

Anticipated acquisition by Mastercard UK Holdco Limited of VocaLink Holdings Limited

Decision on acceptance of undertakings in lieu of reference

ME/6638/16

The CMA's decision to accept undertakings in lieu of reference under section 73(2) of the Enterprise Act 2002 given on 11 April 2017. Full text of the decision published on 21 April 2017.

Please note that [X] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.

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Introduction

1. Mastercard International Incorporated (**Mastercard**) through its subsidiary Mastercard UK Holdco Limited has agreed to acquire VocaLink Holdings Limited (**VocaLink**) (the **Merger**). Mastercard and VocaLink are together referred to as the **Parties**.
2. On 4 January 2017, the Competition and Markets Authority (**CMA**) decided under section 33(1) of the Enterprise Act 2002 (the **Act**) that it is or may be the case that the Merger consists of arrangements that are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation, and that this may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom (the **SLC Decision**).
3. As set out in the SLC Decision, the CMA found a realistic prospect of a substantial lessening of competition in relation to the supply of central infrastructure services (**CIS**) to the LINK ATM network (**LINK**). The CMA based its decision on evidence demonstrating the real risk that if the Merger went ahead there would be a reduction in the already limited number of suppliers of CIS from which LINK would be able to obtain credible bids given the capability and cost advantages that VocaLink and, to a lesser extent, Mastercard and Visa have over other possible bidders (the **SLC**). The SLC Decision described a number of capability and cost disadvantages that other potential suppliers of CIS face, including:
 - (a) the lack of network connectivity to LINK members, which limits other potential suppliers from being able to offer competitive bids;¹
 - (b) the cost associated with the licensing of the LIS5 messaging standard, and the parallel running costs during the migration period;² and
 - (c) the higher level of cost to LINK members of changing to a CIS provider (other than VocaLink, Mastercard or Visa) as a result of requirements such as physical changes required, project costs (staff and governance processes, external consultants), and testing costs to connect to the New Processor.³
4. As a result of the Merger, Mastercard will no longer act as a competitive constraint on VocaLink. The SLC therefore relates to the loss of competition associated with any potential advantages that Mastercard would have had

¹ SLC Decision, paragraph 170.

² SLC Decision, paragraph 160.

³ SLC Decision, paragraphs 161 and 164.

over other potential bidders, rather than any advantage VocaLink may have over any other bidder (including Mastercard and/or Visa).

5. The CMA concluded that, in the absence of effective remedies, the Merger would result in a reduction from three to two in the number of credible bidders for the supply of CIS to LINK.⁴
6. The effect of this reduction in credible bidders would be that, since VocaLink is the incumbent provider, the Merger may result in the loss of the substantial competitive constraint from Mastercard acting as an alternative bidder.⁵
7. On 11 January 2017, the Parties offered undertakings in lieu of reference to the CMA for the purposes of section 73(2) of the Act. The CMA gave notice to the Parties on 18 January 2017, pursuant to section 73A(2)(b) of the Act, that it considered that there were reasonable grounds for believing that the undertakings offered, or a modified version of them, might be accepted by the CMA under section 73(2) of the Act and that it was considering Mastercard's offer (the **UILs Provisional Acceptance Decision**).
8. On 24 February 2017, the CMA issued a notice of consultation on the proposed undertakings (the **Notice of Consultation**). The Notice of Consultation stated that the CMA would have regard to any representations received, and the Parties may need to make modifications to the undertakings as a result of those representations.
9. On 13 March 2017, the CMA extended the time available to reach a decision on whether to accept the undertakings offered by the Parties under section 73A(4) of the Act, resulting in a statutory deadline to reach this decision by 15 May 2017 (the **Notice of Extension**).
10. The text of the SLC Decision, the UILs Provisional Acceptance Decision, the Notice of Consultation, and the Notice of Extension are available on the CMA website.⁶

⁴ SLC Decision, paragraph 171.

⁵ The CMA examines the effect of a merger against a relevant counterfactual which considers what would have happened absent the proposed merger. In the SLC Decision, paragraph 55 states that: *'the relevant counterfactual in this case is one in which VocaLink is acquired by an alternative purchaser which does not raise substantial competition concerns'*.

⁶ See <https://www.gov.uk/cma-cases/mastercard-vocalink-merger-inquiry>.

The undertakings offered

11. As set out above, on 11 January 2017 the Parties offered undertakings to remedy, mitigate or prevent the SLC or any adverse effect which has or may have resulted from it or may be expected to result from it.
12. Those undertakings were subsequently modified slightly, particularly to take account of the responses received to the consultation process (see paragraphs 39-89 below). The final signed version of the undertakings was submitted to the CMA on 6 April 2017 (the **UILs**). The full text of the UILs has been published separately on the case page of the CMA's website.⁷
13. The UILs are a package of measures which in combination remedy the SLC by providing other potential bidders an equivalent level of advantage to that enjoyed by Mastercard, and therefore restore the level of competitive constraint which Mastercard would have exercised on VocaLink absent the transaction.
14. The UILs offer a package of three measures, consisting of:
 - (a) the Network Access Remedy;
 - (b) the LIS5 Remedy; and
 - (c) the Switching Fund Remedy.
15. Each of these are described and discussed in more detail below.
16. The UILs are primarily implemented through (i) a framework agreement entered into by the Parties and LINK Scheme Limited (**LSL**)⁸ on behalf of the LINK scheme and its members (the **Framework Agreement**), and (ii) consequential amendments to the existing processing contract between LINK and VocaLink (ie the Switching and Settlement Agreement). Both documents were approved by LINK's users (the Network Members' Council) on 28 February 2017 with a very large majority ([~~9~~]).

Network Access Remedy

17. Under the UILs, VocaLink is required to give any future new supplier of CIS to LINK (a **New Processor**) access to VocaLink's communications infrastructure, including connectivity with all LINK members.⁹ The Network

⁷ See <https://www.gov.uk/cma-cases/mastercard-vocalink-merger-inquiry>.

⁸ LSL is the operator of the LINK system as set out in the Financial Services (Banking Reform) Act 2013.

⁹ The VocaLink communication infrastructure provides connectivity between the VocaLink ATM switch and the LINK members' points of access.

Access Remedy will, therefore, allow a New Processor the option of using the VocaLink connectivity to the LINK members for a limited period of time rather than having to build their own connectivity immediately.

