering consumers towards alternative payment methods, we have considered consumer's payment habits. This is because it is ultimately the consumers who make the payments and while some may have ready access and be willing to use some alternatives to Mastercard and Visa, many others will not even be aware or interested in using such alternatives.

4.66 As illustrated in more detail in Annex 1, a number of domestic card products (such as Cartes Bancaires in France) and domestic credit transfer-based payment methods (such as iDEAL in the Netherlands and Giropay in Germany) are popular among consumers in their respective national markets. They often cost less for merchants to accept than Mastercard and Visa, especially for UK-EEA CNP transactions. Some EEA consumers are already accustomed to paying with these alternatives in their home country and they may then be easily convinced to do so in a cross-border context.[165]

4.67 A number of acquirers and payment facilitators[166] in the UK offer acceptance solutions for these EEA alternatives.[167] UK merchants could therefore use such alternatives to accept payments by EEA customers.

4.68 However, whilst the marginal acceptance costs (per transaction) may be lower for these alternatives than for Mastercard and Visa cards (see paragraph 4.66), UK merchants would incur non-negligible costs (see paragraph 4.55) to integrate their payment systems with enough of these domestic alternatives to cover most of their EEA customers spread across different countries (see Annex 1 for more details).[168] This is likely to make adopting

163 Such solutions require the user to add funds to their account, if they have it with the selected platform, or to link a payment method (e.g., a card) before processing the transaction. Once the money is added, the platform processes the payment to the merchant. For Revolut Pay see Stripe – Revolut Pay Payments (link visited on 22/10/2024). For Skrill see Skrill – How to Pay (link visited on 22/10/2024).

164 Mastercard defines a 'naked' bank transfer as 'an interbank payment from a consumer account to a merchant account using the relevant inter-bank system, adding: "Naked" refers to the use of such transfers outside the context of a broader scheme or payment service that provides additional security or functionality to the sender or receiver of the payment'. [✁].

165 See paragraph 1.128 in Annex 1.

166 A payment facilitator is a payment service provider (PSP) that enables merchants to accept payments, including card payments, via a payment gateway. For card payments, the payment facilitator contracts with an acquirer who retains responsibility for allowing merchants to access the card payment systems. The acquirer is also liable for the merchant's and the payment facilitator's compliance with the rules set by the card scheme operator.

167 See paragraph 1.134 to 1.135 and 1.138 to 1.141 in Annex 1.

168 See paragraphs 1.150, 1.151, 1.153, 1.155 to 1.158, 1.160, 1.163, 1.165 and 1.166 in Annex 1.

such alternatives costlier than paying the increased outbound IFs for each transaction – at least in the short to medium term. Facing upfront costs, the typical UK merchants affected by IF increases (that is, those with limited cross-border transactions) are unlikely to have sufficient financial incentives to integrate these methods and steer customers. See Annex 1 for more details on this.[169]

4.69 UK acquirers and payment facilitators offer acceptance solutions for other non-domestic (that is, not purely national or regional) alternatives such as Revolut Pay and Skrill.[170] UK merchants could use these to accept payments by all EEA customers from various countries 'in one go'. These solutions are cheaper than Mastercard and Visa (especially cross-border) and would not require multiple integrations costs. However, at present these payment methods are not widely used by EEA consumers.[171] EEA consumers widely use naked SEPA bank transfers, especially in person-to-person (P2P) transfers. In e-commerce, however, their adoption remains limited.[172]

4.70 To steer customers towards these easier-to-integrate payment methods, merchants could use surcharges or behavioural steering (see paragraph 4.50). However, in view of the fact that these payment methods are not widely used by consumers, trying to convince them to pay with alternatives to their usual methods (such as Mastercard and Visa) could not only fail but also generate frictions at point of sale. As a result, it risks inducing cart abandonment and sale conversion losses.[173]

4.71 In deciding whether to steer consumers towards a specific payment method, merchants need to weigh lower IFs against the risk of lost revenue from reduced conversion rates. Any appreciable fall in conversion rates is likely to remove merchants' incentives to use such steering as a response to outbound IF increases. Indeed, merchants have told us they do not typically steer.[174] UK acquirers, representing over 90% of the UK market, also said that their merchants did not take any consumer steering action in response to the outbound IF increases.[175]

4.72 The BRC told us that certain types of low-level steering are commonplace, such as encouraging customers to use a store's own gift cards or loyalty points. But it also told us that merchants often see steering techniques as limited in their effect, because customers typically prefer to use one payment method (for example, for budgeting purposes or rewards), such that steering is ineffective.[176]

169 See paragraphs 1.158 and 1.162 in Annex 1.

170 See paragraphs 1.147. 1.149 to 1.151 in Annex 1.

171 For example, the Global Payments Report (2024) does not even mention Revolut Pay or Skrill among the emerging payment methods used by merchant and consumers in Europe.

172 See paragraphs 1.127, 1.112 and 1.128 in Annex 1.

173 Cart abandonment happens when a user adds items to their online shopping cart but leaves the website without completing the purchase due to, for example, frictions at point of sale. This means lost sales and wasted marketing efforts for the merchant.

174 See paragraphs 1.119, 1.120, 1.131 and 1.145 in Annex 1.

175 Stakeholder responses to PSR information requests dated 11 January 2023 [✁]

176 BRC response to PSR information request dated 11 January 2023 [✁].

4.73 In response to the interim report, one stakeholder told us that card schemes are constrained by dynamic competition and that as more alternative payment methods emerge, the competitive constraints on Mastercard and Visa will increase. In particular, the stakeholder mentioned the development of stablecoin and central bank digital currencies (CBDCs).[177] We note, however, that internal documents from neither Mastercard nor Visa considered the impact of these potential alternative payment methods when increasing the IFs, indicating that they were not regarded as a competitive constraint at the time of the IF increase. Moreover, the emergence of these alternatives as viable payment methods is subject to significant uncertainty (for example whether they will achieve sufficient scale to offer a constraint).[178] Stakeholders' responses to our interim report in relation to consumer steering, and our responses to them, are presented in Annex 1, paragraphs 1.134 to 1.184.

4.74 We therefore conclude that consumer steering did not and does not provide an effective competitive constraint on the outbound IF increases in question.

Upward pressure arising from commercial incentives on the issuing side

4.75 As stated in paragraph 4.8 and explained in the section above, Mastercard and Visa did not face any material downward pressure on the acquiring side when they decided to increase the outbound IFs. This meant that, after the previous caps were removed, there was nothing to stop them from increasing these fees to current levels.

4.76 Outbound IFs are not a direct source of revenue for the schemes. However, for reasons we discuss below, the schemes do have financial incentives to increase them.

4.77 Retail banks offer holders of their personal current accounts (PCAs) a range of services relevant to our market review. In particular, they issue payment cards usable in cross-border transactions and therefore act as issuing banks in those transactions. Issuing banks decide what card scheme their PCA holders will use (typically, either Mastercard or Visa for each type of card, for example, debit or credit).

4.78 Typically, at the point of sale, a cardholder will present and want to use only one of the two card brands (this is called single-homing). So, to be able to receive payments, merchants must accept both card brands (multi-homing).[179] Though Mastercard and Visa have no need to compete for acquirers and merchants, they do have a clear incentive to compete to become the card scheme for each issuing bank, so they can reach the bank's cardholders.

4.79 This competition between card schemes does not imply any pressure to reduce IFs and, on the contrary, puts upward pressure on these: by raising its IFs, a card scheme gives the issuing bank more incentive to adopt its cards. If most merchants accept both types of cards (multi-homing) and most consumers carry or use a single card (single-homing),

177 See paragraph 1.171 in Annex 1.

178 See the interim report on the PSR's Market review of card scheme and processing fees, paragraph 4.82.

179 The European Commission (2020) has estimated that, in 2018, the number of cards issued per capita across the EU Member States (including the UK) was 1.6. This indicates that the average EU consumer has either one Mastercard or one Visa card, but there might be instances in which they may have an additional card. While we cannot exclude multi-homing in the EU based on this figure (i.e., that there are consumers paying with both Mastercard and Visa), multi-homing is not common, and one specific consumer would generally be able to use only one between Mastercard or Visa cards to make payments.

Mastercard and Visa will compete by increasing IFs to attract issuers. This situation is a *competitive bottleneck*.[180]

4.80 When IFs are regulated, the schemes typically set the rates to the maximum levels allowed. Where IFs are unregulated or caps are relaxed or removed – as was the case for outbound IFs in the UK, the schemes have incentives (unconstrained by the acquiring side) to raise and keep the fees high to grow or protect the issuing business.[181]

4.81 In its response to our MIT note[182], Visa said there is nothing amiss about competitive constraints that differ across the two sides of the platform market. It noted that when cardholders on one side of a platform tend to single-home and merchants on the other side multi-home – seeking to accept a range of payment methods – platforms will normally recoup more revenue from the multi-home side where the demand on this side is less elastic. It noted that this competitive outcome is not exclusive to four-party card schemes and that this includes hotel booking websites, price comparison sites, online marketplaces, and general search engines. In particular, Visa said that asymmetric competitive constraints and pricing in two-sided markets cannot be assumed to lead to inefficient or harmful outcomes, which instead require an assessment of actual market behaviour and outcomes using appropriate tools.[183]

4.82 We agree that differences in competitive constraints between the two sides of a platform market are not uncommon. However, for the reasons set out above, we do not consider that competitive pressure on the issuing side would by itself constrain the schemes on their pricing decisions for the acquiring side.

4.83 As we discuss in the next chapter, we consider that the levels of IFs are unduly high, taking into consideration any possible benefits to merchants and their customers which could justify the price increase.

Conclusions

4.84 We assessed whether UK acquirers and merchants would respond to the outbound IF increases in a way that would have an impact on the schemes. We also assessed whether Mastercard and Visa had reasons to believe that this would be the case.

4.85 We found that UK acquirers had very little financial incentive to do so. On the contrary, the must-take status of Mastercard and Visa in the UK meant acquirers could only continue to provide acquiring services for both card schemes. So, UK acquirers' responses did not provide an effective competitive constraint on Mastercard and Visa when deciding to increase the outbound IFs.

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180 See S. Weiner and J. Wright, Interchange Fees in Various Countries: Developments and Determinants, *Review of Network Economics*, Vol.4, Issue 4 – December 2005, p. 314 and pp. 317 to 319.

181 In more general terms, platform markets with single-homing users on one side and multi-homing users on the other will tend to drive up fees on the latter side of the market. Rochet and Tirole (2011) find exactly this result in the context of payment schemes.

182 We shared with Visa and Mastercard a note that explained our initial view on the 2023 MIT 'like' assessment produced by [✂]. See paragraph 5.31to 5.57 in Chapter 3 and Annex 3 for more information on this.

183 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✂].

4.86 We also found that UK merchants do not have access to effective alternatives which would provide them with a means of exerting competitive pressure on the schemes. In particular:

- Declining to accept either Mastercard or Visa is not a viable commercial option for merchants as this would have a major adverse effect on their businesses, most importantly on their domestic business. The lost profits would greatly outweigh any savings achieved on outbound IF transactions successfully completed through alternative payment systems.
- Merchants cannot adopt cross-border acquiring practices to avoid outbound IF increases as these are prohibited by scheme rules, consistently with the criteria for merchant location set in the EU IFR.
- For many merchants, especially SMEs, relocation to avoid outbound IF increases is not commercially viable. Only few very large merchants and some with significant cross-border operations found it economically viable to relocate following the UK's withdrawal from the EU and can now complete transactions without having to pay higher cross-border IFs. Moreover, these relocations largely happened before the announcement of the IF increases. There is therefore no evidence that such relocation would represent any constraint on the schemes' behaviour. [✂]
- We found that the merchants typically affected by the outbound IF increases have limited ability to steer cross-border consumers to payment methods that would avoid the increases.[184] Other alternative methods that would enable the Mastercard and Visa IF fees to be avoided are not yet particularly popular among EEA consumers. Attempting to steer consumers towards such alternatives could create frictions detrimental to merchants' interests. Some EEA consumers use cheaper alternative payment options for the merchants, but these are currently country-specific. Adopting and integrating enough of these national alternatives to cover most EEA customers is unlikely to make economic sense to the typical UK merchant. Steering EEA consumers towards alternatives is therefore unappealing to most UK merchants, for whom the relevant UK-EEA cross-border transactions represent a very small share of all card transactions – as merchants have also confirmed.

4.87 We conclude that there is no realistic response that UK merchants could adopt which would provide an effective competitive constraint on the schemes' increase in IFs.

184 See paragraph 4.68.

5 Why the new outbound IFs are unduly high

The previous chapter explained why we concluded that there was lack of downward pressure on the acquiring side when the schemes decided to increase the UK-EEA consumer CNP interchange fees (outbound IFs). This meant that Mastercard and Visa did not have to consider the interests of service users – organisations that accept cards and their customers.

The schemes adopted significantly higher levels that had been set in another context and in different circumstances: for cards issued in non-EEA (and, at the time, non-UK) countries such as the USA or Japan and used with EEA (including, at the time, the UK) merchants.

Mastercard and Visa told us why, in their view, the new outbound IFs are more appropriate than previous ones, including for merchants and their customers. This chapter explains why we do not consider that to be the case, and as such we consider that the current levels are unduly high.

Introduction

5.1 The UK's withdrawal from the EU meant that the EU IFR caps on intra-EEA fees no longer applied to the UK-EEA CNP transactions. This, and the lack of effective constraints from acquirers and merchants gives the schemes the ability to set IFs at higher levels than if they took into account the impact on end-users (merchants and their customers).

5.2 For the reasons set out in this chapter (and, in more detail, in paragraphs 2.191 to 2.206 of Annex 2), we consider that the outbound IF increases only took into account the interest of issuers and, in turn, of the schemes themselves. [✂]:

a. Visa moved first by announcing in October 2021 a five-fold increase in its outbound Ifs level. While Visa's responses to us did not explicitly mention the need to remain competitive, [✂].[185]

b. Mastercard followed suit in April 2022 to match the uplift and internal documents show that it did so to [✂].[186]

5.3 As part of this review, we have then assessed whether the five-fold increases that occurred in October 2021 (Visa) and April 2022 (Mastercard) were justified, or whether these were unduly high compared to levels that would have emerged if competition on the acquiring side was an effective constraint on the schemes, that is, levels that would have prevailed had the schemes had to take into account the interests of merchants and their customers.

185 See paragraphs 2.201 to 2.202 in Annex 2.

186 See paragraphs 2.194 to 2.199 in Annex 2.

5.4 In assessing the appropriateness of the levels of IFs charged since 2021/22, we have looked at those factors the schemes and some issuers submitted that we should consider in light of their relevance to the interest of merchants and their customers. We therefore considered (see Annex 2 for more details):[187]

a. the **previous IF levels**, which applied before the UK's withdrawal from the EU (by virtue of Regulation 2015/251)[188] (including the schemes' and our views on the relevance of these IFs to determine appropriate UK-EEA outbound IFs)

b. the **new IF levels** introduced under the 2019 Commitments to determine outbound IF levels for RoW-EEA transactions[189] (including the schemes' and our views on the relevance of these IFs to determine appropriate EEA-UK outbound IFs)

c. the **costs of alternative payment methods** that may be used by EEA consumers at UK merchants online[190] (including a study provided by Visa on the cost to merchants of alternative payment methods)[191]

d. other factors which Mastercard, Visa and some issuers identified as relevant when setting outbound IF levels, in particular costs linked to **fraud levels and other issuer costs**[192] (including data provided by the schemes and by one European issuer).

5.5 Having considered these factors, we have not identified any justifications for the increases to the current levels made by the schemes after the UK's withdrawal from the EU. Whilst these factors do not provide a robust basis for identifying an appropriate level of outbound IFs, when looked at in the round, they show that an increase of the magnitude implemented in 2021/2022 was not commercially necessary (as the schemes appeared to suggest) and, moreover, was contrary to the interests of service users that are organisations that accept cards and their customers. We conclude that the current levels do not reflect a market working well – that is, a market where the schemes would face effective constraints from competition on the acquiring side.

Previous IF levels

5.6 Both Mastercard and Visa said that one reason for increasing the outbound IFs was related to methodological flaws in the European Commission's merchant indifference test (MIT) study – the EC's Cost of Cash and Cards study – that informed the previous levels.[193] The schemes considered that the flaws made the study results unsuitable as a basis for IF levels – especially for CNP transactions (not only between the EEA and the UK but also within the EEA).

187 This is based on stakeholder responses, but also on [✁].
188 See paragraphs 2.103, 2.110, 2.135, 2.138 and 2.155 to 2.158 in Annex 2.
189 See paragraphs 2.105, 2.110, 2.161 to 2.169, 2.172 and 2.175 to 2.179 in Annex 2.
190 See paragraphs 2.102 to 2.116, 2.129 and 2.130 in Annex 2.
191 See Annex 3.
192 See paragraphs 2.4 to 2.27, 2.35 to 2.67, 2.74 to 2.93 in Annex 2.
193 See paragraphs 2.109, 2.135 and 2.138 in Annex 2.

5.7 As illustrated in more detail in Annex 2, Mastercard and Visa made several criticisms of the EC's Cost of Cash and Cards study.[194] Regarding outbound IFs, they chiefly criticised the study's exclusive focus on cash as the only comparator to card payments. They told us that cash is not an appropriate comparator in an online and cross-border context. While cash is primarily a comparator for CP transactions, they said that in the CNP context there are more suitable alternatives to four-party card payments.[195]

Our assessment

5.8 In view of these submissions, we have considered whether there is a basis to conclude that the previous IF levels paid by EEA consumers purchasing from UK merchants were inadequate.

5.9 The EU Interchange Fees Regulation (EU IFR) set caps on IF levels for intra-EEA transactions, which included UK-EEA transactions when the UK was part of the EU, using a specific MIT methodology with cash as a comparator payment method. We understand that cash is primarily a comparator for CP transactions.

5.10 As set out in more detail in Annex 2, we recognise that cash may not be an ideal comparator for CNP transactions (such as those subject to outbound IFs). But the fact that it was used for the Commission MIT does not imply that the IF levels adopted were too low for CNP transactions or that the schemes needed to increase them after the UK's withdrawal from the EU and to the levels they did.

5.11 There is no evidence in Mastercard and Visa's internal contemporaneous documents (see Annex 2) that the decision to increase the outbound IFs was based on any specific MIT analysis and using a different, MIT suitable comparator for CNP transactions.[196]

5.12 Moreover, there is no evidence that the previous IF levels caused detriment or had any other negative impact on users of the card systems, including issuers and acquirers, nor that the increase led to countervailing benefits to service users that are organisations that accept cards and their customers. As explained in more detail in Annex 2, contemporaneous internal documents provided by Mastercard and Visa do not suggest that retaining the previous levels would have risked any such detriment, albeit [✂].[197]

5.13 As we discuss below, Mastercard and Visa said that previous IF levels were insufficient to cover fraud and other costs. But in so far as these costs are not shown to be heightened in the case of UK-EEA transactions, these criticisms hold not only for UK-EEA CNP transactions but also for all CNP transactions between EEA countries. The EU IFR still caps intra-EEA CNP transactions at 0.2%/0.3%. We have not seen any sign that fees are too low or that the current levels have negative implications for merchants and consumers (we discuss fraud levels in paragraphs 5.72 to 5.76).

New IFs based on the EC 2019 Commitments

5.14 As explained in more detail in Annex 2, both card schemes told us that, in their views, the MIT comparator (see below) used for the 2019 EEA-Rest of the World (RoW) levels was

194 See paragraphs 2.134 to 2.143, 2.148 to 2.150, and 2.155 to 2.158 in Annex 2.

195 See paragraphs 2.109, 2.114, 2.137, 2.139 to 2.143, 2.148 to 2.150, 2.156 and 2.158 in Annex 2.

196 See paragraphs 2.102 to 2.116 in Annex 2.

197 See paragraphs 2.13 Annex 2.

more suitable for CNP transactions (including UK-EEA) than cash, the comparator used for the previous IF levels. As set out above, cash is a relevant comparator for CP but not necessarily ideal for CNP transactions. The schemes submitted that, following the UK's withdrawal from the EU, they were therefore right to extend to UK-EEA transactions the fees that apply to EEA-RoW transactions.[198]

Our assessment

5.15 In view of the schemes' submissions, we considered the relevance of the levels set by the 2019 Commitments for assessing whether current levels for the UK-EEA corridor are appropriate. In the past, the European Commission considered an MIT methodology as 'a reasonable benchmark for assessing a MIF level that generates benefits to merchants and final consumers'.[199]

5.16 The comparator that the European Commission used in 2019 for assessing EEA-RoW CNP levels would not be *relevant* to setting the levels of similar UK-EEA CNP transactions. This is because the 2019 Commitments, which set the EEA-RoW CNP levels, were based on an MIT that used means of payments funded via *non-SEPA* bank transfers as comparators for CNP transactions (see paragraph 3.27).

5.17 In its decision, the European Commission explained how means of payments funded via non-SEPA bank transfers were used as relevant comparators. It said that 'for inter-regional CNP transactions cash could not be considered a valid alternative' and added:

other alternatives, that are means of payments funded via bank transfers (which are outside the domestic payment systems of the EEA Contracting Parties and the Single European Payment Area, SEPA; 'non SEPA bank transfers'), were identified as plausible payment alternatives for the purposes of the MIT.[200]

5.18 As explained in more detail in Annex 2, both card schemes indicated that by adopting the 2019 Commitments as the relevant benchmark for the UK-EEA CNP transactions, they implicitly considered the comparators used in 2019 as relevant to cross-border CNP transactions.[201]

5.19 However, we do not accept that an MIT like the one carried out by the European Commission in 2019 is appropriate for UK-EEA CNP transactions because, although the UK is no longer part of the EU, it remains part of SEPA (see paragraph 3.28). For reasons we explain below, it is important to take this difference into account.

5.20 Prior to the SEPA regulation[202], cross-border credit transfers and direct debits often took a long time to complete and incurred significant interbank fees. The SEPA regulation effectively created a new class of bank payments, completed in a guaranteed time with no deductions from the amounts transferred and much lower cross-border transaction fees. This improved the efficiency of financial transactions and allowed all merchants, including

198 See paragraphs 2.162, 2.169, 2.172 and 2.173 in Annex 2.

199 Sainsbury's [2020] UKSC 24 (relate to 3 proceedings: (1) Sainsbury's v Mastercard (CAT); (2) Asda, Argos & Morrisons (AAM) v Mastercard (Commercial Court); (3) Sainsbury's v Visa (Commercial Court), recital 134.

200 European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision (April 2019), recital 80. More details on the MIT applied by the European Commission in the context of the inter-regional CNP transactions can be found at footnote 45 and recitals 81 to 86.

201 See paragraphs 2.105 and 2.176 in Annex 2.

202 SEPA was introduced for credit transfers in 2008, followed by direct debits in 2009, and fully implemented by 2014 in the euro area and by 2016 in non-euro area SEPA countries.

UK merchants and SMEs, to receive payments from SEPA countries on a similar basis to their domestic payments. For UK merchants, accepting SEPA payments from EEA consumers (that is, consumers from SEPA countries) costs less than accepting payments from consumers from non-SEPA countries. Hence, any payment solutions that rely on SEPA bank transfers will inevitably reflect such differences in costs.[203]

5.21 It follows that, if one were to apply the logic and methodology underpinning the 2019 Commitments while using one or more suitable comparators – those available across SEPA countries – the resulting MIT IFs would more than likely be lower than the IFs that the schemes adopted.

5.22 We have not seen any contemporaneous specific assessment or consideration from Mastercard or Visa on the costs of these alternatives. However, information obtained during this market review, including from the card schemes, shows that an MIT for cross-border UK-EEA CNP payments could use comparators that would be cheaper (from an avoidable cost perspective, which is the basis for an MIT).[204] In other words, by adopting the 2019 Commitments levels, Mastercard and Visa have not simply considered the wrong comparators, they have specifically neglected comparators that are likely to have lower acceptance costs for merchants and therefore result in lower MIT-based levels for outbound IFs.[205]

Cost of alternative payment methods

5.23 In an attempt to explain their respective decisions to increase IFs to us, the schemes' submissions (after they took those decisions and before and after publication of our interim report) refer to the costs of alternative payment methods (see Annex 2). They told us that the outbound IF increases are justified because the cost to merchants of such alternatives is higher than the cost of accepting Mastercard and Visa payments.[206]

5.24 As set out in more detail in Annex 2, both schemes provided submissions on alternative payment methods – all typically more expensive to merchants – and said that the IF increases were justified if compared with what these other methods would cost merchants. Mastercard mentioned American Express and PayPal.[207] Visa mentioned American Express, PayPal Digital Wallet, China Union Pay, AliPay and bank transfers, and also Buy-Now-Pay-Later (BNPL) provided by **[✂]**.[208]

Our view on the alternative payment methods identified by the schemes

5.25 We considered in detail the scheme submissions set out in Annex 2. However, we found limited evidence in the schemes' internal documents that Mastercard and Visa had considered either alternative payments or merchant acceptance costs when they decided

203 For example, none of the six major UK banks charge their customers for initiating or receiving SEPA payments. Some of these banks, however, apply a charge for receiving non-SEPA payments (PSR analysis based on our online analysis of the top six banks in the UK. [✂]).

204 See paragraphs 5.23 to 5.57 in Chapter 5; see also paragraph 2.175 in Annex 2.

205 Examples are listed in footnote 154 in Chapter 4.

206 See paragraphs 2.102 to 2.116, 2.129 and 2.130 in Annex 2.

207 See paragraph 2.107 in Annex 2.

208 See paragraphs 2.114 and 2.129 in Annex 2.

to increase the outbound fees. As set out in more detail in Annex 2, contemporaneous internal documents provide [✂].[209] The evidence we have gathered indicates that when setting the IF increases, the schemes gave limited considerations to the costs of alternative payment methods for merchants.

5.26 Furthermore, in the scheme submissions put to us, the schemes mention some alternatives that we do not consider to be relevant comparators for assessing the appropriateness of the IFs levels (see paragraph 5.24):

- **China Union Pay** and **AliPay** are not European payment methods and cannot be used by EEA residents to make online cross-border payments within the UK.[210]
- **A BNPL provider's** [✂**]** propositions [✂].[211] Their acceptance costs are particularly high (as also reported by the schemes). It is particularly concerning that the schemes would consider these as alternatives for the purpose of setting IFs, since their inclusion introduces significant upward bias into calculations of IFs. In addition, we note that [✂] payments rely significantly on Mastercard and Visa cards, the cost of which is ultimately reflected in the overall acceptance cost for merchants. This makes them unsuitable as comparators for MIT purposes.[212]

5.27 We also consider that comparison with American Express and PayPal Digital Wallet would not be informative in assessing the appropriateness of IF levels. This is because the merchant acceptance costs of these payment methods are ultimately affected by the acceptance costs of Mastercard and Visa, including their IFs (see also paragraph 5.43).

- **American Express** competes with Mastercard and Visa on both the acquiring side and the issuing side to win cardholders and increase their card usage.[213] With lower card penetration than Mastercard or Visa, American Express needs to give higher rewards to attract cardholders. This competition for additional cardholders means that an increase in Mastercard and Visa IFs is likely to induce American Express to increase the level of transfer to cardholders (their implicit IF) at some point, to ensure that it can still provide them with an attractive proposition. Similarly, a decrease in Mastercard and Visa IFs is likely to induce American Express to decrease, at some

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209 See paragraphs 2.108, 2.112 to 2.113 and 2.115 to 2.116 in Annex 2.

210 In principle, EEA citizens can open AliPay digital wallet accounts. But they need to link a Chinese bank card to their account to access all features and to be able to top up their balance. See Wise, *How to register with Alipay as a foreigner in China* (15 December 2023). In practice it is very complicated for an EEA resident to open a Chinese bank account, as they would need a valid visa or work/student permit, proof of address and a Chinese phone number. See, for example, Bank of China's *Current All-in-One Account.* China Union Pay/Union Pay (CUP/UP) is the primary network for Chinese banks. Using these payment services for an EEA resident would require opening a Chinese bank account with all the difficulties just described.

211 See paragraph 1.117 in Annex 1.

212 Data submitted by [✂] to the PSR shows that more than half of UK domestic transactions in the UK are made using cards.

213 American Express pays its cardholders rewards, including on a per-transaction basis – a transfer from merchants like the transfer of money from acquirers (and ultimately merchants) to issuers (and cardholders through benefits and rewards) that is implied by an IF.

point, the merchant service fee (which includes their implicit IF) to ensure that they can still provide an attractive proposition to merchants.[214]

- **PayPal Digital Wallet** relies heavily on Mastercard and Visa's rails both in the UK and in the EEA. Therefore, for UK-EEA CNP transactions, the cost of its services to merchants incorporates the schemes' IFs (and also their scheme and processing fees). Accordingly, the price of PayPal is inevitably higher than and often correlated with the price of Mastercard and Visa.[215,216,217] PayPal told us that [✂].[218] PayPal told us that [✂].[219] It has been widely reported that PayPal has entered into agreements with Mastercard and Visa (both in the US and elsewhere, including Europe). In July 2016, PayPal signed US strategic partnerships with Visa. PayPal agreed to present Visa cards as a clear and equal payment option, and not to encourage Visa cardholders to link to a bank account. The agreement with Visa also included certain economic incentives and greater long-term Visa fee certainty. [220] In July 2017, the partnership between PayPal and Visa was extended to Europe. [221] In September 2016, a US agreement was signed between PayPal and Mastercard. [222] In October 2017, the agreement with Mastercard was similarly extended to Europe. [223,224] For these reasons, PayPal payment services do not currently represent a suitable alternative for benchmarking the card schemes' pricing.

5.28 In view of the above, we do not consider that the higher costs to merchants associated with these alternative payment methods provide a justification for the current levels of cross-border IFs.

5.29 Finally, we agree with the schemes that (SEPA) bank transfers represent an available alternative for UK-EEA CNP transactions (see Annex 2 for more detail).[225]

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214 For example, a study in Australia (pages 6 to 9) suggested a degree of correlation between the schemes' price changes and those of American Express. The study argues that though American Express is free from the regulatory constraints applied to four-party schemes, it has experienced significant indirect effects from the introduction of caps on Mastercard and Visa. American Express's average merchant service fee has fallen more than Visa's and Mastercard's since the first regulation on IFs in Australia. Another, very recent example is from New, where caps on debit cards introduced in 2022 led to a significant reduction of the IFs and the MSCs related to Mastercard and Visa cards. A New Zealand Commerce Commission document (Retail Payment System Consultation Paper, paragraph 4.73) notes that when caps were introduced, 'American Express reduced its merchant service fees upon the initial pricing standard coming into force in 2022.' They added: 'We would expect it [American Express] to further reduce its fees in response to any further regulation.'

215 Evidence of this is the fact that, when Mastercard and Visa increased their outbound IFs, PayPal decided to increase the fees for UK-EEA cross-border payments from 0.5% to 1.29%. At the time, PayPal stated that this was due to the fact that it was incurring extra costs, such as the rise in Mastercard and Visa IFs between the UK and the EEA (BBC News, *PayPal raises fees between UK and Europe* (9 September 2021).

216 See PayPal Merchant fees (visited on 19/08/2024).

217 See also stakeholder letter to the PSR dated 4 August 2023. [✂].

218 PayPal's response PSR information request dated 2 October 2023 [✂].

219 PayPal's response PSR information request dated 2 October 2023 [✂].

220 See: PayPal and Visa enter new partnership | Visa (visited on 19/08/2024).

221 See Visa and PayPal Extend Partnership to Europe | Business Wire (visited on 19/08/2024).

222 See PayPal and MasterCard End Fight With Agreement on Fees and Data - Bloomberg (visited on 19/08/2024).

223 See PayPal-Mastercard Deal Goes Global (businessinsider.com) (visited on 19/08/2024).

224 See also MR22/1.9: Market review of card scheme and processing fees interim report, Annex 1 paragraph 1.133.

225 See paragraph 2.114 in Annex 2 and Visa response to PSR questions and Visa dated 12 January 2022. [✂].

The cost of alternatives – the 2023 Report

5.30 Shortly prior to the publication of our interim report, Visa asked us to consider a study titled 'Applying the Merchant Indifference Test to Visa's EEA to UK CNP transactions (the [✁] 2023 MIT IF assessment)'. This study was commissioned by Visa from an economic consultancy ([✁]). The study assesses Visa's EEA>UK CNP MIFs *[UK-EEA consumer CNP outbound IFs]* against the MIT – 'a benchmark that has long been used by the European Commission for assessing the appropriateness of multilateral IF levels, including to underpin the interchange caps in the IFR and in the 2019 European Commission Commitments Decision'.[226]

5.31 While the schemes have told us that an MIT assessment (by reference to alternative payment methods) was one way to assess the appropriateness of IFs levels, as noted above, the evidence we gathered indicates that the schemes gave limited consideration to alternative payment methods and did not perform any specific analysis (MIT or other) to determine appropriate outbound IFs.

5.32 We note that previous regulatory interventions by the European Commission (including to set the levels of IFs for EEA-RoW transactions) were based on an MIT methodology. However, it is important to note that this methodology, based on academic publications and further developed by the European Commission, was not endorsed as a test meeting the requirement of the relevant legislation (in that case article 101(3) TFEU) the European Commission was applying. Rather it was used as a 'pragmatic means employed to compromise outstanding investigations in return for commitments'.[227]

5.33 The MIT approach is based on comparators (that is, alternative payment methods) with pricing independent of that of Mastercard and Visa. The methodology used by the European Commission in 2015, however, was designed in a different context – the card present space – where cash was the natural comparator. In 2019, the European Commission adjusted the methodology for CNP transactions made using cards issued outside the EEA and SEPA. There is no existing MIT-based methodology directly applicable to the case of UK-EEA CNP transactions. Developing it requires identifying one or more proper comparators in a cross-border CNP space.

5.34 We agree that an MIT can be a useful tool for assessing the appropriateness of the levels of IFs. However, we consider that this would only be one tool for assessing the appropriateness of a price cap, to be considered alongside other relevant factors, taking into account the theoretical limitations and empirical challenges of a model like the MIT (including, as noted above and further detailed below, the difficulty in identifying appropriate comparators).

5.35 However, prior to the publication of our interim report, Visa asked us to consider an ad hoc study, *Applying the Merchant Indifference Test to Visa's EEA to UK CNP transactions*, which it commissioned from [✁] (the 2023 Report).[228]

5.36 As explained in more detail in Annex 3, the 2023 Report assesses Visa's UK-EEA consumer CNP outbound IFs against what it considers to be 'a benchmark that has long

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226 [✁].

227 See Sainsbury's [2020] UKSC 24 (relate to 3 proceedings: (1) Sainsbury's v Mastercard (CAT); (2) Asda, Argos & Morrisons (AAM) v Mastercard (Commercial Court); (3) Sainsbury's v Visa (Commercial Court), recital 134.

228 See further details in paragraphs 3.1 to 3.9 in Annex 3.

been used by the European Commission' for 'assessing the appropriateness of MIF levels'. This includes the appropriateness of the values used to underpin the interchange caps in the IFR and in the 2019 Commitments Decision.[229,230]

5.37 As a result of that assessment, the 2023 Visa-commissioned report concluded that the MIT-compliant outbound IFs are significantly higher than the current outbound IF levels. The report stated that this 'reflects the fact that the cost of the vast majority of these alternatives is significantly higher than the total cost for UK merchants to accept a Visa card'.[231, 232]

Our assessment of the 2023 Report

5.38 In 2023 we issued an Invitation to Tender (ITT) for an organisation to identify how we could conduct an MIT should we decide to do one. We shared our ITT with Visa on 24 May 2023. Visa responded that, [✂].[233] [✂].

5.39 In what follows we explain what we consider to be flaws in this approach and why we consider it does not constitute a proper MIT for the setting of outbound IFs. In summary:

- it is based on an inappropriate selection of comparators, which overestimates merchant acceptance costs.
- It uses unrealistic or unadjusted list data (public cost data), and
- It uses unrealistic weights.

5.40 All of these flaws led to the overestimation of merchant acceptance costs.

Inappropriate selection of comparators

5.41 The comparators identified in the 2023 Report were BNPL (such as [✂]), three-party schemes (American Express), digital wallets (including PayPal Digital Wallets) and, to a more limited extent, A2A payment solutions (that is, means of payments funded via SEPA bank transfers).

5.42 For the assessment, the 2023 Report included [✂] BNPL among the comparators, although [✂].[234] Given that [✂]'s acceptance costs are particularly high, this significantly overestimates the cost resulting from the MIT. The results are further influenced by the fact that the report also attributes the largest weights to [✂] in the construction of the average (see Table 17 and Table 18 in Annex 3).

5.43 A comparator for an MIT must not have IFs attached to its use, otherwise circularity problems arise.[235] For a three-party scheme like American Express, there is no explicit IF, since the

229 [✂].

230 See further details in paragraphs 3.1 to 3.9 in Annex 3.

231 [✂]

232 See further details in paragraphs 3.1 to 3.9 in Annex 3.

233 Visa, [✂]

234 See also paragraph 1.117 in Annex 1.

235 An important feature of any comparator for the purposes of the MIT is that it should not contain an IF element. This avoids spurious effects related to the fact that the current cost to merchants of potential comparators may be impacted by the IF levels of Visa (and Mastercard) cards. IF levels based on the cost of such alternatives would inevitably be ever increasing: higher IFs would increase the cost of those alternative, which would in turn

issuer is the same as the scheme operator. However, it is possible to impute an implied (or shadow) IF by considering a fictitious competitive acquiring industry within the system.[236] Like an explicit IF, an implicit IF is ultimately paid by merchants and used to incentivise the other side of the network to adopt and use American Express cards. In practice, for the same reasons that Visa and Mastercard are not suitable APMs for each other, any payment method that includes a transfer of money from payees to payers (including an implicit IF) is unlikely to be suitable as an MIT comparator. It will be especially unsuitable if there are reasons to believe that its pricing behaviour is not sufficiently independent of the payment method for which the MIT-IF needs to be calculated – that is, in this case, Mastercard and Visa.

5.44 This is consistent with approaches used previously:

- In 2015, the European Commission said: 'Cash has no MIF attached to its use – an important criterion when selecting a comparator for cards in the context of the MIT, to avoid endogeneity problems.'[237]
- Following its investigations into Mastercard's and Visa's inter-regional IFs, in 2019 the European Commission identified (non-SEPA) bank transfers as plausible payment alternatives for the purposes of the MIT.[238]

5.45 The European Commission did not consider American Express for the purposes of the MIT calculations in 2015 or in 2019, although it was an available alternative for domestic CP transactions (2015) and RoW-EEA CNP transactions (2019) and although Mastercard and Visa said it should be considered in the MIT assessment.[239]

5.46 The 2023 Report included American Express and PayPal Digital Wallet among the comparators despite the fact that their pricing is likely to be endogenous to the pricing of Mastercard and Visa cards (see paragraph 5.27).

Use of unrealistic/unadjusted list data (public cost data)

5.47 The MIT assessment depends on a comparison between the merchant acceptance costs for cards and costs for the alternative payment methods. It is crucial that the cost information used reflects the actual merchant-specific acceptance costs across payment methods.

5.48 The 2023 Report was based on publicly available cost information from the websites of relevant providers (for example, PayPal and Amazon Pay) and Adyen, a payments facilitator and acquirer.[240] This information does not reflect what each merchant pays for accepting

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determine further IFs. This is also explained at paragraphs 77 and 80 of the Visa 2019 Commitments decision and at paragraph 75 of the European Commission's 2017 Cost of Cash and Cards study.

236 Because American Express can delegate its acquiring services to a competitive industry and achieve exactly the same integrated outcome by setting an interchange fee, this shadow IF is equal to the difference between American Express's merchant fee and its acquiring cost. See Tirole, *Payment card regulation and the use of Economic Analysis in Antitrust*, page 140. American Express's implicit IF can therefore be calculated in practice by comparing the total fees a merchant pays when accepting American Express cards to the total fees it pays when accepting Visa or Mastercard (excluding any Mastercard/Visa UK-EEA cross-border MIF).

237 European Commission, 'Survey on merchants' costs of processing cash and card payments, Final results', (March 2025), paragraph 75.

238 European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision and 2019 Commitments, recitals 77 and 80. A similar approach was followed as regards Mastercard's commitments for inter-regional MIFs – see CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision and 2019 Commitments.

239 [✂].

240 [✂].

transactions using these alternatives – the acceptance costs – as many are likely to be able to negotiate lower fees than the websites list. Examples will show these differences in costs:

- Fees published on Adyen's website do not always represent the acceptance costs paid by all merchants, or the 'average' merchant. In certain cases, it applies tiering so that costs per transaction vary depending on transaction volumes. In other cases, merchants might be able to negotiate the rates. For these reasons, published rates are likely to be inflated.[241]
- A recent survey of 700 European merchants from Boston Consulting Group also shows that for merchants, 'direct costs [fees] are heavily influenced by size, due to volume-based discounts. Interviewees revealed discounts of up to 70%, indicating that the cost to serve those clients is generally correlated with their payment volume.'[242]
- Our card-acquiring market review found that even merchants that are not large often secure better price or non-price terms if they choose to negotiate with acquirers.[243]

Unrealistic weights

5.49 Finally, the 2023 Report was based on weighing of different comparators. As weights, it used market shares that represent the relative usage of the various payment methods in domestic markets, which have nothing to do with our corridor of interest. For example, the high weights that the study attributed to BNPL ([✂] for debit and [✂] for credit, see Table 17 and Table 18 in Annex 3) are based on usage in domestic markets and so are not relevant. As mentioned before, [✂].[244]

What we can learn from the 2023 Report

5.50 These significant flaws make the 2023 Report unreliable for its intended purposes. It cannot be meaningfully used to derive the appropriate outbound IF levels or to justify the increase in IF levels.

5.51 However, we consider that the type of analysis developed in the 2023 Report, with some simple amendments to remove payment methods that should not be used in such an analysis, can provide useful evidence in assessing the appropriateness of the current levels of IFs. Indeed, even the analysis commissioned by Visa (with the abovementioned amendments) indicates that the current levels are likely to be materially higher than levels that would be calculated under an MIT methodology with appropriate assumptions and data.

5.52 To reach this view, we have applied the 2023 Report's methodology and considered comparators available for cross-border payments that are not themselves influenced by Mastercard's and Visa's IFs (that is, they are not endogenous). We have also analysed various scenarios to test the sensitivity of the results when changing the set of comparators and using different calculation methods. For further details see Annex 3.[245]

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241 Stakeholder response to PSR Information Request dated 7 May 2024 [✂].

242 Boston Consulting Group, The Hidden Cost of Cash and the True Cost of Electronic Payments in Europe and the UK, White Paper (2022), page 6.

243 CAMR report paragraphs 6.50 to 6.52.

244 See paragraph 1.117 in Annex 1.

245 See paragraphs 3.19 to 3.22 in Annex 3.

5.53 As a baseline, we have only considered comparators that can be used in the cross-border space (not BNPL [✁]), with pricing sufficiently independent from Mastercard and Visa's IFs (not American Express and PayPal Digital Wallet). In practice, this means that we have considered only A2A payment solutions – that is, means of payments funded via SEPA bank transfers – as relevant comparators.[246] We have not made any other changes to the methodology put forward by Visa. In particular, we have used the same published fees that, as discussed in paragraph 5.48, are likely to overstate actual cost to merchants (which in turns means that the results of this analysis may be higher than those which would be calculated using actual costs). For illustrative purposes, we have used weights obtained from the 2023 Report. The results from our analysis show significant differences from the figures in the 2023 Report. Our first set of calculations ('baseline' calculations based on the A2A comparators considered by [✁], using their cost information and weights) show values of 0.86% and 0.59% for debit and credit cards respectively. These are significantly lower than the values of the 2023 Report (2.84% and 2.58%, respectively). As the results are very much subject to the assumptions and methods used, we have provided a number of alternative scenarios, giving a full range of what we consider potentially relevant comparators, to test the sensitivity of the results. These are:

- **Scenario 1**: Of the A2A solutions indicated as having non-zero per-transaction cost, we included only the least costly (Trustly). From the cost information in the 2023 Report, we obtain MIFs of 0.30% for debit cards and -0.15% (negative) for credit cards.
- **Scenario 2**: At the other end of the spectrum, we considered only the most expensive A2A solution (PayPal APM). This is the most popular A2A solution presented in the 2023 Report. From the cost information in the report, we obtain MIFs of 1.13% for debit cards and for 0.82% credit cards.
- **Scenario 3**: We also considered a simple average of (a) the most expensive A2A solution (PayPal APM) and (b) the least costly (Trustly). From this, we obtain MIFs of 0.72% for debit cards and 0.34% for credit cards.

5.54 We show the results of our calculations in Table 3, together with the values obtained in the 2023 Report, and the current and previous IFs values. The limitations of this methodology and data, noted above, make this analysis and the results we reached insufficiently robust for setting caps on outbound IFs. However, the analysis based exclusively on the 2023 Report's data (and to a large extent on its methodology) provides support to the view that the current levels of IFs are unduly high:

- Both the 2023 Report rates and the current rates are higher than the range of values we obtained as part this scenario analysis.
- As noted above, these results are based on published data and as such are higher than the results that would be obtained using the same methodology applied to data relating to the actual costs sustained by merchants using these alternative payment methods.

246 For the purpose of analysis, we have considered payment solutions (and their relevant acceptance costs) included in the 2023 Report, even if we have reason to believe that more solutions are available (for MIT purposes) and that acceptance costs to merchants are lower than those reported in the same MIT IF assessment.

5.55 These results are not surprising, considering that A2A payment methods are significantly cheaper for European merchants than four-party card schemes, as illustrated by the merchant survey from Boston Consulting Group.[247]

Table 3: Summary of IFs (different sources and calculations)

Case	Debit	Credit
Baseline	0.86%	0.59%
Scenario 1	0.30%	-0.15%
Scenario 2	1.13%	0.82%
Scenario 3	0.72%	0.34%
2023 Report	2.84%	2.58%
IFR IFs	0.2%	0.3%
2021 IFs	1.15%	1.5%

Note: Baseline uses a weighted average of A2A payment solutions. Scenario 1 includes the least costly A2A solution (among those indicated having non-zero per-transaction cost). Scenario 2 considers the most expensive A2A solution. Scenario 3 uses a simple average of the most expensive and the least costly A2A solution.

Source: Elaboration and [✂]. [✂].

5.56 We shared with Visa and Mastercard a note that explained our initial view on the 2023 MIT 'like' assessment produced by [✂]. Mastercard's and Visa's replies and our assessment of these are reported in Annex 3.[248]

5.57 In conclusion, we found that an analysis of alternative payment methods, based on the data and to a large extent the methodology put forward to us by Visa in the 2023 Report (a methodology similar to that used in the past, albeit in different context, by the European Commission to assess the suitability of IFs) provides further evidence that the current levels of IFs are unduly high.

Differences in fraud levels and other costs

5.58 The schemes have also submitted that the increases in outbound IFs paid to issuers were appropriate in order to reflect differentials in the costs associated with fraud and other costs incurred by issuers in relation to UK-EEA CNP transactions, on the basis that ensuring that issuers recoup such costs would also be in the interest of service users that are organisations that accept cards and their customers. The assumption behind such a position is that card payments (included UK-EEA CNP payments) represent a product that

247 BCG, White Paper, *The Hidden Cost of Cash and the True Cost of Electronic Payments in Europe and the UK*, (2022), page 6.

248 See paragraphs 3.19 to 3.36 in Annex 3.

issuers offer, which should provide them with revenues enabling them to make a profit or, at a minimum, to recover all of their costs.

5.59 It is not clear, however, why that should be the case, considering that payment services are a service that issuers offer to attract their customers to use various financial products. Issuers generate revenues and profits in various manners, including via the forgone interest on positive balances on personal current accounts (PCAs) and via fees and interest on related products such as mortgages, loans, credit via credit cards, wealth management and insurance products. In practice, issuers offer a bundle of products and services, which may (seen individually) be profitable or loss making, with the former cross-subsidising the latter. Issuers have a choice in how payment services costs are recovered across their full set of products and services and it is not necessarily the case that issuers recover all of their costs through payments (including card payments).

5.60 Submissions made in the course of this investigation have not provided a clear articulation as to why the level of IFs should be set by reference to issuers' payment costs, and why issuers should recover their payment costs entirely through IFs. In fact, as noted above, the European Commission has based IFs with reference to the costs to merchants (and not to the issuers) of other payment methods.

5.61 For these reasons, we have not found that issuers' payment costs should be recovered entirely through IFs. However, in the absence of a clear methodology for assessing the levels of IFs, and in view of the submissions put to us by schemes and issuers, we have considered issuers' costs related to IFs and whether the level of such costs could provide a justification for raising cross-border IFs to the current levels.

Fraud levels

5.62 Like any other payment, a card payment carries a level of risk of fraudulent activity. Banks and financial institutions implement measures to protect cardholders, but sophisticated fraudsters and the evolution of fraudulent techniques mean the risk cannot be eradicated. Issuing banks may incur costs when dealing with fraud disputes and payment defaults – including operational costs, fees and financial losses.

5.63 As illustrated in more detail in Annex 2, both Mastercard and Visa said fraud levels and related issuer costs were among their reasons for increasing UK-EEA CNP IFs.

- Mastercard said cross-border CNP transactions have greater levels of fraud, and related costs, for issuers.[249] It said previous IF levels were always too low, especially for CNP cross-border transactions (whether UK-EEA or intra-EEA).[250] So Mastercard submitted that its increased outbound IFs were justified because they better reflected the higher transaction costs for issuers arising from fraud disputes and payment defaults.[251]
- Visa said that cross-border e-commerce payments present a higher risk of fraud and may require issuers to invest further in risk and fraud detection systems.[252] IFs help to

249 See paragraphs 2.4, 2.28, 2.24 and 2.42 in Annex 2.

250 See paragraphs 2.5 and 2.37 in Annex 2.

251 See paragraphs 2.5 and 2.35 in Annex 2.

252 See paragraph 2.13 in Annex 2.

support issuers with costs and risk associated with card issuing, including fraud, it said.[253] Visa added that IFs are [✂].[254] Visa said it considered that [✂].[255]

5.64 We sought, but did not receive much, information from EEA issuers on costs (see below). We used our evidence-gathering powers to collect information from UK issuers (for more details see Annex 2). Some of them said that fraud rates for CNP cross-border transactions are higher than CP domestic transactions, and that this has an impact on the costs of transactions.[256] As we have no reason to believe that costs for EEA issuers for UK-EEA transactions would differ significantly from UK issuers with respect to EEA-UK transactions, we considered this information as part of our assessment. We are continuing to give issuers the opportunity to provide information in our remedies consultation.[257]

5.65 The European Banking Federation, representing EEA issuers, said there is higher risk of fraud from international transactions, but did not provide further details on risk and fraud levels and related cost to issuers.[258]

5.66 Issuers were also unable to provide any evidence showing that increased IFs are specifically used to re-invest in fraud prevention.[259]

5.67 Acquirers and merchants, however, said that they have not seen visible changes in fraud prevention for UK-EEA CNP transactions following the increases in UK-EEA CNP IFs. Some stated that fraud is already addressed via other funded mechanisms.[260] In their view, fraud levels do not and did not justify the increases (for more details see Annex 2).[261]

5.68 While we have seen nothing to indicate that IFs were introduced to pay in part or in full for the cost of fraud prevention, in the following section we have considered whether the increase in IFs levels could be justified when considering fraud differentials for UK-EEA CNP transactions compared to intra-EEA transactions and EEA-RoW transactions.

Our assessment

5.69 As set out in more detail in Annex 2, we have not seen any contemporaneous evidence that [✂].[262] We asked Mastercard and Visa for fraud-specific information that they had considered when deciding to increase the fees; they did not produce any.

5.70 Nevertheless, as set out above in paragraph 5, we have considered how issuers' costs relating to fraud prevention related to IFs, and whether differentials in fraud levels, in investments in fraud prevention, and the countervailing benefits deriving from it to service users, that is, organisations that accept cards and their customers, could provide a justification for the outbound IF increases. We have therefore collected information to verify whether:

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253 See paragraph 2.15 in Annex 2.
254 See paragraph 2.16 in Annex 2.
255 See paragraph 2.17 in Annex 2.
256 See paragraph 2.24 in Annex 2.
257 See CP24/14 Remedies consultation (December 2024) Chapter 7
258 See paragraph 2.67 in Annex 2
259 See paragraph 2.27 in Annex 2
260 See paragraph 2.26 in Annex 2.
261 See paragraphs 2.63 to 2.65 in Annex 2.
262 See paragraphs 2.7 to 2.9, 2.18 and 2.19 in Annex 2.

