



BRC response to PSR Strategy consultation (CP21/7)

September 2021

Introduction

- 0.1 The British Retail Consortium (BRC) is the trade association for the retail industry – the UK’s largest employer. Our diverse industry spans large multiples, independents, high street, and out of town retailers, from online to bricks-and-mortar, selling goods across all sectors to increasingly discerning consumers.
- 0.2 All BRC members have an interest in UK payment systems as one of their chief end-users. Indeed, along with consumers, retailers are the most significant other end-user group, processing more than 50 million transactions per day and almost £400 billion per year for products & services sold in store, online, and over the phone (2019). A high priority for the BRC is therefore to seek an innovative, transparent, and competitive payments market for all retail end-users and their customers.

Summary

KEY POINTS

- The proposed PSR Strategy lacks essential details required for the PSR to hold itself to account, or for others to do so. There is an absence of specific, measurable and time-limited objectives that would make it difficult to assess the PSR’s success in achieving good outcomes.
- The Strategy document conflates present day *harms* to consumers and businesses from the card payments system, for which action is overdue, as *risks* to be considered at some point in the future.
- There is a conspicuous absence of any meaningful commitment to address current harms within the card payments system despite of the substantial and increasing evidence of excessive and ever-growing costs to users. No measurable outcome has been defined and no timeframe established within which the PSR will intervene in the coming 5 years if competitive outcomes are not seen.
- Following the UK’s departure from the European Union, the UK Government and its regulator have yet to address new opportunities for anti-competitive behaviour and abuse of the card schemes dominant market position in Europe’s largest card payments market where card-based transactions constitute at least 80% of retail payments today.

- 0.3 The proposed PSR Strategy lacks essential details required for the PSR to hold itself to account, or for others to do so. In general, there is an absence of specific, measurable and time-limited objectives within the document. This will make it difficult to assess the PSR’s success in achieving the promised good outcomes for end-users of the UK’s payments systems within the five-year time period covered.



- 0.4 In particular, there is a conspicuous absence in the Strategy of any meaningful commitment to addressing current and longstanding harms within the UK card payments system, despite the substantial and increasing evidence of excessive and ever-growing costs to users, including that which the PSR has itself gathered in the process of its ongoing Market Review on the supply of card acquiring services.
- 0.5 For the coming five years the UK's regulator for payment systems has stated that it will merely "consider the need... to regulate in order to protect consumers and businesses if other measures are not producing the competition outcome we seek", however no measurable competition outcome has been defined and no timeframe established within which to achieve it. There is, therefore, no relevant threshold, milestone or deadline identified by the PSR for when it will commit itself to "intervene robustly" in the card payments market to deliver against its statutory objectives.
- 0.6 The only measure that the PSR is proposing in order to tackle the lack of effective competition within UK card payments is the development of an altogether different system of interbank payments for retail payment use. Yet the Strategy document itself casts significant doubt on whether it is realistic or attainable for interbank payments to challenge the dominance of card-based transactions in retail payments. As the PSR admits on page 6, "the current commercial incentives do not align with the objective of making greater use of interbank to support competition over the longer term." Again, no criteria have been established in the Strategy for what might constitute a successful competitive outcome from interbank systems in retail payments and no time scale identified for its achievement. The Strategy simply offers a pre-emptive admission of likely failure, namely that "this is not a straightforward task and will take some time to deliver."