18. VocaLink will, in effect, act as a subcontractor to the New Processor, providing sufficient capacity at equivalent service levels to those it currently receives from its external communications provider (ie VocaLink's telecoms provider).¹⁰ As part of this remedy, VocaLink will be required to provide monthly reporting on both the service level agreements and key performance indicators to the New Processor. VocaLink is also required to provide network monitoring and management services, and to implement any change requests from the New Processor in a reasonable time.
19. In the event of a New Processor being awarded the LINK contract, there would be a migration period during which two CIS suppliers would be processing LINK ATM transactions. The UILs require VocaLink to reduce or waive the minimum contractual financial commitments¹¹ under its contract with LSL for a transition period of between 6 and 12 months¹² immediately preceding the date on which VocaLink ceases to provide services, which will reduce the costs to LSL of running two CIS suppliers in parallel.
20. Under the UILs, VocaLink will strengthen its existing contractual obligations with LSL about restricting the flow of LINK information, which will ensure confidentiality of any information that could give the Parties a competitive advantage as a result of using the Network Access Remedy. This includes restricting access to network-level LINK information to a list of named VocaLink personnel who can only use this data for the purposes of providing the network access services.
21. As part of the Network Access Remedy, VocaLink will charge the New Processor the following costs in return for providing the network access services:¹³

(a) **External communication provider costs:** the costs incurred in providing the network from the external communications provider, including both

¹⁰ This will be implemented through 'back-to-back' (ie at the same levels as the external communication provider) service level agreements and key performance indicators.

¹¹ This clause in the existing contract between LINK and VocaLink requires LINK members to continue to pay a pre-defined minimum fee to VocaLink, even if LINK transaction volumes fall to the extent which would otherwise have resulted in the fees being below this level.

¹² The UILs specify this period as being a 100% reduction for 6 months, and a 25% reduction for an additional 6 months if LSL gives notice to terminate the S&S Agreement after the end of the fourth year of the term of the S&S Agreement. In addition, the CMA may require the fee reduction for these additional 6 months being increased to 100%, if the CMA (having due regard to the views of VocaLink, LSL and the New Processor) considers it necessary.

¹³ The use of circuits in this cost allocation methodology reflects VocaLink's existing internal accounting approach.

direct costs and an allocation of common costs (eg any management fees). This is calculated based on the directly identifiable cost of any circuits¹⁴ exclusively used for LINK transactions, and an equal share of costs for any circuits which are used by LINK and other payment services (eg 50% of a circuit which is used by both LINK and the Faster Payments System). Any relevant common costs will be allocated on the same basis;

- (b) **VocaLink monitoring and maintenance costs:** direct, reasonable, and substantiated costs in return for VocaLink providing the monitoring and maintaining of the network (capped at a maximum of 10% of the external communication provider costs described above). This is calculated based on the internal costings of the VocaLink connectivity support team, again apportioned between payment systems based on circuit count; and
- (c) **Change costs:** costs associated with connecting the New Processor initially,¹⁵ implementing change requests, and refreshing/upgrading the network when needed. A portion of these would be allocated to the New Processor using the same principles as above for the external communication provider costs (described in paragraph 21(a)).

- 22. The details of the costs to be incurred by the New Processor and of the cost allocation methodology are set out in the Framework Agreement. This information will be available to any potential bidder ahead of the next tender processes.
- 23. Based on 2015 and 2016 figures, the Parties' estimates of the equivalent total ongoing cost to the New Processor of using the Network Access Remedy would have been in the region of [£750k-£1.25m] per annum, with additional change costs of roughly [£100k-£150k] per annum.¹⁶
- 24. For disputes about the level of, or need for, any of these costs, an independent arbiter will be in place to provide a determination.
- 25. The Network Access Remedy will terminate on the earliest of:
 - (a) the start of the first tender cycle, if a New Processor wins the first LINK contract and chooses not to use the Network Access Remedy;

¹⁴ "Circuits" refers to the external communication provider's managed network connections between VocaLink and the LINK scheme members.

¹⁵ The costs of connecting would effectively be borne by the New Processor, as these would have no overlap with other payment systems.

¹⁶ Based on an average of Parties' estimations of the change costs allocation under this approach (including both change projects, and refreshes/upgrades) over the past 3 years.

- (b) the start of the second tender cycle, if a New Processor wins the second LINK contract and chooses not to use the Network Access Remedy, or if VocaLink wins the second LINK contract;
 - (c) the end of the second tender cycle;
 - (d) the date on which the New Processor notifies VocaLink that it no longer requires the Network Access Remedy;
 - (e) 15 years from the start of the first tender cycle; or
 - (f) 20 years from the date at which the CMA accepts the UILs.
26. The UILs also provide for a CMA review of the ongoing necessity of the Network Access Remedy, no later than two years prior to the expected end of the first tender cycle. In its review, the CMA will seek advice from the Payment Systems Regulator (**PSR**) as appropriate.

LIS5 Remedy

27. The LINK ATM scheme currently operates using a messaging standard named LIS5 (the **LIS5 Standard**). This provides a standard format for all transactions taking place on the system, and is integrated with LINK members' existing internal IT systems.
28. Currently, VocaLink owns the LIS5 Standard, and LINK is contractually entitled to sublicense it to any potential competitor of VocaLink. However, under the existing contract between LINK and VocaLink, the New Processor would have to pay VocaLink for this sublicense.
29. Under the UILs, VocaLink is required to transfer the intellectual property rights related to the messaging standard used for all transactions within the LINK scheme (the **LINK LIS5 Standard**) to LSL. The transfer will not include the messaging standard VocaLink uses for non-LINK scheme transactions such as mobile phone top-up (the **VocaLink LIS5 Standard**).
30. The LINK LIS5 transfer will be implemented in the form of a free, unconditional transfer of all relevant intellectual property rights for the LINK LIS5 Standard from VocaLink to LSL. LSL will then be free to develop, use, sublicense and exploit the LINK LIS5 Standard as it wishes within its ATM business, and will be free to specify the use of LINK LIS5 Standard as a condition of any subsequent retendering of the processing contract.
31. This approach will result in an effective split of the existing messaging standard into one which is controlled by LSL (ie the LINK LIS5 Standard), and one which is controlled by VocaLink (ie the VocaLink LIS5 Standard),

although some common parts will be overlapping and therefore used by both LSL and VocaLink.

Switching Fund Remedy

32. Under the UILs, Mastercard is required to commit up to £5 million (inflation-linked)¹⁷ for the purposes of contributing to the network connectivity costs that may be incurred by LINK members associated with a change in CIS provider.
33. The Switching Fund Remedy will allow LINK members to seek a contribution to any increased network connectivity costs which they incur as a result of LSL awarding the LINK CIS contract to a New Processor. Under the UILs, the level of funds available to each individual member will be capped based on the minimum core switching and settlement fee in the VocaLink contract,¹⁸ or as may be requested by LSL and approved by the Monitoring Trustee.
34. In order to access their allocated contribution (or a share of it), the LINK member will need to demonstrate to the Monitoring Trustee that the costs were incurred as a direct result of transitioning to a New Processor (or New Processor's replacement network), and cannot be recovered from another third party.
35. The Switching Fund Remedy will have the same duration as the Network Access Remedy, subject to the availability of total funds and the allocation process described above.