- UK-EEA fraud levels are similar to the EEA-RoW (or UK-RoW) fraud levels, considering that the schemes have adopted IF levels that applied to these transactions (see paragraphs 5.71 to 5.73).
- increasing IFs led to improvements in terms of fraud prevention, which would also benefit merchants and their customers (see paragraphs 5.74 to 5.75).

5.71 We asked Mastercard and Visa to produce data on fraud levels (number of fraudulent transactions as a proportion of all transactions) for UK-EEA CNP cross-border transactions and other CNP cross-border transactions (such as intra-EEA, RoW-EEA and RoW-UK) for the period 2020 to 2023.[263]

5.72 The data submitted by the schemes (see Figure 7 and Figure 8) shows fraud levels for UK-EEA CNP transactions were consistently lower in the period 2022 to 2023 than for RoW-EEA CNP transactions.

5.73 This means that, even if one were to assume that the intra-EEA IFs and EEA-RoW outbound IFs had been set to reflect differentials in fraud levels (and the need to incentivise investments in fraud prevention commensurate to the levels of frauds of each corridor), the data on fraud levels provided by the schemes shows that this would not justify setting the UK-EEA IFs at EEA-RoW level. This is because the fraud levels associated with the transactions in the UK-EEA corridor are significantly lower than those associated with the RoW-EEA corridor. Those specific to Mastercard were already declining before the increases and were very similar to those associated with the intra-EEA cross-border transactions.

Figure 7: Fraud levels for Mastercard: 2020 to 2023 (in relation to yearly transactions)

[✂]

Note: data expressed in basis points (bps). Mastercard increased its MIF in April 2022 (vertical dashed line).

Source: [✂]. [✂].

Figure 8: Fraud levels for Visa: 2020-2023 (in relation to yearly transactions)

[✂]

Note: data expressed in basis points (bps). Visa increased its MIF in October 2021 (vertical dashed line).

Source: [✂]. [✂].

5.74 Furthermore, we have seen no evidence to suggest that improvements in fraud prevention were hindered by the previous, lower IF levels. Indeed, the increased IF levels have not led to a reduction in fraud levels. Rather, fraud levels for UK-EEA CNP transactions appear to have increased following the outbound IFs increases, while fraud levels for intra-EEA cross-border CNP transactions, for which IFs were unchanged, remained stable or even decreased.

263 Fraud levels are calculated by dividing the total value of fraud transactions in a given period of time by the corresponding value of total sales in the same period of time. Note that 100 bps = 1%.

5.75 The lack of improvement in fraud levels for UK-EEA transactions following the outbound IF increases is not surprising considering that we have seen no persuasive evidence from either the schemes or the issuers that shows that individual issuers' fraud prevention investments are directly related to the IF revenue they receive. Statements from UK issuers explain that they do not track the cost of fraud for the specific UK-EEA outbound CNP transactions and have not invested the additional revenue from the higher IF levels to improve fraud prevention for these or other transactions. We have no reason to consider that EEA issuers behave differently. As such, we conclude that there is no reason to believe that the increases in outbound IFs provided EEA issuers with additional incentives to invest in fraud prevention and have had a positive impact on fraud levels to the benefits of service users that are organisations that accept cards and their customers.

5.76 While it is true that CNP and cross-border transactions are typically subject to higher levels of fraud compared to CP and domestic transactions, we conclude for the reasons set out above that there is no clear evidence that the increases in outbound IFs were needed to, or have encouraged issuers to, invest in the security of the relevant transactions to the benefits of service users that are organisations that accept cards and their customers.

Issuer costs

5.77 Mastercard, Visa and some issuers justified higher outbound IFs on the grounds that they reflect the higher issuer costs incurred for CNP and cross-border transactions compared to CP and domestic transactions.[264] As set out above in paragraph 5.60, we have considered how issuers' costs related to IFs, and whether differentials in costs levels for the UK-EEA corridor compared to the intra-EEA corridor could justify increasing IFs to the current levels.

Our assessment

5.78 For the avoidance of doubt, no stakeholder, including the schemes, has suggested that issuers' operational costs for UK-EEA card payments have changed since the UK withdrew from the EU (see paragraphs 2.4 to 2.27 in Annex 2).

5.79 Mastercard, Visa and some issuers have argued that issuers deserve higher outbound IFs as compensation because issuer costs related to UK-EEA CNP transactions have always been higher than those of domestic transactions (see Annex 2 for more details).[265]

5.80 However, there is no evidence from the schemes' internal documents that issuers' costs arising from cross-border transactions were a driver behind the decision to set higher IFs for UK-EEA cross-border transactions. In addition, neither Mastercard nor Visa were able to give us cost information to understand whether and to what extent outbound IF increases were needed to enable issuers to recover all of their costs.

5.81 We did receive a submission from one EEA and UK issuer [✂], which told us that at a minimum, 'the actual costs incurred by issuers must be taken into account when calculating a fair interchange fee for specific transaction types'.[266] We asked the issuer to provide information on 2020 and 2024 issuing costs.[267]

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264 See paragraphs 2.4 - 2.25, 2.27, and 2.35 - 2.62 in Annex 2.

265 See paragraphs 2.4 and 2.13 in Annex 2.

266 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

267 Costs are measured by dividing the overall costs incurred in a given period of time by the corresponding total transaction value in the same period of time. Note that 100 bps = 1%.

5.82 Although we do not treat the results as representative of the sector, they are a useful indicator of the following (for more details see Annex 2, paragraphs 2.100 to 2.102):

- At 115 basis points, outbound IF levels for debit cards are higher than the total costs reported by the only issuer who volunteered relevant information for EEA to UK CNP transactions. According to the figures provided, costs for this specific issuer amount up to [✂] basis points if we consider only direct costs, or up to [✂] basis points when indirect costs are also factored in. Additionally, the gap between IFs and the issuer's direct costs widens when incentives and rebates, provided by the card schemes, on scheme and processing fees are accounted for.
- Fraud-related costs ([✂] and [✂] basis points, for Mastercard and Visa respectively) account for a significant proportion of incurred costs of debit cards, but fall very far short of current outbound IFs (115 basis points). The data from this issuer does not seem to corroborate the claim made by the schemes and some issuers that fraud-related costs are an important factor to explain the increases.
- Fraud-related costs are higher for EEA-UK cross-border debit transactions than for EEA domestic ones. However, we note that the difference between such costs is at most equal to [✂] basis points, that is, only a fraction of the difference between cross-border and domestic debit IFs, which amounts to 95 basis points. Hence, higher fraud-related costs for cross-border transactions cannot justify the fivefold increase in debit IFs, despite what many respondents have told us.[268]

5.83 As mentioned in Annex 2 (paragraph 2.85), later in the review [✂] provided us with data that relates specifically to EEA to UK CNP transactions that it said provides a more accurate reflection of fees and rebates for EEA to UK CNP transactions. The data, included in Annex 2 (Table 14) provides a very similar picture: based on the range of rebates reported by the issuer (see Annex 2, Table 14) we can conservatively assume that the issuer receives rebate payments on scheme and processing fees for over 80% of the fees paid. In that case, based on the scenarios calculated by this issuer (see Annex 2, Table 15), we find that direct cost (net of rebates) can amount to [✂] basis points, whereas total incurred costs (including indirect costs) amount to [✂] basis points.[269]

5.84 So, even if we accepted that IFs should reflect some of the costs that issuers incur, we have seen that outbound IFs set by Mastercard and Visa significantly exceed such costs. The two schemes and some issuers have repeatedly said that the IF increases exist to cover fraud-related costs. But we have seen that IFs significantly below current levels would also cover those costs.

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268 See Table 16: Issuer's fraud and chargeback costs CNP in basis points - (excluding fraud recoveries and indirect costs) in Annex 2 for more details.

269 In providing such data [✂] said that this data is [✂] specific and is likely not representative of EU issuers because each issuer likely has a different deal with the schemes and different economics. [✂] suggested that the PSR should consider rebate rates of [✂] % or lower so that new or smaller issuers are captured. We have no way to verify this information and [✂] did not offer any evidence to substantiate such statements. However, even assuming that rebates of [✂] % are more representative of the circumstances of new smaller issuers we note that they do not represent the circumstances of large issuers, which account for the majority of UK-EEA CNP transactions. In addition, rebates of [✂] % still result in direct costs and indirect costs significantly lower (see Annex 2, Table 15) than the current outbound IF levels.

Conclusion

5.85 As explained in Chapter 4, lack of effective competitive constraints on the acquiring side meant the card schemes did not need to consider the interests of merchants or their customers when increasing outbound IFs. We have found that the schemes raised outbound IFs without considering whether those increases introduced on UK acquirers and merchants would also benefit the same merchants and their customers, and not just the EEA issuers.

5.86 Mastercard and Visa told us why they think the new outbound IFs are more appropriate than previous ones, including for service users (organisations that accept cards and their customers). However, we have not found their justifications persuasive, especially for the extent of the increase set by the schemes.

5.87 The schemes told us previous outbound IF levels were based on considerations that are not relevant today for UK-EEA CNP transactions. However, there is no evidence that the previous levels have caused detriment or had any other negative impact on service users that are organisations that accept cards and their customers. Neither Mastercard nor Visa sought to carry out any analysis to establish that the increases were required. They adopted IF levels that had been established in a context different from UK-EEA transactions, with different characteristics, and as such not directly relevant to the UK-EEA CNP context.

5.88 The schemes also sought to rely on the presence of alternative payment methods that are more costly to the merchants to justify the current levels of cross-border IFs. In particular, Visa submitted an analysis that considered the cost of alternatives, which it claimed showed that current outbound IF levels were still lower than they should be. We were not persuaded by Visa's methodology and selection of comparators. Some of the alternatives included in the analysis were not relevant, because they are not available in the UK-EEA context and /or have acceptance costs to merchants that are directly related to those of Mastercard and Visa. IF levels based on the cost of such alternatives would inevitably be ever increasing: higher IFs would increase the cost of those alternatives, which would in turn determine further IFs (see paragraph 5.43). When we made adjustments to address some of these problems – excluding irrelevant alternatives – the analysis suggested that current levels are likely to be unduly high.

5.89 The schemes also submitted that the increases in IFs paid to issuers were appropriate to incentivise more fraud protection and investments, something that was also in the interest of service users that are organisations that accept cards and their customers. We considered this argument carefully and we saw no evidence that the increased IFs had been used to invest in such measures, nor that fraud levels had reduced since IFs were increased.

5.90 The schemes and some issuers also told us that the increases in IFs were needed to allow issuers to recoup the cost of UK-EEA CNP transactions. As discussed at paragraphs 5.58-5.60, issuers have a choice in how payment services costs are recovered across their full set of products and services and we have not found that issuers' payment costs should be recovered entirely through IFs. We have nevertheless also considered how the increased outbound IFs compared to issuers' costs – this is because the schemes and some issuers told us that the increases in IFs were needed to allow issuers to recoup their cost for UK-EEA CNP transactions. From the information available to us, we found that the new IF rates are above, and likely significantly above, issuers' costs. No stakeholder, including the schemes, has suggested that issuers' operational costs for UK-EEA card payments have changed since the UK withdrew from the EU.

5.91 The lack of a valid rationale for the current outbound IF levels, combined with the results of our adjusted version of Visa's analysis and the lack of evidence that the increases generated benefits for service-users, lead us to conclude that there is no sound basis for the outbound IF increases and that the schemes have raised the outbound IFs to unduly high levels.

6 Effect of the increases

This chapter sets out our assessment of the impact of the increases in UK-EEA consumer CNP interchange fees (outbound IFs) on UK acquirers, merchants and their customers.

Introduction

6.1 In this chapter we consider the extent to which the increases in outbound IFs have had an impact on the acquiring side. Our assessment considers two types of impacts: (1) from acquirers to merchants, and (2) from merchants to consumers. In what follows:

1. we consider how far the increases in outbound IFs have affected and are affecting UK merchants
2. we illustrate how the outbound IF increases have affected and are affecting merchants' customers.

6.2 For (1), we consider how far acquirers may recover the additional cost of outbound IFs via merchant service charges (MSCs), representing an additional cost to the merchants. For (2), we consider the possibility that merchants, in turn, pass part of this cost on to their customers by increasing retail prices.

6.3 We refer to the process of offsetting increased costs by raising prices as *pass-through*. But some of the respondents have referred to this process also as *pass on*. So, we use both terms interchangeably.

Pass-through of fee increases from UK acquirers to UK merchants

6.4 We estimate that in 2022 UK acquirers paid between £150 million and £200 million in additional IFs due to the increases in outbound IFs, that is, in addition to what they would have paid if the outbound IFs had stayed at previous IFR levels (0.2% for debit cards and 0.3% for credit cards). In 2023 they paid a similar amount of additional IFs (see Chapter 3).[270] We have not seen evidence that UK-EEA cross-border transactions would fall significantly in volume in the foreseeable future. So, UK acquirers can expect to pay broadly similar additional amounts in forthcoming years.

270 See paragraph 3.52 in Chapter 3.

6.5 The impact of IFs on UK merchants depends on how much of the additional costs UK acquirers pass on. To estimate the economic impact, we analysed separately the levels of fee pass-through for the different contract types and pricing available to merchants. As Chapter 3 describes, there are four contract types: IC++, IC+, standard, and fixed pricing.[271]

- For IC++ and IC+ pricing, acquirers will automatically pass any IF charge on to merchants. These are defined as 'full pass-through' (or simply 'pass-through') pricing options.
- For standard and fixed pricing options (also known as 'blended' options), acquirers do not pass IFs changes to merchants automatically, but they may choose to do so in periodic contract renegotiations (which can mean passing on fee increases in later periods).

6.6 To estimate the prevalence of each contract type, we asked UK acquirers for the 2022 values of UK-EEA CNP transactions at UK merchants for IC++, IC+, fixed, standard and any 'other' contracts. We obtained data from 15 acquirers which collectively accounts for over 90% of UK-EEA CNP card transactions by value.[272] Twelve of these acquirers use a combination of pass-through pricing and blended contracts; but by value the vast majority of their contracts are pass-through. The remaining three acquirers only use pass-through pricing with their merchants.

6.7 We found that:

- around 80% of transactions, by value, relate to contracts on IC++ and IC+ pricing
- around 20% of transactions relate to contracts on fixed or standard pricing tariffs[273]

6.8 It follows that at least 80% of transactions involve automatic pass-through from acquirers to UK merchants. We then considered in detail how far acquirers also fully or partially passed through the IFs charged under blended options (the remaining 20% of transactions), as this depends on each acquirer's approach to pricing.

6.9 Out of the acquirers that use blended contracts (in addition to pass-through), seven (which account for 14 out of the 20 percentage points in question), told us that as part of their repricing exercises they were passing on the IF increases in full (over 12 to 18 months following the increases).[274] Another acquirer (which accounts for only 2 out of the 20 percentage points in question) said repricing took place 'where appropriate' but did not give more precise details. For the remaining acquirers that also use blended contracts, we could not establish whether the pass-through took significantly longer to happen or happened at all.

6.10 In accordance with the information received, we made the following assumptions:

- The aforementioned seven acquirers representing 14% of total transactions fully passed through additional IF-related costs to merchants within the first 18 months after the increases;

271 See paragraphs 3.12 to 3.17 in Chapter 3.

272 We originally requested data from 15 acquirers in the UK. Two acquirers [✂] merged their activities during this review. [✂]

273 The category 'other' accounted for a negligible 0.03% of transaction values.

274 Some have explained that to do so they reclassified UK-EEA cross-border transactions from domestic to international.

- The one acquirer in paragraph 6.9 that represents 2% of total transactions only absorbed half of the additional IF-related costs to merchants within the first 18 months after the increases; and
- The remaining four acquirers, representing 5% of total transactions, fully absorbed additional IF-related costs to merchants within the first 18 months after the increases.[275]

6.11 Therefore, we estimate that acquirers have passed through approximately three quarters of the increases in blended contracts charges (15 percentage points over total transactions). We recognise the limitations of some assumptions but note that they only influence a small part of overall transactions.

6.12 Based on the above we estimate that[276]:

- Acquirers passed through approximately 95% of the value of all the 'additional' outbound IFs to UK merchants in 2022. They passed through 80% automatically under IC++ and IC+ contracts, and 15% under blended contracts.
- Approximately 5% of the increases were absorbed by a small number of acquirers (these mainly related to merchants on 'fixed' pricing).

6.13 We therefore estimate that in 2022, UK merchants paid approximately 95% of £150 million to £200 million in additional IFs.[277]

6.14 For this analysis, our calculations are based on data that postdates the outbound IF increases. The IF increases may also have led to a further adverse impact on UK merchants, with consumers buying fewer goods or services from them. However, we have not tried to establish the existence of such an additional impact.

What the card schemes told us

6.15 Mastercard said that reliance on qualitative statements, rather than quantitative analysis, to estimate pass-on, is not robust, 'in particular for blended contracts', for the following reasons.

6.16 Firstly, it said that the evidence underlying our assessment of pass-through was not robust:

- Mastercard told us that it is not feasible that the use of qualitative statements from acquirers captures or tests the relevant economic dynamics of pass-through. For example, an acquirer may have adjusted their headline prices to make allowance for the change in interchange rates, and therefore concluded that the change has been passed on. However, whether such changes achieve full pass-on in practice will depend, inter alia, on: the extent to which an acquirer 'has accurately forecast its own transaction mix'; whether 'merchants have negotiated discounts or other modifications to their acquiring contracts'; and whether 'the fee change has prompted merchants to switch to other acquirers offering lower service charges'. According to

275 Please note that this latter is a conservative assumption, as, based on the information provided, we cannot fully exclude that some pass-through actually took place.

276 [✂].

277 Considering that the extra IF amount paid by UK acquirers in 2023 is very similar to the one paid in 2022, it is likely that UK merchants will have paid a similar extra amount in 2023. We have no reasons to believe that arrangements between acquirers and merchants have changed from one year to the other.

Mastercard, these are important effects which can only be captured in a quantitative analysis, which the PSR has failed to conduct.[278]

- Mastercard said that the responses by acquirers reflect a 'subjective and partial view of acquirers' pass-on intentions', not a robust measure of how much pass-on was actually achieved. It said that, even if the qualitative statements on which the PSR relies were reliable, the interpretation we made of such statements is also 'subjective and ambiguous.' It said this is because some statements do not always give a clear picture of the extent of pass-on, nor do they always support our conclusions. As examples, Mastercard referred to the responses from two acquirers: for one, whose response was 'unclear', the PSR assumed 50% pass-through without providing any reasoning; for the other, 100% pass-through was assumed despite the acquirer's response that 'some merchants would not have received the pass-through cost'.[279] Mastercard indicated that differing interpretations of acquirer statements may lead to different conclusions about pass-on.
- Mastercard submitted that it is particularly important as a matter of principle that a methodology is not based on subjective views when the views are those of parties which may have an interest in the outcome of the exercise.[280]

6.17 In addition, Mastercard submitted that our analysis, based on qualitative statements, is not robust especially for merchants on blended contracts:

- Mastercard said that around 95% of UK merchants (and 98% of small merchants) are on blended contracts. Therefore, the PSR's headline figure overlooks the fact that the vast majority of UK merchants (especially small and medium size) 'do not necessarily experience high pass on.' Further, the pass-through on these merchants cannot be estimated using the information and methodology which the PSR has used.[281]
- Mastercard said that, by considering the degree to which IFs are passed on by acquirers, rather than the degree to which IFs are passed on to merchants, the PSR has overlooked the importance players who sit between acquirers and merchants, such as payment facilitators. It said that payment facilitators play an increasingly important role in onboarding smaller merchants, with data from the PSR suggesting that 'over 80% of new merchants onboarded in the UK in 2018 were onboarded by the largest payment facilitators and Stripe'. According to Mastercard, the PSR failed to take into account instances whereby the increases in IFs are not passed-on to merchants, as payment facilitators and other intermediaries 'are likely to absorb some of the increases passed on by acquirers'.[282] Mastercard said that, by ignoring this important development in the payments landscape, the PSR may substantially overestimate the degree of pass-on to merchants. Mastercard stated that the PSR has made no attempt to gather information on this part of the value chain, and has not acknowledged it in its interim report.

278 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

279 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

280 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

281 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

282 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

- Mastercard stated that, while the PSR claims that it has collected data representing over 90% of market value for this channel, Mastercard have not been able to verify this as data on overall CNP transaction value between EEA cardholders and UK merchants has not been disclosed to Mastercard. Further, even if the PSR has collected data representing 90% of the market, the remaining 10% of acquirers 'may represent a proportionately larger share of cross border or card not present transactions, or serve a large proportion of merchants, if their customers are small merchants'.[283] Mastercard stated that this means that the PSR's acquirer information provides an incomplete, subjective, and potentially skewed estimate of the extent of pass-on of UK/EEA IF changes to merchants on blended rates.

6.18 Visa submitted that the interim report was wrong to assume that 'Visa's cross-border CNP IFs have directly harmed UK merchants/SMEs' and was also wrong to state that any change is passed on by acquirers 'almost in their entirety to UK merchants'. Visa provided the following reasons.[284]

6.19 Visa said that we have previously found (as part of our card acquiring market review) that merchants on IC++ are typically large merchants. Visa went on to say that, since Brexit, these same large merchants are also the ones that have organised their transactions to be located in the EEA, hence avoiding the increase in IFs.[285]

6.20 For merchants on blended contracts, where decisions relating to the level and timing of pass on is at the acquirer's discretion, Visa submitted that our estimate of 75% pass-through 'is not based on any quantitative analysis of acquirer data'. It is, instead, based on [✁] and additional derived assumptions which are likely to over-estimate the impact of Visa's revised cross border CNP IFs.[286]

6.21 Visa mentioned our recent Card Acquiring Market Review (CAMR), which 'made clear that changes to IFs are unlikely to be passed on to merchants on blended contracts'.[287]

What issuers told us

6.22 One issuer [✁] made one high-level objection to our assessment of the impact of the fee increases on UK acquirers and merchants. It said that the increase has a negligible impact on the vast majority of UK merchants. It said this is because '95% of UK merchants are on standard pricing' and a very small percentage of merchants on IC+/++ pricing will be exposed, as these are generally the largest merchants who are also the ones with 'the best tools to offer alternative payment methods or otherwise mitigate the impact'.[288]

6.23 No other issuer provided commentary to our calculations of the impacts on merchants.

283 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

284 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

285 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

286 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

287 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

288 Stakeholder response to MR22/2.6 dated 14/02/2024 [✁].

What acquirers told us

6.24 One acquirer, [✂], stated that a significant proportion of the impact we found ('£150-200 million paid by merchants following the increases') is being borne by SME merchants.[289]

6.25 A trade association representing EEA acquirers [✂] said that acquirers and merchants lack a viable alternative to accepting the dominant card schemes. As a result, they are unable to mitigate the cost of this increase. This is especially true for small businesses, who cannot resort to any payment optimisation mechanisms.[290]

6.26 A trade association speaking on behalf of its UK acquirer members [✂] told us that its members confirmed that they 'generally pass on interchange onto merchants'.[291]

What merchants told us

6.27 In response to our interim report findings, merchants have told us the following.

6.28 The BRC pointed to an asymmetrical pass-through of costs in this market, whereby past reductions in card fees 'have not been passed on to most retailers', whereas 'the fees levied by the card schemes have been increasing aggressively for several years'. It said that merchants are losing out 'with fees that constantly rise' (often with no explanation or reasoning).[292]

6.29 A merchant [✂] said it recognised the increase in IFs and indirectly pointed to a pass-through to merchants and customers by submitting that these increases 'ultimately led to higher consumer prices'. The merchant [✂] observed that 'fees are unavoidable for all UK merchants who engage in international trade'. It estimated that the increased fees 'have cost [✂] millions since 2021'.[293]

6.30 A trade association representing merchants [✂] referred to the pass-through analysis in qualitative terms. Its response stated that 'whilst the fees are borne by the payment service providers [i.e., the acquirers], they in turn pass the hike in fees onto small businesses who use their services'. It referred to an Axe the Card Tax coalition's 2023 report which, according to the trade association [✂], found that the cost of using card payments 'has risen significantly for small businesses, up 13% since 2014'. It said the hike in interchange card fees has been profoundly felt, especially since Brexit and that, coupled with other factors (the 'impact of the pandemic, high inflation and now high interest rates') small businesses' margins have been further eroded by the increase in interchange card fees.[294]

6.31 A merchant [✂] commented that the assessment appears to be based on sound rationale and is therefore robust.[295]

289 See paragraph 1.91 in Annex 1.
290 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].
291 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].
292 Stakeholder response to MR22/2.6 dated 26/01/2024 [✂].
293 Stakeholder response to MR22/2.6 dated 02/02/2024 [✂].
294 Stakeholder response to MR22/2.6 dated 02/02/2024 [✂].
295 Stakeholder response to MR22/2.6 dated 25/01/2024 [✂].

What other stakeholders told us

6.32 In response to our interim report findings, other stakeholders have told us the following.

6.33 A trade association representing tech startups [✂] mentioned how 'UK merchants, especially SMEs, and potentially some of their UK customers, are adversely impacted', as 'many merchants face no choice but to accept these fee rises' (all of which has had a considerable impact on their businesses). The trade association [✂] encouraged us to investigate how increases have ultimately impacted consumers.[296]

Our responses to stakeholders' views

6.34 It is clear that the outbound IF increases for transactions on automatic pass-through pricing (IC++/IC+) have been passed on to UK merchants, as the schemes accept at least to some degree. As seen in paragraph 6.19, Visa submitted that merchants on automatic pass-through contracts (IC++/IC+) are typically large merchants that, since the UK's withdrawal from the EU, have relocated their transactions to avoid the increase in IFs. However, our estimated pass-through is after (that is, net of) any relocation that merchants have put in place following the UK's withdrawal. In 2022, transactions on automatic pass-through pricing accounted for 80% of all transactions (by value), and hence of the total increase (see paragraph 6.8). That means 80% of the additional £150 to £200 million has been passed on almost immediately to UK merchants. This has not been challenged by the card schemes.

6.35 For completeness, our interim report also considered any pass-through for the remaining 20% (by value) of outbound IFs on blended contracts. These are typically contracts for smaller merchants.

6.36 The schemes have challenged our assessment of pass-through only for the 20% of transactions that are on blended pricing, that is, 20% of the additional £150 to £200 million. For these, we have estimated that acquirers have passed on around three quarters to merchants in the months following the increases (see paragraph 6.11).

6.37 For these transactions on blended contracts, Mastercard submitted (see paragraph 6.15) that our analysis (based on qualitative statements from acquirers) cannot be accurate because the actual pass-through will depend:

1. on the extent to which an acquirer 'has accurately forecast its own transaction mix'
2. on whether 'merchants have negotiated discounts or other modifications to their acquiring contracts'
3. on whether 'the fee change has prompted merchants to switch to other acquirers offering lower service charges'

6.38 On point 1, we note that acquirers are well placed to forecast the merchants' transaction mix. They observe the merchant transactions from the recent past (for example, the previous month or year), which are a very good predictor of the transaction mix in subsequent periods. Even assuming that acquirers' initial forecast is not correct, they can revisit it at the subsequent contract renewal.

296 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

6.39 On points 2 and 3, we note that the increases apply to all acquirers and affect them all in the same measure. This means the outbound IF increases do not provide them with an opportunity to undercut each other. For the same reason, there is no basis to believe that increases in outbound IFs have improved the merchants' ability to negotiate discounts or other modifications.

6.40 Mastercard said that acquirers' responses for the remaining 20% of transactions on blended pricing only represent their partial views of their pass-on intentions (see paragraph 6.16). However, our analysis is based on responses that describe what acquirers did following the increases and, in particular, whether and to what extent they passed the increases on to merchants. We undertook a detailed analysis of acquirers' responses on the different approaches used for blended contracts. Where it was unclear what the acquirers had done, we took a conservative approach. In most cases, however, it was very clear that IF changes related to blended pricing were passed on to merchants. We estimated that acquirers passed through approximately 75% of the increases in blended contracts charges to merchants.

6.41 As explained in paragraph 6.10, where we were uncertain or had doubts about the answers, we assumed no pass-through (four instances) or 50% pass-through (one instance). That is, we assumed the increases were absorbed totally or partially by the acquirer, not the merchant.

6.42 The schemes have challenged the way we interpreted the acquirers' responses, in particular those of two acquirers. In one of these cases, the meaning is clear: the full response states that the acquirer included the extra cost of IFs in its 2023 repricing. In the second case, the acquirer states that it managed repricing where appropriate. We assumed a 50% pass-through in this case. But even if this acquirer did not pass on the increase, that would not notably affect our main results: the total pass-through across all acquirers would be 94% instead of 95%.

6.43 In response to Mastercard's suggestion that qualitative statements from acquirers may also be potentially biased and may have overstated the actual pass-through (see paragraph 6.16), we note that the acquirers were responding to formal information requests that we sent exercising our powers under section 81(1)(b) of FSBRA. This means that acquirers were under a legal obligation not to provide false or misleading information.[297] In addition, acquirers have no interest in overstating the pass-through. If the increases had affected them, the acquirers would have an interest in understating the pass-through (to exaggerate the amount of increases they absorbed) rather than overstating it.

6.44 As seen in paragraph 6.17, Mastercard also said we had overlooked the fact that the vast majority of UK merchants do not necessarily experience high pass-through, given that 95% of them (98% of small merchants) are on blended contracts. [✂] made a similar point (see paragraph 6.22). First, we note that an increase in IF costs to medium and large merchants is no less concerning than an increase to smaller merchants. Second, our analysis shows that merchants on blended pricing contracts (including smaller merchants) have experienced a pass-through rate of 75% in the subsequent months. Even if they had experienced only a 50% rate, this would still correspond to a significant increase in outbound IFs for these merchants (an extra 0.48 percentage points for debit cards and 0.60 for credit cards).

297 FSBRA, section 90(6).

6.45 In response to Mastercard's suggestion that we had overlooked the importance of payment facilitators (they mentioned [✂]) who could have absorbed some of the increases for small merchants (see paragraph 6.17), we can confirm we sent questionnaires to acquirers and payment facilitators, including [✂], who serve smaller merchants. So, we do not consider that we have inadvertently overlooked this aspect.

6.46 Finally, as seen in paragraph 6.16, Mastercard questioned whether our acquirer sample is sufficiently representative. Our sample of acquirers accounts for over 90% of UK-EEA CNP cross-border transactions (by value). We consider this is a good basis to estimate the impact of the outbound IF increases and pass-through to UK merchants.[298]

6.47 As seen in paragraphs 6.18 to 6.21, Visa suggested that:

1. For merchants on blended contracts, our estimate of 75% pass-through 'is not based on any quantitative analysis of acquirer data'. Instead, Visa argued, we based it on statements from acquirers and additional derived assumptions that are 'likely to over-estimate the impact of Visa's revised XB [cross border] CNP IFs'.
2. Our card-acquiring market review 'made clear that changes to IFs are unlikely to be passed on to merchants on blended contracts'.

6.48 On point 1, for the reasons explained in paragraphs 6.38 and 6.40, we do not believe that we overstated the pass-through to merchants on blended contracts, either because of any acquirer bias or erroneous assessment of their statements. Even if our estimate of three quarters pass-through was excessive and the real pass-through was half, the fact that blended contracts account for 20% of all contracts, by transaction value, means we would still find that 90% of the outbound IF increases was passed on to UK merchants, corresponding to [✂] £150 million to £200 million in additional IFs per year.

6.49 On point 2, we note that our Card-Acquiring Market Review (CAMR) referred to decreases in IFs. The same review found that increases in fees were largely passed through, irrespective of the size of the merchant.[299] We also note that the CAMR review introduced remedies aimed at increasing transparency and competition between UK acquirers that offer blended contracts to their merchants, which in turn should lead to increased cost pass-through in downstream markets.

6.50 Acquirers and merchants who have commented on this point confirmed our findings that the IF increases are significantly passed through (therefore affecting merchants). These stakeholders all refer to the effects of the increases in similar terms:

- Acquirers generally pass on IF increases to merchants.
- Merchants have no choice but to accept these fee rises.
- Fee increases are unavoidable for all UK merchants who engage in international trade.
- The impact is borne by SME merchants.
- Merchants are unable to mitigate the cost of the increase.

298 PSR internal computations based on data submitted by Mastercard and Visa. [✂].

299 The CAMR finding was specific to S&P fees. However, from an acquirer's perspective, there is little difference in IFs and S&P fees. We would expect fee increases to be passed on in a similar way whether they affect IFs or S&P fees. See MR18/1.8 *Market review into the supply of card-acquiring services: final report* (November 2021), paragraph 5.66.

6.51 Although many of the statements are qualitative in nature, they all point to the fact that most of the fees are passed through in a way consistent with our analysis of the data.

6.52 Having considered all the evidence and the responses to our interim findings on pass-through, we concluded that about 95% of the outbound IF increases was passed through from acquirers to merchants.

Pass-through of fee increases from UK merchants to consumers

6.53 The evidence described above indicates that acquirers passed on to UK merchants the vast majority of the increases in outbound IFs. Although our market review findings are not dependent on this, in this section we consider how merchants may pass on the impact to consumers via the prices they charge.

6.54 Economic theory and empirical evidence from several studies suggest that, over time, merchants will pass cost changes at least partly on to consumer prices.[300] How far merchants can pass such additional costs on depends on a range of factors. These include intensity of competition, responsiveness of consumer demand and relevant marginal costs, and whether the cost changes are industry-wide or affect only some firms. Empirical evidence also suggests the degree of cost pass-through can differ significantly between firms in the same industry, even when the cost change is industry-wide.[301]

6.55 Given these differences in cost pass-through rates, it would take significant work to estimate how much of the additional [✂] £150–200 million paid by merchants following the outbound IF increases have been passed through to consumers. In our view, merchants are unlikely to pass on the full amount to consumers under typical market conditions.[302] We expect that UK merchants and their customers will share the adverse effects to some material extent, through reduced margins and higher retail prices respectively.

6.56 In the cross-border setting, where merchants may pass on the outbound IF increases, the question arises as to what proportion of these increases is borne by UK as opposed to EEA consumers. The increase in outbound IFs arises from EEA-issued cards, which are generally held by EEA rather than UK consumers. So, it might be assumed that any resulting increase in consumer prices would mostly affect EEA consumers. However, such an outcome would require prices charged by UK merchants to be tailored to specific groups of consumers based on the location of their card issuer, or (as a proxy) of the consumer.

6.57 The most direct way of targeting the pass-through of higher outbound IFs at those consumers who generate it would be to levy a surcharge on EEA-issued consumer cards. However, as explained in more detail in Chapter 9, merchants do not typically impose surcharges on consumers based on the country where their card is issued. In fact,

300 For a literature review, see RBB Economics, *Cost pass-through: theory, measurement, and potential policy implications, A Report prepared for the Office of Fair Trading* (February 2014).

301 RBB Economics, *Cost pass-through: theory, measurement, and potential policy implications, A Report prepared for the Office of Fair Trading* (February 2014), page 6 and Chapter 8.

302 RBB Economics, *Cost pass-through: theory, measurement, and potential policy implications, A Report prepared for the Office of Fair Trading* (February 2014), footnote 18 and Sections 4, 6 and 7.

this may be neither feasible nor desirable for a merchant, since it could push consumers to abandon their transactions.[303]

6.58 Some merchants set different retail prices for consumers in the UK and those in EEA countries – an approach known as territorial pricing. This may be achieved, for example, by using separate websites, each aimed at consumers in a different country or region. A merchant that engages in territorial pricing could reflect the increase in outbound IFs in its pricing to EEA consumers only, while leaving its UK pricing unchanged.

6.59 However, territorial pricing is not a feasible or desirable practice for all merchants. To be feasible, there must be barriers to prevent large numbers of consumers in the country facing the higher price from purchasing at the lower price intended for the other territory. Otherwise, such arbitrage would undermine the price differential and ultimately eliminate it. Territorial pricing also incurs additional costs for the merchant, such as creating and maintaining separate websites and taking measures to direct customers to the appropriate website for their location. Merchants may conclude that attempting to differentiate their pricing between the UK and the EEA is not worthwhile and instead set a common, uniform price across both regions.

6.60 For merchants that set a common price across the UK and the EEA, pass-through of higher outbound IFs affects their UK customers as well as those in the EEA. As with pass-through rates themselves, arriving at an overall estimate of what proportion UK consumers bear is not necessary or proportionate, as our findings are not dependent on this. However, in our view, for the reasons set out above it is implausible that the entire burden of any pass-through of higher outbound IFs will fall on EEA consumers alone. Accordingly, we consider that there are very likely to be some material impacts on UK consumers too, as well as impacts on UK merchants and, as such, there is a clear UK consumer nexus.

Stakeholders' views and our response

6.61 Views from some stakeholders already presented in the previous sections are consistent with our discussion of pass-through to consumers.[304]

Our conclusion

6.62 As a result of the increases in outbound IFs by Mastercard and Visa, we have estimated that UK acquirers paid, in 2022 and 2023, approximately £150 million to £200 million in additional IFs [✂]. We expect that UK acquirers will pay broadly similar annual amounts in forthcoming years.

6.63 We estimate that approximately 95% of the value of all the 'additional' outbound IFs was passed through in full to UK merchants over the last year (80% as a result of automatic pass-through under IC++ and IC+ contracts, and 15% under blended contracts).

6.64 We have not estimated what fraction of the 'additional' outbound IFs have been passed through to the merchants' UK customers. We do not consider that arriving at an estimate would materially influence our overall conclusion. However, we expect that the effect will

303 See paragraph 9.38 in Chapter 9.

304 See [✂] at paragraph 6.29, [✂] at paragraph 6.30 and [✂] at paragraph 6.33.

be to some material extent shared between UK merchants (in the form of reduced margins) and their customers, including their UK customers (in the form of higher retail prices).

6.65 Given the above, we estimate that, following Mastercard's and Visa's decisions to increase outbound IFs, UK merchants (including SMEs) and potentially some of their customers, are paying approximatively an additional [✂] £150 to £200 million per year (and will likely continue to pay similar amounts in the future) in additional IFs.

6.66 We have not, at this time, conducted our own analysis of what the appropriate level for outbound IFs should be. That calculation may show the correct level is above the levels in place before the fees were raised. Until or unless that work is carried out, we do not know exactly what the level of harm to customers is. However, as we conclude that the current levels of fees are unduly high, that is, higher than what would be paid in a well-functioning market, at least some of this estimate amounts to harm to merchants and (to the extent of pass-through) their customers.

7 Our conclusions

We have sought to assess the appropriateness of the current levels of UK-EEA consumer CNP interchange fees (outbound IFs), and whether these have been set at a level that served the interests of service users (organisations that accept cards and their customers) on the basis of a range of analysis and evidence.

This chapter summarises why, based on the evidence we have seen, we conclude that the increased levels in outbound IFs in recent years indicate that aspects of the market are not working well by reference to our payment systems objectives.

Specifically, this chapter explains why we have concluded that the levels of the increased fees do not reflect effective competition, support innovation, or take into account and promote the interests of users of the schemes' network on both sides of the market, in particular UK service users (organisations that accept cards and their customers). It is UK service users who face the negative impact of the fee increases.

The chapter also explains why we conclude that the increases in outbound IFs by Mastercard and Visa following deregulation were not necessary or appropriate and why there is no valid rationale to explain the current outbound IF levels.

Aspects of the market not working well

7.1 Effective competition supports good outcomes in payments markets, such as low prices, high service quality and continued innovation. Any decisions that Mastercard and Visa make on how much to charge the acquiring side for EEA consumer CNP transactions at UK merchants depend on how far they face competitive constraints on the merchants/acquirers side of the market.

7.2 We considered what response acquirers and merchants could give following the schemes' decision to increase the outbound IFs in October 2021 and April 2022. We found that there was no realistic response that UK acquirers and merchants could adopt, which would provide an effective competitive constraint on the schemes' increase in IFs. This meant that the schemes had the power to increase the fees while at the same time they did not need to consider the interest of merchants and their customers when deciding whether to do so.

7.3 Consistently with this, there was no indication in the evidence we have seen, including the schemes' internal documents, that the interests of UK service users (organisations that accept cards and their customers) who have faced those increases were taken into account when the decision to increase the fees was made.

7.4 The outbound IF increases reflected a strategy based on a reaction to market conditions and in particular the need to remain attractive to issuers relative to the other scheme. This means that while the schemes had no reason to consider the interests of merchants and their customers, they had strong incentives to consider the interests of issuers.

7.5 When setting the outbound IF levels, the card schemes were under no pressure to balance the costs and any countervailing benefits to service users. Both Mastercard and Visa focused predominantly on issuer-side commercial considerations. While issuers and, indirectly, card schemes may benefit from the increases, we have identified no clear corresponding benefit to merchants.

The new outbound IFs are unduly high

7.6 We concluded that the outbound IF increases only took into account the interest of issuers and, in turn, of the schemes themselves, thereby failing to set levels of IFs that would reflect competitive constraints on the schemes on the acquiring side and serve the interests of merchants and their customers.

7.7 To reach this conclusion, we looked at those factors the schemes and some issuers submitted that we should consider in light of their relevance to the interests of merchants and their customers, and in particular those factors which the schemes identified as reasons providing a justification for the increases, in particular costs linked to fraud levels and other issuer costs.

a. **Previous IF levels that applied before the UK's withdrawal from the EU and 2019 non-EEA IF levels that apply between EEA and non-EEA countries**: Both levels have been set on the basis of considerations relating to the transactions covered by those IFs, including the costs to merchants of alternatives (relying to some extent on an MIT methodology). However, neither of these levels reflect circumstances (in terms of available alternatives and costs) identical to those of the UK-EEA CNP corridor (the previous EU IFR caps were based on intra-EEA CP transactions while the 2019 Commitments levels were based on RoW-EEA CNP transactions). Specifically, by aligning outbound IF levels to the RoW-EEA 2019 levels, the schemes adopted a level set by reference relevant to transactions with non-SEPA countries, which present limited and costly alternatives for cross-border transactions (at least at the time). There was no cogent reason to assume that, had a similar analysis been carried out specifically for UK-EEA transactions (which are SEPA transactions), the outcome would have been aligned with that for non-SEPA transactions. In fact, EEA-EEA transactions present closer similarities to UK-EEA transactions both in terms of available alternative payment methods (see paragraph 4.64) and observed fraud levels (see paragraphs 5.71 to 5.73).

b. **Cost of alternative payment methods**: We found that an analysis of alternative payment methods, based on the data and to a large extent the methodology put forward to us by Visa in the 2023 Report (a methodology similar to that used in the past, albeit in a different context, by the European Commission to assess the suitability of IFs) provides further evidence that the current levels of IFs are unduly high.

c. **Possible customer benefits arising from for the increases**: We have seen no evidence showing that the outbound IF increases positively contributed to the quality and efficiency of card payments, and that issuers used the additional IF-related income to fund service improvements (fraud, quality, efficiency or savings) for the benefit of the acquiring side. In particular, we did not find evidence of a direct link between fraud levels for UK-EEA CNP transactions and the new IF levels. Fraud differentials are small and do not explain the five-fold increase in IFs.

d. **Costs to issuers**: While we have not found that IFs should be set at a level enabling issuers to recover all of their costs, we have nevertheless also considered how the increased outbound IFs compared to issuers' costs. This is because the schemes and some issuers told us that the increases in IFs were needed to allow issuers to recoup their cost for UK-EEA CNP transactions. From the information available to us, we found that the new IFs rates are above, and likely significantly above, issuers' costs. No stakeholder, including the schemes, has suggested that issuers' operational costs for UK-EEA card payments have changed since the UK withdrew from the EU.

7.8 Overall, we have found that apart from the UK's withdrawal from the EU, no other factor prompted the schemes to raise outbound IFs to current levels. Beyond this political shift, nothing else has changed to affect these levels.

7.9 Finally, we have not seen evidence that the outbound IF levels prior to the schemes' increases:

- carried any obvious risks
- undermined or otherwise adversely affected the operations of either of the two payment systems to the detriment of service users (organisations that accept cards and their customers)
- distorted competition or impeded innovation

Impact of the increases

7.10 We found that the additional cost of the IF increases has impacted UK merchants in 2022 and 2023, by an additional [✂] £150 to £200 million in IFs. Such annual impact will likely be broadly similar in forthcoming years because, as illustrated in paragraph 3.51 and Figure 4 of Chapter 3, volumes and values of UK-EEA debit and credit CNP transactions resulting in outbound IFs seem to have stabilised since 2022.

7.11 As noted in paragraph 6.12, estimate that approximately 95% of the value of all the 'additional' outbound IFs was passed through in full to UK merchants over the last year (that is, 80% as a result of automatic pass-through under IC++ and IC+ contracts, and 15% under blended contracts). We expect that this adverse impact of the IF increases will affect not only UK merchants but also, to some extent, their customers, as merchants are likely to pass through at least part of these increases through higher retail prices.

7.12 As the current outbound IF levels are unduly high, at least some of the above-mentioned impact amounts to harm to UK merchants and their customers.

Our final view

7.13 We have considered the above in light of our legal framework, including our general duties, objectives, and regulatory principles under FSBRA. As Chapter 2 sets out, we have a statutory objective to:

- ensure that payment systems are operated and developed in a way that takes account of, and promotes, the interests of those who are likely to use services provided by payment systems (our 'service user' objective)
- promote effective competition and innovation in the interests of those users (our 'competition' and 'innovation' objectives respectively).

7.14 For the most part these objectives are mutually supportive.

7.15 Having regard to each of our general duties, objectives, and regulatory principles, and in light of our provisional conclusions set out in this chapter and the wider interim report, we conclude that:

- Mastercard and Visa were subject to ineffective competitive constraints on the acquiring side when deciding to increase the outbound IFs
- Mastercard and Visa are not operating or developing aspects of their card schemes in a way that takes account of the interests of all service-users, in particular UK organisations that accept cards and (to the extent of pass-through) their customers; these factors have resulted in detriment to these service users
- there are no evident countervailing benefits or innovation to account for the IF increases (such as improved fraud prevention, quality, efficiency or economy of the card payments systems to the benefit UK merchants).

7.16 As Chapter 2 sets out, our service-user objective means (among other things) that we expect payment systems to provide good value and be cost-effective.[305] Our findings in this report do not lead us to consider the increased outbound IF levels reflect good value or cost-effective payment systems from the perspective of UK merchants or their customers.

7.17 As Chapter 2 also details, we have regard to the regulatory principles in FSBRA, including the desirability of sustainable growth in the UK economy in the medium or long term.[306] We note in particular that UK acquirers and merchants may face higher costs and prices due to lack of effective competition.[307] We conclude that the issues we have identified (in particular these pricing outcomes) are not conducive to such growth.

7.18 Overall, taking our conclusions separately and together, we conclude the market is not working well and that UK merchants and their customers are suffering harm as a result. In Chapter 9 we consider what remedies may be appropriate to address the harm identified.

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305 *Objectives Guidance* (March 2015), paragraph 6.2.

306 FSBRA, section 53.

307 See paragraph 7.10.

8 Inbound IFs

This chapter considers the fees paid by EEA acquirers to UK issuers (inbound IFs) and the reason why we are proposing to cease considering these fees as part of our review.

Introduction

8.1 Up to now this document has primarily considered outbound IFs that apply to transactions involving UK merchants and EEA-issued cards. This chapter, however, turns to the inbound IFs that apply to CNP transactions involving UK-issued cards and EEA merchants. In exploring this issue, we consider:

- what our terms of reference required us to consider
- what our analysis identified
- our approach to inbound IFs

What we said in our terms of reference

8.2 In the terms of reference for this review, we said that we wanted to understand how increases in outbound and inbound IFs may affect UK services users. We were concerned that IFs represent a cost to merchants for accepting card payments and that merchants may pass them on (at least in part) to some or all of their consumers.

8.3 We also said that this review would prioritise outbound IFs.

What our analysis identified

8.4 As outlined in Chapter 3, Mastercard and Visa agreed to the 2019 Commitments which were accepted by the European Commission.[308] These commitments continue to apply to UK-issued cards used at EEA merchants.

8.5 As a result, UK-EEA CP transactions involving UK-issued cards and EEA merchants (inbound CP IFs) are subject to caps of 0.2% and 0.3% for debit and credit cards respectively, while the equivalent CNP transactions are subject to higher caps of 1.15% and 1.5%.

8.6 The IF levels set by Mastercard and Visa for UK-EEA CNP transactions correspond to the levels for inter-regional commitments accepted by the European Commission as part of the 2019 Commitments. These commitments were due to expire in 2024. On 5 July 2024, the Commission noted the voluntary continuation by Visa and Mastercard of the caps for inter-regional IFs for another five years until November 2029.[309]

308 European Commission, CASE AT.39398 – Visa IF, *VISA 2019 Commitments decision* (April 2019); European Commission, CASE AT.40049 – Mastercard II, *Mastercard 2019 Commitments decision* (April 2019).

309 European Commission Daily News, *Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024* (July 2024).

8.7 In our interim report, we proposed to close our review of inbound IFs on the grounds of administrative priority, and we sought for stakeholders' views on this provisional position.[310]

8.8 Stakeholder views were mixed. Seven stakeholders responded to our consultation question on our proposed approach for inbound IFs. Four said they would like to see the review into inbound IFs remain open. Three agreed with our provisional proposal to close the review into inbound IFs. We explore these views in turn below.

Views in favour of progressing the review into inbound IFs

8.9 A trade association representing EEA issuers [✂] said that 'if a cap were to be implemented, it should be done symmetrically', that is, both for outbound and inbound IFs.[311]

8.10 A trade association representing EEA merchants, EuroCommerce, considered it 'imperative' to ensure equal conditions for its EEA-based members that serve UK cardholders, as well as for the UK merchants serving EEA cardholders. It urged us to engage with the European Commission's department for competition (DG COMP), noting that 'creating this level playing field will pave the way to renew the "commitments" [2019 Commitments] later this year and extend them to CP transactions'.[312]

8.11 The BRC noted that the 2019 Commitments were due to expire in November 2024 and said any cap we impose should be applied to both inbound and outbound IFs.[313] It highlighted that a review of inbound IFs would serve the interests of UK businesses operating in the EU and therefore, recommended 'all interchange fees be capped at 0.2% across all UK & EEA transactions, following the period of 0 to level out reimbursement of the overpayments'.[314]

8.12 An acquirer [✂] said that [✂].[315]

Views in favour of closing the review into inbound IFs

8.13 Two issuers [✂] were supportive of our provisional proposal to close the review on inbound IFs.[316, 317]

8.14 One of the issuers [✂] said that [✂].[318]

8.15 A merchant [✂] was in favour of closing the review into inbound IFs, since such a review would have no impact on them.[319]

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310 MR22/2.6 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023).

311 Stakeholder response to MR22/2.6 dated 2 February 2024 [✂].

312 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

313 Stakeholder response to MR22/2.6 dated 26 January 2024 [✂].

314 Stakeholder response to MR22/2.6 dated 26 January 2024 [✂].

315 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

316 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

317 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

318 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

319 Stakeholder response to MR22/2.6 dated 25 January 2024 [✂].

Our response to stakeholder views

8.16 Inbound IFs are paid by EEA merchants to UK issuers. Our view is that the adverse effects we are seeing for UK service users (organisations that accept cards and potentially some UK consumers) mainly pertain to outbound IFs. Inbound IF increases may present an issue for some UK consumers transacting with EEA merchants, but we expect this to be a small proportion of UK service users. We also think it likely that, like UK merchants, EEA merchants will have to spread the increased costs across a broader section of their customer base.

8.17 Several stakeholders set out the benefits of including inbound IFs in any price cap remedy. However, there would be significant resource implications in progressing the review on inbound IFs sufficiently to make an evidenced decision on remedies. We note that none of the stakeholders who responded to our question on closing down our review into inbound IFs commented on our Administrative Prioritisation Framework (APF).

8.18 We also note that European Commission has recently looked at inbound IFs as the Commitments offered by Mastercard and Visa on these caps were set to be in place until November 2024. On 5 July 2024, the Commission noted the voluntary continuation by Visa and Mastercard of the caps for inter-regional IFs beyond November 2024.[320] The Commission stated that, under the voluntary continuation, inter-regional IFs for debit and credit card transactions under these schemes will remain capped for another five years until November 2029.[321] The Commission observed that 'Mastercard and Visa debit and credit cards are still "must-take" for EEA merchants [and that] in the absence of caps, merchants would face the risk of excessive interchange fees passed on to them through their Merchant Service Charges.'[322]

Our final view

8.19 According to our APF we need to use our resources in the most efficient and effective way to further our statutory objectives, functions and duties, in accordance with section 53(a) of FSBRA. This guides our decisions regarding (for example) which investigations we open and continue, and how we respond to applications and complaints, subject to any specific legal duties we might have.[323]

320 European Commission Daily News, *Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024* (July 2024).

321 European Commission Daily News, *Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024* (July 2024).

322 European Commission Daily News, *Commission takes note of the voluntary continuation by Visa and Mastercard of their antitrust commitments on inter-regional interchange fees beyond November 2024* (July 2024).