Action on card payments is missing and long overdue

- 0.7 The stated intention of the PSR is to "shift our focus to promoting competition between payment systems" (p13), suggesting that the PSR has hitherto focussed on competition within the card payments system and adequately addressed the anti-competitive practices therein. The BRC has observed only limited evidence of this and the PSR's proposals for the card payments industry need to go much further.
- 0.8 The PSR Market Review on the supply of card acquiring services involved a thorough study that confirmed the BRC's own findings that the benefits of legislation to reduce card fees have not been passed on to most retailers (and therefore consumers), and that the fees levied by the card schemes have been increasing aggressively for several years. Yet the Market Review has lacked the scope needed to address the most harmful anti-competitive behaviours within the card payments system and so, in turn, the very modest remedies proposed in the PSR's interim report fail to adequately address these existing and growing harms. Indeed, the remedies are not sufficient or suitable to tackle the problems identified in the PSR's own findings.
- 0.9 The Strategy document appears to conflate present day *harms* to consumers and businesses from the card payments system, for which action is overdue, as *risks* to be considered at some point in the future: "we identify that there is a significant risk that the UK payments market will move towards a future without sufficient rivalry. Over time, this could undermine the outcomes that consumers and businesses receive from payment systems and payment firms." (5.64) These harms, as opposed to risks, are not only current but long-standing. The BRC first formally complained to the European Commission in 1992 that Visa and Mastercard interchange fees unlawfully restrict competition and the annual BRC Payments Survey (formerly Costs of Collection Survey) began spotlighting excessive card costs in 1999.



- 0.10 The Interchange Fee Regulation (IFR), introduced across the EU in 2015 after a generation of pressure from UK & European business, promised to “cut the cost of payments substantially for merchants, especially SMEs and that in turn should lead to a fall in consumer prices”. In practice, it only regulates some interchange fees and no card scheme fees. The PSR have themselves recorded that card scheme fees have “more than doubled over the period from 2014 to 2018, with most of this increase occurring between 2016 and 2018, after the IFR caps came into force” (PSR, 2020).
- 0.11 The cumulative cost to UK merchants of scheme fee increases since the introduction of the IFR reached £2.3 billion this year (CMSPI estimates, 2021) with an annual cost to UK merchants of successive scheme fees increases since IFR of £500 million per year.
- 0.12 Following the UK’s departure from the European Union, the UK Government and its regulator have yet to address new opportunities for anti-competitive behaviour and abuse of the card schemes dominant market position. The impact on UK merchants of the latest scheme fee and interchange fee increases announced since 1st January this year adds a further £60 million in costs which ultimately add to the price of goods and services paid by consumers. Average UK Merchant Service Charges, as a proportion of card turnover, are now higher in 2021 than 2014, prior to the IFR coming into effect.
- 0.13 Last year a UK Supreme Court ruling confirmed that Visa & Mastercard interchange fees are unlawful, creating a considerable anomaly that the PSR continue to allow such fees and have not directly addressed the pressing matter of anti-competitive card fees in its future Strategy.
- 0.14 In October 2020, a number of major British business bodies including the BRC, UK Hospitality, British Independent Retailers Association (Bira), Association of Convenience Stores (ACS), and Federation of Small Business (FSB) all called for action from the PSR to defend British businesses and consumers from excessive card costs.
- 0.15 This year too around 40 Parliamentarians have supported cross-party action calling for robust regulatory measures on card fees in the PSR Strategy, including the regulation of payment card schemes fees and the abolition of interchange fees.
- 0.16 As it stands the PSR Strategy must go much further to address the extant harms within the card payments system. Whilst the BRC fully supports the PSR objective to develop interbank payment systems as fully as possible, this does not remove the obligation on the PSR to take urgent and specific measures to fulfil its statutory objectives in Europe’s largest card payments market where card-based transactions constitute at least 80% of retail payments today.
- 0.17 The time for action on card payment system is already long overdue. As the PSR itself notes, “the costs of operating UK payments are ultimately paid for by consumers and businesses (even if they do not always face the direct cost at the time of making a payment). It is therefore important that payment systems are run efficiently so that they represent value for money.” (4.51)



1. Do you think the key trends we have identified adequately capture the most important system-level changes payments and UK payment systems are likely to experience over the next five years? If not, please explain what we have missed and why it is important.