Implementation provisions

36. The UILs will require the implementation of the Network Access Remedy through a direct agreement (ie between LSL and the New Processor, and an equivalent agreement between LSL and VocaLink) unless LSL opts for a tripartite agreement (ie between LSL, the New Processor, and VocaLink) instead.
37. There are certain technical and operational aspects concerning the LIS5 Remedy and the Network Access Remedy which will be implemented within a specific timeline after the CMA's acceptance of the UILs. These include:
 - (a) Within 6 months, the LINK LIS5 Standard will be transferred to LSL;

¹⁷ Indexed to the Consumer Price Index.

¹⁸ This represents the share of the LINK contractual costs that each member is obliged to pay if minimum volume thresholds are not met.

- (b) Within 6 months, VocaLink will develop the technical and operational arrangements for the Network Access Remedy (to be revised annually), and will agree these with LSL within a further 30 days. This will include details such as the approaches to connect a New Provider's ATM switch into VocaLink's network, and defining connectivity testing;
 - (c) Within 6 months, VocaLink will (at its own cost) develop a detailed implementation plan to enable the separation of LINK scheme and non-LINK scheme transactions into two separate destinations over the VocaLink network, and will agree this plan with LSL within a further 30 days; and
 - (d) 60 days prior to LINK issuing a tender, VocaLink will provide a network access agreement form for LINK to include in its tender, which will include binding provisions for the Network Access Remedy for consideration by potential bidders.
- 38. In addition, the UILs include provisions for the appointment of an independent person, who will carry out the following functions:
 - (a) Act as a Monitoring Trustee to ensure that the Parties are compliant with their obligations under the UILs. This includes investigating any aspects it deems necessary, and providing regular compliance reports to the CMA and the PSR, as well as implementing any instructions or directions the CMA (advised by the PSR as appropriate) may give; and
 - (b) Act as an independent arbiter for disputes associated with issues such as the level of costs which can be charged to the New Provider, performance issues (eg breaches of the key performance indicators or service level agreements), any delays in the implementation process, as well as claims for payments from the Switching Fund Remedy.

Consultation

- 39. On 24 February 2017, pursuant to paragraph 2(1) of Schedule 10 to the Act, the CMA published a Notice of Consultation on the undertakings as offered by the Parties at the time (the **Proposed Undertakings**), inviting interested parties to give their views on the Proposed Undertakings (the **Public Consultation**). The relevant consultation documents are available on the case page of the CMA's website.¹⁹

¹⁹ <https://www.gov.uk/cma-cases/mastercard-vocalink-merger-inquiry>

40. Prior to the Public Consultation, the CMA contacted a number of stakeholders which had previously engaged with the process in order to obtain some preliminary views on the Proposed Undertakings. The aim of this exercise was to identify at an early stage any potential concerns on the suitability of the Proposed Undertakings and to improve their design.
41. In response to these pre-consultation contacts, the CMA received responses from 15 stakeholders. Some of the points raised during the pre-consultation period were addressed prior to the Public Consultation.²⁰
42. For the reasons set out in the Notice of Consultation,²¹ the CMA's preliminary view was that the Proposed Undertakings would address the SLC without giving rise to material doubts about the overall effectiveness of the Proposed Undertakings or concerns about their implementation.²² During the Public Consultation, the CMA particularly invited comments on the following aspects of the Proposed Undertakings, on which it had received submissions during the pre-consultation questions, and believed might have raised concerns regarding the effectiveness of the UILs:
 - (a) the appropriateness of the cost allocation approach;²³
 - (b) the proposed duration of the migration period;²⁴ and
 - (c) the proposed duration of the Proposed Undertakings.²⁵
43. In response to the Public Consultation, the CMA received submissions from 14 stakeholders. This included responses from a number of LINK members, potential competitors, and other interested parties.
44. The majority of respondents to both the Public Consultation and the pre-consultation questions (in particular, the LINK members) were broadly supportive of the UILs. Additionally, some of those which stated that they were broadly supportive raised specific points on the UILs which they believed could be improved. Of the 22 total respondents, a small number ([REDACTED]) stated that they did not consider that the UILs would address the SLC.²⁶

²⁰ For example, [REDACTED] point resulting in the duration of the transition period discussed in paragraph 19 being extended to up to 12 months.

²¹ Notice of Consultation, paragraphs 62-63.

²² In line with the CMA's guidance: *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance (OFT1122)*, December 2010, Chapter 5 (in particular paragraphs 5.7–5.8 and 5.11). This guidance was adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure (CMA2)*, January 2014, Annex D).

²³ See para 34 of the Notice of Consultation.

²⁴ See para 36 of the Notice of Consultation.

²⁵ See para 45 et seq. of the Notice of Consultation.

²⁶ [REDACTED].

45. The CMA liaised with the PSR throughout the UILs assessment process and the PSR submitted that it was supportive of the UILs.
46. LSL, the customer which could potentially be directly affected by any loss of competition, has also stated its support of the UILs.
47. The approach taken by the CMA to address the main comments received during its contacts with stakeholders is discussed below.

Network Access Remedy

48. A number of respondents raised points regarding the cost allocation mechanism in the Network Access Remedy, and commented on the need for both accuracy and transparency in its application.²⁷ Many of these points were made prior to the Public Consultation, and so relied on the partial information available at that time. Following the Public Consultation, one respondent re-emphasised the importance of ensuring that the allocation was accurate, and noted that the CMA should ensure it captures all relevant costs in order to minimise the risks of distortion.²⁸ No specific points were raised about inaccuracies in the proposed cost allocation methodology, or possible improvements.
49. The CMA agrees that both transparency and accuracy are important in ensuring the overall effectiveness of the Network Access Remedy while minimising the risk of distortions. This is discussed in more detail in paragraphs 106-108 below. The cost allocation methodology ensures that the operational costs of the New Processor reflect VocaLink's own operational costs, and are based on objective parameters. Therefore the allocated costs will be difficult to manipulate, either to be too low, and risk future underinvestment in the network; or to be too high, and circumvent the objective of the Network Access Remedy to address any potential advantages that Mastercard would have had over other bidders.
50. Two respondents referenced paragraph 167 of the SLC Decision regarding LINK's views on VocaLink's 'alternative scenario' (in which VocaLink would make its communication infrastructure available to the new provider).²⁹ This

²⁷ [REDACTED].

²⁸ [REDACTED].

²⁹ [REDACTED]; the alternative scenario is described in paragraph 165 of the SLC Decision: *'In the Study, VocaLink also estimates the costs for a scenario in which VocaLink would make its communication infrastructure available to the new provider. In this scenario, the cost of implementation would be lower, but the costs of migration to members would broadly remain the same. The costs were estimated to be c£[REDACTED] for certification and c£[REDACTED] for the members to implement (again based on 40 Members). VocaLink would not retain its role as a central infrastructure provider but would provide managed communication services to the new processor, ie monitor, maintain and upgrade the network.'*

included the statement that *'[LINK] had not considered the scenario put forward by VocaLink to be practicable or viable'*.