323 *Administrative Priority Framework* (March 2015), page 1.

8.20 When deciding whether to take action, we will initially consider the degree to which it enables us to advance one or more of our statutory objectives, functions or duties. We are unlikely to pursue an action that does not clearly do this.[324] As outlined in Chapter 2, paragraph 2.27, our statutory objectives[325] are to:

- promote effective competition in the market for payment systems and markets for services provided by payment systems in the interests of those who use, or are likely to use, services provided by payments systems (the 'competition objective')[326]
- promote the development of, and innovation in, payment systems in the interests of those who use, or are likely to use, services provided by payment systems, with a view to improving the quality, efficiency and economy of payment systems (the 'innovation objective')
- ensure that payment systems are operated and developed in a way that takes account of, and promotes the interests of those who use, or are likely to use, services provided by payment systems (the 'service-user objective')

8.21 When deciding whether to take action, we will then weigh the impact and strategic importance of the action in advancing our statutory objectives, functions and duties, against its risks and resource implications. In other words, we will decide whether taking action would be consistent with our administrative priorities.[327]

8.22 We have considered the commitments that are currently in place (see Chapter 3, paragraph 3.26) and the extent to which progressing with the review would meet the APF requirements. In particular, we have considered the resource and cost implications (as well as the practicalities) of gathering new information from EEA merchants. We conclude that to progress with this aspect of the review would be:

- an inefficient use of our resources
- inconsistent with our administrative priorities

8.23 As such, after carefully considering stakeholder views on this issue and consulting our APF criteria, we have decided to close our review of inbound IFs on the grounds of administrative priority. This does not preclude us from looking at inbound IFs in the future.

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324 *Administrative Priority Framework* (March 2015), page 1.

325 FSBRA, sections 50 to 52.

326 FSBRA, section 50(3) states that, in considering the effectiveness of competition in a market, we may have regard, amongst other things, to the needs of different persons who use, or may use, services provided by payment systems.

327 *Administrative Priority Framework* (March 2015), page 1.

9 Remedies

This chapter outlines the potential actions we have considered for addressing or mitigating the issues we have identified regarding UK-EEA consumer CNP outbound interchange fees and the resulting detrimental effects. It sets out our conclusion that, of the potential remedies available, a price-cap remedy is the only effective potential action to address the detriment to service users we have identified in this report: the detriment to UK merchants and their customers.

If the level of the cap is set appropriately, a price cap would be effective in addressing the service user detriment we have identified in Chapter 7, and in pursuing our other objectives of promoting effective competition and innovation.

In addition, having considered the regulatory principles set out in paragraph 53 of FSBRA, we conclude that in principle a price cap remedy set at an appropriate level would be proportionate to the benefits, considered in general terms, that are expected to result from the imposition of that burden or restriction; be consistent with supporting sustainable growth in the economy of the UK; and represent an efficient use of the our resources in view of the impact of the proposed cap.

We therefore consider that imposing a price cap by way of a general or specific direction under section 54 of FSBRA would be an appropriate intervention for promoting the interests of service users such as UK organisations that accept cards and their customers and that we should take action to design and implement such a direction. Our proposals with regard to taking forward a price cap remedy will be set out in separate consultation documents. These documents will consider and consult on, among other things, how we would calculate a price cap. In addition, given we think that it will take some time to decide on a methodology, conduct the analysis and consult on the proposed cap level, we will also consult on whether the costs, benefits and possible consequences of putting a separate cap in place in the meantime mean that we should do so.

While we have considered very carefully the representations on the risk of unintended consequences of a price cap, for the reasons set out below, we conclude that a price cap is an appropriate remedy and that we should take action to implement such a remedy.

9.1 In light of our findings in this report regarding UK-EEA consumer CNP outbound IFs and the resulting detrimental effects (in particular the impact of the increases on UK merchants and their customers, referred to as 'service user detriment')[328] we have considered what potential action we could take to improve outcomes for UK merchants and customers. In this context, to be effective, a remedy must adequately address or materially mitigate that service user detriment.

9.2 The primary outcome we are aiming to achieve is a reduction in relevant IF levels to a level more in line with what would arise in a market with effective competition on the acquiring side.

328 Our conclusions are set out at Chapter 7.

9.3 As a first step in our remedies appraisal, we have therefore considered the extent to which different remedies are likely to be effective in achieving this aim. When considering effectiveness, we have considered the sufficiency of the likely scale or degree of that remedy and the likely timeliness of that remedy.

9.4 We then considered additional risks associated with any remedy that would otherwise be considered effective, in particular representations relating to potential unintended consequences or harms that may arise from the remedy.

9.5 Our interim report outlined our emerging view of potential mechanisms to address our provisional concerns. We organised these remedies into three categories:

- boosting competition
- encouraging steering
- regulation in the form of (i) changes to scheme rules or (ii) setting a price cap.

9.6 In this chapter, we firstly outline each of these potential mechanisms, and the stakeholder feedback we received. We then set out our conclusions on whether we consider these would, in principle, be effective in addressing the service user detriment we have identified as well as related considerations, including the risk of unintended consequences. In reaching our conclusions we have taken account of all the evidence available to us, including:

- the analysis and findings of the final report
- responses to our interim report
- information submitted to us in response to information and document requests, voluntary questionnaires, roundtable discussions and bilateral meetings (including the roundtable held with trade associations representing EEA issuers[329])
- evidence submitted by stakeholders in our engagement with them (including at the oral sessions held with each of the schemes and a roundtable held with EEA trade associations[330]).

9.7 For the reasons set out below, we conclude that a price cap is an appropriate remedy and that we should take action to implement such a remedy on the basis that

a. a price cap set at an appropriate level would in principle be effective in addressing our finding that current levels of UK-EEA cross-border IFs are unduly high
b. a price cap set at an appropriate level is unlikely to cause any material unintended consequences that would outweigh the benefits of the remedy and can be implemented in an effective manner.
c. the benefits would be to a large extent passed on to UK merchants (whether on IC++ and IC+ contracts or on blended contracts)
d. the technical and/or operational changes required to implement the remedy are capable of being implemented in a timely manner

329 We held a roundtable with six organisations representing EEA trade associations on 16 September 2024 [✂].
330 We held oral sessions with Visa and Mastercard separately on 29 February 2024.

e. we have not identified other effective remedies that would address the detriment we have identified in this report

9.8 In the interim report, we set out initial views on

a. the appropriate level for a price cap

b. our proposed staged approach of the price cap remedy

c. further design considerations

9.9 In view of our conclusion that a price cap is an appropriate remedy, we will undertake a further consultation with a view to preparing a direction or requirement imposing a price cap. This consultation will include our assessment of each of the issues set out at paragraph 9.8, including of stakeholders' submissions received in response to this final report.

Boosting competition

Our initial considerations

9.10 Our interim report considered in principle whether we could do more to boost competition in alternative payment methods for UK-EEA remote transactions.

9.11 We provisionally found that there are very few alternative methods to pay for these transactions.[331] We noted that, in time, alternative methods may boost competition in this context, such as SEPA instant payments for intra-EEA transactions and transactions with SEPA countries.[332] We also considered that we cannot reliably predict when these would be widely available or how widely merchants might adopt them. Furthermore, we observed that we do not expect sufficient growth in this area to alleviate our concerns. We said we had limited ability to accelerate the availability or use of alternative cross-border payments, and knew of nothing we could do that would be enough to alleviate our concerns.

9.12 We also observed that over time, innovation in payments could also provide ways for UK merchants to reduce their IFs. We cited the example of Stripe, a payment facilitator that offers a service to reduce merchants' IFs by using an acquirer in the region where the consumer is located.[333] However, merchants must have a location that supports the sale of local goods or services in that region. We considered that setting up an additional business location or relocation is not possible for most UK merchants, especially SMEs.[334]

9.13 We noted that competition might produce desirable effects requiring less regulatory intervention in the longer term. Such competition might come from other international card schemes, instant SEPA or third-party solutions using bank transfers.[335] However, we have seen no evidence suggesting that competition is producing these effects or that it is likely to in the short to medium term. We considered that the evidence pointed to competition being insufficiently effective to mitigate the detriment identified. Therefore, we were

331 MR22/2.6 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023).

332 European Commission, *Proposal for a regulation of the European Parliament and of the Council amending Regulations (EU) No 260/2012 and (EU) 2021/1230 as regards instant credit transfers in euro* (October 2022), Article 5a COM 546.

333 Stripe, *A guide to managing network costs*.

334 MR22/2.6, *Market review of UK-EEA cross-border interchange fees interim report* (December 2023).

335 Effective competition supports good outcomes in payments markets, such as low prices, high service quality and continued innovation.

concerned that the lack of effective competitive constraints would have implications for the foreseeable future. Because of the limited number of alternative payment methods, we did not consider that information transparency on IF levels or costs, or encouraging merchants or customers to consider payment methods based on these costs, would work at the moment.

9.14 Therefore, our interim view was that:

- any action we could take to boost competition was unlikely to address our concerns effectively
- competition will not achieve the outcomes we want to see on a timescale that would remove the need for other action.

Stakeholder feedback

9.15 Five stakeholders directly responded to our interim report consultation question on boosting competition.[336] Four agreed with our provisional conclusion that any actions we could take to boost competition in this space would likely not remove the need for regulatory intervention. One disagreed. We explore their views in more detail below.

9.16 Neither Mastercard nor Visa specifically responded to our interim report consultation question on whether there is any action we could take to boost competition. However, in other areas of their responses both schemes stated there are various alternative payment methods in the cross-border CNP space (see Annex 1, paragraphs 1.103 to 1.108 and 1.134 to 1.145). Our responses to these submissions are at paragraphs 1.127 to 1.133 and 1.178 to 1.184 of Annex 1. In Chapter 4 we conclude that there are limited options that could in principle represent an alternative for UK merchants for outbound transactions. We discuss the issues with these alternatives at paragraphs 4.57 to 4.74.

Stakeholders who agreed with our provisional conclusion

9.17 An acquirer [✁] agreed that the initiatives we considered to boost competition were unlikely to achieve the outcomes we wanted on a timescale that would remove the need for regulatory intervention. It went on to conclude that only direct regulatory intervention on IF levels can mitigate their harm.[337]

9.18 A merchant [✁] also agreed that there are few alternative payment methods to Mastercard and Visa for merchants to engage in international trade with the EEA and, as such, that boosting competition was unlikely to be a suitable remedy in lieu of regulatory intervention.[338] It [✁] added that, although A2A services will have the potential to provide competition to card schemes in the future, this will be a long-term process until it is fully developed.[339]

9.19 A trade association representing tech startups [✁] stated that there is no effective way to boost competition for CNP IFs within the current market because of the anti-competitive

336 MR22/2.6 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023), page 120, question 14.

337 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

338 Stakeholder response to MR22/2.6 dated 2 February 2024 [✁].

339 Stakeholder response to MR22/2.6 dated 2 February 2024 [✁].

nature of Mastercard and Visa. It went on to conclude that direct regulatory action is required to reduce the increased IFs.[340]

9.20 A merchant [✂] said it agreed that the initiatives we considered to boost competition were unlikely to achieve the outcomes we would want to see on a timescale that removes the need for regulatory intervention.[341]

Stakeholders who disagreed with our provisional conclusion

9.21 An issuer [✂] disagreed, saying that we could deliver the outcomes it wants by focusing on enabling alternatives to card based payments to emerge. It cited its own solution [✂] as an example of a solution merchants can sign up to currently which can enable cross-border transactions not on Mastercard or Visa rails. It also referred to other alternatives based on instant payments and digital wallets emerging onto the market and gave the example of Pix in Brazil and UPI in India, which it said were growing at a rapid pace. It stated that we could encourage awareness and adoption of currently available products. Further, that in the medium term, we should seek to support solutions based on open banking and the development of other emerging solutions, including those based on stablecoins or central bank digital currencies (CBDCs).[342]

9.22 In a separate submission, the issuer ([✂]) suggested that we should focus on allowing EEA domestic card and non-card based payment schemes to be accepted by UK merchants (e.g. CB, Girocard, iDeal, Bizum).[343]

Our response

9.23 We observe that most stakeholders who responded to our question on boosting competition agreed with our provisional view that actions we considered to boost competition would likely not be an effective remedy at this time.

9.24 As we conclude in Chapter 4 (paragraph 4.58 to 4.74), while there are some payment solutions available to merchants which can enable cross-border transactions not via Mastercard or Visa rails, there are still very few *viable* alternative payment methods to pay for these UK-EEA CNP transactions. Moreover, as noted in Chapter 4 (paragraph 4.69), the up-front switching costs UK merchants would need to pay to adopt these alternative payment methods reduces the financial incentives for merchants to integrate with these alternatives especially until such time as any of them have significant traction in the market.

9.25 We note the suggestion that we could raise awareness and encourage the adoption of innovative products such as [✂] and support the development of other emerging payment solutions for cross-border transactions. As noted at paragraph 9.28 below, we are doing work on unlocking account-to-account retail payments, however this work is currently focused on UK domestic payments. While we support the development of other payment solutions to introduce more competition into the cross-border space, we do not promote particular solutions or products, and we do not consider that the type of remedies referred

340 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

341 Stakeholder response to MR22/2.6 dated 25 January 2024 [✂].

342 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

343 Stakeholder response dated 22/05/2024 [✂].

to in this submission would be sufficient to create in a timely manner a level of constraint on the schemes that would lead to a lowering of outbound IF levels.

9.26 In particular, for the reasons set out in Chapter 4[344], we are concerned that most consumers appear to have limited incentives to use alternative products to those they most commonly use - debit and credit cards issued by Mastercard and Visa - regardless of awareness. This means that, even if remedies were to increase awareness or acceptance of these products, it would take time before these could gain a sufficient consumer base to represent effective alternatives to Mastercard and Visa. Until then, it is unlikely that these products could act as a constraint on the schemes when setting the levels of IFs.

9.27 We also note that Pix and UPI, which one stakeholder specifically mentioned, are only available in Brazil and India respectively, so they are currently not available for UK-EEA cross-border transactions. Also, the emergence of stablecoin and CBDCs as viable payment methods is subject to significant uncertainty, and they would take time to grow to a scale where they would be commonly used as alternatives to cards.[345]

9.28 We are currently doing work on unlocking account-to-account retail payments, but its focus is currently on UK domestic payments. We are not envisaging a focus on international account-to-account transactions in the short to medium term. It will take time for account-to-account transactions to become a solution that provides constraints across the whole spectrum of CNP use cases. Finally, we do not consider it appropriate to endorse a specific commercial product or company.

9.29 We did not receive any further suggestions for actions we could take that we consider would accelerate the availability and uptake of alternative payment methods sufficiently enough to alleviate our concerns.

Other remedies suggested by stakeholders to boost competition

9.30 In addition to the representations we received on the feasibility of the remedies we considered in our interim report, one stakeholder ([✂]) provided brief outlines for three other remedies to improve competition and innovation and that it said we should consider developing further [346]

- Supporting open banking payments, by taking action with EU regulators to increase success rates for API (Application Programming Interface) triggered SEPA instant payment to Faster Payment System payments.
- Improving UK acquirer competition by expanding the scope of open banking to enable merchants to pull via APIs their recent transaction history to get a bespoke quote from acquirers – increasing competition in niche segments like merchants with high exposure to EEA–UK CNP transactions, noting this would also help the adoption of non-Visa/Mastercard solutions.
- Accelerating the development of a commercial Variable Recurring Payment (VRP) or a national scheme in the UK, which would have more of a material impact on reducing UK merchants' costs of acceptance rather than focusing on the 2.5% of the cost associated with EEA-UK CNP transactions.

344 See also Annex 1, in particular paragraph 1.178.

345 Chapter 4, paragraph 4.73.

346 Stakeholder submission dated 22/5/2024 [✂].

9.31 In line with our strategic objective, our aim is to promote the use of innovative payment solutions such as open banking to increase competition between payment systems. As a member of the Payments Vision Delivery Committee, we will work to ensure regulatory activity promotes innovation, competition and security within the UK's payments landscape. In the short to medium term, we do not consider that the type of remedies referred to in this submission would be sufficient to create a level of constraint on the card schemes that would lead to a lowering of outbound IFs levels within the requisite time period.

9.32 Therefore, we also do not consider these options to be sufficiently effective in addressing the concerns identified.

Our final view

9.33 Having considered the feedback we received, we conclude that any additional action we could take to boost competition for UK-EEA cross-border transactions is unlikely to be sufficient to address our concerns effectively and in a timely manner.

9.34 We have therefore dismissed this option as a potential remedy in this review.

Encouraging steering

9.35 Merchants may 'steer' their customers to choose a payment method that is advantageous for the merchant. In our interim report, we considered at a principles level the implications of encouraging merchants to:

- provide a benefit or disadvantage of choosing a particular payment option
- use behavioural or visual cues to encourage customers to choose a particular payment option.

9.36 We have considered this potential remedy option further in light of our findings in this report and stakeholder feedback on our interim report. This is set out below together with our conclusions on this potential remedy option.

Surcharging

9.37 We have considered whether encouraging UK merchants to introduce surcharging (which is not allowed in the UK for consumer cards in domestic transactions, but is not prohibited for UK-EEA transactions)[347] or other forms of steering for EEA-issued cards would mitigate the service user detriment we have identified. We have primarily considered methods based on introducing a card surcharge, although other means such as loyalty points or discounts for non-card payments could have a similar effect. We set out here what we heard about the benefits and challenges of steering, and consider whether surcharging could be an effective form of steering. Other forms of steering are considered below.

9.38 As noted in Chapter 4 (paragraph 4.56), steering (including surcharging) raises the risk for merchants that any steering attempt by the merchant will actively deter the consumer and result in the merchant losing the transaction altogether. We concluded in Chapter 4 (paragraph 4.71) that, in deciding whether to steer consumers towards a specific payment method, merchants need to weigh lower IFs against the risk of lost revenue from reduced

347 See paragraph 1.131 in Annex 1.

conversion rates. Any appreciable fall in conversion rates is likely to remove merchants' incentives to use such steering as a response to outbound IF increases. Indeed, merchants have told us they do not typically steer.[348] UK acquirers, representing over 90% of the UK market, also said that their merchants had not take any consumer steering action in response to the outbound IF increases.[349] One acquirer explained that while, in principle, merchants can recognise and surcharge cards issued in another jurisdiction, doing so creates undesirable frictions in the consumer experience and can lead to abandonment of the transaction.[350]

9.39 The BRC (a trade association for UK retail businesses) told us that merchants often see steering techniques as limited in their effect, because customers typically prefer to use one payment method (for example, for budgeting purposes or rewards) and will use it despite any steering.[351]

9.40 Additionally, a paper from Shy and Stavins (2015) on merchant steering highlighted that many retailers in Australia and the US – where domestic transaction steering is permitted – rarely apply surcharging for card payments, as they fear that, by doing so, they will dissuade customers from continuing with a transaction.[352]

9.41 The ability of a UK merchant to use any of these strategies depends on what alternative payment methods, if any, are available and acceptable to EEA consumers as well as to the merchant. As we have concluded at paragraph 4.63 of this report, there are limited alternative methods to pay for UK-EEA consumer CNP transactions.

9.42 At paragraphs 4.66 to 4.68, we note that there are certain EEA domestic payment methods that could provide an alternative to Mastercard and Visa. However, there would be costs for merchants to integrate with enough of these alternatives to cover most of their EEA customers spread across different countries. This is likely to make adopting such alternatives costlier than paying the increased outbound IFs for each transaction – at least in the short to medium term. Facing upfront costs, the typical UK merchant affected by IF increases will have significantly fewer financial incentives to integrate these methods and steer customers.

9.43 Other alternatives, such as Revolut Pay and Skrill, offer acceptance solutions that UK merchants could use to accept payments by all EEA customers from various countries 'in one go'. These solutions are cheaper than Mastercard and Visa (especially cross-border) and would not require multiple integrations and switching costs. However, as we concluded at paragraph 4.69, EEA consumers do not widely use these at present.[353] We note that EEA consumers widely use naked SEPA bank transfers[354], especially in the person-to-person (P2P) transfers. However, in e-commerce, their adoption is currently still limited.[355] We consider that, in view of the fact that these payment methods are not

348 See paragraphs 1.119, 1.120, 1.131 and 1.145 in Annex 1.

349 Stakeholder responses to PSR information requests dated 11 January 2023 [✁]

350 Stakeholder response to PSR information request dated 11 January 2023 [✁].

351 BRC response to PSR information request dated 11 January 2023 [✁].

352 Shy, O. and J. Stavins (2015). Merchant Steering of Consumer Payment Choice: Evidence from a 2012 Diary Survey, in Journal of Behavioural and Experimental Economics, 55, 1-9.

353 For example, WorldPay's Global Payments Report (2024) does not even mention Revolut Pay or Skrill among the emerging payment methods used by merchant and consumers in Europe.

354 Chapter 4, paragraph 4.69.

355 See paragraphs 1.127 and 1.128 in Annex 1.

widely used by consumers, trying to convince them to pay with alternatives to their usual methods (such as Mastercard and Visa) could not only fail but also generate frictions at point of sale.[356]

9.44 We note that surcharging could impose non-negligible costs on UK merchants (see paragraph 4.68). In line with our finding, we consider that the costs for merchants steering EEA consumers to avoid increases in outbound IFs will largely apply to merchants that cannot relocate to mitigate the outbound IF increases, therefore merchants that are not very large.

9.45 Surcharging would increase the costs to the cardholder only, and then all the fees associated with the transaction will be calculated based on the inflated total transaction amount. This would mean acquirer fees, scheme and processing fees and IFs would increase too.

9.46 There is also a risk merchants could see an increase in chargebacks under the reason of excessive surcharging.

9.47 Our preliminary view in our interim report was that surcharging would not address the issues we are seeing and would be likely to have additional negative effects.

Other forms of steering

9.48 We have also considered whether we could encourage UK merchants to introduce other forms of steering. This could include:

- providing information on the fees facing merchants and how they compare to alternative payment methods
- presenting website payment options in a way that nudges consumers to use alternative payment methods (for example, by making these methods more prominent)
- ordering the list of accepted payment methods
- reducing the friction for customers when they select the non-card-payment method rather than the card-payment method

9.49 In theory, if EEA payers had wider access to alternative payment methods, UK merchants could use other ways to steer consumers towards payment methods beneficial to them (for example, methods that avoid higher IFs or processing costs). Encouraging UK merchant steering could theoretically let UK merchants avoid higher IFs. However, as noted above and in Chapter 4, there are currently limited alternative ways to pay for UK-EEA consumer CNP transactions that would allow merchants to do this.[357]

9.50 In our interim report, we set out our preliminary view that these other forms of steering remedies would not be effective in addressing the issues we are seeing.[358]

356 Chapter 4, paragraph 4.70.

357 Chapter 4, paragraph 4.63.

358 MR22/2.6 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023).

Stakeholder feedback

9.51 Of the six stakeholders who responded to our interim report consultation question on surcharging and other forms of steering[359], five stakeholders agreed with our provisional conclusion that surcharging and other forms of steering would not be effective in addressing the issues we have identified. One stakeholder disagreed, providing a detailed proposal for why we should encourage surcharging for EEA to UK CNP transactions. We discuss their views in more detail below.

9.52 Neither Mastercard nor Visa directly responded to our question on surcharging and other forms of steering in their responses to our interim report consultation. However, Mastercard did argue in other areas of its response that it is possible for merchants to exert competitive pressure on Mastercard through steering or 'nudging' consumers to alternative payment methods for cross-border CNP transactions (see Annex 1, paragraphs 1.139 to 1.140). As set out in Annex 1 (paragraphs 1.178 to 1.184), we do not agree with Mastercard's view that steering provides an effective competitive constraint on Mastercard setting UK-EEA outbound IFs.

Stakeholders who agreed with our provisional conclusion

9.53 An acquirer [✂] agreed with us that steering or surcharging (as they currently exist) would not help with the cost or reduce the cost of acceptance. It said this was especially true for smaller merchants who have fewer resources to focus on payment optimisation strategies and have a higher risk of card abandonment.[360]

9.54 A stakeholder [✂] said that it supported our interim view not to pursue initiatives on encouraging cross-border surcharging or other forms of steering as a response to the increase in UK-EEA IFs. [✂] agreed with us that surcharging would create friction in the customer journey, impose additional costs on merchants and potentially place UK merchants at a competitive disadvantage to EEA merchants. [✂] also said that it would be contradictory to encourage surcharging for this specific transaction corridor while the UK government has clearly recognised the benefits of prohibiting surcharging consumer cards in the UK in its payments landscape review.[361]

9.55 A merchant [✂] agreed with us, noting that surcharging penalises customers based on their location and would not provide a fair outcome in the payments market.[362]

9.56 A trade association representing tech startups [✂] agreed with us, noting that a majority of SMEs would not be able to introduce surcharging. It said SMEs would be running the significant risk of customer abandonment and losing business to larger merchants who are able to absorb the cost of the fee rises if they introduced surcharging.[363]

359 MR22/2.6 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023), page 120, question 15.

360 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

361 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

362 Stakeholder response to MR22/2.6 dated 2 February 2024 [✂].

363 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

9.57 A merchant [✁] agreed with us that surcharging and steering are unlikely to remove the need for regulatory intervention.[364]

Stakeholders who disagreed with our provisional conclusion

9.58 An issuer [✁] disagreed strongly with our interim view on steering and surcharging and proposed a surcharging remedy option. It submitted that, instead of reducing interchange by introducing a price cap on outbound IFs, we should work to develop a framework to enable UK merchants to surcharge for EEA to UK CNP transactions (and RoW to UK CNP transactions).[365] It said that our role in this would be to facilitate technical implementation by acquirers and provide legal certainty to ensure merchants feel comfortable applying a surcharge 'at a level which would be seen by the PSR as a "cost" as required by regulation.'[366] It noted that this would allow UK merchants to offset the full cost of interchange and other merchant acceptance fees for EEA to UK CNP transactions.[367]

9.59 The issuer [✁] went on to say that enabling such a surcharging option would:

a. **Support our objective of reducing the costs associated with EEA to UK CNP transactions:** It said that surcharging would provide an immediate mechanism for cost offsetting instead of modifying the IF, especially for small and medium merchants who are likely to be on standard or blended pricing with acquirers.[368] It told us that the surcharging option creates a fair mechanism for all merchants, regardless of their ability to negotiate rates with acquirers or if they are on IC+/IC++ pricing. It went on to say that smaller merchants on blended pricing would be able to surcharge on these transactions and cover their costs rather than rely on acquirers passing through the savings.[369] It finally noted that UK merchants would maintain control over whether they wish to surcharge or not depending on their individual circumstances – for instance, a merchant with limited EEA CNP transactions may decide against implementing a surcharge given the negligible impact of outbound transactions on their cost base.[370]

b. **Support our ability to implement a solution quickly:** The issuer [✁] noted that, while surcharging of EEA to UK CNP transactions is legal today, there are several barriers that have limited merchant adoption of the practice and that we should help remove.[371] It said a technical implementation would need to be facilitated so merchants can identify EEA cards, which we could expedite by either coordinating with UK acquirers or issuing a specific direction.[372] It also said we should provide legal certainty as part of our final report indicating our finding of a standard minimum cost.[373] It said UK merchants could use this finding to clearly communicate to any EEA

364 Stakeholder response to MR22/2.6 dated 25 February 2024 [✁].

365 Stakeholder submission dated 22 May 2024 [✁].

366 Stakeholder submission dated 22 May 2024 [✁].

367 Stakeholder submission dated 22 May 2024 [✁].

368 Stakeholder submission dated 22 May 2024 [✁].

369 Stakeholder submission dated 22 May 2024 [✁].

370 Stakeholder submission dated 22 May 2024 [✁].

371 Stakeholder submission dated 22 May 2024 [✁].

372 Stakeholder submission dated 22 May 2024 [✁].

373 Stakeholder submission dated 22 May 2024 [✁].

consumers that there will now be increased costs in the form of a surcharge when using Visa or Mastercard cards for an online transaction.[374] It told us that the impact on acquirers and issuers would be minimal since surcharging is an existing mechanism and that cross-border purchasers are likely to accept it since it would be a small fee and these consumers are used to paying additional costs (like shipping) for online transactions.[375] It added that merchants could also bundle the surcharge with shipping and handling costs if they felt it necessary.[376]

c. **Shield us from potential negative EEA reactions:** The issuer [✂] submitted that enabling surcharging for other international transactions alongside EEA to UK CNP transactions would reduce the risk of EEA Member States reacting negatively to EEA cardholders being treated discriminatorily, as compared to a remedy focused on outbound IFs such as a price cap. It said that EEA Member States would also be less likely to receive complaints from EEA card issuers as the proposal would not have a direct financial impact on them.[377] It also noted that only EEA consumers making EEA to UK CNP transactions would bear the surcharging costs, as opposed to a price cap which would force issuers to subsidise EEA to UK CNP transaction costs from their general fees and charges applied to all their EEA consumers.[378]

d. **Support innovation in UK payments to reduce reliance on cards:** The issuer [✂] said that maintaining the current interchange framework for cards and allowing UK merchants to recover their costs for UK to EEA CNP transactions via surcharging would support the adoption of alternative, non-card payment solutions. It told us that, in such a situation, alternative payment innovators would have greater scope to create payment solutions which provide similar levels of customer protection as cards in a commercially sustainable way.[379] It added that surcharging could also drive consumers to alternative payment methods which are cheaper for the merchants to accept, if those alternatives are not also surcharged.[380]

e. **Be the most profitable outcome for UK merchants:** The issuer [✂] estimated that enabling UK merchants to surcharge EEA to UK CNP transactions would allow them to offset circa £203 million per annum in transaction costs (assuming 100% uptake of surcharging at 1.15% for debit and 1.5% for credit). It told us this benefit would be shared by all merchants, including smaller ones on blended or standard contracts. It also said surcharging at these rates would allow UK merchants to fully neutralise IF costs for EEA to UK CNP transactions, compared with a domestic transaction.[381]

9.60 The issuer [✂] also provided us with several examples of how surcharging could work for an online transaction between a UK merchant and EEA cardholder, which we have summarised below in Table 4.[382]

374 Stakeholder submission dated 22 May 2024 [✂].

375 Stakeholder submission dated 22 May 2024 [✂].

376 Stakeholder submissions dated 27 June 2024 and 5 July 2024 [✂].

377 Stakeholder submission dated 22 May 2024 [✂].

378 Stakeholder submission dated 22 May 2024 [✂].

379 Stakeholder submission dated 22 May 2024 [✂].

380 Stakeholder submission dated 27 June 2024 [✂].

381 Stakeholder submission dated 22 May 2024 [✂].

382 Stakeholder submissions dated 27 June 2024 and 5 July 2024 [✂].

Table 4: A simplified example of how an online transaction between UK merchant and EEA cardholder with surcharging enabled at 1.15/1.5% may work

Step 1	EEA cardholder is shopping online with UK merchant. They proceed to checkout with £100 of goods in their basket.
Step 2	The UK merchant displays a notice on their checkout page that EEA cards will be subject to a surcharge at 1.15/1.5% depending on whether a debit or credit card is used.
Step 3	The UK merchant identifies whether the cardholder is using an EEA card by: • the shipping/billing address entered by the cardholder • the first six to eight digits in the card number, which indicate which institution issued that specific card. These digits are known as the bank identification number (BIN). To check this, the merchant would need to either maintain and check BIN tables on their website or pay for a third party to do so. Alternatively, the consumer is sent to a payment gateway managed by the merchant's card acquirer. The acquirer identifies whether the cardholder is using an EEA card by the card's BIN.
Step 4	The EEA cardholder is informed by either the merchant's website or the acquirer portal of a surcharge of £1.15/£1.50 and a final price of £101.15/101.50 (depending on whether they used a debit or credit card). The EEA cardholder is asked to complete the transaction.
Step 5	The EEA cardholder either proceeds with the transaction or abandons it.

Our response

9.61 Having carefully considered the points raised by the issuer ([✂]) in favour of a surcharging remedy, we do not agree that it would be an appropriate or effective remedy in the context of UK-EEA CNP transactions. We consider each of its points below:

a. We do not agree with the suggestion that we should develop a framework to enable UK merchants to surcharge for EEA to UK CNP transactions (and RoW to UK CNP transactions). As stated above and in Chapter 4, at paragraph 4.56, imposing a card surcharge (like other steering strategies) raises the risk for merchants that it will actively deter the consumer from completing a transaction and result in the merchant losing the transaction altogether. We do not consider that having a PSR approved level of surcharge would change customer behaviour to any material extent to mitigate the risk to merchants of transaction abandonment. In this regard, we agree with the point raised by a stakeholder in paragraph 9.54 that it would be contradictory to encourage surcharging for this specific transaction corridor while the UK Government has clearly recognised the benefits of prohibiting surcharging consumer cards in the UK. Introducing a surcharge in this corridor would be introducing a new payment structure for UK-EEA transactions, not used for equivalent transactions within the UK, which simply passes on the adverse effect directly to customers without addressing the finding that fee levels are unduly high.

b. We have not seen any persuasive evidence that surcharging would result in the beneficial outcome for small merchants claimed by the issuer. Customers would be unlikely to appreciate the change: they would face a surcharge at some merchants and either pay more than they expected or face the inconvenience of finding somewhere else to complete their purchase. Surcharging would then put smaller merchants at a competitive disadvantage to larger merchants. This is because (as other stakeholders like [✁] mentioned)[383] smaller merchants who introduced surcharging to cover their costs would likely lose business to merchants who could afford not to surcharge and who absorb the cost of fee rises to minimise cart abandonment risks. Smaller merchants may also choose not to surcharge as, while they may undertake CNP cross-border transactions, the volume and values might be too low to benefit from surcharging or take this risk of abandonment. In effect the surcharging approach would either reduce consumer choice and convenience, by introducing a surcharge which might lead to frustration and abandonment, or lead to merchants having to absorb an unduly high fee.

c. We have considered the submission that a surcharging remedy could be implemented relatively quickly. We note that uptake of such a remedy would be dependent on merchant behaviour and decision making. As explained in Chapter 4 (paragraphs 4.51 to 4.74), currently steering (including surcharging) is not widely used, also on the basis of the country where the card is issued, because doing so is not always feasible or desirable for a merchant. We consider that, even in the scenario where we promote surcharging as a remedy, there would not be a quick uptake by merchants of surcharging since many of the issues currently disincentivising them from adopting surcharge would continue to exist. We set these issues out further below.

d. We consider that the technical changes required for both acquirers and merchants would add costs for the parties already facing higher IF costs. Table 4 above gives a breakdown of a hypothetical online transaction between a UK merchant and EEA cardholder with surcharging enabled. As set out in steps 2 and 3 in the table, merchants would either need to make a technical change to their website to help identify whether the cardholder is using an EEA card in order to apply a surcharge correctly or rely on their acquirer's payment portal. In the first case, it would be down to each merchant to change their own website (if they decide to) and pay the associated development costs for checking and maintaining up to date BIN tables. In the second case, acquirers may introduce further charges to maintain this functionality for the merchant. We do note that [✁] told us it would not charge its merchants to identify EEA cards[384], but we consider it possible that other acquirers would.

e. We have addressed the submission that a price cap on outbound IFs could result in reciprocal action by the EU in relation to inbound IFs below. As we state at paragraph 9.120 below, action by the EU (or other jurisdictions) in relation to inbound IFs would likely represent the EU (or other jurisdictions) responding if they identify a similar set of facts and consider it appropriate to take action. We have also addressed the concern that a price cap might have significant adverse impacts on competition between Visa and Mastercard and other schemes. As we note at paragraph 9.103 below, we have seen no evidence that the introduction of the EU IFR in 2015 led to any such competitive advantage for American Express over Mastercard and Visa.

383 Stakeholder response to MR22/2.6 dated 31/01/2024 [✁].

384 Stakeholder submission dated 5 July 2024 [✁].

We also note the comment that only EEA consumers making outbound transactions would bear the additional surcharging costs under a surcharging remedy, whereas, under a price cap, issuers would be forced to subsidise outbound costs from their general fees and charges applied to all their EEA customers. It is not clear to us that issuers would be forced to subsidise outbound costs under a price cap remedy. We note our findings in Annex 2 where we conclude that, for one issuer, current outbound IF levels for debit cards (115 basis points) are higher than their total costs reported for EEA to UK CNP transactions, and significantly higher when the incentives and rebates on scheme and processing fees are accounted for.[385]

f. We note the submission that a surcharging remedy that maintains the current interchange framework and allows merchants to recover costs would support innovation in UK payments. Given points (a) to (e) above, we consider that most merchants would be unlikely to implement a surcharge on UK-EEA CNP transactions, regardless of whether innovation in payments would be supported. In addition, we consider that maintaining the current interchange framework with the related increases in IFs on cards will, if anything, make issuers less interested in alternative payment methods, which may not offer similar IFs on transactions.

g. We have not seen any persuasive evidence that surcharging would be the most profitable outcome for UK merchants. We consider that encouraging surcharging might further harm UK merchants in the form of lost sales. This would be inconsistent with our regulatory principle of the desirability of sustainable growth in the UK economy in the medium or long term.[386] We concluded in Chapter 4 (see paragraph 4.71) that, in deciding whether to steer consumers towards a specific payment method (including by imposing a card surcharge), merchants need to weigh lower IFs against the risk of lost revenue from reduced conversion rates. Any appreciable fall in conversion rates is likely to remove merchants' incentives to use such a response to outbound IF increases. Indeed, merchants have told us they do not typically steer.[387] We also consider that surcharging could put UK merchants at a competitive disadvantage to their EEA competitors. An EEA consumer making an online purchase from a UK merchant who saw the price change once they had entered their bank details might abandon the transaction (see paragraph 9.38 above) and buy instead from an EEA merchant. This risk applies to future and repeat business from EEA customers. Given this, and points (a) to (e) of this paragraph, we consider that most merchants would be extremely unlikely to implement a surcharge on UK-EEA CNP transactions even if steps were taken to make it easier for them to do so on a technical level. Therefore, it is unlikely to be the most profitable outcome for UK merchants.

Our final view

9.62 For the reasons set out above, our final view is that encouraging surcharging and other forms of steering would not be an effective remedy to the detriment we identify in the market. Encouraging surcharging would also likely have additional negative effects. We have therefore dismissed this option as a potential remedy in this review.

385 Annex 2, paragraph 2.94.

386 FSBRA, section 53(c).

387 See paragraphs 1.119, 1.120, 1.131 and 1.145 in Annex 1.

Changes to card scheme rules

9.63 Under the heading of regulation, our interim report considered two forms of potential remedy: (i) changes to the card scheme rules (ii) a price-cap remedy.

9.64 In our interim report, we considered whether we could change card scheme rules to:

- permit cross-border acquiring
- classify transactions as domestic or cross-border based on acquirer location rather than merchant location

9.65 In theory, this could enable UK merchants to partner with EEA acquirers and their UK-EEA transactions to be classed as domestic EEA transactions.

9.66 Mastercard and Visa set the criteria for merchant location in their rule guides and the card schemes' classifications of transactions as either domestic (including EEA intra-regional) or cross-border is linked to merchant location.[388] The EU IFR also sets criteria for merchant and acquirer location for the intra-EEA caps to apply.

9.67 Card schemes may also require merchants to disclose their physical location so that relevant parties can:

- determine whether transaction is domestic or cross-border[389]
- dispute the location assigned by the acquirer and determine the 'correct' location[390]

9.68 Our view as set out in our interim report was that it is unclear how such a potential remedy might be implemented in line with existing regulation.

9.69 Even if this potential remedy could be implemented, our view was that it would put the onus on, and add costs to, UK merchants. They would need to either use an EEA acquirer for all of their transactions, including UK domestic transactions, or adopt a second acquirer only for EEA retail CNP transactions.

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388 For example, rule 5.5 (merchant location) in Mastercard's *Mastercard Rules* (June 2023) states that merchants and acquirers must satisfy the following criteria:
- *The merchant conducts business locally*
- *The merchant holds a permit to operate locally*
- *The merchant complies with local tax laws and regulations*
- *The merchant is subject to local consumer laws and courts*

Similarly, rule 1.5.1.2 of Visa's *Visa Core Rules and Visa Product and Service Rules* (October 2023) says that an acquirer must assign the country of the merchant's principal place of business as their location: *'For a Card-Absent Environment Transaction, the Acquirer must assign the country of the Merchant's Principal Place of Business as the Merchant Outlet location.'*

389 Mastercard (*Transaction Processing Rules,* June 2023) defines 'Domestic/Intra-country Transaction' as being when a transaction occurs at a merchant with a card issued in the same country (page 380). 'Cross-border transactions' are transactions where the merchant is located in a different country from the country where the card was issued (page 373).

Visa (*Visa Core Rules and Visa Product and Service Rules*, October 2023) defines 'Domestic Transaction' as when the card is issued from the same county as where the merchant is located (page 861).

390 Stakeholder response to PSR questions dated 11 January 2023. [✂].

9.70 We observed that it was unclear whether EEA acquirers would see the benefits of this additional business as being worth the cost to them. We considered that it was likely that an EEA acquirer would need to be authorised by the FCA and it was unclear whether changes to scheme rules would suffice to enable cross-border acquiring.

9.71 Given the processing of UK-EEA transactions would likely occur in another jurisdiction outside of the UK under such a potential remedy, we considered effective monitoring to be unlikely.

9.72 Our interim view, therefore, was that these kinds of changes to card scheme rules would not be effective in addressing the issues. We stated that other potential remedies were likely to be less complex to implement and less likely to place significant burdens on merchants.

Stakeholder feedback on changes to card scheme rules

9.73 Five stakeholders responded to our interim report consultation question on changes to card scheme rules.[391] Three agreed with our provisional conclusion that the amendments to these rules we considered would likely not address our concerns. Two stakeholders disagreed with our provisional view. None mentioned alternative amendments to card scheme rules we should consider. One stakeholder who disagreed noted they believed cross-border acquiring could be done already. We explore their views in more detail below.

9.74 We note that neither Mastercard nor Visa answered our question on changes to card scheme rules in their responses to our interim report consultation.

Stakeholders who agreed with our provisional conclusion on changes to card scheme rules

9.75 A merchant [✂] said it agreed that the potential amendments to card-scheme rules we considered would be unlikely to address the concerns we had identified.[392]

9.76 Another merchant [✂] agreed that any changes to card scheme rules to enable cross-border acquiring would not negate the operational and financial challenges involved.[393]

9.77 A stakeholder [✂] agreed that it was unclear how this remedy could be implemented in line with existing regulation. It added that we should carefully consider the potential for broader unintended consequences if it were to pursue implementing such a remedy, particularly with regard to additional cost and complexity for merchants and other industry participants.[394]

391 MR22/2.7 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023), page 120, question 16.

392 Stakeholder response to MR22/2.6 dated 25 January 2024 [✂].

393 Stakeholder response to MR22/2.6 dated 2 February 2024 [✂].

394 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

Stakeholders who disagreed with our provisional conclusion on changes to card scheme rules

9.78 An acquirer [✁] stated that we did not sufficiently explore the potential of implementing changes to card scheme rules to enable cross-border acquiring. It said that enabling acquirers to use any cross-border presence could be an important ongoing tool for them to mitigate continuous fee increases by the schemes.[395] It submitted that we should consider how to enable cross-border acquiring under regulation and card scheme rules while any long-term remedy is considered. It stated enabling cross-border acquiring would allow acquirers to assess the costs and benefits of investing to enable them to cross-border acquire. It concluded that exploring and enabling cross-border acquiring should be done alongside any price cap remedies to enable acquirers to respond and mitigate any increases while they wait for regulatory intervention to come into effect.[396]

9.79 An issuer [✁] told us that cross-border acquiring is already possible with many significant EU acquirers offering services in the UK. It said that, while FCA authorisation would be needed to offer acquiring services in the UK, this would not be a material barrier for new entrants and UK and EU regulators could address this barrier if needed (for instance, by offering passporting for EEA or UK regulated acquirers).[397] It noted that larger merchants would be the ones most likely to benefit from us taking further action to enable cross-border acquiring.[398]

Our response on changes to card scheme rules

9.80 We carefully considered the positions of these two stakeholders ([✁] and [✁]). We still believe that enabling cross-border acquiring carries several risks and implementation issues, including that:

- FCA authorisation would likely be required. Per the FCA's guidance on the territorial scope of the Payment Services Regulations 2017[399], only activities undertaken in the UK are within the FCA's regulatory perimeter. The FCA supports the view that the location of the payment services activity depends on where the performance of the functions that characterise the activity take place.[400] Given this, we consider that cross-border acquiring would therefore likely be within the FCA's regulatory perimeter.

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395 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

396 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

397 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

398 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

399 FCA, *PERG 15.6* (January 2021), questions 45 and 46.

400 When we asked the FCA how it determines where a payments service is carried on, it said it considers that the Commission Interpretive Communication (Freedom to provide services and the interest of the general good in the Second Banking Directive (97C 209/04)) provides a useful starting point. This communication indicates that 'In order to determine where an activity was carried on, the place of provision of what may be termed the "characteristic performance" of the service, i.e. the essential supply for which payment is due must be determined.' The regulated activity acquiring of payment transactions is defined in regulation 2 of the Payment Service Regulations 2017 as 'a payment service provided by a payment service provider contracting with a payee to accept and process payment transactions which result in a transfer of funds to the payee'. It is the acquirer's responsibility to consider whether their activities fall within the FCA's regulatory perimeter based on their specific circumstances, including where each part of the regulated activity takes place.

- UK merchants would either need to send all their transactions (including UK domestic transactions) to an EEA-based acquirer or use a second acquirer for EEA outbound transactions only. Given that these EEA acquirers would likely need to be authorised by the FCA in addition to their relevant local competent authority, EEA acquirers and UK merchants would therefore face a complex regulatory environment with rules that may vary between the UK and EU.
- a payment institution must be a body corporate under UK law in order to be authorised as a payment institution under the Payment Services Regulations 2017.[401] We consider this would limit the number of EEA payment institutions prepared to enter the UK acquiring market given the likely small gains at stake for outbound IFs relative to the costs these acquirers would have to incur to enter.
- offering passporting for EEA regulated acquirers could impose additional costs for UK merchants or disadvantage UK acquirers, as merchants would either need a second acquirer or alternatively send all their transactions through an EEA based acquirer (which may have unintended negative consequences for UK-based companies).

9.81 We additionally note the comments from two stakeholders [✂] on the likely cost and complexity for merchants to gain any benefits from this remedy (referred to above at paragraphs 9.76 and 9.77).

Our final view

9.82 We have considered the feedback we received from stakeholders on this topic. Our final view is that the amendments to card scheme rules we considered to enable cross-border acquiring would not be effective in addressing the concerns we see. We have therefore dismissed this option as a potential remedy in this review.

9.83 We have also reflected on whether or not the options considered above might be effective if utilised in combination with each other. However, for the same reasons as set out above, we do not consider that adopting two or more of these in combination would prove an effective remedy.

Setting a price cap

9.84 Our interim report considered in principle whether a cap on the level of UK-EEA consumer CNP outbound IFs set by Mastercard and Visa may be an appropriate and effective remedy. We also set out some initial considerations as to what such a remedy might look like in practice.

9.85 In the interim report we expressed the preliminary views that:

a. Restricting the maximum level of outbound IFs would likely be effective in mitigating the impact on service users identified in this report, specifically our finding that prices are unduly high and may further increase for UK merchants.

b. A price cap would not address the underlying cause of the detriment we provisionally identified (namely the lack of competitive constraint on the acquiring side).

401 The Payment Services Regulations 2017, paragraph 6(4).

c. Further detailed work would need to be carried out to consider the most effective way to design and implement any potential remedies, including their proportionality.

9.86 We also noted that this type of remedy could continue for as long as appropriate to address the detriment that we identified to service users.

9.87 In this section, we have concluded that a price cap is an appropriate remedy and that we should take action to implement such a remedy on the basis that

a. A price cap set at an appropriate level would in principle be effective in addressing our finding that current levels of UK-EEA cross-border IFs are unduly high. The benefits would furthermore be to a large extent passed on to UK merchants and their customers.

b. A price cap set at an appropriate level is unlikely to cause any material unintended consequences that would outweigh the benefits of the remedy and it could be implemented in an effective manner (although further work needs to be carried out to identify the appropriate level of the cap and design features);

c. We have not identified other effective remedies that would address the detriment we have identified in this report.

9.88 In the section below we set out the following

a. Our views on the aim of the price cap remedy and our approach to assessing its effectiveness

b. Our assessment of stakeholder's submissions on the principle of a price cap and the risk of unintended consequences.

c. Our assessment of stakeholders' submissions on whether the benefits of a price cap would be passed on to UK merchants and their customers as intended.

d. Our assessment of technical and operational challenges in implementing the price cap.

e. Our assessment of other legal and practical challenges in designing and implementing a price cap.

9.89 In the interim report, we further set out initial views on the appropriate level for a price cap, our proposed staged approach of the price cap remedy and further design considerations. We set out responses we received on whether to do a staged cap and if so at what level in a separate consultation document published alongside this report.[402] That consultation also seeks more evidence to inform thinking on the appropriate level of any staged cap. We will also consult in quarter 1 on the methodology for calculating a price cap.[403]

402 See CP24/14 Remedies consultation (December 2024), Chapter 3.

403 See CP24/14 Remedies consultation (December 2024), Chapter 7.

Aim of a price cap remedy and our approach to assessing its effectiveness

9.90 By design, a price cap remedy seeks to ensure that customers do not pay unduly high prices for a given product or service. As such, it is in principle effective in the sense that it addresses directly the type of adverse market outcome (UK-EEA cross-border IFs being unduly high) and detriment we have identified in this report.

9.91 We note that this type of remedy does not address any feature of the market which may give rise to such unduly high prices (or any other adverse effect on competition, service users or innovation) – it merely addresses the adverse effects arising from these. Remedies that are capable of addressing such features directly may be considered more effective or less onerous than a price cap. However, for the reasons outlined above, we have not identified such an alternative remedy that would be effective in addressing the issues we have identified.

9.92 We further note that, in the EU, price caps have been applied by the European Commission both to intra-EU (through the EU regulation) and international corridors (through commitments given within the context of an antitrust enforcement action) and that therefore in principle it should be possible to design an appropriate remedy of that nature for the UK-EEA corridor.

a. To date we have not had reason to believe that the existing price caps are not being complied with (we are responsible for monitoring compliance with the domestic price cap).

b. As set out in this final report, developing a suitable methodology and collecting the relevant data specific to the UK-EEA corridor for setting up an appropriate price cap for this will take time, which might affect the timeliness (and therefore effectiveness) of the remedy, in particular if no remedy is imposed while such work is carried out (we will consult separately on that issue). However, we have seen no evidence suggesting that developing such a methodology and collecting such data would not be possible within a reasonable timeframe, and we have not identified any other effective (and therefore no other more timely) remedy.

9.93 Nevertheless, a price cap may raise some challenges in terms of design and implementation, making the remedy ineffective or disproportionate. This could be the case for example if:

a. the price cap remedy were to give rise to material unintended consequences (for example if a price cap remedy were to cause some distortions in the market that negatively affect competition or service users)

b. design and/or implementation challenges were to prevent the expected benefits to materialise or be passed on to service users (including any reason specific to the UK-EEA corridor or to us that would prevent a price cap remedy being implemented in an effective manner)

9.94 In view of the above, in order to determine whether a price cap is an appropriate remedy, we assess below stakeholders' submissions on the principle of a price cap and on the possible design and implementation risks arising from it set out at paragraph 9.93.

9.95 Having assessed these in the round (and taking into account the experience set out in paragraph 9.92), we did not consider it necessary to seek to determine the appropriate level or more detailed design aspects of the price cap (including our proposal to have a two-staged approach to implementation to improve the timeliness of the remedy) in order to conclude that a price cap remedy would be appropriate and that we should take action to implement such a remedy.[404]

Stakeholders' submissions on the principle of a price cap remedy and possible unintended consequences

9.96 Several stakeholders shared their views on our provisional proposal in the interim report of a cap on the level of UK-EEA consumer CNP outbound IFs set by Mastercard and Visa. We engaged with them through various channels: seventeen respondents provided written representations, including one trade association that submitted separate responses for its acquirer and issuer members. Additionally, we received late written responses from seven trade associations, which we invited to a roundtable discussion, and a letter signed by seven Members of the European Parliament (MEPs), representing different countries. We also engaged with both card schemes through oral representations and bilateral meetings.[405]

9.97 Nine of these stakeholders (made up of two acquirers, a merchant, a trade association speaking on behalf of its acquirer members, a trade association speaking on behalf of EEA acquirers, three trade associations speaking on behalf of merchants, and a trade association speaking on behalf of tech startups and scaleups) agreed that a price cap was needed and/or would be an appropriate remedy.

a. An acquirer [✁] said that our proposed approach to remedies will, in its view, 'benefit all participants of the card payment market.'[406] Another acquirer [✁] said it agreed with us that direct price intervention is necessary.[407]

b. A trade association speaking on behalf of its UK acquirer members [✁] said its members were supportive of reducing cross-border IFs as it will ultimately benefit merchants.[408]

c. The BRC said it was supportive of a cap on UK-EEA cross-border IFs[409] and that its members were relieved to see that we intend to intervene.[410]

d. A trade association speaking on behalf of merchants in the EEA, EuroCommerce, agreed with the principle of a price cap intervention.[411] It said that 'Visa and Mastercard have immediately exploited the fact that the UK left the EU to raise their interchange

404 As noted above, our assessment of these specific design issues (including level of the cap and proposal for a two stage implementation) and relevant stakeholders' submissions made in response to the interim report will be set out separately for further consultation.