Card Payments System

- 1.1 The 2020 BRC Annual Payments Survey showed that cards were used to pay for approximately £309 billion worth of goods in 2019 – accounting for almost 80% of retail spending even before the pandemic. The share of card payments has grown substantially in 2020, further increasing the reliance of British businesses and consumers on card payments – particularly contactless payments – and with it the cost of payment acceptance.
- 1.2 The cost to the retail industry of processing card transactions remains very high, accounting for 61% of retail transactions, but 83% of retailers' cost of acceptance. Debit cards are around four times as expensive as cash to process, whilst credit cards are more than three times as expensive to process than debit cards, on a like-for-like basis.
- 1.3 Costs are only increasing further for end users. The Interchange Fee Regulation (IFR), introduced across the EU in 2015 after a generation of pressure from UK & European business, promised to “cut the cost of payments substantially for merchants, especially SMEs and that in turn should lead to a fall in consumer prices”. In practice, it only regulates some interchange fees and no card scheme fees. The PSR have themselves recorded that card scheme fees have “more than doubled over the period from 2014 to 2018, with most of this increase occurring between 2016 and 2018, after the IFR caps came into force” (PSR, 2020).
- 1.4 The cumulative cost to UK merchants of scheme fees increases since the introduction of the IFR reached £2.3 billion this year (CMSPI estimates, 2021) with an annual cost to UK merchants of successive scheme fees increases since IFR of £500 million per year. Evidence from annual BRC Payment Surveys shows that card scheme fees rose 39% in 2017 and 56% in 2018, measured as a percentage of retailers' turnover.
- 1.5 Following the UK's departure from the European Union, the impact on UK merchants of the latest Brexit-related increases announced since 1st January this year adds a further £60 million in costs which ultimately add to the price of goods and services paid by consumers. Average UK Merchant Service Charges, as a proportion of card turnover, are now higher in 2021 than 2014, prior to the IFR coming into effect.
- 1.6 Merchants providing services online must now also pay new Secure Customer Authentication (SCA)-related fees levied on e-commerce transactions, even if the transaction is declined.
- 1.7 As the PSR itself recognises within the Strategy document, “the bulk of (card) payments still rely on Visa or Mastercard. This is not, in itself, a problem if we think that competition between these firms is effective. Or if we think that new payment companies are able to enter the market and compete with them. But there is a risk that neither of these competitive forces are sufficiently strong to protect people and businesses. Indeed, at the moment, we do not see a likely way in which new entry – such as from a new crypto-based payment system – would address these risks in a timely manner. In which case, we face a long-term risk to competition in retail payments.”
- 1.8 The Strategy document appears to conflate these present day harms to consumers and businesses from the card payments system, for which action is overdue, as risks to be considered at some point in the future. These harms, as opposed to risks, are not only current but long-standing. The BRC first formally complained to the European Commission in 1992 that Visa and Mastercard



interchange fees unlawfully restrict competition and the annual BRC Payments Survey (formerly Costs of Collection Survey) began spotlighting excessive card costs in 1999.

- 1.9 Given this increasing dependency and increasing cost of card acceptance on top of already excessive charges, it has never been so important that the PSR take decisive action to protect consumers and businesses from the adverse impacts of failures in Europe's largest card market. Card fees are a key cost of doing business for all merchants, with the costs of these services ultimately reflected in consumer prices.

Interbank Payments System

- 1.10 The PSR Strategy appears to be entirely dependent on interbank payments to tackle current and future anticompetitive in the card payments system.
- 1.11 The previous PSR Strategy proposed significant changes for interbank payments with plans to create a New Payments Architecture (NPA) overseen by Pay.UK, and action to improve competition targeted at appropriate layers of its stratified model. Much has also been done by the Open Banking Implementation Entity (OBIE) in recent years to enhance functionality of open banking. The BRC has worked with the PSR, Pay.UK, OBIE and relevant providers to develop interbank payment propositions for UK retailers and customers.
- 1.12 Whilst there are high hopes for the future of open banking and the NPA, today interbank channels are negligible in retail payments. The Open Banking Implementation Entity (OBIE) has celebrated 1 million open banking transactions per month but even this milestone is a drop in the ocean against 20 billion retail industry transactions per year. The 2020 BRC Payments Survey showed that cards and cash account for 97.5% of sales, with much of the remaining 2.5% (1.3% by value) made up by solutions like PayPal that also have no relationship to the NPA.
- 1.13 The PSR Strategy document itself casts doubt on whether it is realistic or attainable for interbank payments to challenge the dominance of card-based transactions in retail payments. As the PSR admits on page 6, "the current commercial incentives do not align with the objective of making greater use of interbank to support competition over the longer term." And on page 26, "there is little evidence of significant substitution between debit cards and Faster Payments: this situation may change as take up of Open Banking-enabled services drives more transactions to Faster Payments." (3.12)
- 1.14 No criteria have been established in the Strategy for what would constitute a successful competitive outcome from interbank systems in retail payments and no time scale identified for its achievement. The Strategy simply offers that "this is not a straightforward task and will take some time to deliver."