51. As discussed in paragraph 168 of the SLC Decision, the CMA had insufficient evidence to consider that the alternative scenario described by VocaLink was sufficiently certain to be implemented in a timely manner and to reduce the costs involved with a new alternative provider.³⁰ In contrast, the UILs are binding on the Parties, include specified timelines for implementation, and include other provisions to reduce costs beyond the Network Access Remedy alone. This means the CMA can be confident that the UILs will be implemented in a timely manner. As mentioned above, LSL and the majority of responding LINK members also supported this approach in the UILs.
52. One respondent noted that any transition involving the Network Access Remedy would need to be well managed to ensure that it was a viable alternative to building a separate network.³¹
53. The CMA considers that orderly transition arrangements will be guaranteed through the design of the relevant processing contracts, and is aware of provisions designed to have this effect in the existing LINK contract (ie the Switching and Settlement Agreement). In addition, the UILs now include a clause whereby the Parties have committed to co-operate with the New Processor in support of the Network Access Remedy.
54. A number of respondents raised concerns regarding the length of the migration period during which VocaLink would waive its minimum transaction volume charges (discussed in paragraph 19).³² Originally, this was proposed to be for 6 months. Following responses received during the pre-consultation period, this was extended to 6-12 months. One respondent to the Public Consultation stated that this was insufficient and should be extended to 12-18 months, based on the respondent's internal expertise.³³
55. Furthermore, one respondent stated that the waiver of this minimum transaction volume charge should be independent of the use of the Network Access Remedy.³⁴

³⁰ SLC Decision, paragraph 168: *'The CMA, therefore, considers that it has not been provided with sufficient evidence to consider the alternative scenario considered by VocaLink as sufficiently certain to be timely implemented and to reduce the costs involved with a new alternative provider. As such, the implementation of the scenario put forward by VocaLink is merely hypothetical as no agreement with LINK has been reached and LINK voiced concerns with regard to its feasibility. In addition, the CMA considers that the success of this proposal depends on the willingness of alternative providers to supply a solution that is compatible with VocaLink's current infrastructure set up.'*

³¹ [REDACTED].

³² [REDACTED].

³³ [REDACTED].

³⁴ [REDACTED].

56. The CMA's views on the appropriate duration for this migration period are discussed in more detail in paragraphs 109-110 below.
57. Regarding the independence of the waiver from the Network Access Remedy, the CMA notes that the UILs already include this provision,³⁵ and so no changes are necessary to address this point.

LIS5 Remedy

58. Respondents raised no substantive concerns with the LIS5 Remedy. Indeed, some respondents emphasised the importance of this aspect of the UILs in the overall effectiveness of the remedy package and supported the approach taken in the Proposed Undertakings of ensuring that the LIS5 messaging standard would be available to a New Processor without a licence cost.³⁶

Switching Fund Remedy

Value of the Switching Fund Remedy

59. A number of respondents questioned whether the value of the Switching Fund Remedy (ie £5 million) was sufficient to address fully the SLC. A few respondents specifically stated that they believed the value to be sufficient.³⁷ A larger number of respondents raised concerns that £5 million was insufficient,³⁸ with some of these stating that the average figure of approximately £130,000 per LINK member appeared insufficient.³⁹
60. Only one of the respondents who raised concerns regarding the value of the Switching Fund Remedy proposed an alternative figure. This respondent [REDACTED] proposed that £10 million would be a more appropriate figure. This was on the basis that the necessary changes would go beyond costs associated directly with the connectivity itself, and the £5 million proposed would not include cover these non-technical costs of changes.⁴⁰
61. The respondent's £10 million estimate as an alternative figure was based on [REDACTED].⁴¹

³⁵ Apparent in paragraph 2.1(a)(xiv) of the UILs. The Parties have confirmed this.

³⁶ [REDACTED].

³⁷ [REDACTED].

³⁸ [REDACTED].

³⁹ [REDACTED].

⁴⁰ [REDACTED]; for example, changes to settlement process, internal process documents, reporting processes, LSL documents, and legal costs.

⁴¹ [REDACTED].

62. Two respondents to the Public Consultation also stated that LINK members would be likely to incur other internal costs not simply related to connectivity, such as other IT costs.⁴²
63. The CMA believes that, given the difficulties that LINK members have had in estimating the relevant costs, [redacted]. The CMA therefore put particular weight on this respondent's submission regarding other costs of change. However, upon further discussion, the respondent stated that the additional costs it highlighted would be incurred *'irrespective of who the tender were awarded to'*.⁴³ Therefore, the CMA considers that these costs do not arise as a result of the Merger, and so it would not be appropriate to include them in the value of the Switching Fund Remedy.
64. In addition, as explained [redacted], the Parties' own estimates included a [redacted] which resulted in a total of £5 million. [redacted]. Therefore, [redacted] could be seen as being consistent with the Parties, and supportive of a £5 million Switching Fund Remedy.
65. [redacted] provided cost estimates indicating that the £5 million included in the UILs was sufficient, and raised no concerns about this value in their responses.⁴⁴
66. A small number of respondents to the Public Consultation compared the £5 million fund with other figures stated in paragraph 162 of the SLC Decision.⁴⁵
67. The figures included in paragraph 162 of the SLC Decision reflect a scenario absent the UILs. As explained in paragraph 105 below, the UILs include a Network Access Remedy and LIS5 Remedy, both of which would reduce the cost of switching CIS provider. Therefore, the appropriate figure for the Switching Fund Remedy would differ from the cost estimates included in the SLC Decision, due to both, the inclusion of other UIL components which would substantially lower the LINK members' cost of changing CIS provider,⁴⁶ and the fact that only a proportion of these changing costs relate to the

⁴² [redacted] state "internal costs" and referenced quotes about "cost of changing their internal IT systems".

⁴³ [redacted].

⁴⁴ [redacted].

⁴⁵ [redacted]. SLC Decision, paragraph 162: *'LINK members stated that it was difficult to estimate the exact cost of switching at this stage without the details of the new infrastructure provider's requirements. Even so, estimated switching costs vary significantly between LINK's members, ranging from [£200,000-£50 million] in total. These costs would depend on the size of the LINK member and whether the new tender would be a 'like-for-like' with the current system or significantly different. The costs would also depend on whether or not the messaging standard were to remain the same, ie whether or not LIS5 were used. Given that continued use of LIS5 would require the new provider to sub-license the standard from VocaLink the CMA believes that the messaging standard is an important factor that increases the costs for a new provider.'*

⁴⁶ *'These costs would depend on [...] whether the new tender would be a 'like-for-like' with the current system or significantly different. The costs would also depend on whether or not the messaging standard were to remain the same, ie whether or not LIS5 were used.'* SLC Decision, paragraph 162.