405 MR22/2.6 *Market review of UK-EEA cross-border interchange fees interim report* (December 2023), chapter 9, paragraphs 9.41 to 9.45.

406 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

407 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

408 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

409 Stakeholder response to MR22/2.6 dated 26 January 2024 [✁].

410 Stakeholder response to MR22/2.6 dated 26 January 2024 [✁].

411 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

fees, although materially nothing changed in payments between the EEA and the UK'.[412]

e. Another trade association speaking on behalf of merchants [✂] said it supports our proposal to introduce a price cap to protect UK small businesses from overpaying on IFs.[413]

f. A merchant [✂] said a cap is the most effective way of achieving fair UK-EEA cross-border IFs.[414]

g. A trade association, speaking on behalf of tech startups, [✂] said that 'direct regulator action is required to reduce the fees that have risen'.[415]

h. A trade association speaking on behalf of EEA acquirers [✂] strongly supported the imposition of a cap.[416]

9.98 Eight stakeholders raised concerns with a price cap remedy on outbound IFs (or aspects of it). Comments were received from two issuers, a trade association acting on behalf of its issuer members, a trade association representing card issuers, card acquirers and card schemes, a trade association representing EEA issuers, a card scheme and two other stakeholders.

9.99 We address these representations thematically.

Suggestion that a price cap on outbound IFs will distort competition and put EEA issuers at a disadvantage versus (i) competitors like American Express and (ii) peers in non-EEA markets

9.100 An issuer [✂] said a cap would distort competition and put EEA issuers at a disadvantage to (i) peers in non-EEA markets who will continue to receive current IF rates and (ii) competitors like American Express who will be exempt. It noted that our data shows non-Visa and Mastercard schemes already hold 21% market share for CNP EEA to UK transactions by value, and that capping only part of the market could have serious competition implications for EEA payment and broader retail banking services markets. It went on to say that the likely shift by consumers to uncapped alternatives (such as American Express) would reduce any cost saving for merchants since many of the alternatives may be priced higher than Mastercard or Visa.[417] The stakeholder [✂] also said that a shift to uncapped alternatives, such as American Express, which may be priced higher, may significantly reduce any potential cost reductions for UK merchants of a price cap.[418]

9.101 Six EEA trade associations (Financial Services Ireland, the French Banking Federation, the European Banking Federation, Payments Europe, the Lithuanian Banking Association, and the Romanian Association of Banks) said that imposing a price cap only on EEA issuers (while cross border transactions involving UK and RoW issuers remain uncapped) will put

412 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

413 Stakeholder response to MR22/2.6 dated 2 February 2024 [✂].

414 Stakeholder response to MR22/2.6 dated 2 February 2024 [✂].

415 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

416 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

417 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

418 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

existing EU payments companies at a disadvantage and undermine the scope for new EU card-based fintechs to start up or scale. [419]

9.102 Three of these trade associations (Financial Services Ireland, the French Banking Federation (FSI), and the Lithuanian Banking Association) also argued that a price cap would distort the market in favour of three-party schemes[420], while Financial Services Ireland and the Lithuanian Banking Association also said that innovation and competition would be adversely affected by the cap.[421]

9.103 We note that there is limited evidence of significant changes taking place in market share since Mastercard and Visa increased their outbound IF levels. We do note that in the period 2019 to 2022 (the period leading up to and including the changes in cross-border IF levels) American Express more than doubled its market share in this corridor. However, American Express still has a far smaller market share in the UK-EEA outbound CNP cross-border space than Mastercard and Visa. As highlighted in the interim report, non-Visa and Mastercard schemes accounted for just 21% (by value) of total transactions in 2022, while Mastercard and Visa, together, accounted for the remaining 79%.[422] We have also seen no evidence that the introduction of the EU IFR in 2015 led to any competitive disadvantage to EEA issuers compared to American Express. The issuer also said that a shift to higher priced un-capped alternatives, such as American Express, may significantly reduce any potential cost reductions for UK merchants of a price cap. We have not seen any persuasive evidence in support of this submission. In the case of American Express, we found at paragraph 5.27 that a decrease in Mastercard and Visa IFs is likely to induce American Express to decrease, at some point, the merchant service fee (which includes their implicit IF) to ensure that they can still provide an attractive proposition to merchants.[423]

9.104 We have also considered whether a cap on outbound IFs might put EEA issuers at a disadvantage versus peers in other markets such as the US or China. We consider that it is unlikely that EEA customers would be able to obtain such uncapped cards to use for cross-border transactions because of difficulties taking out a card without a residential address in that country. We therefore do not see EEA issuers facing a competitive disadvantage to retain these customers. We see no significant disadvantage to EEA issuers in this respect from having lower IFs than those for EEA transactions with the rest of the world.

9.105 We note that following the increases in IFs by Mastercard and Visa, UK merchants are at a competitive disadvantage for transactions with EEA customers relative to EEA merchants. It is of course open to the EU to reduce levels of inbound IFs should it wish to do so,

419 Stakeholder response to MR22/2.6 dated 17/07- 01/08/2024 [✂]

420 Stakeholder response to MR22/2.6 dated 17/07- 01/08/2024 [✂]

421 Stakeholder response to MR22/2.6 dated 17/07- 01/08/2024 [✂]

422 PSR analysis of data on transaction values submitted by acquirers through the section 81 notice, and by Mastercard, Visa and American Express.

423 For example, a study in Australia (pages 6 to 9) suggested a degree of correlation between the schemes' price changes and those of American Express. The study argues that though American Express is free from the regulatory constraints applied to four-party schemes, it has experienced significant indirect effects from the introduction of caps on Mastercard and Visa. American Express's average merchant service fee has fallen more than Visa's and Mastercard's since the first regulation on IFs in Australia. Another, very recent example is from New Zealand, where caps on debit cards introduced in 2022 led to a significant reduction of the IFs and the MSCs related to Mastercard and Visa cards. A New Zealand Commerce Commission document (Retail Payment System Consultation Paper, paragraph 4.73) notes that when caps were introduced, 'American Express reduced its merchant service fees upon the initial pricing standard coming into force in 2022.' They added: 'We would expect it [American Express] to further reduce its fees in response to any further regulation.'

which would lead to lower costs to EEA merchants and their customers. Finally, as regards transactions between the UK and rest of the world, we note that our terms of reference for this review are focused on IFs for UK/EEA transactions (and whether the increases in such UK/EEA IFs were justified) and not UK/rest of the world transactions. Any further evidence we receive on potential distortions to competition in the course of our remedies consultation will be considered in the context of setting the level of any price cap.

Suggestion that capping issuers' revenues while taking no action to address issuers' costs will harm new entrants and reduce competition and investment in innovation in cross-border payments in the EEA

9.106 An issuer [✂] said it would be unjustified to cap issuers' revenue while taking no action to address their costs, and doing so would harm new entrants and reduce competition and investment in innovation in cross-border payments in the EEA. For this reason, it suggested that we should complete our scheme and processing fees review before taking action on cross-border IFs (the suggestion being that the scheme and processing market review may result in a remedy which might address the loss of revenue to issuers that a price cap on outbound IFs would entail).[424]

9.107 As noted in Chapter 5[425] and Annex 2[426] of this report, the increased income from IFs does not appear to have been used for cross-border IF-specific improvements by issuers (UK or EEA) such as improved fraud prevention. We therefore do not accept that any price reduction through a price cap would lead to reduction in competition or investment in innovation, or harm new entrants. We note that in principle a price that is set too low fails to balance the interests of service users on both side of the market (both the issuing and acquiring side). As set out above, we are proposing to carry out further work to identify an appropriate level of the price cap so as to ensure that the risks and concerns described in this subsection are considered.

Suggestion that a price cap on outbound IFs will result in a reduction in cardholder benefits and/or result in increased cardholder fees

9.108 Four stakeholders including Visa, [✂], seven MEPs and five EEA trade associations said a reduction in outbound IFs resulting from a price cap could result in a reduction in cardholder benefits, such as rewards, or an increase in other fees.

a. On a similar theme related to EEA issuer funding, a stakeholder from the travel and hospitality sector [✂] said that our proposed price cap on cross-border (CNP) IFs could have negative implications for the UK's tourism and aviation industries. It noted that IF caps could potentially lead to the removal or scaling back of credit card rewards offered by issuers, pointing to the example of debit card rewards disappearing 'overnight' in the US after caps were enacted there. It told us that a reduction or removal of these financial services loyalty programmes would then lead to reduced travel spending.[427]

424 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

425 See paragraph 5.66 in Chapter 5.

426 See Annex 2, paragraph 2.27.

427 Stakeholder response to MR22/2.6 dated 02/02/2024 [✂].

b. Similarly, Visa said that disrupting the balancing role of interchange (such as by a reduction in outbound IFs) could lead to unintended consequences, such as a rise in cardholder fees and/or reduction in cardholder benefits, a growth in transaction declines, greater numbers of lost sales and/or higher costs for UK merchants.[428] It also said that the proposed interim cap would cause significant cost and disruption to the global payments ecosystems operated by Visa (and Mastercard).[429]

c. Similarly, Payments Europe, a trade association who represents EEA issuers, acquirers and card schemes said that we seem 'to be concerned about the cost to UK merchants, not taking into account the importance of interchange received by EU issuers'.[430] It said we should not view IFs as a cost to acquirers/merchants that should be regulated to the lowest possible level, but as balancing the interests of all participants in the ecosystem. It said that IFs provide funds that enable issuers to deliver services to cardholders, which in turn benefits merchants by driving sales.[431]

d. One issuer [✂] stated that a cap on outbound IFs could result in EEA issuers needing to increase fees to cover the costs of payments made at UK merchants. This may take the form of a bank-led charge, passed on to consumers, for general banking or payment services.[432]

e. Similarly, six EEA trade associations (Financial Services Ireland, the French Banking Association, Payments Europe, the Lithuanian Banking Association, and the Romanian Association of Banks) said that if the price cap resulted in EEA issuers losing money on each transaction then 'these costs would be passed on to EU consumers, so potentially disadvantaging them by forcing issuers to curtail services or introduce new fees (such as account fees, foreign exchange fees, etc.'[433]

9.109 We have not seen any persuasive evidence that a cap on outbound IFs will lead to a reduction in cardholder offerings and benefits. Indeed, the European Commission's review of the effectiveness of the EU IFR caps said the resulting drop in IF revenue for issuers had not led to a significant decline in the quality of what issuers offer to cardholders.[434] We are not aware of any indication that there was an adverse impact on cardholder fees before the increase in outbound IFs by Mastercard and Visa, or that the increase led to a reduction in such fees or charge.[435] We also consider any hypothetical potential reduction in cardholder benefits or rewards would in any event likely be counterbalanced by the reduced cost burden for UK merchants and (to the extent of pass-through) their customers.

9.110 On that basis we do not accept that a price cap set at an appropriate level would have such unintended consequences.

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428 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

429 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

430 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

431 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

432 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

433 Stakeholder responses to MR22/2.6 dated 17/07- 01/08/2024 [✂]

434 Commission Staff Working Document, Report on the application of Regulation (EU) 2015/751 on interchange fees for card-based payment transactions, dated 29 June 2020, page 8, paragraph 3.

435 We also note the findings of the European Commission in its Report on the application of Regulation (EU) 2015/751 on IFs for card-based payment transactions, which said that the reduction in IFs resulting from the caps in the EU IFR could not be linked with a systematic increase in cardholder fees. Commission Staff Working Document, dated 29 June 2020, page 8, paragraph 3.

Suggestion that a price cap on outbound IFs could exacerbate barriers to finance and/or lead to issuers cutting services (such as fraud prevention) or offboarding customers

9.111 A merchant from the travel and hospitality sector [✂] said that a cap could threaten revenue issuers need to fund fraud prevention efforts and that, absent this funding, issuers could take other measures such as reducing access to credit to those with a limited current credit history. It said this would impact pensioners, those on fixed incomes, young adults, first time credit seekers and under-banked communities most.[436]

9.112 An issuer [✂] raised a similar point and said if a price cap was introduced, some EEA issuers may choose to cut services or offboard certain customers.[437]

9.113 Similarly, in a joint letter seven MEPs also said they were concerned that the cap would 'negatively affect European consumers', and have an impact on 'the provision of low-cost accounts and cross-border payment services to European consumers.'[438]

9.114 We have considered the risk of reduced fraud prevention if a cap was to be imposed on outbound IFs. As we have set out in Annex 2, UK issuers stated that they have not invested the additional revenue from the higher IFs levels to improve fraud prevention.[439] We have no reason to believe that EEA issuers take a different approach. We also note that fraud levels for outbound transactions were declining or were stable before the increases in outbound and inbound IFs by Mastercard and Visa. This indicates that the previous levels of IFs were not limiting investment in fraud prevention.

9.115 We also do not consider that a price cap on outbound IFs for online transactions at UK merchants for consumers with EEA issued cards will have a significant impact on access to credit or result in customers being offboarded. We note that caps on UK-EEA CNP IFs existed until 2021 before the increase in outbound IFs by Mastercard and Visa. We have seen no evidence that these capped levels had an adverse impact on access to credit or that issuers cut services (such as by offboarding customers) or that the 2021 price increase had a positive impact on those factors.[440]

Suggestion that any price cap on outbound IFs should be symmetrical and cover both outbound and inbound IFs

9.116 One trade association, representing EEA issuers [✂] said that 'if a cap were to be implemented, it should be done symmetrically', that is, both for outbound and inbound IFs.[441] It did not elaborate why.

436 Stakeholder response to MR22/2.6 dated 21 March 2024 [✂].

437 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

438 Stakeholder response to MR22/2.6 dated 20/09/2024 [✂]

439 Annex 2, paragraph 2.34.

440 We note the findings of the European Commission in its Report on the application of Regulation (EU) 2015/751 on IFs for card-based payment transactions, which states that following the implementation of the EU IFR there was "no notable development in terms of issuing consumer cards in the EU" including in relation to the total number of issued consumer cards. Further that "almost three-fourth of issuers reported unchanged or improved card benefits, with variety of products and length of interest-free period for credit cards both unchanged." Commission Staff Working Document, dated 29 June 2020, [page 8, paragraphs 3 and 4.]

441 Stakeholder response to MR22/2.6 dated 2 February 2024 [✂].

9.117 As detailed in Chapter 8, we have decided to close our review of inbound IFs on the grounds of administrative priority. In particular, we think that the adverse effects we are seeing for UK service users (organisations that accept cards and their customers) mainly pertain to outbound IFs.[442] Further, there would be significant resource implications in progressing the review on inbound IFs sufficiently to make an evidenced decision on remedies for this corridor. We also note that EU authorities would be well placed to make such an intervention if they deemed it appropriate in the light of the facts specific to that corridor.

9.118 Any perceived harm relating to a lack of symmetry in outbound and inbound IFs may relate to one side being disadvantaged compared to the other. For the reasons set out in paragraphs 9.104 to 9.105, we do not believe this would be the case. In view of the reasons set out above, we do not consider that an asymmetry between levels of fees would distort competition between issuers or exacerbate barriers to cross-border trade/finance. However, in setting an appropriate level for the stage 2 price cap we will continue to consider whether the difference between the proposed level and the level in place for inbound transactions might create unintended consequences. To the extent that EEA merchants would be at a disadvantage compared to UK merchants in transactions with UK customers, it is open to the EU to consider whether to reduce fees on those transactions.

Suggestion that a price cap on outbound IFs will result in retaliatory action regarding inbound IFs and harm to UK issuers

9.119 Two stakeholders mentioned potential retaliatory action by the EU or other jurisdictions and the impact this would have on UK issuers.

a. An issuer [✂] said a cap would either trigger 'retaliatory action by the EEA' which would hurt UK issuers and consumers or would provide a justification for other jurisdictions to apply price caps only on UK issuers.[443]

b. Similarly, a trade association, Payments Europe, who represents EEA issuers, acquirers and card schemes said that if the European Commission chose to reciprocate and applied a price cap in reverse (for example, at 0.2/0.3%), it would severely impact the interchange revenues of UK issuers, which would reduce their ability to invest on behalf of UK merchants.[444]

9.120 Firstly, we do not see potential action by the EU regarding inbound IFs as 'retaliation'. Rather, it would likely represent the EU (or other jurisdictions) responding in a similar way if they identify a similar set of facts.

9.121 Secondly, we acknowledge that a reduction in inbound IFs would reduce revenue received by UK issuers each time their cards are used online at EEA merchants, while reducing the costs for UK cardholders purchasing from EEA merchants in the long run (see also paragraphs 8.9 to 8.12 in Chapter 8). However, as noted in Chapter 5 and Annex 2 of this report, the increased income from IFs does not appear to have been used for improvements by issuers (UK or EEA) such as improved fraud prevention. We therefore do not expect any material adverse effects if inbound IFs were reduced, such as a material reduction in the ability of UK issuers to invest on behalf of UK merchants.

442 Chapter 8, paragraph 8.16.

443 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

444 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

Suggestion that a price cap on outbound IFs will have negligible impact on the cost of acceptance of card-based payments by UK merchants

9.122 One issuer ([✂]) submitted that a cap on outbound IFs will have a negligible overall impact on card acceptance costs for UK merchants. While we agree that not every UK merchant will have a significant number of transactions which incur outbound IFs (and may not necessarily decrease their charges to customers as a result of a price cap), we consider that the additional [✂] [£150 million to £200 million] a year in outbound IFs is a material sum for those UK merchants that have to pay them, particularly for UK SMEs. Not acting would lead to worse outcomes for UK merchants and (to the extent of pass-through) their customers.[445]

Suggestion that any price intervention should take the form of a legally certain regulated price

9.123 A trade association speaking on behalf of its UK issuer members [✂] said its members considered that any cap should be legally certain and immune from further competition law challenge, given that the interchange concept and rates are (even at a prescribed cap) susceptible to legal challenge based on an alleged breach of competition law.[446]

9.124 On a similar theme, an issuer [✂] said we should be seeking to implement a 'legally certain regulated price, rather than a price cap, implemented as a legal requirement' to avoid the significant litigation which has occurred around the IFR.[447]

9.125 As one of the stakeholders ([✂]) acknowledged, this is not within our gift and would require legislative change. Also, we note that domestic IFs have been set up through legislation as a cap. The underpinning EU regulation explicitly notes (in recital 14 of the EU IFR[448]) that the application of that regulation should be without prejudice to the application of EU and domestic competition rules, and would not prevent member states from introducing lower caps. We have seen no evidence that this has caused issues which would justify an intervention through legislation.

Suggestion that price regulation is not an appropriate measure

9.126 An EEA trade association, Payments Europe, said that price regulation was not an appropriate measure to take in a market that was so competitive and evolving so quickly[449]

9.127 As set out in Chapter 4, we have found that the schemes lacked competitive constraints on the acquiring side, leading to unduly high levels of UK-EEA IFs. We have not identified any other effective remedy to address these adverse effects.

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445 Chapter 6, paragraph 6.13.

446 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

447 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

448 Official Journal of the European Union, Regulation (EU) 2015/751 of the European Parliament and of the Council of 29 April 2015 on IFs for card-based payment transactions (text with EEA relevance), paragraph 14.

449 Stakeholder response to MR22/2.6 dated [✂].

Our overall assessment of stakeholders' submissions on the principle of the price cap and on the risk of unintended consequences

9.128 In view of the above, we note that stakeholders on the acquiring side broadly support the principle of a price cap as being effective in addressing the detriment arising from unduly high prices, while we have seen no persuasive evidence to indicate that, in principle, a remedial measure capping Mastercard and Visa outbound IFs would not be an effective remedy.

Pass-through

9.129 Some stakeholders questioned the benefit of a cap to UK merchants, arguing that a reduction in outbound IFs resulting from a price cap on Mastercard and Visa would not have material benefits to UK merchants and (to the extent of pass-through) their customers.

9.130 How, and the extent to which acquirers will pass on savings resulting from a price cap remedy to their UK merchants will depend on the different pricing options for card-acquiring services (that is, pass-through and blended options). The different pricing options are set out in Chapter 3, paragraphs 3.13 to 3.17. We consider below the likelihood of pass-through under both pricing options.

9.131 An issuer [✄] said a cap on UK-EEA outbound IFs will have a negligible overall impact on merchants' costs to accept cards in the UK. It noted that PSR data shows only 3.6% of all UK merchant card transactions were from EEA issued cards and that only 70% of these were CNP.[450] It said that 95% of merchants who are on standard (blended) pricing models would see no benefit from a cap as acquirers are likely to maintain the Merchant Service Charges for these merchants at the same level, while only the largest merchants will see a minor impact. It also said that there is no evidence from previous interchange interventions that merchants pass on price savings to consumers. Owing to this, it said UK merchants are unlikely to decrease their charges as a result of a cap on outbound IFs.[451]

9.132 Visa said that there is no evidence that any reduction in IFs (particularly if only on a temporary basis) would be passed on to UK merchants by acquirers. It added that 'contrary to the PSR's service-user objective, such an outcome is unlikely to be in the best interests of Visa's users'.[452]

IC++ and IC+ contracts (pass-through options)

9.133 By definition, in IC++ and IC+ pricing, acquirers automatically pass any IF charge on to merchants.[453] As detailed in paragraph 6.7 of this report, we found that around 80% of UK-EEA consumer CNP outbound transactions, by value, relate to contracts on IC++ and IC+ pricing. We therefore consider that a reduction in outbound IFs resulting from a price cap remedy would be passed on to merchants who have these types of contracts. We note that merchants on IC++ pricing are typically the largest merchants, generally with an annual turnover above £50 million.[454]

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450 Stakeholder response to MR22/2.6 dated 14 February 2024 [✄].

451 Stakeholder response to MR22/2.6 dated 14 February 2024 [✄].

452 Stakeholder response to MR22/2.6 dated 14 February 2024 [✄].

453 See paragraphs 3.14 to 3.17 in Chapter 3

454 MR18/1.8, *Market review into the supply of card-acquiring services: final report*, page 7, paragraph 1.15 and *CICC (1441-1444) – Judgment (CPO Applications) from 8 June 2023*, paragraph 86.

9.134 We contacted 14 acquirers and asked about the process and nature of the changes that they might need to make when Mastercard and/or Visa change the level of outbound IFs. We also asked about the likely timescales involved. Several acquirers stated that, for customers on IC+/IC++ contracts, there would be no contractual changes required (with some of these acquirers saying there would also be no requirement to give notice of the change to merchant customers [✂]). In these cases, the contractual terms state that IFs would be passed through in line with the levels charged by card schemes [✂].[455] Other acquirers stated that they would be required to give notice of the change. One acquirer [✂] said that it gave merchants on IC++ contracts 30 days' written notice.[456] Another acquirer noted that a two months' written notice period was required to be given to merchant customers on IC++ contracts of any IF change [✂].[457]

9.135 Overall, we consider that an IF reduction in relation to merchants on IC++ and IC+ contracts would be passed through relatively quickly.

Blended contracts

9.136 Under blended contracts (which includes standard and fixed pricing options), acquirers do not automatically pass IFs on to merchants, but may choose to include the cost of IFs within the pricing arrangements. Under these pricing options, individual cost components of the MSC (IFs, scheme and processing fees, and acquirer margin) are often aggregated. This means that the level of pass-through might depend on each acquirer's approach to pricing, and their incentives to pass-through savings to their customers.

9.137 Around 20% of UK-EEA consumer CNP outbound transactions, by value, relate to contracts on blended (that is, fixed or standard) pricing tariffs.[458] The remaining 80% relates to IC++ and IC+ pricing plans. However, we also note that the vast majority (over 95%) of UK merchants are on blended pricing.[459]

9.138 Whether acquirers will pass on the benefit of any reduction on outbound IFs resulting from a price cap remedy to UK merchants on blended contracts will largely be a commercial decision based on each acquirer's approach to pricing.

9.139 One stakeholder who argued that the benefits of the price cap would not be passed on to customers noted that this risk was heightened on blended contracts. Visa referred to our CAMR final report, which it said 'made clear that changes to IFs are unlikely to be passed on to merchants on blended contracts'.[460]

9.140 We said in the 2021 CAMR final report[461] that there was some evidence that, in the context of S&P fees, acquirers passed through cost increases but not cost decreases. As we note in Chapter 6, paragraph 6.49, the CAMR review introduced remedies aimed at increasing transparency and competition between UK acquirers that offer blended

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455 Stakeholder response to PSR Information Request dated 7 May 2024 [✂].

456 Stakeholder response to PSR Information Request dated 7 May 2024 [✂].

457 Stakeholder response to PSR Information Request dated 7 May 2024 [✂].

458 See paragraph 6.7 above. The category 'other' accounted for a negligible 0.03% of transaction values.

459 See paragraph 3.17, (and our MR18/1.8, *Market review into the supply of card-acquiring services: final report*, in which we stated that IC++ is restricted to the largest merchants, with the overwhelming majority of SMEs being on blended pricing).

460 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

461 See MR18/1.8, *Market review into the supply of card-acquiring services: final report*, paragraph 5.66.

contracts to their merchants, and which should assist in increasing cost pass-through in downstream markets.[462]

9.141 For the purposes of assessing the likelihood of pass-through of reduced IFs under blended contracts, we have sought evidence from a number of acquirers that offer blended contracts, and a trade association representing acquirers.[463]

a. A trade association speaking on behalf of its UK acquirer members, [✁] told us that acquirers accept that they 'generally pass on interchange onto merchants' although they point out that interchange is only one of the factors that impact their final pricing to merchants.[464]

b. Several acquirers noted that, if there was a material change to IF levels, some sort of internal 'repricing' review would typically be conducted in relation to blended contracts before deciding whether to pass on a change (in whole or part) [✁],[465] [✁].[466] Similarly, another acquirer said that the terms of their blended contract may be reviewed and adjusted where it was 'commercially reasonable' to do so following a change in IF [✁].[467]

c. Several acquirers said that the internal repricing process could take around 2 months in addition to any notice period that would be required to be given to merchants to implement a change [✁].[468] A trade association speaking on behalf of its UK acquirer members, [✁] noted that 'portfolio repricing has to be planned and scheduled and usually occurs at periodic intervals'.[469]

d. One acquirer [✁] said that, for existing customers on a blended contract who have significant transaction volumes for the relevant corridor a significant fee reduction would lead to it repricing the merchant quickly in order not to lose the customer.[470]

e. Some acquirers told us that they typically would not make changes to the pricing of blended contracts outside of the usual annual cycle [✁].[471] Others said that repricing may not happen unless the merchant instigates this. For example, one acquirer said that 'fees for merchants on blended pricing contracts are not proactively repriced when interchange fees change'. [✁].[472] While another [✁] said that for merchants on a blended contract with negligible transaction volumes for the relevant corridor, it may not immediately make moves to change their blended rate unless the merchant instigated this conversation. It added that given the competitive nature of this sector,

462 One issuer [✁] said that the 'acquiring market in the UK remains very competitive, and the PSR's existing interventions under the acquiring market review will likely further increase choice for merchants'. Stakeholder response to MR22/2.6 dated 14/02/2024 [✁]

463 On 7 May 2024 the PSR sent section 81 notices to 14 acquirers. Twelve of the acquirers we contacted on this issue use a combination of pass-through pricing and blended contracts.

464 Stakeholder response to MR22/2.6 dated 14/02/2024 [✁].

465 Stakeholder meeting 19 April 2024 [✁].

466 Stakeholder responses to PSR Information Request dated 7 May 2024 [✁].

467 Stakeholder response to PSR Information Request dated 7 May 2024 [✁].

468 Stakeholder responses to PSR Information Request dated 7 May 2024 [✁].

469 Stakeholder response to MR22/2.6 dated 14/02/2024 [✁].

470 Stakeholder meeting 19 April 2024 [✁].

471 Stakeholder responses to PSR Information Request dated 7 May 2024 [✁].

472 Stakeholder responses to PSR Information Request dated 7 May 2024 [✁]

such a move by the acquirer to change the blended rate could come if merchants were approached by other acquirers.[473]

f. One acquirer [✂] said that if a reduction in IFs was of 'great magnitude' – for instance, a cap at 0.2%/0.3% – this would likely lead to a much quicker pass-through given the competitive incentives on acquirers.[474]

g. In terms of the risk of a merchant switching to a different acquirer, one acquirer, [✂] noted the competitive nature of the sector.[475] It stated that the vast majority of its merchants on blended contracts are on rolling one-month contracts. It also stated that the average length of its merchants staying with them (most of whom are on blended contracts) is approximately 12 to 18 months. One acquirer, [✂] said that if it were to make a price change to its blended contracts, there is an attrition risk as their customers can exit their contracts without penalty within two months.[476]

9.142 We note that the benefits of a price cap remedy would not be passed on to merchants on blended contract as quickly as they would for merchants on IC++ and IC+ contracts. However, we consider that a price cap remedy is still likely to significantly benefit UK merchants on blended contracts, by reducing the level of MSC they pay to acquirers, especially in light of the evidence from acquirers in paragraph 9.141.

a. The evidence indicates that there is some competition between UK acquirers that offer blended contracts to UK merchants, which should create incentives on acquirers to pass on price reductions.[477] Also, evidence from acquirers shows that they are aware of the risk of merchants switching to a competing acquirer, and factor this into their pricing decisions.[478,479]

b. Evidence from acquirers indicates that they may be more proactive in passing on a reduction in IFs (whether in whole or in part) if:

  - the UK merchant in question conducts a material volume of transactions in the relevant corridor (see paragraph 9.141d), or
  - the reduction in the level of outbound IFs (such as a reduction following the introduction of a price cap) is significant (see paragraph 9.141f)

c. In any event, even if an acquirer opted not to pass on an IF reduction to its UK merchants on blended contracts, the evidence shows that such merchants could:

  - approach their acquirer directly to seek a repricing of their contract in the event of a price cap (see paragraph 9.141e). This would be the case even if they have low transaction levels in the UK-EEA outbound corridor, or
  - switch to a more competitive acquirer as and when their contract allows them to exit (such as a competing acquirer which has opted to reflect (in whole or in part) the reduced IF levels in their MSC as a result of a price cap) (see paragraph 9.141g).

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473 Stakeholder meeting 19 April 2024 [✂].

474 Stakeholder meeting 19 April 2024 [✂].

475 Stakeholder meeting 19 April 2024 [✂].

476 Stakeholder responses to PSR Information Request dated 7 May 2024 [✂].

477 Stakeholder meeting 19 April 2024 [✂].

478 Stakeholder meeting 19 April 2024 [✂].

479 Stakeholder responses to PSR Information Request dated 7 May 2024 [✂].

9.143 We note however that the evidence indicates that, compared to IC++ and IC+ contracts, the benefits of a price cap remedy will likely take longer to be passed through. In particular, we note that a repricing exercise can take around two months to complete (in addition to any notice that is required to be given) and some acquirers did not envisage making pricing changes outside of their normal annual cycle (see paragraph 9.141c).

9.144 To maximise the benefits to UK merchants on blended contracts, transparency about the price cap – its existence and level – will be important to allow them to seek more competitive terms either with their existing acquirer or with a competing acquirer. We note that the levels of Mastercard and Visa outbound IFs are publicly available on the Mastercard and Visa websites.[480] The design of a price cap remedy could also assist with merchant awareness. For example, a price cap remedy could be designed to (i) indicate clearly, on their websites, any changes in the level of outbound IFs, and (ii) require Mastercard and Visa to ensure that UK merchants are informed by their acquirers of the change in IF level resulting from a price cap.

Our overall assessment of pass-through

9.145 For the reasons set out above, we find that the benefits of the price cap would be to a large extent passed on to UK merchants (whether they are on IC++ and IC+ contracts or on blended contracts).

- IF reductions would be passed through relatively quickly to merchants on IC++ and IC+ contracts. These account for 80% of outbound transactions by value.
- As regards merchants on blended contracts, which account for the remaining 20% of outbound transactions by value, we consider that a price cap remedy is still likely to be of significant benefit to UK merchants on blended contracts (albeit less quickly compared to IC++ and IC+ contracts), and these benefits can be enhanced by including in any remedy measures to increase awareness.

Technical and/or operational challenges with a price cap

9.146 We considered whether there would be any required material, technical and operational changes to effectively implement a price cap on outbound IFs. As part of our stakeholder engagement, we contacted the 14 largest acquirers, that collectively represent over 90% of card transactions at UK merchants[481], and asked about the process and nature of any necessary changes that they might need to make when Mastercard and/or Visa change the level of outbound IFs.[482]

9.147 The card schemes said that at least six months would be required to implement the technical changes involved in any IF changes. Visa said that at least six months would be required to implement the technical changes involved in reflecting any IF changes in Visa's, acquirers' and issuers' systems.[483] Mastercard said 'although fee changes are business as usual activity, each one will impose an additional, incremental cost. More importantly, participants need time to be able to schedule the technical work to make the changes and acquirers need to be able to implement the new fee levels for their merchant customers,

480 See [Visa interchange fees](#) and [Mastercard interchange fees](#)

481 PSR analysis [✁].

482 Section 81 notices were sent to 14 acquirers [✁] on 7 May 2024.

483 Stakeholder response to MR22/2.6 dated 14/02/2024 [✁].

particularly where contractual changes are required. For that reason, Mastercard typically gives 6-9 months' notice of any fee changes'[484]

9.148 The acquirers we contacted said that they have the necessary systems and skills in order to implement changes that might be required if there were to be a change to outbound IFs. By way of example, one acquirer [✂] stated that a change in IF requires that it make technical changes to the existing code of its payment processing system. These changes are the same for card-present and card-not-present transactions and for all merchant contract types it offers.[485]

9.149 We note that some acquirers may require more time to implement a change in level of outbound IFs if they need to create a new region specifically for outbound IFs. Currently, outbound and inbound card transactions are treated as one region. Treating outbound transactions differently to inbound transactions may require the acquirer to split its existing region into two. Such a change would impact IC++ and blended pricing. One trade association speaking on behalf of its UK acquirer members [✂] said that this development work could take over 12 months and that acquirers who created new regions when the new cross-border rates were created would either need to start again or make changes to the system again.[486]

9.150 In their responses to our information request, the majority of acquirers (eight out of 14) said that around 6 months would be usual for such changes [✂].

9.151 In response to [✂]'s point that development work including creating new regions could take up to 12 months, we looked at which acquirers made reference to jurisdictional, regional or qualification criteria changes. Eight acquirers [✂] made reference to jurisdictional, regional or qualification criteria changes, which we interpret as including the creation of a new region.[487] Of those eight, five acquirers [✂] said that six months are generally sufficient to make the required technical and operational changes (including any region changes), with only two acquirers [✂][488] indicating that a longer time frame would be preferable, with [✂] stating that more time would be preferable if the change was more complex. One acquirer [✂] said that, for changes to Mastercard rates, changes to jurisdictional logic might only happen if they are not covered by the Mastercard Parameter Extract Table.[489]

9.152 Only one acquirer [✂] gave a specific reference to the time needed to make technical changes to support country rate changes and it [✂] said 'Technical changes to support country rate changes are typically completed in 20 hours effort, including testing and validation.'[490]

484 Stakeholder response to MR22/2.6 dates 14/02/2024 [✂].

485 Stakeholder responses to PSR information request dated 7 May 2024 [✂].

486 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

487 Stakeholder responses to PSR information request dated 7 May 2024 [✂].

488 Stakeholder responses to PSR information request dated 7 May 2024 [✂].

489 Stakeholder response to PSR information request dated 7 May 2024 [✂].

490 Stakeholder responses to PSR information request dated 7 May 2024 [✂].

Our assessment of technical and/or operational challenges

9.153 We therefore consider that the technical and/or operational changes that would be required to implement the remedy can be designed and implemented in a timely manner. These aspects in relation to design of a price cap remedy will be considered further in separate consultation documents.

Other legal and practical challenges in designing and implementing a price cap

9.154 For a price cap on Mastercard and Visa to be effective we will need to consider its scope and other design features, including its level.

9.155 As set out above, we consider that the appropriate level for any cap could be determined by reference to an appropriate methodology. We set out some preliminary views on this in our interim report. However, this aspect is not considered further in this document, which focuses instead on whether a price cap is an appropriate remedy in principle and whether we should take action to develop and implement one. Our views on the appropriate approach to assessing the appropriate level of a price cap and implementing it will be consulted upon in separate documents, which will include a draft CBA.

Monitoring compliance, enforcement and circumvention risk

9.156 To be effective, a remedy must be capable of being monitored and enforced.

9.157 A price cap remedy could, in principle, be vulnerable to circumvention risk. This issue was raised by two stakeholders in response to our interim report proposal for a price cap.

- An individual submitted that regulating IFs independently of looking at scheme and processing fees would be redundant as card schemes could circumvent any price cap by adjusting fees elsewhere.[491]
- A trade association representing the views of tech startups [✂] said that we should implement strict anti-circumvention rules to protect against increases on other direct or indirect IFs to compensate issuers for the reduction.[492]

9.158 We do not consider the circumvention risk to be insurmountable, and has been addressed in the past in similar circumstances (for example, the IFR and the 2019 Commitments). We will consult separately on the specific measures to include in a direction to address this issue, such that a price cap remedy could remain effective.

9.159 We would also propose that the design of any price cap remedy would incorporate appropriate review provisions to address any material change of circumstances and mitigate the risk of unintended consequences arising from these.

491 Stakeholder response to MR22/2.6 dated 13/12/2023 [✂].

492 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

9.160 In addition, we do not consider there are material concerns around monitoring and enforcing any such price cap remedy. Such a price cap would specifically target Mastercard and Visa outbound IFs. The levels of these IFs are publicly available on the Mastercard and Visa websites respectively[493] and can be publicly monitored. In addition, appropriate provisions can be incorporated into the design of the remedy to assist with effective monitoring and enforcement of the cap and the anti-circumvention provisions.

9.161 These factors will all be considered as part of the design of any longer lasting price cap remedy under this review. We would consult upon any such price cap remedy along with an appropriate CBA.

Scope of the price cap

9.162 One stakeholder [✂] said that price regulation should only be implemented in exceptional circumstances, such as when there is market failure which cannot be remedied in a less burdensome way and only when strictly necessary as a last resort. [✂].[494]

9.163 In our final terms of reference for this review published in 2022, we confirmed that our investigation would focus on 'UK-EEA cross-border CNP IFs in the Mastercard and Visa payment systems.'[495] We are not proposing any remedies which go beyond the scope set out in our final terms of reference.

Powers to impose a price cap

9.164 Both Visa and Mastercard have said that we do not have the legal power to impose a price cap under sections 54 or 55 of FSBRA.[496] This was based on their statutory interpretation of Part 5 of FSBRA, its legislative history, and they referred to the fact this would be the first time we had proposed using sections 54 or 55 to set or cap fees.

9.165 In Visa's view, the proposed caps would expand the scope of UK IFR beyond a domestic jurisdiction, when the UK Government said its application should be limited to UK domestic transactions. Such an approach, it said, would, in effect, bypass the transparent and consultative legislative process required to amend the UK IFR.[497]

9.166 We have considered the schemes' submissions about our powers to impose a cap on Mastercard and Visa EEA-UK consumer CNP outbound IFs. However, we consider that section 54 of FSBRA is drafted with the intention to give us wide-ranging powers to intervene in respect of payment systems if we think it appropriate. This includes the power to direct participants in regulated payment systems to take, or not take, specified actions under section 54 of FSBRA. The UK IFR is based on a European regulation which did not preclude further interventions by domestic or European authorities if deemed appropriate. We therefore conclude that we have the power to impose a price cap in relation to outbound IFs if we conclude this is appropriate.

493 See Mastercard interchange fees and Visa interchange fees (accessed on the 28/11/2024).

494 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

495 PSR MR22/2.2 Final terms of reference for cross-border interchange fees market review, p.7 para 2.3.

496 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂] and Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

497 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

Our final view on the principle of a price cap remedy

9.167 Having considered all the evidence in the round, and after having considered the alternative forms of remedy detailed above, we conclude that restricting the maximum level of outbound IFs by introducing a price cap remedy is the only effective form of remedy open to us at this stage and is proportionate to the aim of addressing the detriment we have identified in this report.

9.168 We acknowledge that a price cap would not address the underlying cause of the service detriment that this report identifies. However, we have found that:

a. A price cap set at an appropriate level would in principle be effective in addressing our finding that current levels of UK-EEA cross-border IFs are unduly high.

b. A price cap set at an appropriate level is unlikely to cause any material unintended consequences that would outweigh the benefits of the remedy and can be implemented in an effective manner.

c. The benefits would be to a large extent passed on to UK merchants (whether they are on IC++ and IC+ contracts or on blended contracts).

d. The technical and/or operational changes required to implement the remedy are capable of being implemented in a timely manner.

e. We have not identified other remedies that would effectively address the detriment we have identified in this report.

9.169 As noted above at paragraph 9.167, before implementing any such price cap we would need to carefully define appropriate parameters for the application of any cap to ensure that the remedy was effective and proportionate to address the detriment to service users. This would include setting the cap at an appropriate level and additional provisions to address the risk of circumvention. We intend to consider these matters in further detail at the design stage of any cap, which would be consulted upon (for more details see the remedies consultation document published alongside this final report).

9.170 Overall, we conclude that, if the level of the cap is set appropriately, a price cap would be effective in addressing the service user detriment we have identified in Chapter 7.

9.171 For the reasons set out above, capping UK-EEA CNP outbound IFs is in line with our statutory objectives of promoting competition and innovation in the UK's payment market and be in the interest of service users, which are organisations that accept cards and their customers. Therefore, as noted in paragraphs 8.19 to 8.21, working towards the implementation of a cap on said IFs represents an efficient use of our resources.

9.172 In addition, having considered the regulatory principles set out in paragraph 53 of FSBRA, we conclude that in principle a price cap remedy set at an appropriate level would:

a. be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction;

b. be consistent with supporting sustainable growth in the economy of the UK;

c. represent an efficient use of our resources in view of the impact of the proposed cap.[498]

9.173 As set out in Chapter 7, we concluded that the UK-EEA cross-border IFs were increased to levels that are unduly high and therefore negatively affect merchants and to the extent of pass-through their customers. As part of that conclusion, we noted in paragraph 7.15 that we found no evident countervailing benefits or innovation to account for the IF increases (such as improved fraud prevention, quality, efficiency or economy of the card payments systems to the benefit UK merchants). We estimate that approximately 95% of the additional IFs has been passed through from acquirers to merchants. In turn, we expect merchants to pass it on to some material extent to their customers in the form of higher retail prices. Therefore, the additional IF-related costs do not translate into increased value reflecting those increases for the service users which are organisations that accept cards and their customers. Hence, we consider the rise in IF levels operated by the card schemes to unduly high levels do not support UK sustainable growth.

9.174 We therefore consider that imposing a price cap by way of a general or specific direction under section 54 of FSBRA would be an appropriate intervention for promoting the interest of service users such as UK organisations that accept cards and their customers and that we should take action to design and implement such a direction.

498 Having had regard to the other regulatory principles set out in section 53 FSBRA (d to g), we consider that an in-principle price cap remedy would not conflict with any of these principles. We also consider that the PSR has exercised its functions as transparently as possible by undertaking a two-year market review and consulting extensively with the schemes and other stakeholders.

10 Next steps

10.1 Our proposals with regard to taking forward a price cap remedy will be set out in separate consultation documents.

10.2 We have published a remedies consultation document alongside this final report. In that report we set out our proposals with regard to taking forward a two-staged approach to a price cap remedy.

10.3 We invite comments from stakeholders on our current views as explained in that document.

10.4 The consultation will end at **5pm** on **7 February 2025**.

10.5 Next steps will depend on our decision making after having considered feedback on that consultation.

10.6 If our view remains that a two-staged approach to a price cap is appropriate, we will publish our reasons for that view together along with a consultation on the proposed level for a stage 1 price cap and a proposed direction.

10.7 If our view changes, we will publish reasons why we have changed our view and will clarify next steps.

10.8 Regardless of whether we ultimately decide a two-staged approach to a price cap is appropriate or not, we are progressing with our work on developing a stage 2, or longer-term, remedy. We intend to consult on the methodology for assessing outbound IFs during early 2025 and the outcome of that consultation will inform our next steps thereafter.

Annex 1
Competitive constraints

In this annex we present the feedback and evidence from stakeholders that have informed our assessment on the lack of downward pressure on the acquiring side discussed in Chapter 4. It includes the information that we received and that informed our provisional findings in our interim report, as well as the responses that we received to such provisional findings. Where stakeholders have provided new evidence and / or new arguments in response to the interim report, we address them in this annex.

Ability of acquirers to constrain any increases

1.1 As explained in Chapter 4, we have considered whether UK acquirers had the ability to constrain the schemes when they increased the UK-EEA consumer CNP outbound interchange fees (outbound IFs). We considered the possible ways acquirers could respond the October 2021 and April 2022 increases in outbound IFs.

What Mastercard and Visa told us

1.2 Visa stated that it does 'not control how acquirers (and other participants in the payments value chain) ultimately price their services to merchants, or the specific level of interchange payable by merchants for each individual Visa transaction, and that Visa does not have full visibility of the merchant pricing models that acquirers use'.[499]

1.3 Similarly, Mastercard stated that ultimately 'it is acquirers, rather than Mastercard which determine the exact fees paid by merchants'.[500]

1.4 We asked Mastercard and Visa to explain and provide supporting evidence of the factors that constrain their ability to increase UK-EEA IFs and how these factors affected their decisions to increase these fees.[501] We reviewed the internal documents provided by the card schemes also with a view to understanding whether and how potential acquirer responses to outbound IF increases were taken into account.

1.5 Internal documents from Mastercard focused on [✂].[502]

1.6 Internal documents from Visa also mentioned [✂].[503]

499 Visa response to PSR questions dated 12 January 2022. [✂].

500 Mastercard response to PSR questions dated 5 August 2022. [✂].

501 Mastercard and Visa response to PSR questions dated 12 January 2022. [✂].

502 Mastercard response to PSR questions dated 12 January 2022. [✂].

503 Visa response to PSR questions dated 12 January 2022. [✂].

1.7 In Mastercard's response to us and in its internal documents [✂]. In Visa's response to us and in its internal documents [✂].

What UK acquirers told us

1.8 The UK acquirers that we asked (representing over 90% of the UK market) confirmed that all UK merchants who accept payments, including from the EEA, accept both Mastercard and Visa branded cards.[504] None knew of UK merchants who accept one card brand but not the other.[505] Some acquirers explained that this is because UK and EEA consumers expect merchants to accept Mastercard- and Visa-branded cards by default.[506] Correspondingly, virtually all acquirers offer acquiring services for both card brands, thus providing a comprehensive service to merchants.

1.9 Acquirers told us that they have to offer acquiring services for both Mastercard and Visa because otherwise they would lose potential customers (that is, merchants) or would fail to acquire them.[507] In practice, acquirers cannot decline to offer either Mastercard or Visa in response to a fee increase, given their must-take status.

1.10 Many UK acquirers also said they could do little to respond to Mastercard and Visa's increases in UK-EEA CNP IFs.[508] Some said this is because, in practice, they cannot negotiate on the level of IFs.[509] These acquirers also said they have no option but to accept increases in IFs, and that they largely passed these increases on to merchants.[510]

Our provisional view in our interim report

1.11 Mastercard and Visa set the default IF level that merchant acquirers pay to issuers. The card schemes do not control how acquirers charge merchants. However, given that the IF is a 'per transaction' cost affecting all acquirers in the same way, it will typically be passed on to the acquirers' customers (that is, their merchants). Hence, an increase in IFs translates into an increase in prices paid by merchants, regardless of whether this is intended by the card schemes. In our interim report, we provisionally found that the two schemes envisaged that some level of pass-through from acquirers to merchants was anticipated or at least possible.

1.12 The increases in UK-EEA CNP IFs apply similarly to all acquirers, who pass most of these increases on to merchants. For the large segment of the market who are on IC++ pricing contracts, the increases are automatically passed on to merchants. Under other contract types, acquirers pass most of the IF increases on to merchants at some point. Acquirers also confirmed to us that they passed on the increases to merchants because there was nothing else they could do to respond.

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504 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

505 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

506 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

507 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

508 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

509 More information on how four-party card schemes work is provided in Chapter 2.

510 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

1.13 This means that the increases have left the acquirers on a level playing field and have had a very limited effect on their margins. This is consistent with the fact that we have not seen evidence of a possible reaction from acquirers to the increase in outbound IFs [✁].

1.14 Considering this, and the importance to acquirers of offering merchants a comprehensive card acceptance service, including both Mastercard and Visa (given their must-take status), in the interim report we provisionally found that UK acquirers have made little response to increases in outbound IFs (beyond passing these on to merchants).

1.15 Accordingly, our provisional view was that UK acquirers' responses do not provide an effective competitive constraint on increases in UK-EEA outbound IFs.

What stakeholders said in response to our interim report

What the card schemes told us

1.16 In relation to the UK acquirers' incentives to respond to the outbound IF increases, Mastercard submitted that we underestimated the IFs absorbed by acquirers and payments facilitators[511] (see Chapter 6, paragraph 6.17) and that this may have led us to undervalue the degree of competitive pressure applied by the acquiring side.[512] It added that we failed to accurately consider constraints from acquirers.[513]

1.17 Visa did not provide any comments to our provisional findings of lack of acquirer responses to the outbound IF increases.

What acquirers told us

1.18 One acquirer, [✁], confirmed that there is a lack of competitive constraints on the acquiring side due to the 'must-take' status at merchant level of Mastercard and Visa, which means that the schemes can charge high IFs to compete for the issuing banks. They explained that the implication of this is that acquirers are price takers when it comes to MIFs, so their ability to set competitive retail prices for the merchant is constrained.[514]

1.19 An industry body representing EEA acquirers [✁], said that both merchants and acquirers are affected by the lack of alternatives to accepting the dominant card schemes, which confirms the 'must-take' status of such cards. It [✁] explained that this implies that acquirers are not able to offset the IFs increases and exert competitive pressure on the card schemes.[515]

What issuers told us

1.20 Neither UK nor EEA issuers have commented on potential responses from UK acquirers to the outbound IF increases.

511 As we set out in more detail in Chapter 6, paragraph 6.45, we don't consider that to be the case.

512 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

513 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

514 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

515 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

What merchants told us

1.21 One merchant, [✂], agreed that acquirers could not and cannot take any actions to respond to the outbound IF increases.[516]

Our response to stakeholders' views on our interim report findings

1.22 As mentioned in paragraph 1.16, Mastercard said that contrary to our finding that most IFs are passed on to the merchants, we underestimated the IFs that acquirers and payments facilitators absorb. As a result, Mastercard said, we may have undervalued the degree of competitive pressure applied by the acquiring side. Chapter 6 explains why this is not the case and why we are confident that pass-through from acquirers to merchants is significant enough to remove any financial incentives on acquirers to countervail the increases.

1.23 We have received no other comments or evidence to challenge our interim report's provisional finding of lack of downward pressure that may have come from acquirers. On the contrary, relevant industry stakeholders seem to confirm our finding (see paragraphs 1.18, 1.19 and 1.21). We then conclude that UK acquirers did not and do not exert any downward pressure on the outbound IF increases.

Potential constraints from merchant responses

Declining or limiting card acceptance to avoid the increases

1.24 We have considered whether declining card acceptance may be deployed to avoid the outbound IF increases. A merchant's decision to accept a particular card brand and product (such as Visa consumer debit) is based on the full 'basket' of transaction types that can be received via the card – for example, domestic and cross-border, both CP and CNP. UK-EEA CNP transactions are just one of these types, and for most UK merchants they represent only a small proportion of transactions using a card brand and category. For example, out of all Visa consumer debit card transactions at all UK merchants, online payments from EEA-issued Visa cards were only [✂] by volume and [✂] by value in 2021.[517, 518]

1.25 Mastercard's and Visa's scheme rules prevent a merchant from choosing or declining transactions (whether CP or CNP) on the basis of the card issuer's location. The Honour All Cards (HAC) rule states that merchants who accept Mastercard and Visa consumer debit or credit cards domestically cannot refuse to accept these cards in a cross-border context.[519] A merchant can choose to accept only consumer credit or debit/pre-paid cards. It can also choose not to accept commercial products. Where a merchant chooses to accept a product, that merchant must accept all instances of that product.