Cash Payments System

- 1.15 In 2019, 23% of all transactions made in the UK were made using cash. The BRC shares the PSR view on the importance of cash for some groups of users and the need to protect their interest, and so we also share the PSR's concerns that "as cash use declines, it is likely to become more costly to maintain the current cash infrastructure." (3.49)
- 1.16 Almost all major bricks-and-mortar retailers accept both cash and card, but with the long-term trend of diminishing use, cash is likely to become less attractive and cost effective to the retail industry as cash handling costs are spread over a lower and lower volume of cash transactions.



- 1.17 Industry concerns have been raised as some retailers have reported finding it increasingly difficult to secure basic cash services – such as store collections, while the cost of these services levied by banks and other providers has begun to climb, even as the number of cash transactions have fallen. This, in turn, can leave merchants with more cash kept on the premises than covered by their insurers, and potentially puts staff at risk.
- 1.18 Retailers fear that the decline in the use of cash may lead to operators leaving the sector, narrowing the choice of cash processors and cash-in-transit (CIT) companies, and further increasing the cost of processing cash. Ultimately there are concerns for what these trends could mean for the UK's cash infrastructure, and competition in that sector.
- 1.19 Given the strategic importance of the national cash infrastructure and distribution network, the PSR should work with the Government and the FCA to consider what interventions must be taken to maintain operation of competitive commercial cash supply services across the UK, and to safeguard cash-dependent consumers. If falling cash volumes adversely impact the viability of cash operators, or if corporate strategies result in harmful outcomes for business and consumer end users, then subsidies may be required to maintain minimum service levels.
- 1.20 Action should also be considered to prevent banks, building societies and other payment firms from leaving the LINK network to address the risk to cash access identified by the PSR in 3.48 of the Strategy document, similar to recent FCA proposals to stop bank closures.
2. Do you think the key outcomes we want to focus on provide the right balance between promoting competition and innovation and doing so in a way that benefits all the businesses and consumers that make payments in the UK? Please explain why or why not.
- 2.1 We agree with the four outcomes that the PSR want to focus on:
- All users have access to payment services that meet their needs in terms of functions, quality, cost and other relevant factors
 - Users' interests are adequately protected when using payment systems so that they can use systems and services with confidence
 - Payment systems are designed and operated to enable effective competition in the provision of payment services
 - Payment systems are efficient and commercially sustainable
- 2.2 Unfortunately the rest of the Strategy document provides little or no assurance that the PSR will achieve these outcomes in a way that benefits all the businesses and consumers that make payments in the UK. In particular, there is an absence of specific, measurable and time-limited detail within the document that would make it difficult to assess the PSR's success in achieving these outcomes within the five-year time period covered.
- 2.3 On 29th July 2020, the PSR announced that its target outcome for its future Strategy was "effective competition at all levels of the supply chain... with detailed economic regulation acting where competition is not enough." The PSR identifies in the Strategy document that Visa and Mastercard account for 99% of all card transactions and that card payments are "...a highly concentrated market with limited opportunities to improve competition between the cards systems" (3.28), yet the Strategy lacks even a roadmap to deliver the promised detailed economic regulation.