Merger.⁴⁷ The CMA has therefore assessed the appropriate value of the Switching Fund Remedy directly, as described in paragraphs 113 to 117 below.

68. Two respondents⁴⁸ highlighted extracts from documents produced during the PSR's market review into the ownership and competitiveness of infrastructure provisions which were related to the difficulty and costs associated with changing infrastructure provider.⁴⁹ This included quoting a figure of up to £15 million (each) as the cost of changing provider estimated by some PSPs.⁵⁰ These same respondents also drew comparisons with previous initiatives undertaken in the payments systems sector (namely the introduction of cheque imaging and the creation of FPS), and noted that the anticipated costs and difficulties had been substantially underestimated by participants compared with the final outcome.
69. Regarding the extracts of the PSR's report invoked by two parties, the CMA believes that the comments regarding difficulties associated with changing payment systems provider:
- (a) were being made with respect to any potential change in CIS provider, and so do not arise as a result of the Merger;
 - (b) do not take account of the UILs themselves, which the CMA believes would reduce the difficulty associated with switching;
 - (c) are not specific to LINK's CIS provider, but are made in respect of payment systems in general; and
 - (d) do not take into account that, to the extent that any of these difficulties exist, the PSR is undertaking its own remedies process to address its concerns.
70. Therefore, the CMA believes that these comments are not a good indication of the appropriate value of the Switching Fund Remedy.
71. Regarding the comparison with other initiatives undertaken in the payment systems sector invoked by two parties, the CMA believes that the level of cost associated with these is reflective of much more significant changes than would be present in the UILs. In particular, the initiatives involve substantial changes to both the necessary connectivity and the internal IT systems of

⁴⁷ *'If Mastercard were to be a bidder absent the Merger, then there would be some additional costs, however they would be lower than those arising from the award of the contract to an alternative provider'*, SLC Decision, paragraph 164.

⁴⁸ [redacted].

⁴⁹ Including the PSR's interim report, the PSR's final report, and some stakeholder responses.

⁵⁰ PSR interim report, paragraph 4.131.

PSPs, both of which are minimised in the UILs (through the use of the Network Access Remedy and LIS5 Remedy). In addition, any degree of cost over-run is not relevant to the CMA's assessment, as it is the perceived costs at the point of tender which would impact the competitive environment of the bidding processes, rather than any subsequently incurred costs.

Other aspects of the Switching Fund Remedy

72. One respondent stated that there was no rationale for capping the indexation applied to the Switching Fund Remedy (as was included in the Proposed Undertakings), and so believed that this limit should be removed.⁵¹
73. Given that the use of the funds is likely to be a number of years in the future, the CMA believes that the inclusion of a mechanism to take account of inflation was a prudent measure. The CMA agrees that the inclusion of a cap on the level of increase could result in an effective decrease in the value of the Switching Fund Remedy in the future, which could risk reducing the effectiveness of the undertakings. Accordingly, the previously proposed cap on indexation has been removed in the UILs.
74. One respondent questioned whether the process for the separation of LINK and non-LINK transactions described in paragraph 37(c) would reside with VocaLink or with LINK members, and was concerned that any development work could result in significant costs to the LINK members.⁵²
75. The UILs state that VocaLink would bear the costs for the design and development work necessary for this process,⁵³ resulting in no additional costs to LINK members.⁵⁴
76. One respondent stated that it should be clarified that certified service bureaus⁵⁵ would be eligible for receiving a cost contribution from the Switching Fund Remedy.⁵⁶
77. The CMA believes that any additional costs that LINK members who rely on certified service bureaus⁵⁷ may incur could impact on the effectiveness of the Switching Fund Remedy to the extent that these cost differences would affect

⁵¹ [REDACTED].

⁵² [REDACTED].

⁵³ Apparent in paragraph 2.1(a)(xiii) of the UILs. The Parties have confirmed this.

⁵⁴ The CMA notes that in order to implement any changes, the LINK member would necessarily need to be involved, but this would not be merger-specific, as discussed in paragraph 82(a).

⁵⁵ Certified service bureaus offer connection services between LINK members and the LINK network, without requiring these certified service bureaus to be members.

⁵⁶ [REDACTED].

⁵⁷ It is the incentives on the LINK members that are relevant, rather than the certified service bureau itself.

the voting intentions of LINK members during the tender process.⁵⁸ Therefore, the UILs have been updated to clarify that increased charges to a LINK member by a certified service bureau which are a direct result of the transition to the New Processor would be considered eligible in the Switching Fund Remedy. This will ensure that the impact of the UILs on incentives for LINK member using certified service bureaus are consistent with those connecting directly.

78. One respondent stated that the Switching Fund Remedy should be available to LINK members independent of whether the New Processor chooses to use the Network Access Remedy.⁵⁹
79. The CMA notes that the UILs already require that the Switching Fund Remedy is independent from the Network Access Remedy,⁶⁰ and so no changes were necessary to address this point.

Other points raised in consultation

80. Two respondents stated that a number of market participants had potential conflicts of interest related to the Merger.⁶¹ In particular, they stated that LINK members who were VocaLink shareholders would have an interest in the transaction completing, which could prejudice their statements and evidence. It was further submitted that other participants (most notably LSL) may have been pressured into supporting actions against the long-term interests of LINK itself.
81. The CMA acknowledges the possibility of conflicts of interest existing with regard to certain LINK members in this transaction, and has considered the implications on the assessment of the UILs. The CMA has critically assessed the range of evidence it has received from all stakeholders, in coming to its decisions. In particular, the CMA notes that its evidence base included the views of:
 - (a) LSL's majority-independent board, appointed to make decisions which are in the interests of LINK. It is not clear why this board would act contrary to this objective, and no evidence has been provided to support this view;
 - (b) LINK members who are not VocaLink shareholders; and

⁵⁸ As described in paragraph 163 of the SLC Decision.

⁵⁹ [REDACTED].

⁶⁰ Apparent in paragraph 2.1(c) of the UILs. The Parties have confirmed this.

⁶¹ [REDACTED].