516 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

517 PSR analyses of data submitted by Mastercard and Visa, and of data from UK Finance.

518 This considers the share of Visa cross-border transactions (CP and CNP) over total Visa transactions in the UK. If we consider CNP only, the percentages drop slightly to [✂] % (volume) and [✂] % (value).

519 The HAC rule states that if a merchant accepts one of a card scheme's products it should then accept all of the card scheme's cards that fall under that product category. For example, if a merchant accepts a Mastercard credit card, it should accept all Mastercard credit cards. This rule appears to be at a product level. See *Mastercard rules* (5 December 2024), Chapter 5 Rule 5.11.1 and Chapter 12 Rule 5.11.1; *Visa core rules and Visa product and service rules* (5 December 2024), Rule 1.5.4.2.

1.26 This means that a UK merchant cannot accept domestic transactions with domestic IFs but refuse those from EEA-issued cards of the same brand with the higher cross-border IFs. With regard to issuer location, the HAC rule makes accepting a card brand an all-or-nothing decision, at least at a product level.

1.27 In the UK, almost 86% of all retail sales are card-based (see paragraph 2.3). There is no national card scheme, and Mastercard and Visa account for around 99% of all card transactions.[520]

1.28 Of all card transactions at UK merchants, 3.6% were UK-EEA cross-border, and only 2.5% of the total were CNP UK-EEA cross-border (the transactions that generate outbound IFs).[521]

1.29 To estimate the potential impact of the increase in UK-EEA CNP outbound IFs on the average UK merchant, we considered an illustrative example using a starting assumption that IFs represent 60% of the MSC they must pay their acquirer on a UK-EEA transaction.[522] We also made an assumption that, before the recent increase in IFs, MSCs on UK-EEA CNP transactions were similar to the average MSC merchants have to pay across other card transactions. This indicates that, for such a merchant, a fivefold increase in UK-EEA CNP IFs implies an increase in the overall MSC of around 5%.[523]

1.30 Owing to the significant market presence of both Mastercard and Visa, we consider that declining either Mastercard or Visa would have a major effect on a merchant's business. In such a scenario, customers denied their preferred payment card might buy instead from an alternative merchant who continues to accept it. Indeed, it is the fear of losing customers that results in merchants typically accepting cards even if these are more costly to them than alternative payment methods – a situation often referred to as the must-take status of the Mastercard and Visa card schemes.[524]

1.31 The HAC rule also prevents merchants from refusing cards on the basis of an issuer's location, but refusing to accept the card brand as a whole would mean losing significant volumes of sales for domestic transactions of all types and not just for CNP transactions using EEA-issued cards. This makes it highly unlikely that UK merchants would stop accepting either Mastercard or Visa branded cards in response to an increase in UK-EEA outbound IFs even if alternatives to these cards were readily available (something that we discuss later). It also shows that Mastercard and Visa do not compete with one another in providing services to merchants and that both have must-take status.

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520 BRC, *Payments survey 2024*, pages 7 and 8.

521 PSR internal analysis of data submitted by acquirers, Mastercard, Visa and American Express as part of the Section 81 notice (2023).

522 The assumption that IFs represent around 60% of the average MSC is based on our card-acquiring market review. See MR18/1.8, *Market review into the supply of card-acquiring services: final report: annex 3: financial review* (November 2021), page 6.

523 For every £100 in MSC, the increase in UK-EEA CNP IFs affects around £1.20 of this (60% of around 2% of all transactions that are of this type, assuming similar average MSCs on these as other transactions). Following a fivefold increase in UK-EEA CNP IFs, this element becomes around £6, giving a total of £104.80, an increase of 4.8%.

524 See also Chapter 2.

1.32 For some UK merchants (such as those operating in the travel industry), UK-EEA CNP transactions may represent a much higher percentage of total transactions. A fivefold increase in IFs will, therefore, have a greater effect on the MSCs these merchants pay. If they changed their behaviour on card acceptance, that could represent a constraint on UK-EEA CNP IFs. We observe, however, that:

- While the greater impact of the fee increase might give this small group of merchants more incentive to respond, in practice, given the must-take status of these cards, they are unlikely to be able to decline or limit the acceptance of these cards. We note, for example, that all merchants that responded to our review said that they accept all Mastercard- and Visa-branded cards and they have not considered changing their acceptance of (that is, declining) any of these cards in the last five years.[525]
- While an individual merchant with very large volumes of UK-EEA trade might exercise some pressure over the card schemes to get a better deal, that does not constrain UK-EEA outbound IFs as a whole. Amazon, for example, told its customers in November 2021 that it would stop accepting payments made with UK-issued Visa credit cards from 19 January 2022, blaming its decision on the 'high fees Visa charges for processing credit card transactions'.[526] However, on 17 January 2022, it was reported that there had been an '11th hour reprieve', and that Amazon had 'started sending affected customers emails telling them they would be able to continue to use their Visa credit cards to pay for items, and for Amazon Prime'.[527] It was subsequently reported in the Financial Times that 'Amazon had reached a global truce' with Visa.[528]

Our provisional view in our interim report

1.33 In our interim report, we provisionally found that due to the must-take status of Mastercard and Visa, very few, if any, UK merchants could be expected to respond to an increase in UK-EEA outbound IFs by declining the card brand as a whole. Accordingly, changes in card acceptance do not provide a mechanism whereby the financial sustainability for Mastercard and Visa of the increase in outbound IFs could be undermined. Thus, our provisional view was that the potential for a merchant to decline the card brand or limit its acceptance does not provide an effective competitive constraint on UK-EEA outbound IFs.

What stakeholders said in response to our interim report

What the card schemes told us

1.34 Mastercard said that 'merchants are able to exert competitive pressure by […] threatening to refuse to accept certain card payment methods if IFs were hypothetically to be raised materially above their optimal levels. This is especially the case as a substantial proportion of payments in this specific channel are PayPal transactions that are not funded by Mastercard and Visa. The growth of alternative payment methods means that cardholders would have other ways to transact'.[529]

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525 Stakeholder responses to PSR information requests dated 11 January 2023 and 18 July 2023. [✂].

526 *Guardian*, Amazon to stop accepting UK-issued Visa credit cards (17 November 2021).

527 *Guardian*, UK Amazon users can continue using Visa credit cards after dispute is settled (17 January 2022).

528 *Financial Times*, Amazon reaches 'global' truce with Visa on credit card fees (17 February 2022).

529 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

1.35 Mastercard said that merchants can switch between payment methods and that such actual or potential response could apply downward pressure on IFs from the acquiring side of the market.[530,531,532]

1.36 Mastercard said that the finding of merchants not having the option of choosing not to accept cards has only been found for the fees being increased to their current levels. It added then from this it does not follow that 'if IFs were hypothetically to be raised materially above their optimal levels, that merchants would still choose to accept Mastercard and Visa card payments given the variety of alternative payment methods available'. Indeed, 'if fees for a particular method of payment are too high, merchants may choose not to accept this method of payment' (in addition to PayPal, EEA cardholders would also have a number of other options, such as GoCardless, American Express and China Union Pay). [533]

1.37 Visa did not provide any comments or evidence in response to our provisional finding that UK merchants cannot decline card acceptance to avoid the outbound increases in IFs.

What issuers told us

1.38 Issuers (including EEA issuers) did not provide any comments or evidence in response to our provisional finding that UK merchants cannot decline card acceptance to avoid the outbound increases in IFs.

What acquirers told us

1.39 An acquirer [✂] said that declining card acceptance is not a viable method to mitigate IFs increases, due to the 'must-take' nature of both card schemes. It submitted that this is particularly relevant in an online cross-border setting, where card transactions are prevalent.[534]

1.40 The same acquirer [✂] also stated that the HAC rule prevents merchants from refusing cards in card-not-present setting, if these have been accepted for card present transactions. It noted that merchants are not allowed to reject a card solely based on the issuer's location. It asserted that even if the HAC rule was altered, the 'must-take' status of Mastercard's and Visa's cards, particularly in the online setting, would still make it impossible for merchants to limit their acceptance of such cards.[535]

What merchants told us

1.41 A merchant [✂] said it agreed with us that merchants' responses do not provide effective competitive constraints on Mastercard and Visa in setting UK-EEA outbound IFs. It mentioned that [✂].[536]

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530 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

531 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

532 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

533 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

534 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

535 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

536 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

What other stakeholders told us

1.42 No other stakeholders provided any comments or evidence in response to our provisional finding that UK merchants cannot decline card acceptance to avoid the outbound increases in IFs.

Our response to stakeholders' views on our interim report findings

1.43 Mastercard said (see paragraphs 1.34 to 1.36) that if outbound IFs had been raised above optimal levels, merchants could refuse (that is, decline) to accept Mastercard and Visa branded cards. This was especially so, they said, because an important proportion of UK-EEA CNP PayPal transactions are not funded via Mastercard and Visa. We do not consider that to be the case. As explained in paragraphs 1.25 to 1.31 above, the Honour All Cards (HAC) rule prevents merchants from refusing cards on the basis of an issuer's location. So, to refuse cards on cross-border CNP transactions, a merchant would have to refusing all card transactions using the same brand of card, losing significant volumes of sales for domestic transactions too.

1.44 Mastercard said (see paragraph 1.35) that merchants can switch between payment methods and that this would present downward pressure on IFs.[537,538,539] It is not clear what 'switch' means here. It could be interpreted to mean 'steering' customers towards alternative payment methods or actively 'declining' Mastercard and Visa cards and asking the customer to pay another way. In any case, for the reasons explained just above (declining) and in paragraphs 1.110 to 1.184 (steering), we conclude that such 'switching' is not possible.

Cross-border acquiring

1.45 In cross-border acquiring, an acquirer in one country processes transactions for a merchant located in a different country. If this were possible, a UK merchant would contract with an EEA-based acquirer who would process its UK-EEA CNP transactions in the EEA instead of in the UK. If such a transaction was then treated as a domestic or intra-regional EEA transaction, it would fall under the EU IFR and incur an IF of 0.2% or 0.3% (for debit or credit, respectively), rather than 1.15% or 1.5% (for debit or credit, respectively) as a UK-EEA CNP transaction.

1.46 However, card schemes' rules classify transactions based on the presence of a merchant in a given geographical area, and not based on the acquirer's or the payment processor's location. Under those rules, IFs are levied according to the location of the merchant.[540] The rules also state that an acquirer must accept transactions only from a merchant located

537 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

538 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

539 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

540 Mastercard sets its default IFs according to its rules (see rule 8.3) and webpage. Visa sets its IFs according to information contained on its website (see 'Frequently asked questions, What does it cost and how is this decided').

within the acquirer's country of domicile.[541, 542] The schemes' rules are consistent with the criteria for merchant location, including for e-commerce, set in the EU IFR.[543]

1.47 It is also likely that an EEA acquirer would need to obtain FCA authorisation to offer services to UK merchants, and acquirers must generally accept transactions from a merchant located within the acquirer's country of domicile.[544] Broadly, when a firm provides regulated payment services in the UK, as a regular occupation or business activity, and neither the firm nor their services fall within an exclusion or exemption, the firm must be authorised or registered by the FCA. It is a merchant acquirer's responsibility to consider whether their activities fall within the FCA's regulatory perimeter based on their specific circumstances, including where each part of their activity takes place. A firm that fails to do so risks committing a criminal offence under regulation 138 of the Payment Services Regulations 2017.

What UK acquirers and merchants told us

1.48 A UK-based acquirer [✁] stated that cross-border acquiring is restricted under card schemes' cross-border acquiring rules. Currently, rules establish that regions are assigned based on the presence of that merchant in a given geographical area, and not based on the acquirer's or the payment processor's location. For CNP transactions, rules state that a merchant must have an entity established in the given country, thus making it inaccessible for most small businesses. This restriction limits competition between cross-border acquirers, who could offer a transaction routing service to merchants to minimise their acceptance costs if the region was based on the acquirer's location. Therefore, acquirers are widely prevented from mitigating this rise in fees.[545]

1.49 The BRC stated that no existing regulation prevents merchants from routing their transactions through their different acquirers in different countries, but card scheme rules negate the importance of acquirer location. It also said that if a merchant has an acquirer in another country, there is an argument to be made that it would make sense for a merchant to be able to route any transactions made with cards from that country through their acquirer in the corresponding country, and therefore be charged as a domestic transaction.[546]

Our provisional view in our interim report

1.50 In our interim report, we concluded that cross-border acquiring is currently not an option for UK merchants engaging in e-commerce with the EEA, so UK merchants can't use it to mitigate the increase in UK-EEA CNP IFs. We then provisionally concluded that cross-border acquiring provides no effective competitive constraint on increases in UK-EEA outbound IFs.

541 See Mastercard rules, p. 38 (accessed 19/08/2024) and webpage (accessed 19/08/2024).

542 See: https://www.visa.co.uk/content/dam/VCOM/download/about-visa/visa-rules-public.pdf, p. 101 (accessed 30/05/2024).

543 European Parliament and European Council, Regulation (EU) 2015/751 of the European Parliament and of the Council, Article 2, section 29.

544 European Parliament and European Council, Regulation (EU) 2015/751 of the European Parliament and of the Council, section 29.

545 Stakeholder response to PSR information request dated 11 January 2023 [✁].

546 BRC response to PSR information request dated 11 January 2023. [✁].

What stakeholders said in response to our interim report

What the card schemes told us

1.51 Mastercard agreed that there is limitation to cross-border acquiring in the UK. It said that these limits are part of the FCA regulation rather than the card schemes', as the FCA demands that acquirers must be authorised in the UK in order to operate in the UK and acquire UK merchants. It said that a core feature of the FCA's authorisation requirements is that the acquirer is located in the UK.[547]

1.52 Visa did not provide any comments or evidence in response to our provisional finding that cross-border acquiring provides no effective competitive constraint on increases in UK-EEA outbound IFs.

What issuers told us

1.53 An issuer [✁] said that FCA authorisation to offer acquiring services in the UK is not a material barrier for new entrants, and that various significant EU acquirers also offer services in the UK. It said that UK and EU regulators could address the requirement, for instance, by offering passporting for EEA or UK regulated acquirers. It noted that it is the scheme rules that hinder cross-border acquiring.[548]

What UK acquirers told us

1.54 An acquirer [✁] said it agreed with our analysis that cross-border acquiring is not currently possible. It noted that this occurs because the rules of the card schemes require categorising a transaction based on the merchant's location rather than the acquirer's.[549]

What UK merchants told us

1.55 A merchant [✁] stated that the cross-border acquiring is not feasible for the vast majority of merchants. It noted it would demand considerable in-house expertise in payments for a merchant to initiate cross-border acquiring.[550]

1.56 A merchant [✁] said it agreed with our views and provisional finding that cross-border acquiring is not currently possible and does not, therefore, provide an effective competitive constraint on increases in UK-EEA outbound IFs.[551]

What other stakeholders told us

1.57 No other stakeholders provided any comments or evidence in response to our provisional finding that cross-border acquiring provides no effective competitive constraint on increases in UK-EEA outbound IFs.

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547 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

548 Stakeholder response to MR22/2.6 dated 02 February 2024 [✁].

549 Stakeholder response to MR22/2.6 dated 31January 2024 [✁].

550 Stakeholder response to MR22/2.6 dated 02 February 2024 [✁].

551 Stakeholder response to MR22/2.6 dated 25January 2024 [✁].

Our response to stakeholders' views on our interim report

1.58 All stakeholders confirmed that merchants cannot use cross-border acquiring in response to outbound IF increases, though there is no consensus as to whether this is because of regulation or scheme rules. Either way, we conclude that cross-border acquiring does not represent a possible response from UK merchants to the outbound IF increases. As such cross-border acquiring did not – and does not – represent a source of downward pressure on those increases.

Merchant relocation

1.59 Under the card scheme rules, which levy IFs according to the location of a merchant, merchants can relocate their transactions by changing the geographic locations where they accept payments.[552] For example, a UK-located merchant selling online to consumers in France (a transaction that would generate an outbound IF) could establish a presence in the EEA and use an EEA-based acquirer to process these transactions. What would previously have been a UK-EEA cross-border transaction would then become an EEA domestic transaction, subject to the lower IFs capped under the EU IFR.

1.60 For the (lower) EU IFR caps to apply, the card must be issued within the EEA and the merchant's acquirer must be located there, too.[553]

What Mastercard and Visa told us

1.61 Mastercard provided internal documents showing that [✂] could result from the outbound IF increases. [✂].[554]

1.62 Visa provided internal documents showing that [✂] could result from the outbound IF increases. [✂][555]

1.63 We asked Mastercard about merchant relocation and how it would alter the impact of the increases in UK-EEA CNP IFs.[556]

1.64 Mastercard explained that, in the context of IFs, 'localisation' (meaning relocation) is when a merchant changes its location to convert a cross-border transaction into a domestic transaction. It provided the following example:

- [✂] sells certain products to consumers using UK-issued cards ('UK consumers') through an entity based in the EEA. This is a UK-EEA cross-border transaction which would be subject to the increases in inbound IFs.

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552 Mastercard sets its default IFs according to its rules (see rule 8.3*)* and webpage. Visa sets its IFs according to information contained on its website (see 'Frequently asked questions, What does it cost and how is this decided').

553 European Parliament and European Council, Regulation (EU) 2015/751 of the European Parliament and of the Council, section 29.

554 Mastercard, [✂]

555 Visa, [✂].

556 Mastercard response to PSR questions dated 5 August 2022. [✂].

- If [✂] decides to sell those same products to UK consumers through an entity based in the UK, the transaction becomes a UK domestic transaction, no longer subject to cross-border IFs.[557]

1.65 Mastercard stated there may be other online merchants who might decide to 'localise' and serve consumers through an entity based in the same domestic market as their consumers, in order to avoid paying cross-border IFs.[558]

1.66 Mastercard also said that there are many reasons, other than IFs differentials, why a merchant may consider changing its location for some transactions. These include tax optimisation, corporate restructuring, risk management (for example, to have higher issuer approval rates) and reducing currency conversion risks.[559]

1.67 Mastercard explained that, while it requires merchants to provide accurate location information, it does not know enough about their underlying behaviour to predict when and why they may localise. There is also [✂]. In addition, Mastercard submitted that localisation does not mean that all transactions are either cross-border or domestic (localised). Rather, it can be seen as a partial movement of some transactions over time.

1.68 Mastercard said that a significant number of merchants accept transactions in both the EEA and UK. It said that this means they have entities in both locations and hence could easily relocate some of their CNP cross-border transactions to domestic ones, if that met their commercial aims.[560]

1.69 Mastercard provided internal documents that suggest that [✂].[561]

1.70 We asked Mastercard to provide the names of the merchants that have relocated part or all of their CNP UK-EEA transaction volumes. Mastercard's analysis shows that the merchants that it believes may have relocated their transactions are very large merchants, such as [✂].[562]

1.71 Visa similarly explained that a merchant with a principal place of business in the EEA and multiple other locations across Europe (including in the UK) could configure its operations to shift transaction volume across locations. For example (under certain criteria), a merchant can shift some volume to its UK location, so fewer transactions are subject to the higher UK-EEA IFs (and more transactions are subject to the lower UK domestic IFs).[563]

1.72 Visa also said that, because of the UK's withdrawal from the EU, many large e-commerce merchants wanted to ensure they had both UK- and EEA-based operations. As these merchants made this shift, many consumer transactions that were previously cross-border became localised. Visa said that if this trend were to continue, the proportion of transactions impacted by the increases in question would fall.[564]

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557 Mastercard response to PSR questions dated 5 August 2022. [✂].

558 Mastercard response to PSR questions dated 5 August 2022. [✂].

559 Mastercard response to PSR questions dated 5 August 2022. [✂].

560 Mastercard response to PSR questions dated 5 August 2022. [✂].

561 Mastercard response to PSR questions dated 12 January 2022. [✂].

562 Mastercard response to PSR questions dated 5 August 2022. [✂]

563 Visa response to PSR questions dated 5 August 2022. [✂]

564 Visa, *Visa response to Treasury Select Committee on Cross-border Interchange*, page 5.

1.73 Internal documents from Visa also show that it [✂].[565] [✂]:

- [✂].
- [✂].

What UK acquirers and merchants told us

1.74 We asked UK acquirers and merchants whether:

- merchants can relocate their UK-EEA CNP cross-border transactions to UK domestic or EEA domestic
- acquirers may enable or facilitate relocation
- merchants have already relocated any transactions.[566]

1.75 Some large e-commerce merchants (for example, [✂]) told us that they relocated at least some of their operations following the UK's withdrawal from the EU.[567] This meant that they avoided at least some of the UK-EEA outbound IF increases.

1.76 Acquirers confirmed that some of their larger merchants have relocated.[568] However, some said that, on average, the number of merchants that actually relocated was small, due to the considerable costs involved.[569]

1.77 Acquirers and merchants explained that relocation from the UK to the EEA (and vice versa) appears to only be an option for:

- the biggest merchants who already have a presence in both jurisdictions
- merchants who do not have a presence in both jurisdictions but have a significant proportion of cross-border transactions[570]
- large merchants operating in specific sectors, such as e-commerce platforms, online booking services, online entertainment and fintech.

1.78 Acquirers and merchants confirmed that a merchant can relocate some cross-border transactions to turn them into domestic transactions only if it has a legal entity where it wishes to relocate them. They said that card scheme rules stipulate this entity must be the one that is actually responsible for the sales of goods or services for the jurisdiction.[571]

1.79 Acquirers and merchants also said that, for most merchants, the financial and logistical burden of setting up a new legal entity precludes doing so.[572]

565 Visa response to PSR questions dated 5 August 2022. [✂]

566 PSR merchant questionnaire and PSR acquirer questionnaire. [✂]

567 Stakeholder responses to PSR information requests dated 11 January 2023. [✂]

568 Stakeholder responses to PSR information requests dated 11 January 2023. [✂]

569 Stakeholder responses to PSR information requests dated 11 January 2023. [✂]

570 Stakeholder responses to PSR information requests dated 11 January 2023. [✂]

571 Stakeholder responses to PSR information requests dated 11 January 2023. [✂]

572 Stakeholder responses to PSR information requests dated 11 January 2023 [✂].

Our provisional views in our interim report

1.80 In our interim report, we set out that the evidence available to us indicated that relocation had helped, and may continue to help, a few large merchants avoid or at least mitigate outbound IF increases. However, we said that the available evidence also showed that relocating is likely to be a possibility only for very large merchants, and that it is not a possibility for UK SMEs (because it is not economically viable for their businesses). As a result, SMEs are effectively unable to avoid any of the outbound IF increases. This was consistent with our findings in Chapter 6 of our interim report that in 2022 an extra [✂] £150 million to £200 million was paid by UK acquirers and [✂] £150 million to £200 million was paid in turn by UK merchants due to the increases in outbound IFs.

1.81 We noted that merchants who can relocate (typically the large merchants) can reduce the volume of cross-border transactions for a given card, reducing their exposure to increased cross-border IFs. However, we said that relocation does not change the total number of card transactions for the card schemes involving those merchants. We said that only in some unlikely scenarios, such as where merchants relocate in full, may there be some small losses for card schemes associated with relocation and related to lower scheme and processing fees. Overall, we provisionally found that the card schemes suffer little or no detriment from such relocation.

1.82 Considering the above, our provisional view was that merchant relocation does not provide an effective competitive constraint on increases in UK-EEA outbound IFs.

What stakeholders said in response to our interim report

What Mastercard and Visa told us

1.83 Mastercard said a merchant might move for various reasons, such as reducing cross-border fees. For instance, relocating a UK-based online sales portal to the EEA could mean lower fees for transactions with EEA-issued cards. Other considerations that might influence these decisions include tax benefits and corporate restructuring.[573]

1.84 Mastercard also said it does not attempt or have the ability to influence merchants in deciding where to locate their business and has no knowledge of the factors that drive those decisions. It does not see relocation as the solution to merchants on reducing IFs costs; however, it believes that by adopting this approach merchants exert competitive constraints on how Mastercard sets IFs.[574]

1.85 Mastercard also mentioned that determining the optimal IF rate involves considering various factors, and confirmed that the merchants' ability and incentives to relocate transactions are particularly strong for CNP transactions, where the 'branch' location may not need to provide customer service but solely process the transaction.[575]

1.86 Even if only a few merchants can relocate, Mastercard stated that the evidence suggests that the merchants who have the ability to relocate are large in size. It also noted that its analysis indicates that several e-commerce giants such as Amazon, Airbnb, Alibaba, Expedia, among others have relocated, comprising a large volume of transactions in the

573 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

574 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

575 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

UK-EEA CNP channel. It also said that its analysis previously submitted to us showed that a significant number of the largest merchants accept transactions in both the EEA and UK, meaning that they have entities in both locations and hence could easily relocate some of their CNP cross-border transactions to domestic ones, if that met their commercial aims. It noted that there is evidence from acquirers and merchants in PSR's interim report that if major merchants were to move, it could significantly impact issuer earnings from CNP cross-border IFs, potentially affecting the schemes.[576]

1.87 Mastercard said that our argument that both schemes were able to increase IFs following the UK's departure from the EU on these transactions does not provide sufficient evidence that relocation does not provide competitive constraint. This is because UK-EEA consumer IFs were previously set below their optimal level.[577]

1.88 Visa told us that since the UK's withdrawal from the EU, large merchants have typically organised their operations in a way that enables their transactions to be located in the EEA which, as a result, does 'not involve the application of Visa's cross-border CNP IFs'.[578] Visa says that merchant relocation is 'a business decision which takes into account a wide range of factors including tax optimisation, corporate restructuring, regulation, among others' and that Visa understands that many merchants with significant cross-border transactions 'relocated their operations in order to ensure that they had both UK and EEA-based operations following the UK's exit from the European Union'.[579]

1.89 According to Visa, this is confirmed by acquirer and merchant's feedback received by us, which notes that relocation is an option for 'the biggest merchants who already have a presence in both jurisdictions; merchants who do not have a presence in both jurisdictions but have a significant proportion of cross-border transactions; [and] large merchants operating in specific sectors, such as e-commerce platforms, online booking services, online entertainment and fintech'. Such feedback also notes, according to Visa, that merchants had been reviewing their corporate organisational structures as a result of Brexit, with [✂], for example, 'having confirmed that they [✂].[580]

What UK acquirers and merchants told us

1.90 In response to our interim report findings, an acquirer ([✂]) explained that because card rules prevent cross-border acquiring, this makes merchant relocation the only way to constrain IF costs. [✂] explained that this would involve 'creating entities in the UK or EEA respectively to render such transactions intra-regional and thus apply the previous IF levels'.[581] In its response, [✂] noted that this would only be feasible for large enterprises and SMEs would be unable to relocate as they do not have the resources to create entities in other jurisdictions and facilitate the selling of goods through that new entity.[582]

576 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

577 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

578 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

579 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

580 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

581 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

582 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

1.91 [✂], stated that [✂][583]

1.92 A merchant [✂] agreed with the our view and provisional finding that merchant relocation does not provide an effective competitive constraint on increases in UK-EEA outbound IFs.[584]

What issuers told us

1.93 In response to our interim report findings, [✂] said it does not agree with our assessment that merchant relocation does not provide an effective competitive constraint. It said that large merchants with significant amounts of EEA-UK CNP can be directly impacted by increases in IFs as they are often on IC +/++ pricing models. According to it [✂], these merchants have capacity and incentive to relocate their operation for that portion of their volumes.[585]

What other stakeholders told us

1.94 In response to our interim report findings, a trade association representing tech startups [✂] said that merchant relocation is only an option available to large merchants.[586]

Our response to stakeholders' views on our interim report findings

1.95 In response to the interim report, most stakeholders confirmed that relocation is currently only an option for large merchants, not for the majority.

1.96 In response to Mastercard's argument that the merchants' ability and incentives to relocate transactions are particularly strong for CNP transactions, as the 'branch' location may not need to provide customer service but solely process the transaction (see paragraph 1.85), we note that Mastercard and Visa's rules impose strict requirements for relocation. Mastercard's rules state that a merchant's location for CNP must satisfy all of the following criteria: the merchant conducts business locally, merchant holds a permit to operate locally, merchant complies with local tax laws and regulations, and the merchant is subject to local consumer laws and courts.[587] Similarly, Visa rules require that a merchant must use its principal place of business as the merchant outlet location for CNP transactions – that is the fixed location where the merchant's executive officers direct, control, and coordinate the entity's strategy, operations, and activities.[588]

1.97 Moreover, Visa confirmed that relocation was mainly due to factors such as tax optimisation, corporate restructuring and regulation because of UK's recent exit from the EU (see paragraph 1.88). Also Mastercard confirmed that merchants may decide to relocate for other reasons (see paragraph 1.83). Mastercard said it recognises that relocation is not a solution for merchants wishing to reduce IF costs (see paragraph 1.84). Feedback and data on volume of transactions (see Chapter 3, Figure 4) indicates that most of the relocation happened before the IF increases: it was not a response to these but was

583 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

584 Stakeholder response to MR22/2.6 dated 25 January 2024 [✂].

585 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

586 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

587 MasterCard, Mastercard Rules, available at: https://www.mastercard.us/content/dam/public/mastercardcom/na/global-site/documents/mastercard-rules.pdf, p.107 (accessed 17/06/2024)

588 Visa Merchant Data Standards Manual (April 2024 – Page 9), available at: https://usa.visa.com/content/dam/VCOM/download/merchants/visa-merchant-data-standards-manual.pdf

due to other commercial and business considerations that the merchants made, likely as a consequence of the UK's withdrawal from the EU. So, relocation did not represent a competitive constraint on the outbound IF increases.

1.98 In response to Mastercard's argument that the fact that the schemes were able to increase outbound IFs does not provide sufficient evidence that relocation does not provide competitive constraint, as IFs were previously set below their optimal level (see paragraph 1.87), we refer to our analysis in Chapter 5. There we conclude that the schemes have been able to raise the outbound IF to unduly high levels, without considering whether these were desirable also from the perspective of UK merchants and their customers. This was only possible because of a lack of effective competitive constraints on the acquiring side.

1.99 Relocation has helped a few large merchants to avoid or at least mitigate the outbound IF increases. However, that did not have an impact on the schemes and did not happen in response to the outbound IFs. So, we conclude that merchant relocation does not provide an effective competitive constraint on increases in UK-EEA outbound IFs.

Consumer steering towards alternative payment methods

1.100 As also illustrated in Chapter 4, we have considered whether UK merchants could lower their exposure to the increases in outbound IFs by steering EEA consumers towards alternative payment methods. This could be done by:

- introducing card surcharges or offering discounts or bonuses for using an alternative payment method
- providing information on the fees facing a merchant and how they compare to alternative payment methods
- asking the consumer to choose an alternative payment method
- presenting website payment options in a way that nudges consumers to use alternative payment methods (for example, by making these methods more prominent).

1.101 The ability of a UK merchant to use any of these strategies crucially depends on whether and what alternative payment methods are available to EEA consumers as well as the merchants themselves.

What Mastercard and Visa told us

1.102 In this regard, we asked both Mastercard and Visa to explain, with supporting evidence, the factors that constrain their ability to increase UK-EEA cross-border IFs.[589]

1.103 Mastercard told us that, whenever setting IFs, it considers various factors, including the cost of alternative payment methods.[590] It stated that alternative cards, such as American Express, and digital wallets, such as PayPal, are important for cross-border transactions.[591]

1.104 Mastercard also stated that the European Commission, in evaluating the levels that informed the 2019 Commitments, considered a range of different service providers relevant to cross-

589 Mastercard and Visa responses to PSR questions dated 12 January 2022 [✂].

590 Mastercard response to PSR questions dated 5 August 2022 [✂].

591 Mastercard response to PSR questions dated 5 August 2022 and 16 March 2023 [✂].

border transactions, including between the EEA and the rest of the world. This included three-party card payment schemes, other means of payments that can be funded by bank transfers, such as e-wallets (digital wallets), e-payments or bank transfer payments.[592]

1.105 Visa told us in its response that, when setting IFs, it takes account of [✂].[593]

1.106 Mastercard stated that the range of specific alternatives will depend on the country in which the customer is based. It also said that alternatives, such as three-party cards, are generally more prominent in cross-border transactions.[594]

1.107 Mastercard stated: 'On the merchant side, the cross-border EEA interchange fees apply to a much smaller proportion of overall transactions than domestic interchange fees, and merchants are able to apply surcharges when these cards are accepted.'[595]

1.108 Visa told us that its decisions on IFs are taken in the context of the competitive environment within which it operates. It also understands that merchants, particularly those operating in CNP environments, have options to complete e-commerce transactions and that these will be selected if they are preferred.[596]

1.109 However, a 2019 report produced for Visa [✂]. The report said that [✂]. The report also said [✂]. In addition, the report said [✂].[597] Visa told us that [✂].[598]

What UK acquirers, merchants and other stakeholders told us

1.110 Merchants and acquirers both mentioned that the following payment options, in addition to Mastercard and Visa, can be used for UK-EEA cross-border transactions: [599, 600]

- American Express and Diners Club cards
- Apple Pay, Google Pay and PayPal
- BNPL solutions (such as [✂])
- bank transfers and third-party solutions that rely on the same bank rails[601]

1.111 However, some stakeholders said that Apple Pay and Google Pay simply store card details and pass them to a merchant and its payment processor.[602]

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592 Ultimately an estimate of the cost of bank transfer payments informed the CNP IF levels that the European Commission used to determine the interchange caps that were part of the 2019 Commitments.

593 Visa response to PSR questions dated 5 August 2022 [✂].

594 Mastercard response to PSR questions dated 12 January 2022 [✂].

595 Mastercard response to PSR questions dated 12 January 2022 [✂].

596 Visa response to PSR questions dated 12 January 2022 [✂].

597 [✂].

598 Visa response to PSR questions dated 17 August 2023. [✂].

599 Stakeholder responses to PSR information requests dated 11 January 2023 [✂].

600 Stakeholder responses to PSR information requests dated 11 January 2023 [✂].

601 SEPA bank transfers, which allow consumers to send and receive cross-border payments in euros. SEPA bank transfers work the same way as domestic bank transfers as long as both countries are part of SEPA. Trustly, which uses Open Banking to offer consumers the ability to pay directly from their bank account without a debit or credit card. See https://www.trustly.com/cross-border-payments/what-are-open-banking-payments

602 Stakeholder response to PSR information request dated 11 January 2023 [✂].

1.112 We were told by [✂] that if EEA domestic cards attempt a cross-border transaction and are co-badged with an international scheme, the transaction will flow through the international schemes network. If they are not co-badged with an international scheme, the services do not work because their underlying domestic schemes do not offer that capability.[603, 604, 605]

1.113 A digital wallet provider [✂] also confirmed that it is a pass-through digital wallet. It does not offer payment processing services to merchants. Broadly, its digital wallet shares the retail customers' card details with the relevant merchant and their payment processor, who in turn processes the payment transaction.[606]

1.114 As such, Apple Pay and Google Pay they cannot be considered real alternative payment options to Mastercard and Visa cross-border CNP payments – at least not additional to other international card options.

1.115 A digital wallet provider [✂] offers different funding sources, including card payments and bank transfers. In 2022, nearly [✂] of all EEA consumer transactions at UK merchants via this provider's digital wallet were card based [✂)]. In addition, the digital wallet provider said that [✂]. [607, 608]

1.116 [✂] is [✂] and was mentioned by stakeholders, including the schemes, as a potential alternative. We were told by [✂] that the cross-border nature of a transaction can be dependent on the billing address (country) of the consumer and the merchant location. In addition, it is possible, albeit rare, for a consumer residing in the UK to make a purchase at a UK merchant that is settled with a cross-border payment (such as a Visa/Mastercard transaction or a direct bank transfer from a bank in another country).[609]

1.117 [✂] said that [✂]. [✂] explained that [✂]. [✂] explained that [✂].'[610, 611]

1.118 Online bank transfers and other third-party payment solutions that rely on the same bank payment rails can also be used for remote payments. In these cases, consumers can make a purchase by transferring funds to a merchant's account from their bank account. Other third-party solutions that rely on the same bank rails are becoming increasingly popular in some EEA countries (for example, iDEAL in the Netherlands and Blik in Poland). However, they are rarely available outside of their respective domestic borders. Acquirers and merchants said that these third-party solutions are generally not available in the UK, and that it would be too costly and not economically viable for merchants to adopt each of these.[612]

603 Stakeholder response to PSR information request dated 20 July 2023 [✂].

604 Stakeholder response to PSR information request dated 20 July 2023 [✂].

605 Stakeholder response to PSR information request dated 20 July 2023 [✂].

606 Stakeholder response to PSR information request dated 7 August 2023 [✂].

607 Stakeholder response to PSR information request dated 20 July 2023 [✂].

608 [✂].

609 Stakeholder response to PSR information request dated 20 July 2023. [✂]

610 Stakeholder email to PSR dated 17 May 2024 [✂]

611 [✂] noted that [✂]. Specifically, [✂]. [✂] explained that [✂]. Clearly, [✂].

612 Stakeholder responses to PSR information requests dated 11 January 2023 [✂].

1.119 We asked merchants if they steer consumers away from cards for UK-EEA transactions by encouraging them directly or indirectly to pay using alternative methods (despite the limited options available).

1.120 All the merchants that responded to the questionnaire told us that they do not steer their consumers towards a specific payment method.[613] Rather, they let the consumers choose their preferred payment method. A merchant representative body, the BRC, stated that, in its view, steering techniques other than surcharging (such as asking the consumer to pay with a different payment method) may have limited effectiveness, as consumers typically have a preferred payment method for different reasons (for example, budgeting or rewards) and will use it despite encouragement to do otherwise.[614]

1.121 Specifically on the possibility of introducing card surcharges, we asked UK acquirers and merchants:

- whether merchants can differentiate between CNP consumers that use EEA-issued cards rather than UK-issued cards [615]
- if so, whether merchants can or do apply a surcharge based on the jurisdiction where the card was issued for transactions that use EEA-issued cards[616]

1.122 One acquirer explained that while, in principle, merchants can recognise and surcharge cards issued in another jurisdiction, doing so creates undesirable frictions in the consumer experience and can lead to abandonment of the transaction.[617] Other acquirers said they are not aware of any such practice.[618] Overall, no acquirer we spoke to said it is easy or common to surcharge based on the location of the issuer.[619]

1.123 We also asked UK acquirers if they know of, or have facilitated, any actions other than relocation that the merchants they serve have taken (or plan to take) to avoid or mitigate higher UK-EEA cross-border CNP IFs. [620] This question received no responses.[621]

1.124 Finally, we asked acquirers and merchants if they must accept any particular cards or alternative payment methods, including for UK-EEA remote transactions, or risk losing a significant number of consumers and transactions.[622]

1.125 The UK acquirers and one merchant representative body, the BRC, that responded said that UK merchants must be able to accept Mastercard- and Visa-branded cards for remote transactions, including with EEA consumers. They said there are no merchants that accept only one of the two. This is because consumers expect merchants to accept Mastercard- and Visa-branded cards by default.[623] One respondent stated that Mastercard and Visa are

613 Stakeholder responses to PSR information requests dated 11 January 2023. [✁].

614 BRC response to PSR information requests dated 11 January 2023. [✁].

615 PSR acquirer questionnaire [✁].

616 PSR merchant questionnaire [✁].

617 Stakeholder response to PSR information request dated 11 January 2023 [✁].

618 Stakeholder responses to PSR information requests dated 11 January 2023 [✁].

619 Stakeholder responses to PSR information requests dated 11 January 2023 [✁].

620 PSR acquirer questionnaire [✁].

621 Stakeholder responses to PSR information requests dated 11 January 2023 [✁].

622 PSR merchant questionnaire and PSR acquirer questionnaire [✁].

623 Stakeholder responses to PSR information requests dated 11 January 2023 [✁].

'a bare minimum setup for most merchants interacting with our platform', and 'not offering Visa or Mastercard would entail critical and existential losses' for them and most likely for any payment processing provider.[624]

1.126 Some respondents said they also accept other payment methods, but Mastercard and Visa are the payment methods that consumers most commonly use and must be accepted to avoid 'conversion losses'. Other payment methods are much less commonly used and in some cases are offered mainly to expand consumer choice, but consumers are less aware of them or less likely to use them.[625]

Our provisional views in our interim report

1.127 The availability of alternative payment methods depends on the location of both the consumer initiating the payment and the merchant receiving it. Our provisional view was that, in the UK-EEA context, UK merchants who want to engage in retail e-commerce with the EEA must take both Mastercard and Visa. In addition, our provisional view was that UK merchants who engage in international trade with the EEA have few alternative payment methods besides Mastercard and Visa, and namely:

- SEPA bank credit transfers and third-party solutions that rely on the same bank rails
- other international card schemes (such as American Express and Diners Club)
- PayPal payments (to the extent that these are funded via a bank transfer and not via a Mastercard or Visa card).

1.128 In our interim report, we also provisionally found the following:

- Digital wallets such as Apple Pay and Google Pay are also popular payment solutions. However, they are currently proxy payment services for cards, including in the cross-border space for international cards. So, they can't be considered real alternatives to Mastercard and Visa for UK-EEA cross-border CNP payments – at least not in a sense different from other international card options.
- PayPal is also often based on Mastercard and Visa card rails and funding, and [✂].[626] In 2022, EEA online retail payments to UK merchants made either with PayPal methods that are not based on international cards, or with international cards other than Mastercard and Visa, accounted for [✂] of total volumes and [✂] of total values.[627] In addition, [✂]. So, PayPal represents a weak alternative to Mastercard and Visa.
- [✂] does not currently represent an alternative to Mastercard and Visa because, [✂].
- There are other third-party solutions for e-commerce, such as iDEAL and Blik, that rely on bank rails. But these are national offerings. iDEAL offers limited cross-border transactions services, facilitating SEPA payments from consumers in the Netherlands using SEPA Credit Transfer.[628] Blik is still confined to its domestic borders and does not offer a cross-border payment service. So, these third-party solutions do not

624 Stakeholder response to PSR information request dated 11 January 2023. [✂].

625 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

626 Stakeholder response to PSR information request dated 20 July [✂].

627 PSR analysis [✂] and [✂].

628 See information available at: https://ideal.nl/en/offer-ideal and https://ideal.nl/en/faq-overview.

represent strong alternative payment methods for UK merchants who want to engage in international trade across the EEA.

1.129 So, our provisional view was that the number of alternatives to Mastercard and Visa for UK-EEA CNP transactions is limited, given that some existing payment solutions, such as digital wallets, are also based on Mastercard and Visa payment rails. Currently, the only available alternatives for these transactions are other international cards (such as American Express and Diners Club), PayPal (to the extent that transactions are not based on Mastercard and Visa), SEPA bank transfers and third-party solutions that rely on the same bank rails.

1.130 In light of the evidence described above, our provisional view was that UK merchants who engage in international trade with the EEA must take both Mastercard and Visa. Mastercard- and Visa-branded cards, therefore, appear to be 'must-take' for merchants engaging in UK-EEA cross-border CNP transactions. There are very few alternatives to Mastercard and Visa for merchants who engage (or want to engage) in international trade with the EEA, and those that do represent an alternative offer only a very limited constraint on Mastercard and Visa. Such an outcome reinforces the must-take status of Mastercard and Visa.

1.131 Turning to how merchants might steer consumers' choice of payment method, we provisionally found that surcharging[629] is legal for UK-EEA transactions (unlike domestic transactions). Regulation 6A(1) of the Consumer Rights (Payment Surcharges) Regulations 2012 lays out a ban on surcharging by a payee to a payer for using a particular payment method.[630] Regulation 6B specifies that such a ban only applies when both the payer and payee are located in the UK.[631] Regulation 6A(2) states that the payee must not charge a fee that exceeds the cost it incurs for using that specific payment method.[632] But surcharging for UK-EEA transactions is likely to create consumer journey frictions, which may discourage merchants from introducing it. Merchants we have engaged with said that they do not typically surcharge.[633] UK merchants may also find themselves at a competitive disadvantage compared to EEA merchants selling the same products or services to those consumers.

1.132 Finally, we provisionally found that while merchants could use some behavioural steering of consumers towards a specific payment method, this typically involves some costs – for example, in designing the consumer interface. While a few merchants who are particularly impacted by the increase in UK-EEA outbound IFs may have some incentive to do this, it is unlikely that most UK merchants would be financially motivated to engage in such measures because the relevant transactions represent a very small share of all card transactions.

1.133 Given the above, our provisional view was that consumer steering is unlikely to represent an effective competitive constraint on UK-EEA outbound IFs at this time.

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629 Surcharging is when a merchant adds an additional cost to a transaction depending on the payment method.

630 Consumer Rights (Payment Surcharges) Regulations 2012 (SI 2012/3110), section 6A, paragraph 1. See also: Department for Business, Energy and Industrial Strategy, *Guidance on the Consumer Rights (Payment Surcharges) Regulations* (June 2018), page 7, paragraphs 7.1 to 7.3.

631 Consumer Rights (Payment Surcharges) Regulations 2012 (SI 2012/3110), section 6B, paragraphs 1 to 3.

632 Consumer Rights (Payment Surcharges) Regulations 2012 (SI 2012/3110), section 6A, paragraph 2.

633 Stakeholder response to PSR questions dated 11 January 2023. [✁].

What stakeholders said in response to our interim report

What card schemes told us

1.134 Mastercard submitted that, when considering the alternative payment methods for EEA online transactions at UK merchants, the analysis should focus on behaviour of households based in the EEA. It submitted that EEA consumers have a range of payment methods alternative to Mastercard or Visa, and that these are widely used.[634] While the exact range of alternatives will vary by country, Mastercard submitted that:

- Research conducted by Worldpay indicated that in 2022, payment methods alternative to Mastercard- and Visa-branded cards were the most popular payment method for e-commerce transactions in 9 out of 12 EEA countries featured in the report.[635] It also referred to Worldpay data showing that about 50% of payments in Europe are made by alternative payment methods, such as PayPal, BNPL, credit transfer-based payment methods.[636] It submitted that the fact we neglected to carry out a thorough analysis of alternative payment methods within the appropriate geographic region led us to undervalue the constraints faced by Mastercard.[637]
- There are many different alternative payment methods available for cross-border (EEA-UK) CNP transactions: digital wallets, such as PayPal,[638] Revolut Pay and Skrill; international card payment methods, such as American Express, China Union Pay; BNPL solutions; and credit transfer-based payments, such as Trustly.[639] It stated that alternative cards, such as American Express, and digital wallets, such as PayPal, are important for cross-border transactions.[640]
- There are many domestic card products, such as Cartes Bancaires, and domestic credit transfer-based payment methods, such as iDEAL and Giropay, which can be used by merchants in the UK to accept payments by customers in EEA countries.[641] In this regard, it added that '[…] if there are only one or two alternative payment methods, this can be sufficient to impose competitive constraints in a market with network effects'.[642]

1.135 Mastercard submitted that there is a significant set of acquirers, payment facilitators and processors in Europe, including in the EEA and the UK, that sell consolidated, multi-product acceptance solutions to merchants as a one-stop-shop.[643] For example, it said that payment facilitators, such as Stripe, offer these payment methods to merchants in the UK.[644] These new players have quickly made new payment methods available to retailers

634 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

635 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

636 Stakeholder response to MR22/2.6 dated 29 February 2024 [✁].

637 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

638 Mastercard noted that 65% of PayPal payments in the EEA are funded by credit transfers and direct debits (and domestic cards) Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

639 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

640 Mastercard response to PSR questions dated 5 August 2022 and 16 March 2023. [✁].

641 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

642 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

643 Stakeholder response to MR22/2.6 dated 29 February 2024 [✁].

644 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

in the UK, and domestic payment methods such as Blik and Giropay are now available to UK retailers too.[645]

1.136 Mastercard said that merchants can make available and persuade consumers to use different payment methods, which leads to downward pressure on IFs by acquirers and merchants.[646]

1.137 Mastercard stated that, over the past few years, there have been technological changes, new entrants and regulatory changes such as PSD2 and Open Banking, all of which has led to growth of new forms of payment methods available for EEA consumers and UK merchants.[647] Mastercard said that there is a wide range of new players, increase in multi-homing, BNPL providers, various credit-transfer- based payment methods, digital wallets and merchants' own platforms such as Amazon Pay. All of these have been growing rapidly in the past few years. In addition, along with regulation and technology coming together, payment methods have easy access to account-to-account infrastructure to fund the transaction.[648]

1.138 Mastercard mentioned the following examples of UK merchants that currently accept alternative payment solutions:

- Matches Fashion accepts American Express, PayPal, Alipay and Cartes Bancaires
- Joseph Ltd accepts UnionPay, Apple Pay, PayPal, American Express, Alipay, JCB, Giropay, iDeal and Sofort
- DAZN accepts PayPal
- Sofa.com accepts American Express, prepaid card and PayPal
- Heelys and the British Museum both accept PayPal.[649]

1.139 Specifically on PayPal, Mastercard mentioned that 65% of PayPal payments in the EEA are funded by credit transfers and direct debits (and domestic cards). It added that in Germany the proportion of PayPal transactions which are not funded by Mastercard and Visa is even higher, with 80-85% of PayPal transactions funded by credit transfers and direct debits.[650] Mastercard also noted [✂].[651] Furthermore, [✂].[652]

1.140 Also because of the existence of above-mentioned alternative payment methods, Mastercard said that it believes that merchants can steer or 'nudge' consumers to these alternatives if IFs were hypothetically to be raised above their optimal levels.[653,654]

645 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
646 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
647 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
648 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
649 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
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653 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
654 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

Specifically, Mastercard stated that UK merchants are able to apply surcharges when EEA consumers present a Mastercard card.[655]

1.141 Finally, Mastercard noted how entry and expansion of new payment providers is not required in order to be competitively constrained, as it is the 'credible threat of entry' which leads to relevant competitive constraints, even if the market shares of entrants are small.[656] It added that the payments landscape is continually evolving. Payment services may start domestically before expanding internationally and the threat of expansion of these services provides a competitive constraint to Mastercard.[657]

1.142 Visa stated that different alternatives are available to merchants, and that we wrongly assumed that 'it is appropriate to ignore all of the payment alternatives that are used by EEA consumers when transacting with UK merchants'.[658]

1.143 Visa submitted that alternative payment methods for cross-border CNP transactions include three-party card schemes such as American Express, digital wallets such as PayPal, and BNPL providers like [✂].[659] It submitted evidence that [✂] of cross-border CNP transactions are already taking place using alternative payment methods other than Visa or Mastercard cannot be ignored.[660] In particular:

- Three-party schemes have strong adoption in both the UK and the EEA; in particular, American Express is accepted by half of all UK card-accepting merchants, and there were 18.4 million American Express cards issued in Europe in 2019. The PSR's own analysis also indicates that other card schemes represent approximately 21% of the value of cross-border CNP transactions.[661]
- Digital wallets have become an increasingly important payment method for e-commerce transactions in Europe and the UK.[662] 'Staged wallets' such as PayPal and Amazon Pay enable consumers to fund their wallets via mechanisms which do not involve Mastercard and Visa. [✂].[663]
- BNPL providers are becoming increasingly important payment alternatives for consumers in both the EEA and the UK. BNPL providers such as [✂] are well established within the EEA, with a 10% market share of European e-commerce transactions in 2022 according to Global Payments, and are predicted to continue to grow. A BNPL provider [✂] has more than [✂] users across Europe and is accepted by more than [✂] UK merchants. Like digital wallets, BNPL can be funded by a variety of different mechanisms, such as American Express and bank transfers.[664]

655 Mastercard response to PSR questions dated 12 January 2022. [✂]
656 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
657 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
658 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
659 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
660 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
661 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
662 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
663 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
664 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

- The PSR did not properly reflect some stakeholder submissions in reaching the conclusions set out in the interim report. Such representations identified three-party card schemes, BNPL and digital wallets as alternatives to Mastercard and Visa and stated the payment alternatives a merchant accepts is essential for its business and another stated that that removing any of the payment options would have a detrimental impact on its business, including due to consumer preferences towards such methods.[665]
- Popular payment alternatives to the Visa (and Mastercard) card schemes for EEA to UK CNP transactions are more costly for UK merchants to accept than a Visa or Mastercard (see para 2.131 of Annex 2 for further info).[666]

1.144 Visa said that competition is always present on both sides of the market. It also said that an example of this is Germany, where in the card-not-present arena, there is a strong preference for PayPal on the acceptance side.[667]

1.145 Visa told us that merchants can steer customers toward other payment methods; however, there may be situations in which merchants might not want to steer, for example, when comparing Visa with the alternatives looking at for example Visa's-lower cost acceptance utility (that is, convenience for both merchants and consumers) and ubiquity.[668] It added merchants are also sensitive to the fact that friction for consumers may lead to lost sales, for example, where the consumer would need to open their banking app and add payee bank account details in order to pay using a bank transfer.[669] Merchants might think of steering the customer towards bank transfer, but may refrain from doing so in order to avoid this friction and not to risk losing the transaction, including when they might also get a high margin from it.[670]

What UK acquirers and merchants told us

1.146 Acquirers [✂] all confirmed that they do not offer EEA alternative payment methods to UK merchants.[671] One acquirer, [✂], said this was linked to a lack of demand from merchants for such alternative payment methods.