- 2.4 There are numerous providers of card-acquiring and value-added merchant services in the UK, where enhanced competition could play a major role in driving better outcomes for merchant end users and, in turn, consumer welfare. Other layers of the card payments system lack effective competition, or even the market forces to drive down costs, where a different approach must be taken.
 - 2.5 Perverse incentives continue in the card-issuing level of the supply chain as card schemes use kickbacks to win over card-issuing banks, creating a similar impact on the costs borne by end users as regulated fees in contravention of the IFR – for which the PSR is responsible for enforcing.
 - 2.6 At the network level of the supply chain, the card schemes levy hundreds of fees on transactions across countless variables making it impossible for even the largest merchant to accurately forecast card costs, and consumers ultimately pay the bill in the form of higher prices. Complex billing structures have further become a powerful tool to bamboozle political, regulatory or legal attempts to rein in increasing abuses of the schemes' dominant market positions, which has seen scheme fees billed to merchants double since implementation of the IFR. The evident lack of competition among cards schemes – or even a market mechanism to exert a downward pressure of costs – demands a measure of public intervention as exists for telecoms, energy, and water services to correct the failure in the market.
3. Do our strategic priorities provide the coverage, focus and flexibility we need to achieve the outcomes we want to focus on over the next five years? Please explain why or why not.
- 3.1 We do not consider that as they currently stand the strategic priorities provide the needed levels of coverage, focus and flexibility. In 2020, more than 80% of all retail sales in the UK were made using a debit or credit card. There is a conspicuous absence of any meaningful commitment to addressing current harms within the card payments system in spite of the substantial and increasing evidence of anti-competitive behaviour, including that which the PSR has itself gathered in the process of its Market Review on the supply of card acquiring services. This Strategy therefore sets up the PSR to fail to achieve half of its outcomes:
 - All users have access to payment services that meet their needs in terms of functions, quality, cost and other relevant factors
 - Payment systems are operated to enable effective competition in the provision of payment services
 - 3.2 The PSR's Market Review on the supply of card acquiring services marks the continuation of 30 years of UK and EU regulatory and competition law investigation into payment cards, first raised in BRC complaints to the EU in 1992. The retail industry welcomes some of the individual remedies set out in the interim report however the package of remedies does not go far enough to tackle the problems identified in the PSR's own findings. Indeed, the alarming increases in scheme fees – which are captured only in part by the Interim Report, given the limited window of data collection – are not addressed in the PSR remedies whatsoever.
 - 3.3 The BRC fully anticipates that – absent regulatory action – scheme fees will continue to rise rapidly. This expectation is based on combination of Mastercard and Visa statements (chiefly aimed to their shareholders), and on evidence of Mastercard and Visa scheme fees in other markets, especially the US. We therefore do not consider that the PSR's proposed measures, which focus exclusively on card acquirers and hopes for distant competition from interbank



payments, will have any material impact on the concerns that merchants have consistently raised and which the PSR Market Review Interim Report now confirms.