- (c) non-LINK members (eg potential competitors, and the PSR) which are not subject to these same potential conflicts.
82. A number of responses raised points which the CMA believed were not relevant to the assessment of the UILs. These points can be broadly grouped under the following three topics:
- (a) **Not Merger-specific:**⁶² a number of respondents raised concerns related to potential incumbency advantages enjoyed by VocaLink, particularly with regard to the costs of changing provider. To the extent that any such advantages would also exist in the counterfactual, the CMA believes these not to be Merger-specific. As discussed in paragraph 95 below, the UILs should address any potential advantages that Mastercard (absent the transaction) has over other potential bidders.
 - (b) **Not related to the SLC:**⁶³ a number of respondents raised concerns which were unrelated to the SLC. This included aspects assessed in other theories of harm in the SLC Decision (such as the vertical effects – ATM switching services),⁶⁴ but in relation to which no substantial lessening of competition was found. The UILs are specifically aimed at addressing the SLC.
 - (c) **Alternative remedies outside of the CMA’s powers:**⁶⁵ a small number of respondents proposed alternative remedies which involved binding third parties (eg LSL or LINK members) to particular terms or to undertake particular actions. The CMA considered that these proposals would not address the SLC as they did not relate to the level of competition in future LINK tenders. Furthermore, this approach would be beyond the scope and powers of the CMA in its merger-review capacities. The remedies accepted by the CMA cannot compel third parties who are not parties to the transaction to undertake specific actions.
83. One respondent which was broadly supportive of the UILs said that the best way to guarantee competition would be to require a divestment of VocaLink’s LINK business (including the LINK contract and a range of supporting infrastructure). It also stated that this approach would not be overly difficult, and a technical separation is achievable.⁶⁶
84. As it is further explained below (see paragraphs 100-102), the CMA is satisfied that the proposed UILs are both effective and more proportionate

⁶² [REDACTED].

⁶³ [REDACTED].

⁶⁴ See paragraphs 241-266 of the SLC Decision.

⁶⁵ [REDACTED].

⁶⁶ [REDACTED].

than a more intrusive divestiture remedy. Therefore, the CMA has not considered this alternative remedy further.

Conclusion

85. As discussed above, the CMA has carefully considered the submissions and additional evidence received from stakeholders both prior to and during the Public Consultation.
86. For the reasons set out above, these stakeholders' submissions did not cause the CMA to change its preliminary view set out in the Notice of Consultation that the Proposed Undertakings could be acceptable. With regard to the areas in which the CMA particularly requested feedback, the responses did not raise any specific issues regarding the cost allocation approach or duration of the Proposed Undertakings. Points raised about the proposed duration of the migration period are discussed in paragraphs 54-56 above.
87. However, the Proposed Undertakings were slightly amended where the submissions received showed that it was appropriate to do so. In particular, the Proposed Undertakings were amended to:
- (a) include a clause ensuring the Parties are required to co-operate with LSL and the New Processor during the transition period of the Network Access Remedy;⁶⁷
 - (b) clarify that increased charges to a LINK member from a certified service bureau as a direct result of the transition to the New Processor would be considered eligible costs for the Switching Fund Remedy;⁶⁸ and
 - (c) remove the cap on the indexation of the Switching Fund Remedy.⁶⁹
88. In addition, the UILs include a minor change to the reduction in minimum fees charged by VocaLink during the migration period (discussed in paragraph 19), which has the effect of strengthening the UILs (as a 25% waiver may be applied between months 6 and 12). A full waiver within this period remains applicable if the CMA, following appropriate considerations, confirms that an extension is necessary. Therefore, all the circumstances in which a full waiver would be granted which were included in the Proposed Undertakings remain in the UILs.⁷⁰

⁶⁷ See paragraph 2.1(a)(iii) of the UILs.

⁶⁸ See footnote 7 of the UILs.

⁶⁹ See footnote 6 of the UILs

⁷⁰ See paragraph 2.1(a)(xiv) of the UILs, and the associated definitions.

89. The CMA considers that these changes will not materially impact the overall design of the remedy, but will provide greater certainty and clarity to the New Processor hence enhancing the effectiveness of the UILs.

Assessment

Legal framework

90. Under section 73(2) of the Act, the CMA may, for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned or any adverse effect which may be expected to result from it, accept from the merging parties, undertakings in lieu of reference to take such action as it considers appropriate. Under section 73(3) of the Act, the CMA must have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the substantial lessening of competition and any adverse effects resulting from it.
91. The Exceptions to the Duty to Refer Guidance (referred to as **UILs Guidance** for the purposes of this decision) published by the Office of Fair Trading (**OFT**, the CMA's predecessor dealing with phase 1 mergers) and adopted by the CMA,⁷¹ notes that the ability under the Act for parties to give undertakings in lieu of a reference allows for transactions to be structured to allow the benign or pro-competitive part of the merger to proceed while at the same time guarding against a potential substantial lessening of competition in markets representing a sub-set of the overall transaction.⁷² It further notes that when deciding whether to accept undertakings in lieu of a reference, the CMA's starting point is to seek an outcome that restores competition to the level that would have prevailed absent the merger, thereby comprehensively remedying the substantial lessening of competition.⁷³
92. The UILs Guidance states that undertakings are appropriate only where they are clear-cut, and that this clear-cut standard has two dimensions:⁷⁴
- (a) first, the CMA must be satisfied that, if the undertakings are accepted, there is no material doubt about their overall effectiveness; and

⁷¹ *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance (OFT1122)*, December 2010. This guidance was adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure (CMA2)*, January 2014, Annex D).

⁷² UILs Guidance, paragraph 5.2.

⁷³ UILs Guidance, paragraph 5.11.

⁷⁴ UILs Guidance, paragraphs 5.7 and 5.8.

(b) second, the undertakings must not be of such magnitude and complexity that their assessment and implementation would require unworkable resources at Phase 1.

93. Since a merger involves a structural change to a market, the UILs Guidance states that structural undertakings, or in appropriate cases quasi-structural undertakings, will normally be the most appropriate remedy.⁷⁵ However, the UILs Guidance notes that the CMA will not inevitably refuse behavioural remedy offers, and will consider behavioural undertakings in particular where a structural remedy would be clearly impractical or is otherwise unavailable, and where mergers take place in markets in which there already exists a significant degree of regulation.⁷⁶
94. Under section 73(3) of the Act, it is also incumbent on the CMA to ensure that undertakings are proportionate to the concerns identified in its decision.⁷⁷ This includes the obligation to select the least intrusive remedy where there is a choice of equally effective remedies.⁷⁸ The CMA's obligation to accept undertakings only in so far as they are necessary to remedy its competition concerns does not mean that it will take a less effective remedy simply because its belief in the likelihood of the substantial lessening of competition is lower than in other cases. To the extent that the duty to refer is met (that is, there is a realistic prospect of a substantial lessening of competition), any UILs must remedy the concerns identified to the clear-cut standard.⁷⁹

Framework for analysis of the present case

95. The SLC (as described in paragraph 3-6 above) relates to the loss of competition associated with any potential advantages that Mastercard would have had over other bidders, rather than any advantage VocaLink may have over any other bidder (including Mastercard and/or Visa). The UILs are a package of measures which in combination remedy the SLC by providing other potential bidders an equivalent level of advantage to that enjoyed by

⁷⁵ UILs Guidance, paragraphs 5.20 and 5.24.

⁷⁶ UILs Guidance, paragraphs 5.38-43.

⁷⁷ See also UILs Guidance, paragraph 5.15.