1.147 [✂] said it does offer EEA alternative payment methods on their platform to its UK merchants which do not require the merchant to have a local presence in the EEA. [✂] told us the rates and fees for these alternative payment methods are negotiated between it and its merchants, under a fee-per-transaction model. [✂] does not charge one-off cost or subscription fees for these alternative payment methods.[672]

1.148 [✂] said the main reasons for the limited adoption of EEA alternative payment methods by UK merchants may include, amongst others, lack of demand, as UK consumers predominantly use cards, and lack of functionality, such as a lack of recurring or stored card

665 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

666 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

667 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].

668 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].

669 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].

670 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].

671 Stakeholder response to PSR information requests dated 7 May 2024[✂].

672 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

features. Price may also be a factor as these methods may not always be cheaper to the merchant. For instance, BNPL or digital wallets can be more expensive than cards.[673]

1.149 An acquirer [✂] said it has the ability to offer [✂] to merchants in the UK. It said it [✂] offers alternative payment methods if it sees significant client demand and a strong business case.[674]

1.150 The same acquirer [✂] told us that local and alternative payment methods are successful as they meet the specific needs of the consumer base of that specific country; this also means that they may not be appropriate payment methods for UK merchants. [✂] stated that these alternative payment methods would only be appropriate if a merchant is making significant sales in the country in which the payment method operates. For example, if a UK merchant makes an insignificant number of sales in Germany, then Giropay would not be appropriate for that merchant.[675]

1.151 An acquirer [✂] stated that it offers some EEA alternative payment solutions. It said it only offers the few ones which can settle funds directly into its UK accounts, which then allows it to settle into the UK merchants' accounts. It told us it [✂] does not offer any EEA alternative payment solutions which are unable to settle into its UK accounts.[676]

1.152 The same acquirer also [✂] said there is limited adoption from UK merchants due to the different levels of sophistication of merchants, both UK and non-UK. It said some merchants have greater knowledge and resources then others, and this allows them to adopt other payment solutions. It told us that those merchants with less knowledge and/or resources are not willing to invest in adding alternative payment solutions and stay with cards.[677]

1.153 [✂] said it supports various alternative payment methods; UK merchants can access these via a direct integration or via a third-party payment solution which [✂] has a partnership with. If the UK merchant is required to use the 3rd party solution to use an alternative payment method, [✂] will be required to undertake development as there is a need for each alternative payment solution to have its own integration. In these instances, there may be a 'one-off' development cost for that solution in order support the required alternative payment solution.[678]

1.154 [✂] stated that UK merchants do not adopt EEA alternative payment methods mainly due to lack of trust, differing levels of protection lack of protection, and the fact that these methods are generally less mature and are not as smooth as cards from a consumers' point of view.[679]

1.155 An acquirer [✂] told us they offer a number of alternative payment methods, through a combination of direct integration and integration via a third party. [✂] stated that their UK merchants would require an additional agreement with a third party that will take

673 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

674 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

675 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

676 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

677 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

678 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

679 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

ownership of the acquiring (settlement and funding of the payment methods), but this is managed as a referral agreement that [✁] facilitates.[680]

1.156 The same acquirer [✁] said that the main reasons for the lack of adoption from UK merchants are Brexit, lack of awareness, the cost and complexity to access solutions and the payment methods' costs, which they say are higher than card processing.[681]

1.157 An acquirer [✁] told us they offer several EEA alternative payment method solutions. This is via either a direct integration or by integrating using a third party. If a third-party integration is required this would require an additional agreement with that third party.[682]

1.158 An acquirer [✁] said that the main reasons for the lack of adoption from UK merchants are Brexit, lack of awareness, the cost and complexity to access solutions and the payment methods', extra effort required for reconciliation, costs, which they say are higher than card processing.[683]

1.159 [✁] told us they offer EEA alternative payment methods to UK merchants that have access to their platform. It added that it does not onboard merchants to accept these alternative payment methods only – the merchants must still accept the major card brands.[684]

1.160 [✁] said the lack of adoption by UK merchants of EEA alternative payment methods is due to little or no exposure to alternative payment methods and to how they operate, the size of the merchants and their resources, and fluctuating exchange rates. It also stated that UK consumers are comfortable and confident with market leading schemes such as American Express, Mastercard and Visa, with PayPal and especially with digital wallets for their ease and simplicity.[685]

1.161 An acquirer [✁] said it offers its own alternative payment method – [✁] – to UK merchants. It stated it offers its their own service as it is led by its merchants' needs.[686]

1.162 The same acquirer [✁] said that UK merchants do not adopt EEA alternative payment methods as there is a perceived lack of incentives to the merchant. In order for UK merchants to adopt these alternatives there must be a cost advantage compared to cards, so that merchants are incentivised to implement these methods. It [✁] added that the lack of availability is another reason, as acquirers have to be incentivised to offer these methods to merchants and to do it with ease, but most acquirers have not integrated with EEA alternative payment methods. It [✁] also said that other reasons for merchants not adopting these methods relate to cost, speed, trust/security and reach.[687]

1.163 An acquirer [✁] said it offers EEA alternative payment methods to UK merchants, but will only add additional methods if there is sufficient demand from its merchants. The acquirer

680 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

681 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

682 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

683 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

684 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

685 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

686 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

687 Stakeholder response to PSR information requests dated 7 May 2024 [✁].

[✂] added that some alternative payment methods have additional Merchant Category Code restrictions, which means that some merchants would not be able to use them.[688]

1.164 The same acquirer [✂] said that EEA local payment methods, by virtue of being tailored to their countries' regulatory, technical and customer-related factors to appeal to local merchant, may lack sufficient attractiveness and ease of use for UK merchants to want to accept them. It added that the UK's traditional reliance on major card networks may contribute to UK merchants lacking understanding or confidence in EEA local payment methods as options to accept cross-border payments. It said that, for merchants who build their own checkout experiences, these alternative payment methods may require different integration design, resulting in additional integration and operational work for merchants. It also told us that a lack of consumer confidence or understanding in these payment methods could also be behind a lack of adoption. Finally, it said that the changing economic landscape in Europe over the past 8 years as the UK exited the European Union may have led to the UK having a less joined-up approach in collaborating with its EU counterparts. It added that uncertainty caused by the UK's withdrawal process may have also led to greater caution by UK merchant in adopting EEA alternative payment methods.[689]

1.165 An acquirer [✂] told us that, as a leading payment provider in the UK, it is committed to providing its merchant with a wide range of payment options that do not involve card payment systems. The alternative payment methods it offers are driven by its merchants' demand, which could include a combination of factors depending on the merchants' specific circumstances. Cost savings may be a factor for some, while convenience/frictionless experience, safety, and higher sales conversion may be more important for others.[690]

1.166 The same acquirer [✂] said that currently alternative payment solutions do not offer merchants the same level of convenience and frictionless experience as card-based payments.[691]

1.167 An acquirer [✂] told us they 'believe that there are no meaningful competitive constraints on Mastercard and Visa in setting all MIFs, not just UK-EEA outbound IFs.'[692]

What issuers told us

1.168 An issuer [✂] said that it considers that we have not shown that there is a lack of competition specifically in the CNP EEA to UK transactions. It told us it considers that a comprehensive analysis is required to assess the evolving trend, considering rapid changes in volume and value market share due to recent technological advancements.[693]

1.169 The same issuer [✂] submitted that 'merchants already have alternatives for cross-border payments, and that the largest merchants already have the power to choose to use them and promote them to end users'.[694] It [✂] stated that Mastercard and Visa already face competition for cross-border transactions and observed that PSR's own data shows these

688 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

689 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

690 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

691 Stakeholder response to PSR information requests dated 7 May 2024 [✂].

692 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

693 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

694 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

methods already hold a reasonable market share in EEA to UK CNP transactions (10% volume, 21% value).[695]

1.170 The same issuer told us it [✁] believes there are a number of constraints on Mastercard and Visa. It said we have not explored the changing dynamic of EU payments, especially the European Payments Initiative. It said 'the combination of strong national instant payments schemes (such as iDEAL) into a European scheme could further erode Mastercard and Visa's market share for EEA to UK cross border transactions. [696]

1.171 The same issuer [✁] also referred to the concept of dynamic competition and how this can constraint the existing card schemes. It believes that, as more alternative payments to cards emerge, the competitive constraints on Mastercard and Visa will increase. It [✁] mentioned alternative payment methods such as [✁], Digital Wallets, Pix in Brazil and UPI in India, which are all growing. It also believes that Stablecoins and CBDC will offer new low-cost solutions.[697] It submitted it believes that, as Open Banking, Stablecoins and other digital wallets gain traction, the share of cross-border CNP transactions on Mastercard and Visa rails will fall.[698]

1.172 A trade association speaking on behalf of its UK issuer members [✁] commented on the interim report finding that alternatives to cards either do not exist or are too expensive. They said that both statements can be challenged as, for example, e-wallets funded by e-money are widely available to consumers and businesses.'[699]

What other stakeholders told us

1.173 A trade association representing tech startups [✁] and a trade association representing acquirers [✁] said that there are only a very limited number of alternative payment methods to Mastercard and Visa and not necessarily a competitive threat to these.[700] A merchant[✁][701], a trade association representing tech startups [✁][702] and a trade association representing EEA acquirers [✁][703] said that Mastercard and Visa are not subject to effective competitive constraints when setting IFs.

1.174 A stakeholder [✁] noted that [✁] [704]

1.175 A trade association representing tech startups [✁] said that merchants could not provide adequate competitive constraints on Mastercard and Visa on their outbound IFs.[705]

695 Stakeholder response to MR22/2.6 dated 02 February 2024 [✁].

696 Stakeholder response to MR22/2.6 dated 02 February 2024 [✁].

697 Stakeholder response to MR22/2.6 dated 02 February 2024 [✁].

698 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

699 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

700 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁] & Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

701 Stakeholder response to MR22/2.6 dated 25 January 2024 [✁].

702 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

703 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

704 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

705 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

1.176 The BRC noted that merchants cannot negotiate or refuse when IFs rise, due to the 'must-stake' status of the card schemes.[706]

1.177 Another merchant trade association [✂] noted that small businesses have limited options and alternative technologies to undertake card transactions. [707]

Our response to stakeholders' views on our interim report

1.178 As illustrated in paragraphs 1.141 to 1.162 above, we have asked UK acquirers and payment facilitators whether, and to what extent, they can help merchants switch between payment methods. Their feedback confirms our finding that switching is unfeasible for UK merchants affected by the increases. It would involve integration costs for each additional EEA payment method which could not be justified by the limited number of EEA consumer transactions that each method could facilitate.

1.179 The availability of some of these alternative payment methods is not sufficient to prove a competitive constraint. In addition to being available, the alternatives would have to be feasible as well as large enough to constrain the card schemes from making such increases in fees. Chapter 4 explains that, of the alternative payment methods mentioned by Mastercard and Visa in their submissions:

- [✂] BNPL solutions are [✂].
- PayPal digital wallet reflects in its fees the full cost of Mastercard and Visa cards also when the wallets is funded by other means (paragraph 4.60).
- Other international card schemes are typically more expensive than Mastercard- and Visa-branded cards. As such, for UK merchants they do not represent a valid alternative for UK merchants to avoid or mitigate the impact of outbound IF increases (paragraph 4.62).
- Other payment methods either are not widely used by EEA consumers or require merchants to incur non-negligible costs to integrate with enough of these alternatives to cover most of their EEA customers spread across different countries (paragraphs 4.68 and 4.69).

1.180 Moreover, in deciding whether to steer consumers towards a specific payment method, merchants need to weigh lower IFs against the risk of lost revenue from reduced conversion rates. Any appreciable fall in conversion rates is likely to remove merchants' incentives to use such steering (paragraph 4.71).

1.181 We therefore conclude that consumer steering did not and does not provide an effective competitive constraint on the outbound IF increases (paragraph 4.74).

1.182 An issuer [✂] said that (see paragraph 1.163) the largest merchants have the power to choose to use available alternatives and to promote them to end users. We believe this is not the case, with one or two exceptions. But even if it were the case (as explained in paragraphs 4.33a and 4.33c) these very large merchants had no need to promote alternatives to cards in response to the increases in outbound IFs:

706 Stakeholder response to MR22/2.6 dated 26 January 2024 [✂].

707 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

- The largest, international merchants had already relocated part of their activities in response to the UK's exit from the EU, so they were less exposed to increases in outbound IFs.
- The largest merchants have enough bargaining power to negotiate with the schemes over scheme and processing fees for the transaction volumes that have not been relocated. In other words, the largest merchants can find alternative ways to mitigate the increases. These negotiations, however, do not result in a constraint on outbound IFs for other, smaller merchants.

1.183 [✁] told us that card schemes are constrained by dynamic competition and that as more alternative payments to cards emerge, the competitive constraints on Mastercard and Visa will increase (paragraph 1.166). We note, however, that the lack of evidence in contemporaneous internal documents that Mastercard or Visa considered the cost to merchants of alternative payment methods when implementing the current level of cross-border IFs (see Annex 2, paragraphs 2.109 and 2.117) indicates that they were not constrained by the current or prospective availability of alternative payment methods. We also note that, of the alternative payment methods mentioned by [✁]:

- Digital wallets and Open Banking solutions have been assessed in Chapter 4, where we conclude that consumer steering did not and does not provide an effective competitive constraint (paragraph 4.74)
- Pix and UPI are only available in Brazil and India respectively, so they are irrelevant to UK-EEA cross-border transactions
- The emergence of stablecoin and CBDC as viable payment methods is subject to significant uncertainty[708]

1.184 Other stakeholders agreed with our provisional conclusions that the potential response of merchants does not provide a credible competitive constraint on Mastercard's and Visa's pricing decisions.

708 See the interim report on the PSR's Market review of card scheme and processing fees, paragraph 4.82.

Annex 2
Stated rationale for the increases

This annex summarises what Mastercard and Visa told us about the considerations they made and the reasons they gave for increasing the outbound IFs to the current levels, when we asked about those. Where applicable, it also presents what third parties have told us in relation to such possible considerations and reasons. Finally, it provides our assessment of that information.

Introduction

2.1 As part of this review, we asked Mastercard and Visa to explain and justify their increases to outbound IFs. We requested access to internal documents and information to help us understand their respective positions. We also asked questions to third parties (UK acquirers, merchants and issuers) to better understand the key issues.

2.2 Mastercard and Visa explained that when deciding to increase the UK-EEA CNP inbound and outbound IFs, they considered:

- **Fraud levels and related issuer costs:** Mastercard said higher IF levels were justified because they better reflect the cost that issuers incur due to the higher fraud levels seen in CNP cross-border transactions. Visa said that cross-border e-commerce payments present a higher risk of fraud and may require issuers to invest further in risk and fraud detection systems. IFs help to support issuers with costs and risk associated with card issuing, including fraud. Visa said IFs [✂].
- **Cost to merchants of alternative payment methods:** Mastercard told us that they considered the cost of alternative payment methods when setting IFs for UK-EEA CNP cross-border transactions. Visa indicated that it had considered [✂].
- **Methodology underpinning the 0.2%/0.3% capping of CNP cross-border IFs:** Mastercard stated that the previous caps were not fit for purpose for all transactions in general, including for UK-EEA outbound IFs. It said that neither the underlying comparator (cash) nor the evidence underpinning the 0.2%/0.3% capping of cross-border IFs is appropriate in relation to any CNP IFs, including UK-EEA IFs. Visa stated that the approach used to set the 0.2%/0.3% IFR caps is not fit for purpose for all transactions in general, including for UK-EEA outbound IFs. It said that the underlying approach, which focused solely on cash as the only comparator, and [✂] are not appropriate for assessing any CNP IFs, including UK-EEA IFs today.
- **The 2019 Commitments and the UK's withdrawal from the EEA:** Mastercard said that after the UK's withdrawal from the EU, there was no objectively justifiable reason

for not increasing inbound IFs up to the existing European Commission 2019 caps for transactions between the EEA and the rest of the world (RoW). Visa explained that [✂].

- **Competitive dynamics on the issuing side:** Mastercard said it felt compelled to increase its fees to remain attractive to EEA issuers following Visa's announcement that it would raise outbound IFs.
- **Merchant-related considerations:** Visa said that it considered [✂].[709]
- **Practical benefits of aligning IFs for EEA cards at UK merchants with other IF levels:** Mastercard said that aligning outbound IFs with IFs for non-EEA cards transacting with UK merchants provides greater simplicity for UK acquirers and their merchants. Visa said that [✂].

2.3 We set out more detail on each of in the sections that follow, in which we summarise:

- what Mastercard and Visa told us, including what we have identified in their internal documents
- what third parties told us, where applicable
- our provisional view in our interim report
- what Mastercard, Visa and third parties responded to our provisional views, where applicable
- our final responses and views.

Fraud levels and related issuer costs

What the card schemes told us

2.4 Mastercard told us that its IFs for UK-EEA CNP transactions better reflected the higher issuer transaction costs that characterise UK-EEA CNP transactions, particularly those related to fraud disputes and payment defaults.[710]

2.5 Mastercard explained that 'cross-border transactions have greater levels of fraud for issuers and are of higher value to merchants'.[711] It further stated that transaction costs (including as regards fraud and payment defaults) are one of the factors that Mastercard takes into account whenever setting IF rates.[712] Mastercard told us that it 'always held the view that the prevailing rates were too low and had fallen below costs over time (particularly given those related to cross-border CNP transactions), since the Interchange Fee Regulation used a benchmark based only on cash (and even then only a limited range

709 Visa response to PSR questions dated 12 January 2022. [✂].

710 'Fraud disputes' are disputes when cardholders' accounts are debited for transactions they did not authorise. These usually occur when an individual's card details have been compromised and someone who has gained access performs unauthorised transactions, or when a fraudulent merchant is processing questionable transactions through to the consumer's account. They can also arise when a consumer disputes a transaction they made. This could be for several reasons, such as goods not received, goods not as described/damaged, cardholder charged incorrect amount, or processing errors. Mastercard Rules or Chargeback Guide, 'Cardholder dispute chargeback', page 46, and 'Fraud related chargebacks', page 76. 'Payment default' refers to situations when a consumer misses a payment or payments on a credit agreement they have entered.

711 Mastercard response to PSR questions dated 5 August 2022. [✂].

712 Mastercard response to PSR questions dated 5 August 2022. [✂].

of cash costs)'.[713] In other words, even before the UK's withdrawal from the EU, the previous rates for UK-EEA CNP transactions, and (implicitly, by extension) for other intra-EEA CNP transactions, failed to reflect the higher costs that CNP cross-border transactions generate for issuing banks.

2.6 In the internal documents that were shown to senior decision makers at Mastercard and that were subsequently provided to us, specific fraud levels are not mentioned to justify increasing UK-EEA CNP IFs. Mastercard told us that fraud was a relevant factor when developing options involving higher fees. However, the evidence we saw indicated that the main concern and consideration was [✂].

2.7 Mastercard was not able to provide us with specific information on the costs incurred by issuers due to fraudulent UK-EEA CNP transactions.

2.8 When asked, Mastercard explained that it [✂] when setting the revised IF rates on EEA-UK CNP transactions and said that 'the rates which we set were based on the levels which had been set/accepted by the European Commission at the end of its long-running investigation. But that investigation did consider fraud as part of the reason for setting interchange at the rate which it did.'[714]

2.9 Mastercard also explained that it 'does not have direct information on the specific costs of fraud and payment default, as these costs are primarily met by issuers. However, as noted in our previous response, these are factors that inform Mastercard's commercial judgment with respect to appropriate interchange fee levels. In particular, Mastercard is aware that the risk of fraud is elevated in the case of card not present and cross-border transactions, a payment specific factor that supports the differential interchange rates applied to CNP cross-border transactions in the UK and EEA.'[715]

2.10 Mastercard subsequently provided the following fraud-level data.[716]

2.11 Table 5 illustrates the fraud levels, measured in basis points, reported by Mastercard for the period 2020 to 2022. It includes: i) the levels of fraud for UK domestic and intra-EEA cross-border CNP transactions (UK cards at UK merchants; EEA cards at EEA merchants); ii) the levels of fraud for UK cards used at EEA merchants and for UK cards used at non-EEA merchants; and iii) the levels of fraud for EEA cards used at UK merchants and for EEA cards used at non-EEA merchants.

2.12 The table indicates that domestic transactions within the UK and domestic and cross-border transactions within the EEA are subject to fraud less often than cross-border transactions between the UK and the EEA and with non-EEA countries. Specifically, for cross-border transactions, transactions that take place between the UK and the EEA appear less subject to fraud than transactions involving non-UK and non-EEA countries. The table also indicates that fraud levels declined between 2020 and 2022 for both domestic and UK-EEA CNP transactions.

713 Mastercard response to PSR questions dated 5 August 2022. [✂].

714 Mastercard response to PSR questions dated 30 June 2023. [✂].

715 Mastercard response to PSR questions dated 16 March 2023. [✂].

716 Mastercard response to PSR questions dated 6 July 2023. [✂].

Table 5: Fraud levels 2020 to 2022 reported by Mastercard (in basis points)

CNP transactions

	UK card at UK merchants	UK card at EEA merchants	UK card at non-EEA merchants
2020	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]

CNP transactions

	EEA card at EEA merchants	EEA card at UK merchants	EEA card at non-EEA merchants
2020	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]

2.13 Visa told us that [✂].[717] We note that in its submission to the Treasury Select Committee, Visa stated that 'Cross border, ecommerce transactions have unique characteristics, including higher risk of fraud and the need for greater vigilance and investment by issuers to ensure their security and efficiency.'[718]

2.14 Visa also explained that 'cross-border payments involve different patterns of spend, which may require issuers to invest further in: (i) risk and fraud detection systems to ensure that they strike the right balance between the risk of fraud and the inconvenience of card declines; and (ii) consumer service, to handle and resolve fraud complaints'.[719]

2.15 Visa also said that 'interchange fees received by card-issuing entities help to support them with the costs and risk associated with card issuing, including, but not limited to, the administrative costs of maintaining a card issuing business, and fraud and bad debt costs. [✂].'[720]

2.16 Visa also told us that [✂].'[721]

717 Visa response to PSR questions dated 5 August 2022. [✂]

718 https://committees.parliament.uk/publications/28459/documents/171158/default/

719 Visa response to PSR questions dated 5 August 2022. [✂].

720 Visa response to PSR questions dated 5 August 2022. [✂].

721 Visa response to PSR questions dated 5 August 2022. [✂].

2.17 In addition, Visa said that its decision to revise its interchange structure was [✂]'. It considered that, [✂].[722]

2.18 We asked Visa to provide any existing documents relating to information that it had considered and/or any analysis it had used/carried out in support of the above statements and in particular that 'Cross-border, ecommerce transactions have unique characteristics, including higher risk of fraud'. [✂]. Visa explained that [✂].[723]

2.19 Visa said it does not have visibility of the costs incurred by issuers due to fraudulent UK-EEA CNP transactions.

2.20 Visa shared with us a report from the European Central Bank (ECB) that presents fraud rates for different types of transactions (for example, CP versus CNP) and in different areas (that is, domestic versus cross-border). The report contains information showing that cross-border CNP transactions are more prone to fraud but does not include anything specific to UK-EEA CNP transactions and does not provide any assessment of the cost impact of this.[724]

2.21 The report explains that in 2019: 'domestic transactions accounted for 89% of the value of all card transactions, but only 35% of fraudulent transactions. Cross-border transactions within SEPA represented 9% of all card transactions in terms of value, but 51% of reported fraud. Although only 2% of all transactions were acquired outside SEPA, they accounted for 14% of fraud.'[725]

2.22 We also asked Visa to provide fraud-level information, specifically for UK domestic and UK-EEA cross-border transactions (both CP and CNP). Visa said that it did not have such information readily available as this [✂]. Visa stated that sourcing the information required time, and, as such, it was not able to share that information with us in the initial timeframe. Subsequently, Visa provided data on fraud levels, and a note that outlined the role of interchange in managing transaction risk and described the provided data.[726] Data were provided in basis points (bps).[727, 728]

- Table 6 shows fraud levels, measured in basis points, reported by Visa for the period 2020 to 2022. Separately, for CP and CNP transactions, it includes: i) the level of fraud for UK domestic transactions (UK cards used at UK merchants; ii) the level of fraud for EEA cards used at UK merchants; and iii) the level of fraud for UK cards used at EEA merchants.
- Table 6 also shows that [✂]. In addition, it shows that [✂].

722 Visa response to PSR questions dated 5 August 2022. [✂].

723 Visa response to PSR questions dated 5 August 2022. [✂].

724 ECB, *Seventh report on card fraud* (October 2021).

725 ECB, *Seventh report on card fraud* (October 2021), page 3.

726 [✂]

727 Fraud levels are calculated by dividing the total value of fraud transactions in a given period of time by the corresponding value of total sales in the same period of time. Note that 100 bps = 1%.

728 Data for 2020 fraud levels refers only to Q3 and Q4 of 2020.

Table 6: Fraud levels 2020 to 2022 reported by Visa (in basis points)

CNP transactions			
Year	**UK card at UK merchant**	**EEA card at UK merchant**	**UK card at EEA merchant**
2020	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]
CP transactions			
Year	**UK card at UK merchant**	**EEA card at UK merchant**	**UK card at EEA merchant**
2020	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]

What third parties told us

2.23 We asked 13 UK issuers, which collectively account for over 90% of UK card transactions by value, for information and opinions on operational costs, including any changes to these, following the UK's withdrawal from the EU when comparing UK-EEA cross-border CNP transactions with UK or EEA domestic transactions.[729]

2.24 Most issuers we contacted told us they had not experienced any changes in operational costs after the UK's withdrawal from the EU.[730] Some issuers told us that fraud rates for CNP cross-border transactions are higher than CP domestic transactions, and this has an impact on the costs of transactions. A few issuers said that UK-EEA cross-border CNP transactions incur higher costs in scheme and processing fees and foreign exchange fees, which are charged by, and represent revenue for, the card schemes.[731]

2.25 Regarding Visa's statement that [✂], we asked several UK acquirers and merchants whether they:

- have experienced any positive impact in terms of fraud levels for UK-EEA CNP transactions following the increases
- know if the increases were used for investments in fraud prevention

729 PSR analysis. [✂].

730 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

731 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

- have experienced a reduced number of rejected UK-EEA cross-border CNP transactions.[732]

2.26 Acquirers and merchants said that they have seen no visible change in fraud prevention for UK-EEA CNP transactions following the increases in UK-EEA CNP IFs. Some also stated that fraud is already addressed via other funding mechanisms.[733]

2.27 We also asked UK issuers how they use the additional income derived from the UK-EEA cross-border CNP IF increases and, in particular, if they re-invested it to increase security and anti-fraud measures.[734] Those who responded confirmed that they do not purposely re-invest this additional income to set up new anti-fraud measures or improve existing ones.[735] We have no reason to believe that EEA issuers take a different approach. However, most respondents said it is difficult for them to keep track of this particular revenue and to keep it separate from other sources: each issuer combines its income streams and bases investment on the overall availability of resources.[736]

Our provisional view in our interim report

2.28 As set out above, the card schemes have said that the risk of fraud in CNP cross-border transactions is higher than in domestic and CP transactions. In our interim report, we set out our understanding from various public statements that IFs can be used towards the costs and risk associated with card issuing, including, but not limited to, the administrative costs of maintaining a card issuing business, and fraud and bad debt costs**.** However, we noted that we had seen no evidence that the structure of IFs is linked to fraud risk and costs, or that it provides incentives for issuers to invest in fraud prevention.

2.29 We also set out that we had not seen any contemporaneous evidence that card schemes' decision makers considered fraud differentials for UK-EEA CNP transactions when deciding to change IF levels on these transactions. We said we had also not seen any direct link between (or calculations relating to) UK-EEA CNP transaction fraud levels and the new IF levels. We noted that we asked Mastercard and Visa for fraud-specific information they had considered when deciding to increase the fees but they could not produce it.

2.30 We set out our understanding that the IF caps relating to transactions where RoW cards are used at EEA merchants set out in the 2019 Commitment decisions took into account fraud costs associated with alternative payment methods to cards.[737] However, we said it was unclear how the fraud costs taken into account in the 2019 Commitments process compare with the fraud rates for card transactions between various countries and regions set out above.

2.31 We also noted that the transactions relevant to the 2019 Commitments (CNP transactions between EEA merchants and consumers from non-EEA countries) are not the same as those relevant to UK-EEA outbound IFs (which are CNP transactions between UK merchants and consumers holding EEA-issued cards). In addition, we observed the UK

732 PSR merchant questionnaire and PSR acquirer questionnaire. [✂].

733 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

734 PSR issuer questionnaire. [✂].

735 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

736 Stakeholder responses to PSR information requests dated 11 January 2023. [✂]

737 European Commission, CASE AT.39398 – Visa MIF, Visa 2019 Commitments decision, recital 78; European Commission, CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision, April 2019, recital 77.

was part of the EEA at the time and so was not among those non-EEA countries. We said that Mastercard's and Visa's decisions to raise UK-EEA outbound IFs to the same level as the IFs governed by the 2019 Commitments suggested that Mastercard and Visa may consider that fraud levels considered when setting the 2019 Commitments for the types of transactions governed by those commitments are comparable to fraud levels for UK-EEA CNP transactions. However, we noted there is little reason to assume that fraud levels for the types of transactions governed by the 2109 Commitments and UK-EEA transactions are the same.

2.32 We said that, while we have not seen the fraud data underpinning the 2019 Commitments levels and therefore cannot draw a direct comparison with that for UK-EEA CNP transactions provided by Mastercard and Visa in the tables above, the data made available to us by Mastercard is suggestive of higher fraud rates for transactions involving countries outside the EEA and the UK (that is, non-SEPA countries) than for transactions between the UK and EEA Member States. We said that, if this is the case, the allowance made for fraud costs in the 2019 Commitments is likely to overstate that which would be reached from an analysis of fraud affecting the transactions relevant to UK-EEA outbound IFs. We noted similarly the ECB data referred to by Visa also suggests that, in relative terms, when non-SEPA countries are involved, fraud levels appear to be higher than for transactions happening within SEPA.

2.33 We said we recognised that if issuers want to, they can use part or all of their revenue from IFs to cover costs and risks associated with card issuing, including investments to mitigate fraud. However, we set out that we had seen no persuasive evidence that shows that individual issuers' fraud prevention investments are directly related to the IF revenue they receive. Indeed, we said we had identified no evidence to suggest the structure or level of IFs is linked to fraud costs or that it provides incentives to invest in fraud prevention.

2.34 Moreover, we said Mastercard and Visa do not appear to have considered data or other evidence of such a relationship in their decision to increase UK-EEA outbound IFs. We said our view on this was confirmed by statements from UK issuers that they do not track the cost of fraud specifically for UK-EEA outbound CNP transactions and have not invested the additional revenue from the higher IF levels to improve fraud prevention for these or other transactions.[738] Accordingly, our provisional view in our interim report was that there is no direct link between the IF levels set by the schemes for UK-EEA transactions and the fraud levels characterising these transactions.

What stakeholders said in response to our interim report

What the card schemes told us

2.35 Mastercard said interchange is a critical revenue stream for issuers, which contributes towards the costs which they incur in relation to payment card transactions, including the cost of guarding against fraud and the cost of remediating it once it has occurred.[739] It said that channels which have higher fraud rates therefore require higher IFs to support any given approval rate.[740] Mastercard stated that merchants benefit directly and indirectly from an

738 Stakeholder responses to PSR information requests dated 11 January 2023. [✂].

739 Stakeholder response to PSR's Fraud Data request [✂].

740 Stakeholder response to PSR's Fraud Data request [✂].

optimal set IF, as issuers can continue to provide card payments and invest in services which make them attractive to consumers through convenience and reduction in fraud.[741]

2.36 Mastercard also stated that CNP transactions always have higher fraud levels than CP transactions ([✂] of card fraud occurs in the CNP space[742]). It reported that, on average, the fraud level is six to seven times higher for CNP transactions than for CP transactions.[743] Mastercard said that for most cardholders a cross-border transaction is unusual, which makes it difficult for Mastercard to identify any patterns to help in preventing fraud. Therefore, issuers will be potentially and often are authorising more fraudulent transactions.[744]

2.37 Mastercard said the 0.2/0.3 IFs were simply too low and would not allow issuers to recover their costs or reflect the value the merchants were receiving.[745]

2.38 Mastercard told us that interchange affects issuers behaviour in two ways:

- It said first that if IFs are set too low for a certain channel, issuers may choose to adjust their risk appetite for this channel directly, and that they have incentives to do so when IFs are too low, as less revenue is generated to cover the cost of each potential fraudulent transaction. It noted that when IFs are too low, an issuer is less likely to approve transactions with fraud risks which it may otherwise have been prepared to approve, leading to lower transaction approvals.[746]
- It added that if interchange is set too low, issuers may invest less in fraud prevention tools. Less refined fraud prevention approaches may lead to a lower tolerance for the potential fraud for each transaction, meaning that a higher proportion of transactions will exceed the risk threshold of the issuer and be rejected.[747]

2.39 Mastercard suggested that we ask EEA issuers if fraud prevention investments are directly related to IF revenue they receive. Issuer investment should consider fraud prevention measures as well as mitigation.[748] It also said that a number of issuers did mention that cross-border CNP transactions are perceived to be more risky or more exposed to fraud.[749]

2.40 Mastercard said that we should conduct analysis on the effect of higher IFs on fraud levels, and the impact on fraud levels and investments if higher IFs were not applied.[750]

2.41 Mastercard said it considers fraud levels as one of the contributing factors in setting IF rates: though it does not have direct information on all fraud costs incurred by issuers, it said that their knowledge of the higher fraud levels for cross-border CNP transactions informed the decision to set a higher level for EEA-UK CNP rates than for UK domestic rates.[751]

741 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
742 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
743 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
744 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
745 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
746 Stakeholder response to PSR's Fraud Data request [✂].
747 Stakeholder response to PSR's Fraud Data request [✂].
748 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
749 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
750 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
751 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

2.42 Mastercard said that it believes that fraud levels that have been recorded for EEA-UK transactions are significantly higher than fraud levels for intra-EEA transactions and therefore justify the increase in UK-EEA outbound IFs.[752] In fact, Mastercard stated that the fraud levels for EEA-UK CNP transactions are [✂] and appropriately reflect costs issuers face for CNP transactions in EEA-UK channel).[753]

2.43 Mastercard said fraud levels on CNP transactions involving EEA cards at UK merchants is closer to fraud levels on CNP transactions for EEA cards at non-EEA merchants, and both are significantly higher than fraud levels for UK domestic CNP transactions.[754]

2.44 In this regard, Mastercard provided the following data:[755]

Table 7: Fraud levels* for different corridors: Mastercard, 2020-2023 (in basis points)

CNP transactions

	EEA cards at EEA Merchants (cross-border only)	EEA cards at UK merchants	RoW cards at EEA merchants	RoW cards at UK merchants
2020	[✂]	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]	[✂]
2023	[✂]	[✂]	[✂]	[✂]

Note: * Fraud transactions as a proportion of all transactions (excluding 'declines').

Source: [✂]. [✂]

2.45 Mastercard told us that the IF affects the approval rates for specific channels of transactions by impacting the risk threshold for that channel of transaction. If IFs are set at sub-optimal levels for a particular channel, the issuer may invest less in fraud prevention tools, causing more transactions to fall above the risk threshold for that particular type of transaction and subsequently be rejected. The issuer may also choose to adjust its risk threshold for that type of transaction directly, leading to lower approvals for that channel.[756.] For example, Mastercard said that, in spite of the higher fraud rates compared to domestic transactions, approval rates for interregional transactions are higher than expected: UK CNP domestic transactions have an approval rate equal to [✂], interregional transactions (including UK-EEA transactions) have an approval rate of [✂] despite showing a threefold fraud rate compared to domestic transactions. Therefore, to keep approval rates at this level, a higher MIF rate is required for UK-EEA CNP transactions.[757] Additionally, increased approval rates imply higher

752 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

753 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

754 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

755 Mastercard response to PSR questions dated 24 April 2024 [✂].

756 Stakeholder submission to the PSR dated 7 March 2024 [✂].

757 Stakeholder submission to the PSR dated 7 March 2024 [✂].

likelihood for merchants to attract and keep consumers, thus generating more revenues. Mastercard stated that there is a causal relationship between higher transaction approval and higher merchant revenues.[758]

2.46 Mastercard said that while they have a rule that prevents issuers from declining a certain set of transactions (selective authorization)[759], [✂].[760]

2.47 Mastercard mentioned that the data provided on outturn fraud rates does not provide full information on fraud risks, as, for example, it does not capture the costs incurred in mitigating fraud risks. It noted that the observed fraud rates always relate to fraud which has occurred despite fraud prevention efforts, and for a given risk appetite, all of which may in turn be influenced by the IFs.[761]

Table 8: Rejected transaction* levels for different corridors: Mastercard, 2020-2023 (in %)

CNP transactions

	EEA cards at EEA Merchants (cross-border only)	EEA cards at UK merchants	RoW cards at EEA merchants	RoW cards at UK merchants
2020	[✂]	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]	[✂]
2023	[✂]	[✂]	[✂]	[✂]

Note: * Rejected transactions ('declines') as a proportion of all transactions (approved and declined).

Source: [✂]. [✂]

2.48 Mastercard noted that in the data submitted to us, in general, [✂]. It said further that a comparison of channels over time shows that in 2023, after interchange rates on CNP transactions between EEA cardholders and UK merchants increased, [✂]. Rejection rates for other channels for which IFs remained unchanged (e.g. rest-of-world cardholders at UK merchants) [✂].[762]

2.49 Finally, Mastercard said that this is consistent with Mastercard's understanding that issuers consider IFs when approving transactions and that UK merchants are likely to have also benefitted from improved approval rates as a result of the change in IFs. Mastercard stated that there are many factors influencing approval rates and so, while this data is not inconsistent

758 Stakeholder submission to the PSR dated 7 March 2024 [✂].

759 See Mastercard Rules (accessed on 20/08/2024), section 6.4 'Selective Authorization'.

760 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].

761 Stakeholder response to PSR questions dated 24 April 2024 [✂].

762 Stakeholder response to PSR questions dated 24 April 2024 [✂].

with the expected underlying relationship, observing approval rates under the revised IFs for only a single year is not a sufficient evidence base to draw strong conclusions.[763]

2.50 Visa said that fraud levels for EEA to UK CNP transactions are around [✁] times higher than fraud levels for intra-EEA transactions, and that fraud levels for EEA to UK CNP credit transactions are similar to fraud levels for RoW to UK ([✁]).[764]

2.51 Visa said that, for the reason mentioned above, IFs are essential in balancing issuers' incentives to manage the inherently higher risks and costs associated with cross-border transactions. It said that this was recognised in the European Commission's 2019 Commitments Decision, which noted that one respondent 'welcomed higher caps for CNP transactions, as they allow issuers to set up the necessary fraud mitigation tools and better invest in the well-functioning of inter-regional transactions'. It also added that this is consistent with the approach undertaken by the European Commission in its 2002 Exemption Decision of Visa's interchange levels at that time.[765]

2.52 Visa said cardholders benefit from significant built-in fraud protection and guarantees, this contributes to a lower average value of fraud incidents on Visa cards, which is £178 for CNP transactions. It also contributes to 98% of funds that were lost to transaction fraud being returned to the customer.[766]

2.53 Visa said that one of the relevant factors as part of the assessment of the level of IF is that for issuers – particularly in the cross-border transaction context – interchange revenue contributes to incentivising investment in transaction risk management, including fraud prevention, and to contribute with associated costs. Visa confirmed that these can include: (1) liability for the cost of any underlying fraudulent transaction; and (2) the cost of maintaining a system for detecting and preventing fraudulent transactions, and also for handling and resolving fraud complaints, including the cost of having a system for handling complaints.[767]

2.54 Visa said that where issuers are not supported with the correct balance of incentives, they may decide to take a more conservative approach to minimise their costs, and that they could, for example, decline a greater number of transactions. Visa stated that IFs contribute to incentivising issuers to invest in transaction risk management, including fraud prevention, and that these investments help issuers authorise transactions in a way that minimise transaction declines.[768]

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763 Stakeholder response to PSR questions dated 24 April 2024 [✁].

764 [✁]. Stakeholder response to PSR's Fraud Data request [✁].

765 Stakeholder response to PSR's Fraud Data request [✁].

766 UK Finance 2023 Annual Fraud Report, p.13-15.

767 Stakeholder response to PSR's Fraud Data request [✁].

768 Stakeholder response to PSR's Fraud Data request [✁].

2.55 In relation to differences in fraud levels between UK-EEA transactions and intra-EEA transactions and similarities with RoW transactions, Visa provided the following data:[769]

Table 9: Fraud levels* for different corridors: Visa, 2020-2023 (in basis points)

CNP transactions				
	EEA cards at EEA Merchants (cross-border only)	**EEA cards at UK merchants**	**RoW cards at EEA merchants**	**RoW cards at UK merchants**
2020	[✂]	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]	[✂]
2023	[✂]	[✂]	[✂]	[✂]

Note: * [✂].

Source: [✂]. [✂]

Table 10: Rejected transaction* levels for different corridors: Visa, 2020-2023 (in %)

CNP transactions				
	EEA cards at EEA Merchants (cross-border only)	**EEA cards at UK merchants**	**RoW cards at EEA merchants**	**RoW cards at UK merchants**
2020	[✂]	[✂]	[✂]	[✂]
2021	[✂]	[✂]	[✂]	[✂]
2022	[✂]	[✂]	[✂]	[✂]
2023	[✂]	[✂]	[✂]	[✂]

Note: * [✂].

Source: [✂]. [✂]

What issuers told us

2.56 [✂] said that [✂]

- [✂]
- [✂]

769 Stakeholder response to PSR's Fraud Data request [✂].

- [✂]
- [✂][770]

2.57 That same issuer also said that (generally speaking) 'the revenues from interchange fees go into a pot that will inform rewards (e.g., cashback on cards) and investment decisions including on fraud'; and that just because this cannot be readily tracked 'it does not mean that it should be so dismissed by the PSR'.[771]

2.58 Another issuer, [✂], justified the IF on the basis of different costs. It said fraud and chargeback costs 'would justify a higher inter-regional interchange rate being applied'.[772] The same issuer said that fraud and chargeback costs for UK-EEA transactions are higher than those for domestic transactions: '[✂] fraud/ chargeback costs for EEA-UK transaction are [✂] higher than EEA domestic CNP transactions (although this can vary over time due to the dynamic nature of fraud).'[773] It also said that fraud is not the only cost issuers face for CNP transactions, and listed other range of fees issuers face, such as 'scheme fees, [✂], servicing costs, operational costs, etc'.[774]

2.59 The same issuer[✂] said 'costs for such transactions are in excess of 20bps, and in some cases can be multiples of 20bps. We would also note that the 20bps applied to domestic EEA CNP transactions pre-dated new fees being introduced, [✂], and therefore may not be the correct benchmark to use. This underlines why it is a major concern for the PSR to apply an interim cap at 20bps before a full study has been conducted.'[775]

2.60 The same issuer [✂] told us that the total Fraud Losses and Fraud Prevention costs in Q1 2024 were [✂] for Visa and [✂] for Mastercard.[776]

2.61 A trade association speaking on behalf of its UK issuer members [✂] said it is likely that issuers operate at a loss for cross border UK-EEA transactions on the old IFR rates. It stated that, in the interim report, there is insufficient exploration of the costs issuers incur for cross border transactions compared to domestic transactions.[777]

2.62 A trade association speaking on behalf of its UK issuer members [✂] said UK issuers state UK-EEA transactional costs, fraud costs and cost of handling non-fraud disputes are all higher than for domestic transactions.[778]

770 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].
771 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].
772 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
773 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
774 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
775 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
776 Stakeholder response dated 13 June 2024 [✂].
777 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
778 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

What acquirers and merchant told us

2.63 An acquirer [✂] said that fraud levels for UK-EEA CNP transactions do not justify the increase in UK-EEA IFs.[779] It also agreed with our findings that issuers have not experienced sufficient changes in their operational costs since the UK's withdrawal from the EEA so as to justify the increase, and that acquirers and merchants (and [✂] itself) have not seen any improvements by issuers in fraud prevention.[780]

2.64 A merchant [✂] said that, with the increased rollout of Strong Customer Authentication (SCA) across the EEA, it did not believe fraud levels justify the five-fold IF increase.[781] In terms of fraud levels more generally, it considers there is no conclusive evidence to show that these are higher for UK-EEA transactions.[782]

2.65 Another merchant [✂] said that fraud levels do not justify the increase IFs.[783]

What other stakeholders told us

2.66 The other stakeholders consulted had mixed views on the question of fraud. A trade association representing EEA acquirers [✂] agreed with our view and said the 'structure and level of the IFs are neither linked to any fraud risk nor any innovation objective.' It also said there is no material change in the UK-EEA transaction that justifies the increase and is strengthened by the fact that the UK remains part of SEPA.[784]

2.67 A trade association representing EEA issuers [✂] said there is higher risk of fraud from international transactions.[785]

Our response to stakeholders' views to our interim report findings

2.68 Card schemes told us that fraud and fraud-related costs in CNP cross-border transactions are higher than in domestic and CP transactions, and that those differentials justified the increases in outbound IFs for cross-border transactions. The issuers made similar arguments. We have seen no evidence that the schemes considered such differentials when deciding to change the IF levels on these transactions.

2.69 In addition, Mastercard and Visa's data shows that, over the period 2020–23, fraud levels for UK-EEA CNP transactions were consistently lower than for those from RoW to the EEA (see Table 7 and Table 9). Therefore, this shows no apparent justification to increase the IFs to the levels used for RoW-EEA transactions. Data from Mastercard also shows UK-EEA fraud levels were declining before the increases, at a very similar pace to intra-EEA CNP transactions. This shows that IFs increases cannot be justified by the need to improve fraud prevention. Data from Visa shows imperceptible variations through the same period.[786]

779 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

780 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

781 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

782 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

783 Stakeholder response to MR22/2.6 dated 25 January 2024 [✂].

784 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

785 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

786 [✂], see: [✂].

2.70 In relation to fraud levels for EEA to UK CNP transactions, Visa said that these are higher than the levels for intra-EEA transactions and that, for credit transactions, these are similar to the levels for RoW to UK. We have reviewed the data provided by Visa and noted that the evidence it mentions relates only to the last year, 2023. A comparison of fraud levels for EEA to UK in relation to intra-EEA transactions shows a lower ratio if the year preceding the increases is considered. For example, fraud levels for EEA to UK are just [✂] larger than for intra-EEA personal credit and debit transactions in 2020, which is the year before the increases in IF took place. In relation to the difference encountered between EEA to UK and RoW to UK, the comparison provided by Visa is also for 2023 and refers only to credit transactions. Taking numbers for both personal credit and debit transactions and year 2020 (the year before the increases) we observe that the difference is of [✂] basis points or [✂] higher for RoW to UK compared to EEA to UK (the same numbers are [✂] basis points and [✂] times when comparing EEA to UK with intra-EEA personal credit and debit transactions in that same year).The analysis for 2020, the year before the IF increase, does not show fraud levels for EEA to UK to be close to ones observed for RoW to UK. The fraud levels for EEA to UK lie between those of intra-EEA and RoW to UK, and are shown to be closer to those of RoW to UK. Therefore, the analysis of fraud levels for these different channels shows that fraud levels could not have been a justification for a need for an increase IF for EEA to UK CNP transactions.[787]

2.71 Both schemes also provided data on rejected transactions for different corridors between 2020 and 2023. Mastercard said these show a decline in rejections for UK merchants after the increase in IFs. In contrast, they said, rejected RoW transactions increased for UK merchants, where IFs remained unchanged (see paragraph 2.48). We do not believe this argument proves a relationship between IFs and fraud costs, as Mastercard intends to imply. As Mastercard recognises, the evidence is not sufficient to draw strong conclusions (approval rates under the revised IF are only observed for a single year; see paragraph 2.49). In addition, the decline in rejected transactions happened at the same time of an increase in the fraud levels: if a positive effect existed derived from fraud prevention investments (related to IF revenue received) this should have been observed alongside an improvement or at least no change in fraud rates for the same period, but this was not the case. Finally, though we would expect any relationship between IFs and fraud costs to hold for other players in the industry, we have not seen similar trends in Visa's data.

2.72 The above findings allow us to conclude there is no clear relationship between the outbound IF increases and the fraud levels for the corresponding transactions. CNP and cross-border transactions are typically characterised by higher fraud levels than CP and domestic transactions, but there is no evidence that the outbound IF increases were needed to (or have encouraged issuers to) invest in the security of the relevant transactions to the benefit of merchants and consumers.

2.73 EEA CNP fraud levels do not justify the UK-EEA IF increases, and issuers have experienced no changes in their operational costs that could explain the five-fold IF increase.

787 PSR analysis of data submitted by Visa [✂], see: [✂].

Issuer costs

What stakeholders said in response to our Interim report

2.74 Visa said issuers take on the vast majority of the risk associated operating expense, particularly for cross border and CNP transactions which involve more risk than domestic and CP transactions, and because of this, issuers need sufficient incentives (which includes revenue from IFs) to optimally invest in cross-border transactions.[788]

2.75 A trade association speaking on behalf of its UK issuer members [✂] said that the IFR and EC 2019 Commitment cast 'did not consider issuers' costs'. However, it considered that consideration of such costs (specific to card industry elements or 'card platform costs, card fraud prevention technologies, customer servicing and handling claims, amongst others') is needed. It said that placing caps below input costs 'is not going to increase competition in the issuing sector, nor support further development in innovation or fraud protection'.[789]

2.76 The same trade association [✂] told us that issuers 'invest and incur costs, such as claims, service, security, fraud, digital wallets, card specific platform and innovation', all of which are relevant long-run costs.[790] It also said that in the context of cross border UK-EEA transactions, issuers operate at a loss at the old IFR rates, due to high costs related to 'cross border transactional costs, fraud costs and the cost of handling non fraud disputes'.[791]

2.77 The same trade association said that a more consistent policy approach is needed [✂], that the value and proposition of payment service providers requires solutions that 'cover costs and pay for innovation and investment'.[792]

2.78 A trade association who represents EEA issuers, acquirers, and card schemes [✂] said that interchange provides economics that underpin key elements of the payment ecosystem, including acceptance, innovation, security, fraud protection, and guaranteed payments to merchants. Interchange is crucial for a healthy acquiring ecosystem, driving acceptance among new merchants, therefore it should be at a high enough level that it incentivises new players in the space and low enough for merchants to adopt digital payments.[793] It said the levels of 0.2/0.3 are insufficient and do not cover issuer costs, in particular fraud costs, of cross border CNP transactions. The trade association offered to provide assistance on further supporting this point.[794]

2.79 An issuer [✂] told us that at minimum, 'the actual costs incurred by issuers must be taken into account when calculating a fair interchange fee for specific transaction types'.[795]

788 Stakeholder response to MR22/2.6 dated 29 February 2024 [✂].
789 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
790 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
791 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
792 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
793 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
794 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].
795 Stakeholder response to MR22/2.6 [✂].

2.80 Following the publication of our interim report, one issuer [✁] provided data on its issuing costs for EEA CNP debit transactions at UK merchants, for 2020 and for the first quarter of 2024 (Table 11).

Table 11: Transaction costs (excluding rebates) for EEA CNP debit transactions at UK merchants, in basis points: 2020 and 2024 (first quarter).