- 3.4 The BRC has proposed several additional remedies to complement the PSR's own remedies. Primarily, this involves reform of the IFR – as it now applies in the UK (the “UK IFR”) – to ensure effective regulation of all wholesale payment card fees (interchange fees and scheme fees). We also proposed a “portable accreditation” scheme for merchants to support ease of switching.
- 3.5 In particular, two chief reforms of the UK IFR are now needed and as part of its future Strategy the PSR should now use its existing powers to:
- **Abolish Interchange Fees:** This would bring regulation into line with the decisions of UK courts, in particular the 2020 Supreme Court judgment that Mastercard and Visa interchange fees are unlawful.
 - **Regulate Scheme Fees:** Bringing scheme fees within scope of the UK IFR. The level of scheme fees must be subject to “utility-style” economic regulation. This is what the PSR was set up to do.
- 3.6 The BRC considers that abolition interchange fees and bringing scheme fees within scope of the UK IFR are fully within scope of the PSR's powers (and duties), without need for new legislation. This reflects that the PSR was primarily established as a “utility-style” economic regulator, namely, with powers and duties to regulate wholesale access prices to payment systems, such as interchange fees and scheme fees, in a similar way as the other main UK economic regulators, namely, Ofcom (electronic communications), Ofgem (energy), and Ofwat (water and sewerage services).
- 3.7 Additionally, we call on the PSR to refer the supply of services provided by card scheme operators to the Competition and Markets Authority (“the CMA”) for market investigation under the Enterprise Act 2002 – given the clear evidence in the Interim Report of features of the market that adversely impact competition – an option that the PSR outlined in its Terms of Reference for the current Market Review.
4. [Do these strategic priorities provide clarity on the choices we make, and especially on why and when we choose to intervene? Please explain why or why not.](#)
- 4.1 No. For the forthcoming five years the PSR proposes merely to “consider the need... to regulate in order to protect consumers and businesses if other measures are not producing the competition outcome we seek”, however no measurable competition outcome has been defined and no time frame established within which to achieve it. There is, therefore, no anti-competitive threshold, milestone or deadline identified by the PSR for when it would be required to “intervene robustly” in the card payments system to deliver against its statutory objectives.
- 4.2 On 29th July 2020, the PSR announced that its target outcome for its future Strategy was “effective competition at all levels of the supply chain... with detailed economic regulation acting where competition is not enough.” The PSR identifies in the Strategy document that Visa and Mastercard account for 99% of all card transactions and that card payments are “...a highly concentrated market with limited opportunities to improve competition between the cards systems” (3.28), yet the Strategy lacks even a roadmap to deliver the promised detailed economic regulation.



5. Do you think the measures we propose will help us to assess whether we are achieving our strategic priorities? Please explain why or why not.
- 5.1 No. As outlined above, the proposed PSR Strategy lacks essential details required for the PSR to hold itself to account, or for others to do so. In general, there is an absence of specific, measurable and time-limited objectives within the document that would make it difficult to assess the PSR's success in achieving good outcomes for end-users of the UK's payments systems within the five-year time period covered.
- 5.2 The Strategy says the PSR will “consider the need... to regulate in order to protect consumers and businesses if other measures are not producing the competition outcome we seek”, however no measurable competition outcome has been defined and no time frame established within which to achieve it. There is, therefore, no anti-competitive threshold, milestone or deadline identified by the PSR for when it would be required to “intervene robustly” in the card payments system to deliver against its statutory objectives.
- 5.3 The only measure that the PSR is proposing in order to tackle anti-competitive behaviour within the card payments system is the development of an altogether different system for interbank payments. Yet no criteria have been established in the Strategy for what would constitute a successful competitive outcome from interbank systems in retail payments and no time scale identified for its achievement. The Strategy simply offers that “this is not a straightforward task and will take some time to deliver.”
- 5.4 In fact, the Strategy document includes many phrases that obfuscate the need for the PSR action or measure its success:
- “the impact of our work may be indirect and difficult to measure”
 - “it may sometimes be difficult to interpret what the data we collect is telling us”
 - “we do not have all the data and information we would like... we will develop our ability to measure over the coming years”
- 5.5 Even where a measure has been identified the Strategy does not commit the PSR to taking action at any given threshold: “we think that market shares or at least shares of supply, could provide a useful and straightforward measure of how the structure of payments markets is changing over time and, if switching occurs, where payments transactions are migrating to and from.” (6.20) However the document goes on to say that “trends in market shares are unlikely to be sufficient, in themselves, to reach a firm view on whether actions to promote competition are having the effects we anticipate.” (6.23)

6. What other criteria do you think are central to measuring our effectiveness and should those complement or replace those we propose in this document?

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7. Do you know any existing sources of data we can use to assist our metrics?

- 6.1 As payment systems designated to the PSR, the Regulator should be notified when Visa and Mastercard make changes to their fees and track the full range of fees that the card schemes levy across all forms of payment cards and card-based transactions.
- 6.2 It should be a mandatory requirement for all schemes to brief the PSR prior to announcing any changes in fees, rates, etc. to enable the PSR to investigate the validity and competitiveness of these



changes for both consumers and merchants. This should also include changes in commissions and charges to acquirers and issuers.

For further information

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