⁷⁸ UILs Guidance, paragraphs 5.15-19. This approach is in line with the proportionality test that was set out by the CAT in Phase 2 remedies cases, based on the CJEU's Fedesa judgment (see *Tesco plc v CC* [2009] CAT [6], paragraph 137; *BAA Limited v CC* [2012] CAT [3], paragraph 20; and *Ryanair v CC* [2014] CAT [3], paragraph 187). It is also consistent with the finding of the CAT in *British Sky Broadcasting PLC v Competition Commission* and *Virgin Media v Competition Commission* [2008] CAT 25, where the CAT rejected the assertion by Virgin Media that the Competition Commission should have required the full divestiture of BSkyB's shareholding in ITV. The Competition Commission had found that both full divestiture and partial divestiture would be effective remedies but that partial divestiture would be more proportionate. Accordingly, the Competition Commission was not required to adopt a remedy that went beyond what was necessary to ensure that there was no realistic prospect of a substantial lessening of competition persisting.

⁷⁹ UILs Guidance, paragraph 5.17.

Mastercard, and therefore restore the level of competitive constraint which Mastercard would have exercised on VocaLink absent the transaction.

96. In light of the particular facts and circumstances of this case, the CMA gave careful consideration to the UILs and has consulted to obtain the views of market participants on whether the UILs should be accepted pursuant to the CMA's statutory powers.
97. As it is further explained in paragraphs 103-129 below, the CMA believes that the UILs will address the SLC to the clear-cut standard (ie the UILs are an effective and workable set of behavioural commitments), taking into account all the relevant circumstances of the present case.
98. In assessing the effectiveness of the UILs, the CMA put significant weight on the fact that the Parties operate in a regulated sector in which the PSR is currently highly engaged in reviewing the ownership and competitiveness of infrastructure provision.⁸⁰ This provided the CMA with greater information and guidance, and helped to develop a more in-depth understanding of the relevant market(s) than would otherwise have been possible in the time available. This in turn gave the CMA greater confidence that the UILs are as comprehensive a solution to the SLC as is reasonable and practicable.
99. Furthermore, the increased regulatory scrutiny that can be expected as a result of the PSR's ongoing role in the sector gives the CMA greater confidence in the ongoing effectiveness of the UILs than it might have if the sector were unregulated,⁸¹ as well as providing the opportunity for the CMA to seek advice from the PSR as appropriate (eg on technical aspects of the cost allocation approach and technicalities of the Network Access Remedy).
100. Given the ongoing involvement of the PSR and the significant degree of regulation applying to the relevant markets, devising a workable and effective set of non-structural elements to the remedies has not proven to be an obstacle in this case. In particular, the CMA notes that the facts of this case are consistent with the circumstances in which, according to the UILs Guidance, remedies involving a significant non-structural component are potentially more suitable.
101. In addition to assessing the effectiveness of the UILs, the CMA assessed the proportionality of the UILs, as required in both the UILs Guidance and section 73 of the Act. In order to be reasonable and proportionate, the CMA is

⁸⁰ See [Market review into the ownership and competitiveness of infrastructure provision \(PSR MR15/2\)](#).

⁸¹ Non-structural remedies may be more suitable in markets experiencing a significant degree of regulation; [Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance \(OFT1122\)](#), December 2010, paragraphs 5.43. This guidance was adopted by the CMA (see [Mergers: Guidance on the CMA's jurisdiction and procedure \(CMA2\)](#), January 2014, Annex D).

required to accept the least intrusive remedy where there is a choice of equally effective remedies. If the CMA is satisfied that the UILs are as effective as, and less intrusive than an alternative remedy (most obviously divestiture), the CMA may decide under section 73 to accept those undertakings in lieu of a Phase 2 reference.

102. In the present case, the CMA did not identify any other remedies which would be equally effective and less onerous on the Parties. In particular, the CMA considers that any reasonable divestment remedy would be more intrusive than the UILs. In this context, the Parties have emphasised that a divestiture remedy would be more complex and costly to implement mainly because there is both shared technology (eg Circuits) and integrated processes (eg network monitoring) which would need to be separated. Therefore, the CMA considers that, even if this alternative possible remedy was effective, the combination of measures captured in the UILs is the least onerous effective option.

Clear-cut remedy

103. The clear-cut standard that applies to the UILs has regard to the UILs' (i) effectiveness; and (ii) practical workability of their assessment, implementation, and monitoring. The CMA's assessment of the UILs against each of these points is set out below.

Effectiveness of the UILs to address the SLC

104. When assessing the effectiveness of the UILs to address the SLC, the CMA has assessed both the expected impact on the SLC and the resulting adverse effects, as well as the appropriate duration and timing of the UILs which should be applied. These are discussed in more detail below.

Impact on the SLC and the resulting adverse effects

105. For their duration, the UILs will address the key underlying causes of Mastercard's cost advantages (as described in paragraph 3) and ensure that other potential CIS providers are well placed to bid for LINK's next CIS contracts, thereby remedying the SLC. This will create the conditions for an increase in the number of credible alternative providers for the duration of the UILs, as described below:
- (a) The advantage over a New Processor arising from existing connectivity (see paragraph 3(a) above), as well as parallel running cost differences (see paragraph 3(b) above), will be addressed by the Network Access Remedy. The Network Access Remedy will avoid the need for a New

Processor to replace the network routers at LINK members' sites and replicate the current network connecting the LINK members. It will also reduce the level of testing required by the New Processor and, therefore, the LINK members' costs of changing CIS provider;

- (b) LIS5 licensing costs will be directly addressed by the LIS5 Remedy; and
- (c) LINK members' costs of changing CIS provider will be reduced by each component of the UILs (including the Switching Fund Remedy).

106. The cost allocation methodology for the Network Access Remedy is well defined, includes all relevant costs, and relies on objective criteria. This ensures that it accurately reflects the operational costs to VocaLink, and is difficult to manipulate. An accurate cost allocation also ensures that VocaLink's network should continue to receive sufficient ongoing investment to support its requirements, and does not lead to other potential distortions. The functions of the Monitoring Trustee include monitoring compliance with the cost allocation methodology.
107. The VocaLink monitoring and maintenance costs fairly reflect the costs associated with the provision of a necessary service which any provider of CIS services to LINK would incur. The Parties told the CMA that, due to the fact that parts of the LINK network overlap with other payment systems services, it would not be possible or desirable for a third party to provide the monitoring and maintenance service for the LINK part of the network alone. Furthermore, the Parties stated that this approach avoids the duplication of these costs, as the New Processor no longer needs to provide these services itself.
108. The CMA considers that there is a very low risk of service degradation (either intentional⁸² or unintentional) for the Network Access Remedy which VocaLink would provide to the New Processor. This is because any reduction in service levels would be highly visible to the New Processor, LSL, and to any customers affected. Given the protection afforded in the UILs, this would be expected to result in:
- (a) Breaches in the UILs, resulting in intervention by the Monitoring Trustee and/or the CMA, including the potential for financial penalties;
 - (b) Contractual breaches of the bilateral/tripartite agreement between the New Processor and VocaLink; and

⁸² For example, the selection of disruptive timings for network updates to the LINK network and/or overlapping payment systems networks.