	Mastercard 2020	Visa 2020	Mastercard 2024 (Q1)	Visa 2024 (Q1)
Direct costs	[✁]	[✁]	[✁]	[✁]
Scheme costs	[✁]	[✁]	[✁]	[✁]
Switch costs	[✁]	[✁]	[✁]	[✁]
FX-related costs (if applicable)	[✁]	[✁]	[✁]	[✁]
Digital-wallet-related costs	[✁]	[✁]	[✁]	[✁]
Fraud-related costs	[✁]	[✁]	[✁]	[✁]
Cashback costs	[✁]	[✁]	[✁]	[✁]
Other vendor costs	[✁]	[✁]	[✁]	[✁]
Total direct costs	[✁]	[✁]	[✁]	[✁]
Indirect costs	[✁]	[✁]	[✁]	[✁]
FinCrime/ Support costs	[✁]	[✁]	[✁]	[✁]
Digital-wallet-related costs	[✁]	[✁]	[✁]	[✁]
Operating costs	[✁]	[✁]	[✁]	[✁]
Top-up costs	[✁]	[✁]	[✁]	[✁]
Total indirect costs	[✁]	[✁]	[✁]	[✁]
Total direct + indirect costs	[✁]	[✁]	[✁]	[✁]

Note: Data refers mainly to debit transactions [✁].
Source: [✁] submissions dated 17 May 2024 and 5 June 2024 [✁]. [✁]

2.81 The issuer [✁] also provided data on the values of fees paid to the card schemes and the rebates received from card schemes, for UK and Europe debit card activities. There is some variation in the rebate rates throughout the period, but most of them are close to [✁] in recent years (see Table 12).

Table 12: UK and Europe card scheme and processing fees and rebates for [✁]

	Mastercard Paid (€ million)	Mastercard Rebated (€ million)	Mastercard Rebate rate (%)	Visa Paid (€ million)	Visa Rebated (€ million)	Visa Rebate rate (%)
2024	[✁]	[✁]	[✁]	[✁]	[✁]	[✁]
2023	[✁]	[✁]	[✁]	[✁]	[✁]	[✁]
2022	[✁]	[✁]	[✁]	[✁]	[✁]	[✁]
2021	[✁]	[✁]	[✁]	[✁]	[✁]	[✁]
2020	[✁]	[✁]	[✁]	[✁]	[✁]	[✁]

Note: Fees paid to the card scheme and incentives and rebate payments received from card schemes (includes [✁).

Source: PSR internal calculations using [✁] submission dated 13 June 2024 [✁]. [✁]

2.82 To estimate the effect of rebates on costs, we assumed three different rebate rates: 80%, 90% and 95%. The results show that, when rebates are excluded from the costs, total costs for debit cards are far below the MIFs charged by Visa and Mastercard: even in the extreme 80% case, the value of MIFs for debit cards (115 basis points) is significantly higher than the reported costs (see Table 13).[796]

796 Stakeholder response to PSR information request dated 13/06/2024 [✁]

Table 13: Transaction costs for UK-EEA outbound CNP transactions 2024 (first quarter): assumptions for different rebate rates 80%, 90% and 95%.

	Mastercard	Visa
Rebate Rate = 80%		
Scheme costs	[✂]	[✂]
Total Direct Costs	[✂]	[✂]
Total Direct + Indirect Costs	[✂]	[✂]
Rebate Rate = 90%		
Scheme costs	[✂]	[✂]
Total Direct Costs	[✂]	[✂]
Total Direct + Indirect Costs	[✂]	[✂]
Rebate Rate = 95%		
Scheme costs	[✂]	[✂]
Total Direct Costs	[✂]	[✂]
Total Direct + Indirect Costs	[✂]	[✂]

Note: Data refers mainly to debit transactions [✂]. Scheme costs calculated using different rebate rates assumptions.

Source: Stakeholder submission dated 17 May and PSR calculations [✂]. [✂]

2.83 The above data represents aggregate UK and Europe fees and rebates that [✂] received from each of the schemes for all UK and Europe transactions, and not just for EEA to UK CNP transactions. This was the only information that the issuer was able to offer us initially.

2.84 Later in the review [✂] provided us with data that relates specifically to EEA to UK CNP transactions that it said provides a more accurate reflection of fees and rebates for EEA to UK CNP transactions. [✂] said that the reasons for offering such more granular data only much later in the process is that the schemes do not report on specific transaction corridors. [✂] has then calculated the actual rebates received against EEA to UK CNP transactions using its own data. [✂] then sought approvals from both Visa and Mastercard to share such confidential rebates data with us. Having obtained the required consent, [✂] was able to add the rebates data to the table previously shared with us, to illustrate the evolution of fees and rebates for EEA to UK transactions since 2019.[797]

797 See Stakeholder letter to PSR dated 24/07/2024, submitted as part of the putback process [✂].

Table 14: Scheme and Processing costs for EEA to UK CNP

Mastercard	2019	2020	2021	2022	2023	2024*
Scheme & Processing Fees	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Mastercard Rebates (%)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]***
Transaction Volumes (No.)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Transaction Values (GBP)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Visa						
Scheme & Processing Fees	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Visa Rebates (%) ([✂])	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Visa Net Rebates** ([✂])	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Transaction Volumes (No.)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Transaction Values (GBP)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total Mastercard+Visa	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

* 2024 figures reflect up to Apr.24

** [✂].

*** [✂].

2.85 In providing such data [✂] said that this data is [✂] specific and is likely not representative of EU issuers. They said that in their view most EU issuers will not receive rebates at the levels included in Table 14, because each issuer likely has a different deal with the schemes and will have very different economics (both in terms for scheme and processing fees and potential rebates). [798]

2.86 [✂] said that the level of rebates that they received in 2024 is due to [✂]'s increased ability to negotiate preferential terms from Mastercard and Visa considering [✂]. [✂] also said that the rebates also come with contractual targets which [✂] must meet to avoid having the rebates reduced. [799]

2.87 [✂] said that new or smaller issuers would likely be unable to negotiate similar rebate structures with the schemes given their [✂]. It is for this reason that [✂] suggested we should not consider [✂] data to be indicative of the levels of rebates EEA issuers are able to secure from the card schemes. [800]

798 See Stakeholder letter to PSR dated 24/07/2024, submitted as part of the putback process [✂].

799 See Stakeholder letter to PSR dated 24/07/2024, submitted as part of the putback process [✂].

800 See Stakeholder letter to PSR dated 24/07/2024, submitted as part of the putback process [✂].

2.88 [✂] said it believes it would then be useful to consider rebate rates of [✂] or lower so that also above mentioned new or smaller issuers are captured. [801]

2.89 [✂] shared the following scenarios, that is, scenarios that consider different rebate levels against the scheme and processing fees, including the level of rebates that they currently receive from the schemes ([✂]) and the level of rebates that would be more representative of what new and smaller issuers are likely to receive ([✂] or lower). [802]

Table 15: Transaction costs for UK-EEA outbound CNP transactions 2024 (first quarter): assumptions for different rebate rates

	[✂]	[✂]
Rebate Rate = 0%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 30%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 40%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 50%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 60%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps

801 See Stakeholder letter to PSR dated 24/07/2024, submitted as part of the putback process [✂].

802 See Stakeholder letter to PSR dated 24/07/2024, submitted as part of the putback process [✂].

	[✂]	[✂]
Rebate Rate = 75%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 80%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 90%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps
Rebate Rate = 95%		
Scheme costs	[✂] bps	[✂] bps
Total Direct Costs	[✂] bps	[✂] bps
Total Direct + Indirect Costs	[✂] bps	[✂] bps

2.90 The issuer [✂] also provided information on fraud and chargeback costs for EEA domestic CNP transactions and for EEA to UK CNP transactions, for both Mastercard and Visa (average calculations for 2022, 2023 and the first quarter of 2024). The results (see Table 16) show that the differences between EEA domestic and EEA-UK are in the order the order of [✂] basis points (2023 and 2024), [✂] (2022). [803]

Table 16: Issuer's fraud and chargeback costs CNP in basis points – (excluding fraud recoveries and indirect costs)

	Mastercard EEA to UK	Visa EEA to UK	Mastercard EEA domestic*	Visa EEA domestic*
2022	[✂]	[✂]	[✂]	[✂]
2023	[✂]	[✂]	[✂]	[✂]
2024 (Q1)	[✂]	[✂]	[✂]	[✂]

Note: Data as provided by [✂]. Figures reflect actual costs in bps (averages rounded up). * Figures reflect CNP transactions where both merchant and issuer are in the same country.

Source: [✂][✂]

803 Stakeholder response to PSR information request dated 17/05/2024 [✂]

2.91 An acquirer [✂] submitted that issuers' relevant costs are not linked to the IF in practice. It said the 'safety, reliability, simplicity, and technological benefits' of card networks are already 'related to the scheme and processing fees' (and not to the IFs).[804] It told us this is also the case for the 'payment guarantee' provided by issuers, which is already accounted for by collateral from issuers ('the payment guarantee arrangement involves Visa and Mastercard taking collateral from issuers to ensure payments are settled').[805]

2.92 In relation to issuer costs, [✂] the same acquirer also said that past issuer cost analyses have 'erroneously assumed that issuers should be compensated for their entire cost of issuing and processing' a card. Instead, it said one should really ask what are the costs that are borne 'by issuers which create a benefit to the system which merchants exclusively benefit from'.[806] [✂] The acquirer said that these costs do not exist.

2.93 In consequence, [✂] submitted that there is no need for IFs and that this is something that has already been found in past decisions. It provided us with the example that, in the IFR, the European Commission found multiple times during its Impact Assessment that 'the complete prohibition of MIFs would be the best Regulatory outcome'.[807] It said this is also made clear in the recitals of the IFR: 'a prohibition of interchange fees for debit card transactions would be beneficial for card acceptance, card usage, the development of the single market and generate more benefits to merchants and consumers than a cap set at any higher level'.[808]

Our response to stakeholders' views to our interim report findings

2.94 Neither Mastercard nor Visa were able to give us cost information to understand whether and to what extent outbound IF increases were needed to enable issuers to recover all of their costs. We did receive a submission on this point from one EEA (and UK) issuer [✂], who told us that at a minimum, 'the actual costs incurred by issuers must be taken into account when calculating a fair interchange fee for specific transaction types'.[809] We asked this issuer to provide information on 2020 and 2024 issuing costs.[810] Based on that information, we note the following:

- Total direct costs for debit cards[811] account for [✂] basis points (for Mastercard and Visa respectively) in 2024, and can reach [✂] basis points if indirect costs are also included (see Table 11).[812]

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804 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

805 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

806 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

807 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

808 Stakeholder response to MR22/2.6 dated 31/01/2024 [✂].

809 Stakeholder response to MR22/2.6 dated 14/02/2024 [✂].

810 Costs are measured by dividing the overall costs incurred in a given period of time by the corresponding total transaction value in the same period of time. Note that 100 bps = 1%.

811 The information provided relates to debit transactions mainly [✂].

812 According to the issuer, these include financial crime / support costs, digital-wallet-related costs, operating costs and top-up costs.

- However, the schemes typically provide incentive and rebate payments on scheme and processing fees[813]. Based on the range of rebates reported by the issuer (see Table 12) we made various calculations of the different net costs. We find that direct cost (net of rebates) can amount to between [✂] and [✂] basis points, whereas total incurred costs (including indirect costs) amount to between [✂] and [✂] basis points for debit cards (see Table 13). In both cases the costs are significantly lower than the MIF value charged for debit cards: 115 basis points. This result holds regardless of the assumption used for the rebates.[814]
- Fraud-related costs account for [✂] and [✂] basis points, for Mastercard and Visa, respectively[815], which is around [✂] of the total incurred costs (net of rebates) by the issuer on each of the cards.

2.95 The issuer also provided information on fraud and chargeback costs for EEA to UK transactions and domestic[816] CNP EEA transactions, for both Mastercard and Visa in the period from 2022 to the first quarter of 2024 (costs exclude any fraud recoveries and indirect costs). The data reflects the following (Table 16):

2.96 Fraud-related costs for EEA to UK CNP shows high figures: in the period 2022-2024(Q1) these range between [✂] ([✂], 2022) and [✂] basis points ([✂], 2023).

2.97 For EEA domestic CNP transactions, fraud-related costs are much lower and range between [✂] ([✂], 2024, Q1) and [✂] basis points ([✂], 2023).

2.98 The difference between cross border costs (EEA to UK) and EEA domestic CNP yields values that range from [✂] basis points ([✂], 2022) to [✂] basis points ([✂], 2023). The values obtained this way are small in relation to the 95 basis points difference that can be obtained comparing in the IF for debit cross-border (115) and domestic (20) transactions.

2.99 Although we do not treat the results as representative of the sector, they are useful to show that, for one issuer, outbound IF levels for debit cards (115 basis points) are higher than the total costs reported for EEA to UK CNP transactions, and significantly higher when the incentives and rebates on scheme and processing fees are accounted for.

2.100 We have also noted that fraud-related costs for Mastercard and Visa account for a significant proportion of incurred costs of debit cards but fall very short of current outbound IFs. The data from this issuer does not seem to corroborate the claim made by the schemes and some issuers that fraud-related costs are an important factor to explain the increases.

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813 See also MR22/1.9: Market review of card scheme and processing fees interim report, para 5.39.

814 As mentioned in paragraph 2.84, later in the review [✂] provided us with data that relates specifically to EEA to UK CNP transactions that it said provides a more accurate reflection of fees and rebates for EEA to UK CNP transactions. The data included in Table 14 provide a very similar picture: Based on the range of rebates reported by the issuer (see Table 14) we can conservatively assume that the issuer receives rebate payments on scheme and processing fees for over 80%. In that case, based on the scenarios calculated by the same issuer (see Table 15), we find that direct cost (net of rebates) can amount to [✂] basis points, whereas total incurred costs (including indirect costs) amount to [✂] basis points.

815 Total fraud losses and fraud prevention costs have been calculated adding 59% of FinCrime costs, for both schemes, as instructed by the issuer (follow up question received from [✂] on 12 June 2024).

816 EEA domestic CNP figures are defined as those transactions for which both the merchant and the issuer are from the same country.

2.101 Finally, we have seen that fraud-related costs are higher for UK cross-border than UK domestic debit transactions, but the difference between both type of transactions is small, and it only accounts for a fraction of the difference between cross-border and domestic debit IFs. Hence, fraud-related costs for cross-border transactions cannot justify the increase in debit IFs, despite what many respondents have told us.

Cost to merchants of alternative payment methods

What the card schemes told us

2.102 Mastercard explained to us in its response that the cost to merchants of relevant alternative payment methods is an important factor it considers when setting IFs for UK-EEA CNP transactions, 'not least because it is an indication of the value of card payments to merchants'.[817]

2.103 Mastercard explained that it 'always held the view that the prevailing rates were too low and had fallen below costs over time (particularly given these related to cross-border CNP transactions), since the Interchange Fee Regulation used a benchmark based only on cash (and even then only a limited range of cash costs)'.[818]

2.104 It appears that Mastercard's view is that the merchants would face higher costs for alternative payment services, especially for costs relating to accepting cross-border CNP transactions.[819]

2.105 For inbound IFs, Mastercard explained that it applied the IF rates contained in the 2019 Commitments in relation to inter-regional transactions 'which had been accepted based on a consideration of the alternative transaction methods available for those transactions, recognising cash was not such an alternative for card not present transactions'.[820]

2.106 In terms of alternatives, Mastercard stated that the European Commission investigation that concluded with the 2019 Commitments had considered three-party schemes, cash, bank credit transfers and e-money transfers as alternative measures, 'with the European Commission placing more weight on the latter options in determining the interchange fee levels which should apply'.[821] However, in another response, it stated that 'an estimate of the cost of bank transfer payments ultimately informed the card not present rates the European Commission used to determine the interchange caps that were part of those Commitments'.[822, 823]

817 Mastercard response to PSR questions dated 5 August 2022. [✂].

818 Mastercard response to PSR questions dated 5 August 2022. [✂].

819 [✂].

820 Mastercard response to PSR questions dated 12 January 2022. [✂].

821 Mastercard response to PSR questions dated 5 August 2022. [✂].

822 Mastercard response to PSR questions dated 12 January 2022 and 16 March 2023. [✂].

823 European Commission, CASE AT.40049 Mastercard II, Mastercard 2019 Commitments Decision, April 2019, recitals 78 and 85.

2.107 Mastercard also told us that some of the main alternatives for cross-border transactions are:

- cash
- alternative cards, such as American Express
- PayPal[824]

2.108 Internal documents from Mastercard [✁]. Mastercard told us that the documents specific to the decision taken at the time when developing options involving higher fees include an implicit understanding by Mastercard and its senior team that the regulated rates of 0.2%/0.3% did not represent a level that would ensure efficient outcomes, particularly for CNP transactions, given the alternatives merchants would turn to instead of cards.

2.109 Visa said that the previous IF levels were established by the European Commission based on an assessment of the costs of processing CP payments versus cash payments. Hence, there was no consideration of e-commerce environments because cash is not a ‘comparator’ for CNP transactions, which take place in different environments. It added that it considered [✁].[825]

2.110 Visa also said that it [✁].[826]

2.111 In addition, Visa said that [✁].[827]

2.112 For example, one of the internal governance documents that Visa shared with us states that [✁]. The document also states, [✁].[828]

2.113 We asked Visa for details [✁] of alternative payment methods.[829] In response, Visa said that [✁].[830]

2.114 Visa, however, further stated that ‘CNP payments have a multitude of alternative options, including Amex, PayPal, China Union Pay, AliPay and bank transfers’.[831]

2.115 Internal governance documents from Visa, produced at the time of its decision in relation to proposed changes to IFs, show that when deciding to increase the IF for UK-EEA CNP transactions, it considered [✁].[832, 833]

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824 Mastercard response to PSR questions dated 12 January 2022. [✁].

825 Visa response to PSR questions dated 5 August 2022 [✁].

826 Visa response to PSR questions dated 5 August 2022 [✁].

827 Visa response to PSR questions dated 5 August 2022 [✁].

828 Visa, [✁].

829 Visa response to PSR questions dated 5 August 2022 [✁].

830 Visa response to PSR questions dated 5 August 2022 [✁].

831 Visa response to PSR questions and Visa dated 12 January 2022 [✁].

832 Visa response to PSR questions dated 12 January 2022 [✁].

833 Visa response to PSR questions dated 12 January 2022 [✁].

2.116 We then asked Visa to provide any contemporaneous documents that support these statements.[834] Visa stated that, when making these statements (and considerations), it [✂].[835] [✂], Visa also said that there was publicly available information [✂]. For example, it stated:

- Account-to-account and/or digital wallet solutions, such as PayPal, cost UK merchants/acquirers between approximately between 2.49% and 4.19% per transaction
- For American Express, merchants are charged 3.95%, on average, for global transactions, plus a fixed fee
- For [✂], a BNPL provider, a typical fee is between 2.60% and 2.99%, plus a fixed fee

Our provisional view in our interim report

2.117 In our interim report, we said that where IFs need to be set by a regulator, they can be set based on the cost to merchants of accepting other payment methods. We said this is one possible approach and it is also the approach that sits behind the MIT – a test that has been used by the European Commission to cap specific IF levels set by Mastercard and Visa (EU IFR and 2019 Commitments). We said the evidence we have seen gives no specific information that the card schemes used the costs of other payment methods in the UK-EEA context in setting the new IF levels; as such, it appears they did not use an MIT or appropriate alternative to calculate these levels. We noted that the schemes set out a qualitative argument about alternative payment methods but did not provide any quantitative analysis as to how these costs related to the actual fee increases.

2.118 We set out that, collectively, Mastercard and Visa directly or indirectly mentioned the following payments as alternatives:

- PayPal
- three-party card payment schemes (such as American Express)
- cash
- other means of payment that can be funded by bank transfers, such as e-wallets, e-payments or bank transfer payments.

2.119 We noted that a digital wallet ([✂]) heavily relies on Mastercard and Visa rails both in the UK and in the EEA. We set out its scale first in the UK, second in the EEA, and then cross-border. In 2022, [✂] of this digital wallet's total UK domestic transactions by value were card based, and Mastercard and Visa alone accounted for [✂] of its total UK domestic transactions (that is, just [✂] of its total UK domestic transactions by value were made using alternative card schemes).[836] Within the EEA, [✂] of this digital wallet's transactions by value were card based, and [✂] of total transactions were made with a Visa- or Mastercard-branded card. In terms of cross-border payments, [✂] of transactions, by value, made by EEA consumers at UK merchants using this digital wallet were card based, with [✂] made using Visa- or Mastercard-branded cards (that is, just [✂] of these transactions by value were made using

834 Visa response to PSR questions dated 5 August 2022. [✂].

835 Visa response to PSR questions dated 5 August 2022. [✂].

836 PSR internal analysis of data submitted by a digital wallet [✂] as part of the Section 81 notice. [✂].

alternative card schemes).[837] We noted that the cost of its services to merchants will incorporate Mastercard or Visa IFs (and scheme and processing fees), including for UK-EEA CNP transactions. As such, we said that this digital wallet's payment services do not represent a suitable alternative for benchmarking the card schemes' pricing.

2.120 We set out our understanding that cash was mentioned by Mastercard only as a relevant alternative in the context of CP, not CNP, transactions.[838]

2.121 We said we had not seen any evidence that Mastercard or Visa considered the cost of relevant or appropriate alternatives, such as bank transfer payments and the other payment methods that bank transfers can fund, such as e-wallets. We said, as Mastercard also stated, the European Commission relied on an estimate of the cost of non-SEPA bank transfer payments when it evaluated the levels informing the 2019 Commitments.[839] We went on to say that, in the UK-EEA context, SEPA bank transfers would be the relevant alternative to consider. We noted that, despite this, we had not seen any specific assessment or consideration from Mastercard or Visa on the costs of this alternative.

2.122 We also noted that for the 2019 Commitments made by both Mastercard and Visa, the relevant comparator for CNP cross-border transactions was (non-SEPA) bank transfers.[840] PayPal and American Express were not included as comparators.

2.123 Our provisional view in the interim report was that the current levels have been set seemingly arbitrarily and free from competitive constraints, representing a failure on the part of the card schemes to consider what might be an appropriate methodology or benchmark for UK-EEA CNP IFs.

What stakeholders said in response to our interim report

What acquirers told us

2.124 UK acquirers did not provide any comment on this issue.

What merchants told us

2.125 UK merchants did not provide any comment on this issue.

What issuers told us

2.126 An issuer [✁] said that it considers that we have not shown that there is a lack of competition specifically in the CNP EEA to UK transactions, or that it is creating negative effects on a scale significant enough to materially impact UK merchants or consumers. It told us it considers that a comprehensive analysis is required to assess the pricing and availability of alternative payment methods, aiming to ascertain whether the charges to merchants are below, above, or on par with current Mastercard and Visa solutions.[841]

837 PSR internal analysis of data submitted by a digital wallet [✁] as part of the Section81 notice. [✁].

838 Mastercard, Letter to the Treasury Select Committee (2 August 2022), page 7.

839 European Commission, CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision (April 2019), recitals 78 and 85.

840 European Commission, CASE AT. 40049 – Mastercard II, Mastercard 2019 Commitments decision (April 2019) recital 79(b) and European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision (April 2019), recital 80(b).

841 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

What the card schemes told us

2.127 Mastercard noted that alternative payment methods, when facing cross-border transactions, tend to charge higher fees to merchants.[842]

2.128 Mastercard said competitive pressure from Visa is not the only consideration which Mastercard takes into account when setting IF levels. It considers the interests of all parties in the payments ecosystem and not issuers alone and selects the optimal rate that would benefit all parties (including merchants). Competition between issuers is intense, and if IFs were to be lowered, issuers would have to make up the revenue shortfall from elsewhere, such as through reduced services, worse foreign exchange rates or the introduction of transaction fees, which would affect merchants either directly or indirectly through discouraging sales (or diverting them to online merchants based elsewhere to whom such charges may not apply). It could also drive consumers to alternative, competing payment methods, such as three-party cards or BNPL, that are likely to be more expensive for merchants to accept.[843]

2.129 Visa said that popular payment alternatives to the Visa (and Mastercard) card schemes for EEA to UK CNP transactions are more costly for UK merchants to accept than a Visa or Mastercard. It said that publicly available information indicates that the cost to UK merchants of accepting transactions from EEA consumers using, e.g., a three-party card scheme such as American Express is approximately 3.95%, PayPal is 4.19% together with an additional fixed fee of £0.20-0.40 per transaction, and **[✂]** (based on an average fee) is 2.68% together with an additional fixed fee of £0.37 per transaction.[844]

2.130 Visa added that this also ensures UK merchants continued to benefit from it participating in a level competitive playing field, particularly in circumstances where IFs comprise issuer revenue, and the consequence of cardholders turning to popular non-four-party card scheme alternative payment methods (such as American Express, PayPal and **[✂]**) is that UK merchants would pay significantly more, and not less, than the cost of accepting a Visa card.[845]

Our response to stakeholders' views

2.131 Mastercard and Visa mentioned different alternative payment methods in their responses, all of which are provided at higher prices. However, the alternatives mentioned relate to payment systems which include an explicit or implicit IF, as they either are three-party schemes (American Express) or heavily rely on underlying card transactions (PayPal). We also note that **[✂]** BNPL solutions are [✂]. We therefore do not think the comparators being proposed are suitable.

2.132 Furthermore, we have not seen evidence that Mastercard or Visa considered the cost of bank transfer payments (for example SEPA bank transfers) when setting the increase in IFs. We note that the European Commission relied on an estimate of the cost of non-SEPA bank transfer payments when it evaluated the levels informing the 2019 Commitments.[846]

842 Stakeholder response to MR22/2.6 dated 29 January 2024 [✂].

843 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

844 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

845 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

846 See European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision recital 80(b) and CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision recital 79(b).

In the UK-EEA context, we consider that SEPA bank transfers would be the relevant alternative to consider.

2.133 For these reasons, our final view is that the current IFs have been set seemingly arbitrarily and not in accord with what would be an appropriate methodology or benchmark for UK-EEA CNP IFs.

Methodological issues raised

What the card schemes told us

2.134 Both Mastercard and Visa explained that one of their reasons for increasing their UK-EEA CNP IFs was methodological flaws in a study commissioned by the European Commission in 2015 (the European Commission study).847 They considered that these flaws made the study unsuitable as the basis to set IF levels for UK-EEA CNP transactions.

2.135 Mastercard told us that in its view the 0.2%/0.3% IF levels were too low and had fallen below costs over time, particularly for cross-border CNP transactions. Mastercard also told us that this was because the European Commission study[848], which underpinned the IFR caps, used a benchmark based only on cash and even then included only a limited range of cash costs.[849]

2.136 Mastercard provided two 2016 presentations from the consultancy [✂][850] providing 'further details on Mastercard's view on the limitations of the assessment underpinning the imposed IFR rates'.[851]

2.137 In particular, one of the two 2016 documents included a number of criticisms of the European Commission study in general and in relation to the applicability of its findings to the costs incurred by EEA merchants for accepting payments from outside the EEA. The document mentioned:

- **The non-suitability of cash as a comparator:** In an inter-regional context, due to the high proportion of credit and online transactions, cash may not, even in principle, be a suitable alternative, while other alternatives to four-party card payments exist. The analysis from the consultancy [✂] adjusted the European Commission study estimates by considering American Express and PayPal among the relevant comparators – that is, it was not based solely on cash and did not include bank transfers.
- **Limited and non-representative merchant sample:** The number of merchants that responded to the merchant survey was too low and the sample turnover was dominated by large merchants in the retail sector, which is a poor representation of the 'average merchant' for the purposes of a MIT. The analysis from the consultancy [✂] adjusted the European Commission study estimates by considering a merchant size that

847 European Commission, *Survey on merchants' costs of processing cash and card payments: final results* (March 2015).

848 European Commission, *Survey on merchants' costs of processing cash and card payments: final results* (March 2015).

849 Mastercard response to PSR questions dated 5 August 2022. [✂].

850 [✂].

851 Mastercard response to PSR questions dated 5 August 2022. [✂].

in its view was likely to be a better estimate of the overall average MIT MSC than an estimate based on the merchant size considered by the European Commission.

- **Self-selection and reporting bias:** Participation depended on whether the MIT was likely to be in the merchant's 'best interest' – that is, whether it perceived cost of cards was high relative to cash, leading to low MIT IF estimates by construction. In addition, merchants in the sample would have had an incentive to provide responses in line with the desired final result. Questions that require an element of judgement are likely to be particularly susceptible to such biases.
- **Cost of processing payments:** The European Commission study focused too much on the short term and did not sufficiently consider long-term scenarios where fixed costs become variable. The analysis from the consultancy [✂] adjusted the European Commission study estimates by using econometric techniques to give more prominence to the longer run and the related absence of fixed costs.

2.138 Visa told us that its decision to increase the level of UK-EEA consumer cross-border IFs was taken as [✂].[852]

2.139 Visa explained that: 'A clear difference between a CP transaction and a CNP transaction is that cash is not a "comparator" for CNP transactions, which take place in different environments. This is important because the pre-existing interchange levels of 20/30bps (mandated by the EU IFR) were established by the European Commission on the basis of a single methodology which used surveys conducted in 2012/2013 across 10 different Member States. These surveys focused only on analysing merchants' costs of processing CP card payments versus cash payments in order to support the European Commission's view of an appropriately harmonised level of EEA-wide interchange at that time. There was no consideration of ecommerce environments, and for this reason alone, levels of 20/30bps would not be appropriate for CNP transactions, particularly in light of the substantial growth in the proportion of CNP transactions since that time.'[853]

2.140 Specifically, on 'the nature of the underlying analysis that established the rates of 20/30bps', Visa told us that 'The European Commission established interchange caps of 0.2%/0.3% in the EU IFR on the basis of the so-called "Merchant Indifference Test" (MIT), based on which the European Commission sought to equate merchants' costs of accepting card payments only with those of accepting cash.' The analysis mentioned by Visa is the one included in the 'European Commission Survey on merchants' costs of processing cash and card payments' (that is, the European Commission study).[854]

2.141 Visa said that, in its view, the European Commission study contained a number of methodological flaws that make it inappropriate to be used as a basis for supporting UK-EEA cross-border interchange at a level of 0.2%/0.3% today.[855] In particular, Visa stated that the European Commission study:

- Did not specifically analyse EEA cross-border transactions; Visa stated that [✂].'[856]

852 Visa response to PSR questions dated 5 August 2022. [✂]

853 Visa response to PSR questions dated 5 August 2022. [✂]

854 European Commission, *Survey on merchants' costs of processing cash and card payments: final results* (March 2015).

855 Visa letter to the PSR dated 14 October 2022. [✂]

856 Visa, [✂].

- [✁] Visa stated that [✁].' [857]
- Did not include any analysis of CNP transactions; Visa stated that [✁].'[858]
- Focused exclusively on cash as the only comparator to card payments; Visa stated that [✁]. Visa added that [✁]. As such, [✁].' [859]

2.142 Internal governance documents from Visa also address this issue. For example, in one of its internal governance documents, Visa stated that 'The current consumer EEA interchange rates (0.20% Debit and 0.30% Credit) were based on a domestic cost of cash study. The study did not take account of the fact that domestic cash is not a comparator for cross-border CNP transactions (as recognised in the different rates for CNP transactions agreed with the Commission in the European Commission Commitments).' In the same document, it also stated: 'We have consistently argued, and we believe, it has been demonstrated, that [✁] and [✁][860]

2.143 Visa provided evidence consistent with it holding the view that the 20/30 bps levels at which interchange was capped were inappropriate, including:[861]

- [✁]
- [✁]
- Finally, [✁].[862] [✁].

Our provisional view in our interim report

2.144 In our interim report, we recognised that, prior to the UK's withdrawal from the EU, caps on IF levels for UK-EEA transactions were set using cash as the comparator payment method, and that cash is primarily a comparator for CP transactions.

2.145 We said that this argument would hold also for all CNP transactions between EEA countries, and not just for UK-EEA CNP transactions. We noted that Intra-EEA CNP transactions are still capped at 0.2%/0.3% under the EU IFR; however, we said that we did not see any sign of these fees being too low – that is, having negative implications for merchants and consumers. We said that fraud levels, for example, are declining for both CP and CNP cross-border transactions capped at 0.2%/0.3%, such as intra-EEA transactions and UK-EEA transactions (before the caps were increased).[863]

2.146 In our interim report, we considered that, by increasing the outbound IFs for CNP transactions to levels included in the 2019 Commitments, the parties have adopted a benchmark that is not suitable – that is, they have replaced one not relevant comparator (cash) with another not relevant comparator (non-SEPA bank transfers). This means that the IFs have been raised higher than the level that would likely have been obtained from a commonly established methodology based on appropriate comparators. The additional

857 Visa, [✁].

858 Visa, [✁].

859 Visa, [✁].

860 Visa, [✁].

861 Visa, response to PSR questions dated 12 January 2022 [✁].

862 [✁].

863 ECB, Card fraud in Europe declines significantly (May 2023). See also Mastercard's data in Table 3.

evidence provided by the parties in this context includes methodological assumptions that are not necessarily appropriate for this market review. This is discussed in more detail below. We also noted the European Commission is likely to have considered studies commissioned by the card schemes when making its decisions and there is a reasonable expectation that there is a sound rationale for why it produced studies and set the IF cap levels as it did.

2.147 [✁]. We said that the European Commission has instead considered the MIT, given the merchants' need to accept cards even when they cost them more than alternative payment methods, for fear of losing customers (see Chapter 4). Given both the age and the purpose for which [✁], we said we do not consider them or their results to be relevant, both in general and in the context of this market review.

2.148 We noted that the [✁][864] and [✁].[865] Visa told us that [✁]. We noted that one of Visa's main criticisms of the European Commission study of 2015 (*Survey on merchants' costs of processing cash and card payments*) is that cash as a comparator to card payments is inappropriate for CNP transactions.

2.149 [✁]. We noted that as part of the 2019 Commitments decision, the European Commission took 'into account that in inter-regional transactions there are the following main groups of payment service providers: four-party card payment schemes; three-party card payment schemes; other means of payments that can be funded by bank transfers, such as e-wallets (digital wallets), e-payments or bank transfer payments.'. On the basis of the information it collected, the European Commission identified a distinct comparator for inter-regional CNP transactions. The European Commission said that: 'For inter-regional CNP transactions cash could not be considered a valid alternative. Other alternatives, that are means of payments funded via bank transfers (which are outside the domestic payment systems of the EEA Contracting Parties and the Single European Payment Area, SEPA; "non-SEPA bank transfers") were identified as plausible payment alternatives for the purposes of the MIT'.[866]

2.150 We said that, similarly, the analysis that the consultancy [✁] produced for Mastercard is now over six years old and relies heavily on comparators such as American Express and PayPal, and did not consider bank transfers. Mastercard told us that the consultancy's [✁] analysis identified alternative comparators as being more relevant than 'naked' bank transfers for that case, and therefore used these in the MIT.[867]

2.151 We noted the card schemes' argument that cash, which represented the only comparator utilised in the European Commission study of 2015, may be less relevant and potentially inappropriate as a comparator to cards in the CNP cross-border context. However, in adopting the benchmarks underpinning the 2019 Commitments for EEA-RoW transactions and their

864 [✁].

865 [✁].

866 European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision (April 2019), recital 80; European Commission, Antitrust: Commission accepts commitments by Mastercard and Visa to cut inter-regional interchange fees (April 2019). More details on the MIT applied by the European Commission in the context of the inter-regional CNP transactions can be found at footnote 45 and recitals 81 to 86 of the Commitments decision.

867 Mastercard defined a 'naked' bank transfer as '*An interbank payment from a consumer account to a merchant account using the relevant inter-bank system. 'Naked' refers to the use of such transfers outside the context of a broader scheme or payment service that provides additional security or functionality to the sender or receiver of the payment*'. [✁]

corresponding IF levels for UK-EEA transactions, we provisionally concluded that Mastercard and Visa appear not to have considered likely differences that characterise UK-EEA transactions compared to RoW-EEA transactions, including: i) that the UK is part of SEPA but the RoW-EEA caps used non-SEPA bank transfers as a comparator; ii) even if we agreed fraud levels were relevant, the fraud levels could be lower for UK-EEA transactions than RoW-EEA transactions. We said that both of these elements are likely to represent lower costs to UK merchants of accepting payments in a SEPA context compared to a non-SEPA one.[868]

2.152 We provisionally concluded that, on the evidence and reasoning provided, we were not persuaded that the card schemes' methodologies and the information in their submissions to us form a sound basis for the current UK-EEA CNP IF levels.

What stakeholders said in response to our interim report

What merchants told us

2.153 UK merchants did not provide any comment on this issue.

What issuers told us

2.154 Issuers did not provide any comment on this issue.

What the card schemes told us

2.155 Mastercard said that the 0.2/0.3 levels were set in 2015 based on data gathered earlier, in 2012 and 2013, and have not been updated since then to reflect changes in the payments landscape, particularly the growth of cross-border CNP. It noted that CNP payments were not considered at all in determining these 0.2/0.3 rates; and that the European Commission justified this at the time on the basis that 'Only a minority of the merchants that have face-to-face transactions do have an online activity as well' and that 'in 2012, online card payments accounted for only 5.6% of the total volume of card transactions and 9.3% of the total card value in the European Union'. The firm stated that neither is likely to be true today, and that based on UK Finance data, the CNP proportion for the UK for the period September 2022 to August 2023 is 34% by value and 14% by number of transactions.[869]

2.156 Mastercard added that the 0.2/0.3 levels were based on an MIT methodology that used cash as the alternative payment method. This makes these rates inappropriate in the CNP context, as cash is not an alternative payment method to CNP transactions. It noted that this MIT did not consider the basket of payment methods to which cardholders would most likely switch in a CNP context, which may comprise online retail payment methods and three-party schemes such as American Express.[870]

2.157 Visa said that the central bank studies used by the European Commission to support the EU IFR caps were compiled almost 20 years ago and they did not focus on the merchant sectors most relevant for cross-border transactions. Those studies focused on the cost of a cash-based alternative, which is not relevant for CNP or the vast majority of cross-border transactions, as is recognised in the interim report and by the European Commission.[871]

868 PSR analysis based on our online analysis of the top six banks in the UK. [✂]

869 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

870 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

871 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

2.158 Visa also mentioned the EC's Cost of Cash Study and noted that the study included no assessment of cross-border CNP Transactions, and instead focused on face-to-face transactions; cash as the only relevant payment comparator; historic data derived from studies carried out between 2012 and 2013; domestic transactions within ten EU Member States; and domestically focused merchant sectors, such as supermarkets which are not representative of typical cross-border CNP Transactions.[872]

Our response to stakeholders' views

2.159 The card schemes argued that cash may be less relevant and potentially inappropriate as a comparator to cards in the CNP cross-border context. We note this comment, and note that this was already acknowledged by the European Commission when it identified a distinct comparator for inter-regional CNP transactions – one that included alternatives based on other means of payments that can be funded by bank transfers.

2.160 The schemes also noted that the previous caps were based on an outdated data and methodology. We note, however, that Mastercard and Visa's internal documents show that their decision to increase the outbound IFs was not based on any specific MIT analysis using a different, more suitable comparator for CNP transactions.

The 2019 Commitments and the UK's withdrawal from the EEA

What the card schemes told us

2.161 Mastercard explained to us that, for inbound IFs, it applied the IF levels contained in the 2019 Commitments in relation to EEA-RoW interregional transactions 'which had been accepted based on a consideration of alternative transaction methods available for those transactions'.[873]

2.162 In Mastercard's view, following the UK's departure from the EU, aligning the IFs for transactions at EEA merchants using UK-issued cards with the IFs that apply to transactions at EEA merchants using (other) non-EEA-issued cards was a logical approach. In this regard, it stated that 'as the UK was now outside of the EEA, there was no objectively justifiable reason to apply different rates to UK-issued cards compared with any other non-EEA issued cards (for transactions at EEA merchants)', and 'it is likely that questions would have been raised by UK issuers had that change not been made'.[874, 875]

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872 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

873 Mastercard response to PSR questions dated 12 January 2022. [✁]

874 Mastercard response to PSR questions dated 12 January 2022 and 5 August 2022. [✁] See also Mastercard, *Mastercard response to TSC* (August 2022), page 7.

875 As mentioned in Chapter 3, IFs related to transactions involving RoW cards at UK merchants are capped by the 2019 Commitments.

2.163 Mastercard internal documents show that the levels in the 2019 Commitments [✂].[876] These rates were seen as [✂] while potential 'new' lower rates (that is, above 0.2%/0.3% [✂]) were [✂]. The same internal documents also show that [✂].[877] Mastercard subsequently told us that [✂].'[878]

2.164 Contrary to the purpose of setting IFs, for the purpose of setting scheme and processing (S&P) fees relevant to UK-EEA CNP transactions, Mastercard considered the UK's SEPA membership as a reason not to change these S&P fees.[879] This was because, as per their internal documents, [✂].[880]

2.165 Even before it became known that [✂], Mastercard [✂] Internal documents from 2017 show that Mastercard's UK team suggested that Mastercard [✂].[881] The same approach could have been applied for UK-EEA IFs. Our provisional view is that the fact that both the UK and the EEA are part of SEPA is a reason for not raising outbound IFs to levels that have been defined for transactions where cards are issued in non-SEPA countries.

2.166 Indeed, internal documents on UK-EEA pricing considerations stated that [✂]. This was because [✂]. The same internal documents also stated that [✂]. However, Mastercard identified that one of the main challenges to doing so was [✂].[882]

2.167 Visa said that its changes reflected the fact that the previous IFs were determined on the basis of the UK being subject to the EU IFR. It explained that now that the UK is no longer a member of the EEA, it (Visa) had moved 'to an interchange structure that represents levels that are consistent with cross border transactions'. It also told us that the previous IF rates for UK-EEA CNP transactions [✂].[883]

2.168 Visa also explained that 'as a global organisation, it is necessary to have a global interchange structure that reflects the geopolitical and trading status of the countries we operate within and between. [✂].[884]

2.169 Visa stated in its submissions to us that [✂]. Those submissions included an overview of the card scheme's considerations when Visa decided to change IFs at the time, as well as the documents that relate to those decisions.[885]

876 Mastercard, [✂]
877 Mastercard, [✂]
878 Mastercard, [✂]
879 Mastercard, [✂]
880 Mastercard, [✂]
881 Mastercard, [✂]
882 Mastercard, [✂]
883 Visa response to PSR questions dated 12 January 2022 [✂]
884 Visa response to PSR questions dated 5 August 2022 [✂]
885 Visa response to PSR questions dated 5 August 2022 [✂]

Our provisional view in our interim report

2.170 We noted that the 2019 Commitments were based on a merchant indifference test (MIT) (see Chapter 3) that used non-SEPA bank transfers as a comparator for CNP transactions. We noted that, although the UK is no longer part of the EU, it is part of SEPA (see Chapter 3). As such, we said the evidence used to set the IFs in the 2019 Commitments is not relevant to UK-EEA transactions.

2.171 While increasing IFs to the levels permitted by the 2019 Commitments is appealing for Mastercard and Visa, this is not necessarily in the interests of UK merchants and their consumers. Our provisional view was that the fact that both the UK and the EEA are part of SEPA is a reason for not raising outbound IFs to levels that have been defined for transactions where cards are issued in non-SEPA countries. There is no technical reason for the UK to be treated any differently from its fellow SEPA member countries.

2.172 We said that Visa also stated that [✂].[886] [✂].

2.173 However, we said that, even following the UK's withdrawal from the EU, the UK's trading status with the EEA remains more similar and closer to the EEA than to many RoW countries. We noted that the new fee structures, however, consider that the trading status of the UK is the same as that of any other RoW country, which is not the case.

2.174 In our assessment of the evidence and reasoning provided to us by the card schemes, we said we were not persuaded that the UK's withdrawal from the EU represents a sound basis for concluding that higher IF levels are appropriate.

What stakeholders said in response to our interim report

What the card schemes told us

2.175 Mastercard recognised that the UK has remained part of SEPA and this means that consumers in the EEA can use SEPA transfers to transfer money to households and corporates in the UK. Mastercard noted that SEPA sets standards for credit transfers and direct debits and this means, for example, that transactions between two SEPA countries are typically faster than transfers between a SEPA and a non-SEPA country.[887] However, SEPA transfers will not be convenient or provide the same protection a card payment will and, in fact, SEPA transfers are very rarely used for retail payments from EEA consumers to UK merchants.[888]

2.176 Visa said it is also concerned that the interim report 'fails to reflect that IFs applicable to XB [cross-border] EEA to UK 'Face-to-Face'(F2F) transactions and UK domestic transactions have not changed, and remain at 0.2%/0.3%. On that basis, and following the UK's departure from the EU, Visa took a carefully balanced decision to revise its EEA to UK XB [cross-border] CNP IFs in line with:

a. the IF levels that it had agreed to apply for UK to EEA XB [cross-border] CNP transactions with the European Commission (EC) (the EC's 2019 Visa Commitments Decision) following an extensive competition law investigation.

886 Visa response to PSR questions dated 5 August 2022 [✂]

887 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

888 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

b. the PSR having expressly acknowledged the changed status of UK/EEA transactions by referring to them in its post-Brexit statement as transactions now involving "third countries (for example, the USA or Australia), including the UK", and by making clear that such transactions would be "subject to interchange fee caps set out in the commitments made by Visa and Mastercard to the European Commission in 2019" and that "the PSR does not monitor or have any role with respect to them"; and

c. the harmonised EU Single Market Interchange Fee Regulation (EU IFR) ceasing to apply to the UK, coupled with the UK Government expressly deciding against retaining the EU IFR caps for anything other than UK domestic transactions in the "UK onshored IFR". Again, the PSR stated at the time that "consumer cross-border card payments between the UK and EU (or any other third country), where either the acquirer or issuer is based outside the UK's jurisdiction, are no longer subject to the interchange fee caps established under either the UK IFR or EU IFR".'[889]

2.177 Visa said that it is wrong for the interim report to assume that SEPA bank transfers are "the relevant alternative" against which Visa's cross-border CNP IFs should be assessed and on this basis for the IR to assert that Visa's cross-border CNP IFs are "likely to be unduly high".[890] Visa said that, 'setting aside that the IR [interim report] does not, in any event, undertake this assessment [of Visa's cross-border CNP IFs], this underlying assumption is fundamentally flawed because SEPA bank transfers are rarely (if ever) used for XB [cross-border] CNP Transactions.' It said this is unsurprising given:

a. the nature of XB CNP Transactions – which typically comprise travel (e.g. transport, hotel, tourism) and other discretionary transactions. For such transactions, EEA consumers are significantly more likely to use alternative payment methods such as American Express, PayPal and **[✁]** rather than a SEPA bank transfer (particularly if they require credit functionality which a SEPA bank transfer does not offer);

b. that SEPA bank transfers do not feature in any leading payment industry reports regarding EEA consumers' payment preferences for online transactions. This includes Worldpay's 2023 Global Payments Report (Global Payments Report 2023) which does not list SEPA bank transfers as a 'popular alternative payment method' in any European country, but instead lists for example PayPal, **[✁]**, Apple Pay and Google Wallet, alongside popular card brands such as American Express and domestic card schemes;

c. The lack of consumer demand, very few UK merchants accept SEPA bank transfers – even when looking at large merchants such as Airbnb, Booking.com, Expedia, Ryanair, British Airways, Uber, ASOS, Harrods, John Lewis and Selfridges, which are most likely to benefit from significant volumes of cross-border CNP Transactions, none list SEPA bank transfers as an available payment option. This is consistent with the merchant feedback received by the PSR in which [✁] and in which two such merchants stated that "bank-rail-based account-to-account solutions are available in some European countries but not in the UK, and that importing these would require too much effort from merchants, considering the limited market share they would bring" ([✁]), and that account-to-account payments have not been enabled because "they are cumbersome to implement in a cross-border environment" ([✁]). Such considerations are likely to be more acute for smaller merchants, particularly as SEPA bank transfers are Euro-denominated and so UK merchants must either have a Euro

889 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

890 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

bank account (which many smaller merchants will not have), or pay costly currency conversion fees to receive payments in GBP; and

d. That SEPA bank transfers involve significant added friction compared with Visa and other popular payment methods – which, particularly in an online and cross border context, consumers and merchants are more likely to be conscious of. These considerations include, for example: (i) the time, inconvenience, information sharing and error risks associated with needing to manually enter a merchant's transaction details from a personal consumer bank account; (ii) the lack of reassurance associated with not receiving any immediate merchant order confirmation; (iii) the lack of consumer payment protection guarantees, with SEPA payments typically being irrevocable once processed, and (iv) the potential for additional consumer fees of up to €12.00 per transaction for Instant Credit Transfers."[891]

2.178 Visa said that it 'is not aware of any regulatory IF analysis having ever been undertaken on the basis of a comparison against only the cost of bank transfers (let alone SEPA bank transfers). This includes the analysis undertaken by the EC when establishing the EEA-wide IF caps set out in the IFR, and (contrary to what the IR claims) when agreeing the IF levels set out in its 2019 Visa Commitments Decision. Rather, the EC's 2019 Visa Commitments Decision considered the costs of a wide variety of commonly used alternative payment methods, including "four-party card payment schemes; three-party card payment schemes; other means of payments that can be funded by bank transfers, such as e-wallets (digital wallets), e-payments, or bank transfer payments", including specifically American Express and PayPal."'[892]

2.179 Visa said that the interim report 'contradicts its own reliance on SEPA bank transfers being an important – or indeed "the relevant" – payment alternative for cross-border CNP Transactions given its own dismissal of popular EEA account-to-account (A2A) payment providers such as iDEAL (which facilitates bank transfers based on underlying SEPA infrastructure) and Blik on the basis that they "are national offerings" where "iDEAL offers limited cross-border transactions services" and "Blik is still confined to its domestic borders and does not offer a cross-border payment service".'[893]

What issuers told us

2.180 A trade association speaking on behalf of its UK issuer members [✂] stated that SEPA payments for UK-EEA cross border payments is not a viable alternative to cards, and therefore questioned whether SEPA membership is justified to differentiate the UK-EEA relationship from the EEA-Rest of World (non UK) relationship.[894]

2.181 An issuer [✂] told us it does not believe UK being part of SEPA is a material factor impacting costs incurred by EEA issuers when enabling EEA to UK transactions. Even if it was, there is no rationale for it to be so significant as to justify an 82% lower interchange cost for EEA-UK versus Rest of the World-UK.[895]

891 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

892 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

893 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

894 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

895 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

What acquirers told us

2.182 An acquirer [✂] said it [✂].[896]

What merchants told us

2.183 A merchant [✂] said that the schemes failed to consider that the UK remains a part of SEPA.[897]

What other stakeholders told us

2.184 A trade association representing tech startups [✂] said that the UK has remained a sustained member of SEPA, which implies that both EEA and UK continue to have strong economic, regulatory and technological links.[898] It also said that aligning fees as proposed would complement the recently signed Memorandum of Understanding between the UK and the EU establishing a framework for structured regulatory cooperation in the area of financial services.[899]

2.185 According to a trade association representing EEA acquirers [✂], there has been no material change of UK-EEA transactions which could justify the increase in IFs, something that is further strengthened by the fact that the UK remains part of SEPA.[900]

Our response to stakeholders' views

2.186 Card schemes told us that using the fees that apply to EEA-RoW transactions was the appropriate decision following the UK's withdrawal from the EU. However, the IF for EEA-RoW transactions, as per the 2019 Commitments, was based on an MIT-based analysis that used non-SEPA bank transfers as a comparator. As both the UK and the EEA are part of SEPA, the use of non-SEPA transfers as a comparator is incorrect, as there is no technical reason for the UK to be treated differently from other SEPA countries.

2.187 The schemes and issuers, however, have questioned the relevance of SEPA bank transfers as a comparator, raising three arguments.

- The first argument was that SEPA bank transfers are not an appropriate comparator because they are very rarely, if ever, used for cross-border transactions and do not offer the same protections to consumers (see paragraphs 2.176, 2.178 and 2.180). We observe, however, that all the other comparators suggested by stakeholders are inappropriate for an MIT-based analysis. Suitable comparators cannot include a MIF component, as recognised by the European Commission (see Chapter 3, paragraph 3.32) or have fees that are likely to correlate with Mastercard and Visa's MIF. As shown in Chapter 5, paragraph 5.27, all the payment methods other than SEPA bank transfers available for EEA-UK transactions suffer from this issue. SEPA bank transfers, therefore, remain the only relevant comparator.

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896 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

897 Stakeholder response to MR22/2.6 dated 25 January 2024 [✂].

898 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

899 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

900 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

- The second argument was that we contradicted ourselves by considering SEPA bank transfers as the relevant alternative while at the same time dismissing the constraints from A2A-based payment providers (see paragraph 2.180). We consider that there is no contradiction in this approach. The need for IF regulation emerges from the lack of effective competitive constraints on IF levels. When used in the context of regulatory intervention, the MIT therefore is necessarily based on comparators that do not pose effective competitive constraints on IFs.
- The third argument was that no regulatory IF analysis has ever been undertaken on the basis of a comparison against only the cost of bank transfers (see paragraph 2.179). This claim is demonstrably false. As we explain in Chapter 3, paragraph 3.33, the MIT analysis conducted by the European Commission in the context of the 2019 Commitments was uniquely based on non-SEPA bank transfers. Other payment methods were acknowledged but not considered for the purpose of the MIT.

2.188 Finally, we note that, unlike as claimed by Visa (see paragraph 2.178), our finding that the current outbound IF levels are unduly high is not uniquely based on a comparison with SEPA bank transfers. The arguments that support our conclusion are discussed at length in Chapter 5.

2.189 Overall, in our assessment of the evidence and reasoning provided to us by the card schemes, we are not persuaded that the UK's withdrawal from the EU represents a sound basis for concluding that higher IF levels are appropriate.

Competitive dynamics on the issuing side

What the card schemes told us

2.190 In its letter to the TSC, Mastercard said that 'to remain competitive and continue to offer benefits of electronic payments to consumers, Mastercard must be able to attract issuing and acquiring banks to the scheme. Interchange fees at the right level allow this by ensuring the costs of issuing and acceptance are properly and fairly balanced in the system. The rates Mastercard offers must be comparable with its competitors, otherwise its cards will simply not be issued.'[901]

2.191 Mastercard explained to us that they are a two-sided platform facing 'the commercial imperative to attract, and keep on board, both types of users' (for example, cardholders and merchants).[902] In this regard cardholders are customers of the issuers and are on the issuing side of the platform as compared to merchants who are on the acquiring side. Mastercard further explained that: 'in competing with other payment platforms, [it] faces the challenge of keeping issuers and acquirers participating in the platform, and keeping sufficient consumers and merchants using the platform where it is available to them.'[903]

2.192 It explained this means that card schemes that rely on IFs 'are competitively constrained both from increasing and decreasing these fees too far from the commercial optimum,

901 Mastercard, *Mastercard response to TSC* (August 2022), page 6.

902 Mastercard response to PSR questions dated 12 January 2022 [✂].

903 Mastercard response to PSR questions dated 12 January 2022 [✂].

given the risk of business being lost to any rival platforms or payment services with a more competitive pricing structure'.[904]

2.193 Mastercard stated that 'in the absence (or in advance) of any potential alternative regulatory benchmark which applied specifically to the UK, Mastercard decided to apply the same IFs as those contained in the 2019 Commitments in relation to RoW-EEA transactions.' It did so 'with an awareness of the competitive considerations related to rival payment services who also provide cross border transactions.'[905]

2.194 Mastercard also said that in March 2021 Visa announced it was increasing its inbound and outbound IFs to the maximum set by the 2019 European Commission Commitments. Mastercard explained [✁]. It continued: [✁].[906]

2.195 Mastercard then told us that in view of this [✁] and 'in the absence of any alternative regulatory benchmark which applied specifically to outbound IFs, it revisited its position on these [outbound] rates and decided to increase also these to the levels allowed by the 2019 Commitments.'[907]

2.196 From Mastercard's internal documents it is clear that its main concern, when deciding what to do with UK-EEA CNP IFs following the UK's withdrawal from the EU, was the [✁]. For example, one document, which considers competitive dynamics, shows that [✁]. However, the same document also shows that [✁].[908]

2.197 Internal documents from Mastercard show that the [✁].[909] Mastercard then stated that: 'any commercial advantage would be short-lived' (because Visa was likely to match the rates). Likewise, any commercial disadvantage if Visa raised the rates a few months before Mastercard was likely to be short-term. However, Mastercard was also very concerned about a long term/permanent commercial disadvantage if Visa's interchange rates remained at a higher level that was better aligned with the level required to ensure the success of a four-party scheme.[910]

2.198 Internal Mastercard documents also show that [✁]. In internal documents it produced [✁].[911, 912]

2.199 In addition, internal Mastercard documents show that, [✁].

2.200 In its response to us, [✁].

2.201 Visa did not mention this as a reason for increasing the fees, [✁].

904 Mastercard response to PSR questions dated 12 January 2022 [✁].

905 Mastercard response to PSR questions dated 12 January 2022 [✁].

906 Mastercard response to PSR questions dated 5 August 2022 [✁].

907 Mastercard response to PSR questions dated 5 August 2022 [✁].

908 Mastercard, [✁].

909 Mastercard, [✁].

910 Mastercard, [✁].

911 Mastercard, [✁].

912 Mastercard, [✁].

2.202 We saw evidence in internal documents that Visa considered it a relevant factor that, [✁]. In particular, in internal documents, Visa noted that [✁]. It also noted that [✁].[913] In addition, Visa's documents noted that [✁] and that [✁].

Our provisional view in our interim report

2.203 In our interim report, we considered that an increase in IFs may increase (or at least maintain) the attractiveness of cards to card issuers. In light of the available evidence, we considered that Mastercard and Visa wanting to remain attractive to issuers (particularly to EEA issuers for outbound IFs) is a reason why the card schemes raised their outbound IFs after the UK's withdrawal from the EU.

2.204 Visa announced it was increasing its outbound IFs level and Mastercard followed suit to match the uplift [✁]. This was despite Mastercard's statement that, as a two-sided platform, it has a commercial imperative to attract, and keep on board, both types of users: in this case their only concern was issuers and not the users on the acquiring side, such as merchants. While Visa's response to us did not explicitly mention the need to remain competitive, [✁].

2.205 We therefore provisionally concluded that schemes have a commercial incentive on the issuing side to raise IFs.

What stakeholders said in response to our interim report

What the card schemes told us

2.206 Mastercard competes with Visa for customers on the issuing side and competitive pressure from Visa was therefore one of the reasons that prompted Mastercard to review its rates, to ensure that it was not competitively disadvantaged by continuing to apply the artificially low intra-EEA CNP rates, which Mastercard has consistently maintained are set below the optimal level.[914]

2.207 Mastercard said it considers the interest of all parties in the payments ecosystem and not just issuers, when setting an optimal rate which will benefit all parties. It also said competition between issuers is intense, and if IFs were to be lowered, issuers would have to make up the revenue shortfall from elsewhere, such as through reduced services, worse foreign exchange rates or the introduction of transaction fees, which would affect merchants either directly or indirectly through discouraging sales (or diverting them to online merchants based elsewhere to whom such charges may not apply).[915]

What issuers told us

2.208 [✁] said IFs are a critical tool to balance the benefits and costs of card payments. They ensure each participants pays their fair share of costs associated with processing and protecting card payments.[916] The current commercial model, it said, balances incentives in the market and encourages inter-platform competition and innovations in the payment industry. This has benefitted consumers and merchants by 'increasing choice, quality of

913 Visa, [✁].

914 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

915 Stakeholder response to MR22/2.6 dated 14 February 2024 [✁].

916 Stakeholder response to MR22/2.6 dated 31 January 2024 [✁].

payment product services and improving prices'. Future innovation will continue to 'create value by improving the quality of services, methods of payment protection, efficiency and convenience of the payment process'. Given the important role played by banks in 'supporting investment in innovative solutions' in the industry, there is 'no rational argument that supports zero or near-zero price for card scheme interchange received by issuers' (if banks are to be correctly incentivised to invest.[917]

2.209 An issuer [✂] said it could not comment on Visa and Mastercard's motivations for the changes they took on cross-border interchange. However, it disagreed with the analysis we provided. It stated that we had argued that UK merchants have no alternatives to Visa and Mastercard for EEA to UK transactions, and that Visa and Mastercard increased the cross-border interchange rates to remain attractive. The issuer [✂] said that it did not believe these propositions were correct, as

- if there are no alternatives there would be no need for Visa and Mastercard to additionally incentivise issuers to choose them
- if the competition is just between Visa and Mastercard, the starting and ending point remains the same where both schemes offer the same amount of interchange (meaning there would be no benefit for the scheme which moved first to do so).[918]

What acquirers told us

2.210 An acquirer [✂] stated it believes that remaining attractive to issuers was the primary reason for schemes to raise UK-EEA CNP IFs. It 'believes that the reason the schemes increased the UK-EEA CNP IFs following Brexit was to maximise the revenue they could provide issuers.' If one scheme was to increase IFs, the others will match the level to ensure they do not lose issuer business.[919]

What merchants told us

2.211 A merchant [✂] said it agrees with our assessment, 'given previous observations about how the IFR preceded increased fees elsewhere.'[920]

What other stakeholders told us

2.212 A trade association representing tech startups [✂] agreed with us that it was the schemes' desire to remain attractive to issuers the main reason they raised their outbound IFs. It said the schemes experience 'reverse competition', allowing the schemes to continue to raise fees to remain attractive to issuers.[921] It said it believes there are anti-competitive measures which act as barrier to competition and have caused fees to rise. It stated that IFs are subject to 'reverse competition', this means the competition between Mastercard and Visa to attract issuers leads to higher IFs and, consequently, MSCs.[922]

917 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

918 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

919 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

920 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

921 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

922 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

2.213 A trade association representing EEA acquirers [✂] said that 'the findings of the PSR confirm the relevant MIF is set solely to attract more issuing volume, and that the issuers and acquirers in question does not indicate that there was any countervailing benefit as a result of the MIF. The PSR should leverage these important findings and make a principled decision over the necessity of a MIF for this class of transactions.'[923]

2.214 A trade association speaking on behalf of its UK issuer members [✂] said that our conclusion that the purpose of all IFs is to incentivise issuers to sign up to one four party card scheme is generalised and unsubstantiated. It said that the industry strongly rejects this assertion.[924] The trade association relates IFs to the need of an 'end-to-end proposition for all users'. This includes taking into account merchant costs, but also the costs and investments that develop value for both merchants and consumers alike ('including speed, security, fraud protection, resilience, consumer experience and consumer recourse').[925]

Our response to stakeholders' views to our interim report findings

2.215 Most stakeholders responding to our interim report agreed with our conclusion that Mastercard and Visa have a commercial incentive on the issuing side to raise IFs. A few, stakeholders, however, were critical. In this section, we respond to their criticism.

2.216 We note that some stakeholder submissions relate more generally to the purpose of IFs rather than to the reasons for the outbound IF increases (see paragraphs 2.209 and 2.215). We note that, contrary to what was submitted by [✂] (see paragraph 2.215), we have not argued that the purpose of all IFs is to incentivise issuers to sign up to one four-party card scheme.

2.217 Mastercard submitted that, were issuers to lose revenue through reduced IFs, they would look to make up this shortfall by reducing services, worsen foreign exchange rates, or by introducing transaction fees (see paragraph 2.208). We recognise that IFs need to balance the economic incentives on both sides of the market. However, as explained in Chapter 5, our finding is that the current outbound IF levels are higher than what would be required to appropriately balance the interests of the two sides.

2.218 Finally, an issuer [✂] challenged the logic of our argument, submitting that (i) if there are no alternatives to Mastercard and Visa, there is no need for Mastercard and Visa to additionally incentivise issuers to choose them; and (ii) if the competition is just between Mastercard and Visa, there is no benefit for the scheme which raises IFs first, as the other would quickly match the increase (see paragraph 2.210).

2.219 The first point confuses competition on the acquiring and the issuing side. We have argued that Mastercard and Visa do not face effective competition on the acquiring side, including from each other. This, however, does not exclude competition on the issuing side: Mastercard and Visa do compete against each other to attract issuers. The second point misunderstands the logic of competition. The short-term disadvantage to a scheme that increases IFs later than its competitor can provide sufficient incentive to move first and

923 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

924 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

925 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

give more IF revenues to issuers. This is what the European Commission in the past has described as ‘reverse market mechanism’ that drives card IFs up.[926]

Merchant-related considerations

What stakeholders told us

2.220 Visa explained to us that [✂].[927]

2.221 We asked Visa to explain how higher IFs enable merchants to make better-informed decisions about their payment options. Visa said that [✂]. Visa also said [✂].[928]

2.222 We asked Visa to provide any existing documents (including presentations and reports either prepared internally or by third parties relating to information that they considered, or analysis that they carried out) that support the statement that [✂].[929]

2.223 Stakeholders did not provide any additional evidence in relation to this point.

Our final view

2.224 We have not seen any evidence indicating how an increase in IFs could benefit merchants to make better-informed choices.

2.225 We are also unaware of any allocative inefficiencies that historical regulatory intervention may have created. Visa (and Mastercard) are widely used in both the UK and the EEA and their use has increased over time despite regulatory interventions.

Mastercard and Visa’s statements on the value of their card propositions

What the schemes told us

2.226 Mastercard and Visa have both told us the value their card-scheme networks bring to different participants – issuers, cardholders and merchants.

2.227 Visa stated that its mission is to be the best way to pay and be paid, everywhere.[930] It said that IFs are an integral feature of four-party card schemes and that it does not earn revenue from them.[931] Instead, Visa provides a value transfer from acquirers, playing an essential role in balancing the costs and incentives of issuers, cardholders, merchants and acquirers. Taking each in turn:

- **Issuers:** Visa states that IFs help issuers to offer many of the banking services that are typically free to UK cardholders, including the ability to use a card online and across

926 See European Commission (2015) *Interchange Fee Regulation*, Competition Policy Brief, Issue 2015-3.

927 Visa response to PSR questions dated 12 January 2022 [✂].

928 Visa response to PSR questions dated 5 August 2022 [✂].

929 Visa response to PSR questions dated 5 August 2022 [✂].

930 Visa response to PSR questions dated 12 January 2022 [✂].

931 Visa response to PSR questions dated 5 August 2022 [✂].

borders, while enjoying the protections and security they expect. Visa also considers that IFs help enable competition, incentivising issuers to provide innovative products and services.

- **Cardholders:** Visa states that cardholders benefit from services such as a convenient yet secure checkout experience, which challenges bad actors without creating unnecessary frustrations for legitimate customers.
- **Merchants:** Visa states that merchants benefit from increased sales, due to cardholders being able to buy from them safely and reliably, including online and across borders.[932] They also benefit from the protections and security of the transaction and authorisation checks.

2.228 We have not seen in internal documents contemporaneous to the setting of the higher IF levels any evidence supporting the above representations.

2.229 Mastercard stated that merchants benefit strongly from the ability to accept CNP transactions from cardholders in other countries. It is confident that the UK-EEA CNP rates implemented ensure that both merchants and cardholders in the UK and the EEA share in the benefits that arise from the scheme and its activities.[933] Mastercard stated that the value it brings to users includes improved payment efficiency, increased security and stability, innovative payment products, and – for merchants – reduced barriers to entry, increased sales and expansion of the consumer base. Mastercard stated that:

- Its technology and expertise make payments safe, simple and smart.
- Its security systems continuously protect the Mastercard network and the transactions and data that cross it against fraud and cybercrime. New products and services that help protect users include SCA, tokenisation, biometrics, machine-learning and the latest EMV chip card security.
- It guarantees the settlement of Mastercard transactions between its principal issuers and acquirers. It explains that this helps enable global acceptance of Mastercard-branded cards by providing acquirers and merchants with a recourse in the event that a cardholder fails to settle.
- It transforms new ideas and emerging technology into attractive, scalable services – for example, contactless payments.
- Merchants and cardholders both benefit from higher-value transactions thanks to direct access to current accounts and credit lines. Merchants therefore directly benefit from the higher profit margins linked to more and higher-value transactions.

2.230 We have not seen in internal documents contemporaneous to the setting of the higher IF levels any evidence supporting the above representations.

Our provisional views in our interim report

2.231 In our interim report, we said that, though the card schemes have said that IFs provide a value transfer from acquirers and are essential in balancing the costs and incentives of issuers, cardholders, merchants and acquirers, we had not seen any evidence that they

932 Visa response to PSR questions dated 5 August 2022 [✁].

933 Mastercard response to PSR questions dated 5 August 2022 [✁].

sought to 'balance' the costs to and incentives of issuers, cardholders, merchants and acquirers in deciding to increase outbound IF fees.

2.232 We went on to say that, while the card-scheme networks may aim to bring value to different participants, we had not seen any evidence identifying a benefit to UK merchants that would explain the increases in UK-EEA CNP IFs. We said that, for example, we had seen no evidence of any particular innovation to account for IF increases – such as improved fraud prevention, quality, efficiency or economy of the card payments systems benefiting UK merchants. We said this suggests that the card schemes have been able to extract the value from the increase in UK-EEA CNP IFs to the benefit of issuers with no comparable increase in value to other participants.

What stakeholders said in response to our interim report

What the card schemes told us

2.233 Mastercard said that merchants benefit both directly and indirectly from IFs set at an optimal level; and that these revenues allow issuers to continue to deliver card payments and to invest in services which make them more attractive to cardholders, through improvements in payment convenience and reductions in fraud. It said that this in turn encourages cardholders to continue to use cards, rather than alternative payment methods, which leads to incremental sales and/or reduced costs for merchants.[934]

What issuers told us

2.234 An issuer [✂] told us that UK merchants are already receiving the benefits of having a payment method that non-UK consumers can use to make purchases with 'very high reliability, low fraud and low abandonment' in addition to transactions being often enabled with 'a credit risk falling on the issuer'.[935]

2.235 An issuer [✂] submitted that IFs promote a 'strong, competitive and efficient global electronic payments system for consumers, merchants and society' and serves as a 'critical tool to balance the benefits and costs of card payments', as well as it ensures that 'each participant pays their fair share of the costs' associated with processing and protecting payment card transactions.[936]

2.236 According to the same issuer[✂], the current commercial model 'has benefitted consumers and merchants by increasing choice, quality of payment product services and improving prices'.[937] It said merchants particularly benefit strongly from increased sales by facilitating online payments which creates, according to [✂], a 'significantly wider customer prospect base both domestically and internationally, and can save merchants valuable costs to support a storefront if fully digital'.[938]

934 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

935 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

936 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

937 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

938 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

2.237 [✂] said that IFs are needed for future investments (for 'further benefits to be realised, banks need to be correctly incentivised to continue to invest and, as such, there is no rational argument that supports zero or near-zero price for card scheme interchange received by issuers').[939]

What acquirers told us

2.238 An acquirer [✂] told us that the rationale for the IF cannot be attributed to a need to compensate issuers for the costs to issue and manage cards. According to [✂], the use of IFs in exchange for benefits provided to merchants is something that has already been rejected in recent case law. It said that 'following the Mastercard Infringement proceedings by the Commission in 2007, it abandoned the issuer cost methodology' that assumes that 'MIFs are charged by issuers in exchange for a benefit that they provide to merchants'.[940] It told us the Commission decided to use the MIT, which relied on 'a comparable payment instrument as a benchmark' instead.

2.239 The use of an MIT was, according to the same acquirer [✂], to stimulate the use of payment systems (as mentioned in the IFR recital, the MIT 'stimulates the use of efficient payment instruments').[941] Because of this, it submitted there is now no need for MIFs: the widespread use of digital payments implies there is no need for IFs ('there is no policy reason to allow for a positive MIF to incentivise card issuance given they are already a universally utilised commodity').[942]

What merchants told us

2.240 The BRC said that if IFs were originally 'introduced to encourage card usage', as the UK is a mature card market one would expect to see rates for a UK market below the caps.[943]

2.241 In a similar vein, another merchant trade association [✂] recommended that we consider, in the review, a rate that is more reflective of the high uptake in card-transactions in the UK (near 90% card penetration, compared to many of the EU cash-dependent countries that were used in setting previous fees).[944]

Our response to stakeholders' views on our interim report

2.242 Some stakeholders (issuers and a scheme) have commented on the benefits that merchants receive from using cards. In particular, Mastercard said that merchants benefit both directly and indirectly from IFs set at an optimal level (see paragraph 2.233). We do not doubt that the use of cards provides benefits to merchants. However, in Chapter 5 we have shown that the current outbound IF levels are higher than what would be required to appropriately balance the interests of the acquiring and issuing sides, and are therefore higher than the 'optimal level'.

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939 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

940 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

941 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

942 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

943 Stakeholder response to MR22/2.6 dated 26 January 2024 [✂].

944 Stakeholder response to MR22/2.6 dated 02 February 2024 [✂].

2.243 Merchant trade associations and an acquirer submitted that, as IFs were originally introduced to encourage card usage, in a market where usage is widespread lower rates would be justified. According to an acquirer [✂], there is no policy reason to allow for a positive MIF to incentivise card issuance given they are already a universally utilised commodity (see paragraph 2.239). We note these submissions. However, in the context of this market review, we have assessed whether, following increases in October 2021 (Visa) and April 2022 (Mastercard), the current levels of EEA-UK outbound IFs are appropriate to balance the interest of the two sides of the market. We have not conducted a wider analysis of the appropriateness of IF levels in the UK, nor have we explored whether an alternative commercial model could ensure the viability of card payments.

Practical benefits of aligning IFs for EEA cards at UK merchants with other IF levels

What stakeholders told us

2.244 Mastercard told us that in the absence of regulatory certainty or guidance and in light of potentially conflicting priorities of issuers and acquirers in the UK and the EEA, it was seeking an approach that fairly balanced the interests of all parties within its ecosystem. It explained that consistency and predictability was a key consideration. It therefore considered alignment/reciprocity was an objective, non-discriminatory and logical basis for IF rates that could readily be understood [✂] by any participant.[945]

2.245 Mastercard considered that aligning IF rates for transactions at EEA merchants on UK-issued cards with the rates for transactions on (other) non-EEA-issued cards was a logical approach, following the UK's departure from the EU.[946]

2.246 We asked whether and how these benefits had been measured and compared to the additional cost imposed on merchants by the outbound IF increases. Mastercard explained that: 'as the benefit being referred to is not a direct financial benefit to issuers or Mastercard, it is not possible to weigh it against any costs to merchants. As explained, it is the benefit of consistency and objectivity at the scheme level overall, which therefore accrues to acquirers/merchants as much as to issuers'.[947]

2.247 In response to our interim report, Mastercard also said that the increase in IFs between the UK and EEA benefits all players in the ecosystem, because it provides consistency and stability by aligning with interregional IFs for CNP transactions. It noted that maintaining consistency and stability within the scheme is important for all players in the ecosystem, including merchants who benefit from transparent and stable MSC costs.[948]

2.248 We have not seen specific mention of any positive benefits to merchants from alignment with non-EEA-to-UK IFs in Mastercard's internal documents.

945 Mastercard response to PSR questions dated 5 August 2022 [✂].
946 Mastercard response to PSR questions dated 5 August 2022 [✂].
947 Mastercard response to PSR questions dated 5 August 2022 [✂].
948 Stakeholder response to MR22/2.6 dated 14 February 2024 [✂].

2.249 Visa stated in its response to our questions that the new outbound IF levels meant that, from a UK merchant perspective, all incoming transactions (from non-UK consumer cards such as the USA, Australia or France) would have the same interchange rates applied.

2.250 Visa told the TSC that these changes harmonised the interchange levels for non-UK consumer cards being used online with UK merchants. For example, irrespective of whether a consumer debit card is issued in the USA, Australia or France, a UK merchant will pay the same level of interchange on a cross-border e-commerce purchase.[949]

2.251 Visa explained that: 'a simpler interchange structure [✁].'[950]

2.252 Visa also explained that this is consistent with 'Visa's 2013 antitrust commitments with the European Commission in which, at the European Commission's request, Visa committed to reducing the number of different interchange levels by at least 25% to aid transparency and comparison between rates.'[951]

2.253 We asked Visa to provide us with any contemporaneous documents it had considered showing the alleged simplicity benefits. Visa told us [✁].[952]

2.254 Stakeholders did not provide any additional evidence in relation to this point.

Our final view

2.255 While Mastercard refers to the benefit of consistency and predictability in applying the same IF levels in relation to both inbound and outbound UK-EEA IFs, we note that [✁]. This suggests that **[✁].** Its suggestion that there was no direct financial benefit to issuers of this benefit was not one we found convincing.

2.256 It is also not clear to us how raising IFs would generate 'consistency' and/or 'predictability'. We consider that leaving inbound and outbound IF levels at the levels they were before the UK's withdrawal from the EU would have achieved a higher degree of 'consistency' and 'predictability' at no extra cost to merchants, and that those existing levels were capable of being readily understood by participants.

2.257 Harmonising the interchange structure for non-UK consumer cards used online with UK merchants was mentioned as one of the elements that Visa considered when deciding to increase UK-EEA CNP IFs. However, it is unclear to us how any alleged benefits from such a claimed simpler structure for merchants would outweigh the detriment imposed on the same merchants by the increased IFs they would face. We have seen no evidence that merchants were seeking 'a simpler interchange structure'. Nor have we seen any evidence that merchants have welcomed the 'simpler interchange structure' notwithstanding the increased IFs that accompanied it. Indeed, the evidence we have received from merchants has been that these extra costs are not welcomed and did not provide any benefits to them. In addition, by keeping the levels as they were before, the existing relatively simple interchange structure could have continued, but at no cost for merchants.

949 Visa, Visa Response to Treasury Select Committee on Cross-border Interchange.

950 Visa response to PSR questions dated 5 August 2022 [✁].

951 Visa response to PSR questions dated 5 August 2022 [✁].

952 Visa response to PSR questions dated 5 August 2022 [✁].

2.258 Therefore, our view is that the increase in fees was not justified by reference to the practical benefits put forward by Visa or Mastercard.

Annex 3

The [✂] (2023) MIT assessment

The [✂] 2023 MIT IF study

3.1 Shortly prior to the publication of our interim report, Visa asked us to consider a study titled 'Applying the Merchant Indifference Test to Visa's EEA to UK CNP transactions (the [✂] 2023 MIT IF assessment)'. This study was commissioned by Visa from an economic consultancy ([✂]). The study assesses Visa's EEA to UK CNP MIFs *[UK-EEA consumer CNP outbound IFs]* against the MIT – 'a benchmark that has long been used by the European Commission for assessing the appropriateness of multilateral IF levels, including to underpin the interchange caps in the IFR and in the 2019 European Commission Commitments Decision'.[953]

3.2 The [✂] 2023 MIT IF assessment computed the MIT benchmark using current and commonly used alternative payment methods, including three-party card schemes such as American Express, non-card funded digital wallets such as PayPal, BNPL providers such as [✂] and account-to-account providers. We are told that the 2023 Report has been reviewed and endorsed by a co-creator of the MIT, Professor Jean-Charles Rochet, who has been paid by Visa for his advice. [✂] compared the cost for UK merchants to accept these alternative payment methods against the total cost for UK merchants of accepting payments using a Visa card. The report found the MIT MIF 'benchmark' for EEA>UK consumer CNP transactions to be [2.70-2.90%] for debit and [2.50-2.70%] for credit. When applying sensitivity adjustments which Visa described as conservative in order to "stress test" these results, for example by [✂], the relevant MIT 'benchmark' reduces to [2.00-2.20%] for both debit and credit card transactions.

3.3 At a high level, the [✂] 2023 MIT IF assessment involved:[954]

a. [✂]

b. [✂]

c. [✂]

d. [✂]

e. [✂].

3.4 Each of the consultant's steps are considered below.

a. [✂]

953 [✂]

954 [✂]

3.5 [✂].[955]

b. [✂]

3.6 [✂].[956] [✂].[957]

c. [✂]

3.7 [✂].[958] [✂].[959]

d. and e. [✂]

3.8 [✂].

Table 17: [✂][960]

[✂]

Table 18: [✂][961]

[✂]

[✂]

3.9 [✂].[962]

Our provisional view in our interim report

3.10 In the interim report we provisionally made the following observations.

[✂]

3.11 [✂].[963] [✂]. Visa also told us that [✂].[964]

[✂]

3.12 [✂].

955 [✂].
956 [✂].
957 [✂].
958 [✂].
959 [✂].
960 [✂]. [✂].
961 [✂].
962 [✂].
963 Visa, [✂].
964 Visa, [✂].

3.13 [✂].

3.14 [✂].

3.15 [✂].[965] [✂].[966]

3.16 [✂].

[✂]

3.17 [✂].

[✂]

3.18 [✂].

Visa and Mastercard responses to our note on the [✂] 2023 MIT assessment

3.19 On 15 April 2024 we shared with Visa and Mastercard a note that explained our initial view on the 2023 MIT assessment produced by [✂]. The note illustrated our observations on the methodology and comparators applied by [✂] and presented our assessment of the robustness of the data and methodology that [✂] applied.

3.20 In the note, we state that [✂].

3.21 The consultancy [✂] used the following comparators in their assessment: [✂].

3.22 Furthermore, information on costs included in the [✂] report was gathered [✂].

3.23 Visa responded to our note on 29 April 2024 and made the following points.

3.24 Visa said that, in contrast to what is stated in the our note, three-party card schemes are suitable comparators in an MIT study because there is not sufficient evidence of endogeneity. Following PSR's comment, Visa said that our concept of 'implicit interchange fees' is unsatisfactory as all payment methods operate in two-sided markets and almost all payment methods tend to recoup all (or the majority of) their costs on the merchant side of the market while offering their services to consumers largely for free. There is always likely to be a subsidy from the merchant to the consumer side (that is, an implicit IF), but such a price structure is not necessarily an indication of endogeneity.[967]

965 An important feature of any comparator for the purposes of the MIT is that it should not contain an IF element. This avoids spurious effects related to the fact that the current cost to merchants of potential comparators may be impacted by the IF levels of Visa (and Mastercard) cards. This is also explained at paragraphs 77 and 80 of the Visa 2019 Commitments decision and at paragraph 75 of the European Commission's 2017 Cost of Cash and Cards study.

966 European Commission, CASE AT.39398 – Visa MIF, VISA 2019 Commitments decision and 2019 Commitments, recitals 77 and 80. A similar approach was followed as regards Mastercard's commitments for inter-regional MIFs – see CASE AT.40049 – Mastercard II, Mastercard 2019 Commitments decision and 2019 Commitments.

967 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✂].

3.25 Visa said that, in contrast to what stated in our note, the MIT should not only include the cheapest possible alternatives. Consumers choose their preferred form of payment and the merchant is not able to steer them only to the cheapest payment method. Additionally, Visa said, this is inconsistent with the original design of the MIT, which aims at identifying a level of MIF at which the merchant cost of accepting Visa does not increase the overall cost for the merchant.[968]

3.26 Visa said that, in contrast to what stated in our note, the MIT assessment by Visa's economic advisors [✁] is consistent with the MIT methodology originally developed by Rochet and Tirole (2011). Visa said that its economic advisors' [✁] assessment correctly compares the avoided cost for merchants of accepting a card payment with an alternative payment method when one ignores the benefits to merchant not losing a transaction.[969]

3.27 Visa said that in contrast to what is stated in our note, Visa's economic advisors' [✁] MIT assessment only included digital wallets when they do not rely on card rails. It said, therefore, they cannot be excluded from an MIT study. Additionally, Visa told us that we are wrong to exclude BNPL on the basis that it offers credit functionality, since credit cards would need to be excluded as well.[970]

3.28 Visa stated that the weights used in its economic advisors' [✁] MIT assessment reflect the likely usage of each alternative payment method considered in the report. Therefore, in contrast to what is written in our note, weights are not inflated to give more emphasis to more expensive comparators: the market reality, Visa said, is that almost all comparators for EEA to UK CNP transactions are more expensive than a Visa (or Mastercard) card, save for some A2A payment methods which are rarely used for these transactions.[971]

3.29 Visa said that in contrast to what is stated in our note, its economic advisors' [✁] MIT assessment did not overstate acceptance costs for merchants for alternative payment methods to Visa cards. It said its economic advisors [✁] sourced cost information for Visa cards and alternative payment methods from public sources. Visa told us this methodology ensures the consistency of the data collected and it allows to compare costs that small merchants face when accepting different forms of payment.[972]

3.30 Visa stated that our note did not include enough evidence to substantiate the claim that the pricing of A2A methods is materially independent from Visa and Mastercard's MIF. Additionally, it said some of the A2A methods we mentioned are rarely used by EEA consumers to make transactions in the UK.[973]

3.31 The consultancy [✁] replied on behalf of Mastercard to our note. The response was received on 10 May 2024.

3.32 The consultancy [✁] stated that our approach to the MIT in the note is not consistent with the relevant economic literature and with previous applications of the test by the European Commission. The consultancy stated that the cheapest alternative payment method is not

968 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

969 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

970 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

971 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

972 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

973 Stakeholder response of 29/04/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

always the best solution for merchants, because they value other characteristics such as security, convenience and reliability. The consultancy also stated that competition on the merchant side is not a race to the bottom on price.

3.33 The consultancy [✂] deeply criticised the mix of comparators used in our note. The consultancy said that we are wrong in focusing solely on A2As: they do not all offer the same benefits to cardholders and merchants as cards and they offer limited fraud protection. The consultancy also said that BNPLs should be included as comparators: they provide a credit service, other than being a payment method, thus representing an appropriate comparator for credit cards. Additionally, the MIT should incorporate the cost of providing a credit service, in as much as it should include the cost of credit related to credit cards. BNPL would also be appropriate comparators for debit cards, because if a merchant accepts BNPL payments would make it available for all cardholders, including debit.[974]

3.34 The consultancy [✂] stated that consumers' choices need to be taken into account when doing the MIT, and we should not exclude payment methods that are most preferred by consumers. Given the nature of the usage externality which the MIT addresses, the relevant alternative payment methods cannot be the cheapest alternatives to four-party cards but must be selected based on those which consumers would switch to in the absence of four-party cards. If only the cheapest alternatives are included, under certain conditions, the MIT IF will be set too low and this will not be in merchants' interests as it will not address the usage externality. In such a scenario, the low IFs will, in the long run, encourage cardholders to choose alternatives to cards as issuers reduce services levels or increase transaction fees.[975]

3.35 The consultancy [✂] rejected the claim in our note that American Express should be excluded for endogeneity reasons. The consultancy suggested testing whether American Express's fees react to movements of EEA-UK IFs before postulating any endogeneity concern. If such relationship would exist, the consultancy suggested adjusting American Express's costs by removing any MIF-related cost rather than excluding American Express altogether. The consultancy suggested that a similar approach could be adopted also in regard to card-funded digital wallets. The consultancy observed that there was no change in PayPal prices following the implementation of the IFR, when the MIFs were lowered and capped to 0.2/0.3%. Therefore, no endogeneity could be detected.[976]

3.36 The consultancy [✂] replicated the analysis in our note by performing some scenario analyses. In the first scenario, they use the original weights and comparators in [✂] and correct the cost of PayPal to include all the types of transactions (not only the ones marked as 'APM' on PayPal's website). They obtain a MIF of 3.19% for debit and 2.75% for credit. In the second scenario, the consultancy included, as comparators, payment methods which offer consumer protection that is comparable to cards. Therefore, they excluded pure SEPA bank transfers, GoCardless and Trustly. Costs for PayPal were computed as in the previous scenario. The consultancy obtained a MIF of 3.36% for debit and 2.83% for credit. The third scenario is a modified version of the first one, where the consultancy adjusted the price of American Express downwards by 50bps for any possible endogeneity. They obtained a MIF of 3.15% for debit and 2.70% for credit. The fourth and last scenario was a modified version of the second scenario, where, once again the price

974 Stakeholder response of 10/05/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✂].

975 Stakeholder response of 10/05/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✂].

976 Stakeholder response of 10/05/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✂].

of American Express was adjusted downwards by 50bps. They obtained a MIF of 3.32% for debit and 2.77% for credit.[977]

Our response to Mastercard and Visa's views

3.37 We disagree with the claims in paragraphs 3.24 and 3.35 that three-party schemes are not affected by endogeneity and, therefore, suitable comparators for MIT purposes. As explained in paragraphs 5.27 and 5.44, American Express pricing is endogenous to Mastercard and Visa's pricing and as such cannot be used for MIT purposes. Problems related to endogeneity and why endogenous comparators cannot be used for an MIT have been clearly explained by the European Commission in the past.[978] Additionally, the endogeneity of American Express has already been discussed in previous investigations.[979, 980] We also note that, consistent with this issue, the EC did not use American Express as a comparator for MIT purposes despite this being available both in 2013[981] (at the time of cost of cash and card study) for card-present transactions and in 2019[982] (at the time of EC 2019 commitments) for card-not-present cross-border transactions.

3.38 Furthermore, contrary to what Visa says in paragraph 3.24, not all payment methods are characterised by an implicit IF (a flow of money, benefits or any other rewards paid by the acquiring side to the benefit of the payers/cardholders). While for American Express rewards and other benefits (funded by the fees paid by the merchants) are paid to the cardholders and are often on a per-transaction basis, many other payment methods (for example, A2A) do not provide for these type of benefits and rewards.

3.39 We note the comment made in paragraphs 3.25 and 3.26 that the MIT should not only include the cheapest possible alternative. However, this does not mean that all alternative payment methods should be included among possible alternatives for MIT purposes. As noted above, alternative payment methods that present an element of IF (for example because they are based on Mastercard and Visa cards) or that imply a flow of money, benefits or any other rewards paid by the acquiring side to the benefit of the payers/cardholders cannot be considered for MIT purposes to avoid spurious results. This means that alternatives that include forms of merchant-funded benefits to buyers, which are often the most expensive alternatives for the merchants, cannot therefore be considered for MIT purposes.

977 Stakeholder response of 10/05/24 to PSR's Note on 2023 MIT report dated 15 April 2024 [✁].

978 See European Commission, Directorate-General for Competition, Survey on merchants' costs of processing cash and card payments – Final results, March 2015, Publications Office of the European Union, 2015 – p. 22 para. 75-77.

979 See American Express Australia Submission to the Reserve Bank of Australia Review of Retail Payments Regulation Issues Paper (January 2020), Pages 6-9.

980 See the interchange fee investigation from Commerce Commission of New Zealand https://comcom.govt.nz/regulated-industries/retail-payment-system/monitoring.

981 See European Commission, Directorate-General for Competition, Survey on merchants' costs of processing cash and card payments – Final results, March 2015, Publications Office of the European Union, 2015.

982 See European Commission, Case AT.39398 – Visa MIF, VISA 2019 Commitments decision and 2019 Commitments; Case AT.40049 – Mastercard II, Mastercard 2019 Commitments decision and 2019 Commitments.

3.40 In paragraph 3.27, Visa said that in contrast to what is stated in our note, **[✂]** MIT assessment only included digital wallets when they do not rely on card rails. While some digital wallets payments do not rely on cards, we note that:

- Many of these still rely on Visa or Mastercard cards and as such they incorporate their cost including IFs.
- As reported in paragraph 5.27, PayPal Digital Wallet heavily relies on Mastercard and Visa's rails both in the UK and in the EEA. Therefore, for UK-EEA CNP transactions the cost of its services to merchants incorporates the scheme's IFs (and also their scheme and processing fees). So, the price of PayPal is inevitably higher than and often correlated to the price of Mastercard and Visa[983,984,985]. In addition to this, PayPal told us that [✂].[986] PayPal told us that [✂].[987] It has been widely reported that PayPal has entered into agreements with Mastercard and Visa (both in the US and elsewhere, including Europe). In July 2016, PayPal signed US strategic partnerships with Visa. PayPal agreed to present Visa cards as a clear and equal payment option, and not to encourage Visa cardholders to link to a bank account. The agreement with Visa also included certain economic incentives and greater long-term Visa fee certainty. [988] In July 2017, the partnership between PayPal and Visa was extended to Europe. [989] In September 2016, a US agreement was signed between PayPal and Mastercard. [990] In October 2017, the agreement with Mastercard was similarly extended to Europe. [991,992] For these reasons, PayPal payment services do not currently represent a suitable alternative for benchmarking the card schemes' pricing.

3.41 On views in paragraph 3.27 as to whether BNPL should be included in an MIT considering that also credit cards present credit functionality, we note that credit cards have never been used in previous MIT applications as a comparator for MIT purposes. We also note that these arguably include a form of merchant funded benefit to buyers that is free credit at the point of sale and as such their use for MIT purposes is questionable. We also note that very often BNPL transactions rely on Visa and Mastercard cards and, as such, they are characterised by the usual endogeneity issues described in paragraph 3.37. Finally, for UK-EEA cross-border transactions, in 2023, a BNPL provider [✂] confirmed that they [✂][993]. As such, contrary to what Mastercard and Visa have said and contrary to what the consultancy [✂] did in their MIT assessment, **[✂]** BNPL solutions cannot be used as a comparator for UK-EEA CNP payments.

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983 Evidence of this is the fact that, when Mastercard and Visa increased their outbound IFs, PayPal decided to increase the fees for UK-EEA cross-border payments from 0.5% to 1.29%. At the time, PayPal stated that this was due to the fact that it was incurring extra costs, such as the rise in Mastercard and Visa IFs between the UK and the EEA (BBC News, *PayPal raises fees between UK and Europe* (9 September 2021).

984 See PayPal merchant fees (visited on 19/08/2024).

985 See also stakeholder letter to the PSR dated 4 August 2023. [✂]

986 PayPal's response to PSR information request dated 2 October 2023 [✂].

987 PayPal's response to PSR information request dated 2 October 2023 [✂].

988 See: PayPal and Visa enter new partnership | Visa (visited on 19/08/2024).

989 See Visa and PayPal Extend Partnership to Europe | Business Wire (visited on 19/08/2024).

990 See PayPal and MasterCard End Fight With Agreement on Fees and Data - Bloomberg (visited on 19/08/2024).

991 See PayPal-Mastercard Deal Goes Global (businessinsider.com) (visited on 19/08/2024).

992 See also MR22/1.9: Market review of card scheme and processing fees interim report, Annex 1 paragraph 1.133.

993 Stakeholder submission to PSR dated 2 August 2023 [✂]

3.42 In regard to the claim made in paragraph 3.28, we note that the weights do not refer to the usage of payment methods in the UK-EEA online space, but only to usage in their domestic markets, which have nothing to do with what happens in the cross-border space. In this regard, we note that they have attributed significant weight to BNPL [✂], which may be popular in some domestic markets, but, as we note in paragraph 3.41, [✂].

3.43 With regards to paragraph 3.29, acquirers and payment facilitators have confirmed that the listing prices available on their websites (that is, the ones used by those used by the consultancy [✂]) represent only an upper threshold for merchant acceptance costs, as they are often negotiated with the merchants.[994]

3.44 In addition [✂].[995,996]

3.45 In regard to the claim made in paragraph 3.30, as explained paragraph 3.38, many A2A solutions do not provide for a transfer (be it in the form of money, benefits or other rewards) from the acquiring side to the payers, and as such are less prone to endogeneity issues. If those payment methods are the only ones left, after we have eliminate those that are affected by endogeneity and those that are unavailable for UK-EEA CNP transactions, then the fact that they are rarely used does not make them unsuitable for the MIT.

3.46 Contrary to the claims made in paragraph 3.32, 3.33 and 3.34, the approach described in our note is consistent with how the European Commission applied the test, as it suggests that only non-endogenous alternatives can be considered for MIT purposes. We agree that security and reliability for the merchants are important considerations for choosing APMs. However, this represents different costs and benefits to merchants that should be taken into account and, when possible, quantified in an MIT.

3.47 Finally, we note the scenario analyses performed by [✂] and summarised at paragraph 3.36. However, the scenarios, which result in proposed IFs that are high and in one scenario even higher than the original [✂] assessment, fail to address the comments we made on the [✂] assessment itself.

994 Stakeholder submission to PSR information request dated 7 May 2024 [✂].

995 Stakeholder submission to PSR information request dated 7 May 2024 [✂].

996 Stakeholder response to MR22/2.6 dated 31 January 2024 [✂].

Annex 4
Glossary

Term	Definition for the purpose of this document
Account-to-Account (A2A) payment solutions	Account-to-account (A2A) payments move money directly from a payer's bank account to a payee's bank account without the need for intermediaries, such as credit or debit cards.
Acquirer	A bank or other licensed payment service provider that contracts with one or more merchants to provide card-acquiring services for card payment systems.
Alternative payment methods (APMs)	Non-card payment methods.
Approved transaction	A transaction that has been authorised by the issuer.
Blended pricing	Pricing offered by acquirers to merchants for card-acquiring services, whereby for any given transaction the acquirer does not automatically pass through at cost the interchange fee applicable to the transaction.
BNPL	Buy now, pay later. BNPL solutions allow buyers to pay a purchase in instalments, often with zero interest rate.
Bps	Basis points (one hundredth of 1 percent).
BRC	British Retail Consortium.
Brexit	The withdrawal of the United Kingdom from the European Union. The transition period following the UK's withdrawal from the EU ended on 31 December 2020.
CAMR	Card acquiring market review.
Card-acquiring services	Services to accept and process card transactions on behalf of a merchant, resulting in a transfer of funds to the merchant.
Cardholder	A person who is issued a payment card and authorised to use that payment card.
Card-not-present/CNP transaction	A transaction that is completed online, by phone or by mail, so a card (be it physical or tokenised) is not present when the merchant is taking payment.

Term	Definition for the purpose of this document
Card payment system	A payment system that enables a holder of a payment card to make a payment.
Card payment system operator	Organisations that manage the 'scheme rules' on card payments and set the terms on which issuers, acquirers, merchants, cardholders and other parties participate in the card payment system.
Card-present/ CP transaction	A card transaction in which the cardholder is present at the outlet and presents the payment card.
Card schemes	Operators of card payment systems (such as Mastercard and Visa). These are organisations that license issuers and acquirers to recruit cardholders and merchants, respectively. They manage the 'scheme rules' that govern how card payments are made and set the basis on which issuers, acquirers, merchants, cardholders and other parties participate in the card payment system.
Card transaction	A transaction carried out under a card payment system that results in the transfer of funds between a cardholder and a merchant. This includes purchase transactions, refunds and transactions related to the chargeback process.
CAT	The Competition Appeal Tribunal.
CBDC	Central bank digital currency.
Chargeback	When a customer disputes a debit or credit card transaction, this is a way for their card issuer to claim money from the retailers' bank for the goods or services the cardholder paid for.
Court of Appeal/CA	The Court of Appeal of England and Wales.
Co-badged cards	A card supporting two or more payment networks.
Court of Justice/CJEU/CJ	The Court of Justice of the European Union.
Credit card	A card whose holder has been granted a revolving line of credit. It enables the holder to make purchases and/or withdraw cash up to a prearranged ceiling; the credit granted can be settled in full by the end of a specified period or can be settled in part, with the balance taken as extended credit. Interest may be charged on the transaction amounts from the date of each transaction or on the outstanding balance where it has not been settled in full.

Term	Definition for the purpose of this document
Cross-border transactions	Card transactions where the issuer and the acquirer are located in different countries or where the card was issued by an issuer located in a different country from that of the point-of-sale location (the merchant location).
Debit card	A card enabling the holder to have their purchases directly charged to funds in their account.
Declined transaction	The cardholder's bank has not approved an authorisation request for a transaction.
Digital wallet	An application on an electronic device that stores payment details, which allows the holder to securely make payments without the physical card.
EC	The European Commission.
EEA	The European Economic Area.
EEA acquirer	An acquirer who provides services to EEA merchants.
EEA cardholder	A cardholder whose card is provided by an EEA issuer.
EEA merchant	A merchant with at least one EEA outlet.
ECB	The European Central Bank.
EU	The European Union.
EU IFR	The EU Interchange Fee Regulation 2015, Regulation (EU) 2015 / 751 of the European Parliament and Council.
Four-party card scheme	A card system in which the operator (such as Mastercard or Visa) licenses third-party issuers and acquirers to recruit cardholders and merchants, respectively.
FSBRA	The Financial Services (Banking Reform) Act 2013.
Fraud disputes	Disputes where cardholders' accounts are debited for transactions they did not authorise. These usually occur when an individual's card details have been compromised and someone who has gained access performs unauthorised transactions, or when a fraudulent merchant is processing questionable transactions through to the consumer's account. They can also arise when a consumer disputes a transaction they made. This could be for several reasons such as that the goods were not received, goods were not as described or damaged, the cardholder was charged an incorrect amount, or processing errors.

Term	Definition for the purpose of this document
FX	Foreign exchange.
General Court/GC	The General Court of the European Union.
Honour All Cards/HAC rule	Mastercard and Visa's scheme rules that prevent a merchant from choosing or declining transactions on the basis of a card issuer's location.
IC++ pricing	Pricing offered by acquirers to merchants for card-acquiring services, whereby for any given transaction the acquirer automatically passes on at cost the interchange fee and scheme fees applicable to the transaction.
Inbound interchange fees (Inbound IFs)	IFs for transactions using UK-issued cards to make payments to merchants located outside the UK. For UK-EEA transactions, these IFs relate to payments made with UK-issued cards at EEA merchants. These fees are paid to UK issuers and represent a cost to EEA merchants. Note: In the interim report we use 'CNP inbound IFs' and 'inbound IFs' interchangeably to refer to UK-EEA consumer CNP inbound IFs.
Interchange fee/IF	A fee that acquirers pay to issuers each time a card is used to buy goods or services. This is a per-transaction fee and is usually levied as a percentage of the transaction value. The IF charged can vary depending on transaction and IF type.
Issuer	Banks or other organisations licensed by card payment system operators to provide cards to cardholders. The issuer pays an acquirer the money a merchant is owed for the transaction (retaining IFs) and debits a cardholder's account.
Merchant	An organisation that accepts card payments.
MIF	Multilateral interchange fee.
MIT	Merchant indifference test.
MSC	Merchant service charge, which is the total amount merchants pay to acquirers for card-acquiring services. This comprises interchange fees, scheme and processing fees and acquirer net revenue.
Monitoring trustee	An independent person, approved by the PSR, who has the duty to monitor compliance with certain conditions and obligations and report to the PSR.
Nudging	A form of behavioural steering.

Term	Definition for the purpose of this document
Open Banking	A system which facilitates the secure sharing of customer financial information using application programming interfaces (APIs). Open Banking enables consumers and small and medium-sized enterprises (SMEs) to share their bank and credit card transaction data securely with trusted third parties, who are then able to provide them with applications and services. It also enables consumers and SMEs to initiate payments directly from their payment accounts to the bank account of their payee, without the use of cards.
Outbound interchange fees (Outbound IFs)	IFs for transactions using non-UK-issued cards to make payments to merchants located in the UK. For UK-EEA transactions, these IFs relate to payments made with EEA-issued cards at UK merchants. These fees are paid to EEA issuers and represent a cost to UK merchants. Note: In the interim report we use 'CNP outbound IFs' and 'outbound IFs' interchangeably to refer to UK-EEA consumer CNP outbound IFs.
Payment system	A system that is operated by one or more persons in the course of business for the purpose of enabling persons to make transfers of funds.
Payment default	A situation where a consumer misses a payment or payments on a credit agreement they have entered into.
Payment facilitator	A payment facilitator is a payment service provider (PSP) that enables merchants to accept payments, including card payments, via a payment gateway. For card payments, the payment facilitator contracts with an acquirer who retains responsibility for allowing merchants to access the card payment systems. The acquirer is also liable for the merchant's and the payment facilitator's compliance with the rules set by the card scheme operator.
Processing fees	All fees paid to a card scheme operator by customers for the processing of card transactions (the authorisation, clearing and settlement of purchase transactions) that arise as a result of them being party to any card transactions involving one or both of: • payments to (or from) a UK merchant • payments from (or to) a UK cardholder
Rebates and incentives	Monies and non-monetary benefits that Mastercard and Visa give to issuers.

Term	Definition for the purpose of this document
Retail transaction	A transaction between a consumer and a merchant.
RoW	Rest of the world
Scheme fees	All fees paid to a card scheme operator that arise as a result of customers being party to any card transactions involving one or both of: • payments to (or from) a UK merchant • payments from (or to) a UK cardholder This includes fees that are directly attributable to a card transaction as well as fees that are not directly attributable to a card transaction but are paid as a condition of participation in the payment scheme. This does not include fees directly attributable to card transactions at non-UK outlets, unless a UK cardholder was involved. This does not include processing fees and international fees.
Scheme rules	All rules, policies, procedures, regulations and standards that relate to the operation and administration of a card payment system (whether published or not).
SEPA	The Single European Payment Area.
SEPA credit transfer	This is a payment method to send funds from one bank within SEPA to another.
SEPA direct debit	Direct debit authorization system that allows to send recurring payments from one bank within SEPA to another.
Section 75	Is part of the Consumer Credit Act 1974 that means the cardholders credit card issuer is jointly responsible for any breach of contract or misrepresentation by a retailer or trader.
Section 81 notice	Notices in writing requesting information or documents pursuant to section 81 of FSBRA.
Supreme Court	The Supreme Court of the United Kingdom.
UK	The United Kingdom,
UK IFR	UK version of the EU IFR: the EU IFR is assimilated into UK Law by the Retained EU Law (Revocation and Reform) Act 2023 in accordance with the Financial Services and Markets Act 2023.

Term	Definition for the purpose of this document
TFEU	Treaty on the Functioning of the European Union.
Tokenisation	The process of replacing a card's primary account number (PAN) – the 16-digit number on the plastic card – with a unique alternate card number, or 'token'. Tokens can be used for mobile point-of-sale transactions, in-app purchases or online purchases.
UK acquirer	An acquirer who provides services to UK merchants.
UK cardholder	A cardholder whose card is provided by an UK issuer.
UK merchant	A merchant with at least one UK outlet.
2019 Commitments	Commitments offered by each of Mastercard and Visa and accepted by the European Commission to cap IFs on transactions involving cards issued outside the EEA and merchants in the EEA in Commission cases AT.40049 and AT.39398 respectively.

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