- (c) Reputational damage to the Parties with LINK members, which may affect not only the likelihood to win any future LINK tenders, but may potentially adversely impact other business/services where the Parties are competing.
109. The removal/reduction of the minimum contractual financial commitments for a transition period of six to twelve months (as described in paragraph 19) covers the expected migration period for which there would be two processors in place.
110. Although one respondent stated that this process may take up to 18 months (as discussed in paragraph 54 above), no supporting evidence for this position was provided. In addition, the POC Exercise indicates that 6-12 months is sufficient, with none of the participants raising concerns about the duration of this period even when it would be applied in a 'live' setting rather than simply as a proof of concept. A duration of 6-12 months was also supported by respondents to the pre-consultation questions from the CMA.
111. The confidentiality undertakings mentioned in paragraph 20 ensure that VocaLink and Mastercard do not have access to commercially sensitive information of LINK members or the New Processor that would give them an advantage over other market participants, including in bidding for future LINK tenders.
112. Following the split of the LIS5 Standard into the LINK LIS5 Standard and the VocaLink LIS5 Standard, the Parties stated that their incentives are aligned with LSL to cooperate with each other to ensure that any services which rely on both standards will continue to function and develop well. The CMA spoke to [REDACTED] (a major user of both standards), which raised no concerns regarding the level of ongoing co-operation between the Parties.
113. The SLC Decision stated that LINK members found it difficult to estimate the likely cost of changing provider, but provided a very wide range from [£200,000 to £50 million].⁸³ However, the CMA notes that these estimates were not provided in the context of the UILs, and are unlikely to account for the continued use of the VocaLink connectivity or the LIS5 Standard. The Parties estimated that the cost to LINK members of changing to a New Processor, but using the VocaLink connectivity and LIS5 Standard (ie using the Network Access Remedy under the UILs) would be approximately [£20k-£30k] each, implying a total of [£750k-£1.25m] for all of the 39 LINK members.

⁸³ SLC Decision, paragraph 162.

114. In order to ensure the remedy was sufficiently clear cut, the Parties included a contribution to address any remaining concerns about LINK member implementation and adaption costs (ie the Switching Fund Remedy). The value of this fund was based on the following calculation:⁸⁴

(a) [REDACTED]

(b) [REDACTED]

(c) [REDACTED]

(d) [REDACTED]

(e) [REDACTED]

The total of these equals £5 million.

115. The relevant cost advantage identified in the SLC Decision for LINK members relates to any difference in these members costs of changing to Mastercard (absent the transaction) compared with another provider (which is not VocaLink or Visa).⁸⁵ Although LINK members were not able to quantify the exact level, a change to Mastercard would still have incurred a cost. By allowing a New Processor to use VocaLink's existing connectivity, the level of costs which LINK members would incur could be at or below that of changing to a different connectivity network such as Mastercard's. Given that some uncertainty remains about the exact level of these costs, the Switching Fund Remedy then provides additional assurance that any cost differences to LINK members which do remain would be covered at the Parties' expense.

- *POC Exercise*

116. The Parties, following a CMA request, conducted a proof of concept exercise (POC Exercise) to test the viability of the Network Access Remedy. To conduct this POC Exercise VocaLink chose a subset of LINK members which it understood to be capable of participating in the time available.⁸⁶ The POC Exercise consisted of building an external test network environment onto VocaLink's existing network. This external environment included a test VocaLink ATM switch and a simulated New Processor ATM switch connected via an external telecommunications link. Members then tested a series of cash withdrawals and balance enquiries across a combination of these switches in order to validate that both processors could coexist during any

⁸⁴ As stated in the Remedies Form.

⁸⁵ SLC Decision, paragraph 164.

⁸⁶ This included 4 card-issuing banks/building societies which are VocaLink shareholders: [REDACTED].

migration activity, and that the New Processor could independently handle transactions post-migration. The findings of the POC Exercise provide additional evidence about the efficacy of the UILs, and are as follows:

- (a) The simulated New Processor was successfully able to use VocaLink's connectivity to process transactions from the LINK members;
- (b) During the transition period, transactions were able to be correctly routed between migrated and non-migrated LINK members;
- (c) The migration period for the LINK members took place in two weeks or less which, assuming capacity to commence three to six migrations per week, supports the view that the migration period of 6 to 12 months is sufficient, even accounting for contingency requirements;⁸⁷ and
- (d) The costs for a LINK member to connect to a New Processor using the VocaLink network can be completed for less than £10k per member. The Parties noted that during a 'live' migration, the costs are likely to be somewhat higher (eg due to tighter change management, additional network-level proving, back-up connections and additional fallback planning in case of change failure), but should not exceed the funds available in the Switching Fund Remedy.

117. More detailed conversations with the LINK members involved in the POC Exercise supported VocaLink's characterisation of success, and raised no additional issues or risks. They all stated that the exercise was completed in less than 2 weeks, that VocaLink was very supportive during the process, and that the overall costs and resources were relatively small (eg [REDACTED]),⁸⁸ particularly as the necessary changes were restricted to the network connectivity rather than requiring additional changes to their IT infrastructure. Although all participants noted that a live migration would likely necessitate additional time and/or costs (eg about the level of testing which would be conducted), it would also involve access to greater time and planning which would mitigate additional risks. Overall, a number of the participants described the process as 'smooth', 'uncomplicated', and/or 'business as usual for a change team'. Therefore, the CMA believes that the POC Exercise is supportive of the effectiveness of the UILs.

⁸⁷ This appears to be based on commencing an average of 4.5 migrations per week, with each migration taking 2 weeks would result in $(39/4.5)+1 = 10$ weeks (2.5 months) for all of LINK's 39 members.

⁸⁸ [REDACTED].

Appropriate duration and timing

118. The duration of the Network Access Remedy and Switching Fund Remedy balances the need to provide sufficient time for LINK to attract additional credible bidders, against the potential costs of longer-term intervention including the risk of distortions to the market. The CMA also notes that there is a review clause within the UILs which enables it to assess the effectiveness of the remedy before the expiry of the first tender cycle.
119. The LIS5 Remedy is a one-off structural change, and so does not require specifying an endpoint. The implementation timing requires the transfer of all the relevant intellectual property within 6 months of the CMA's acceptance, which will allow LINK sufficient time to provide clarity regarding its use by potential bidders during its next tender.
120. The CMA expects that the Network Access Remedy and Switching Fund Remedy will be in place for the first LINK tender for CIS, and will address the SLC through increasing the number of credible bidders available. Subsequently, there are a range of circumstances in which these provisions may no longer be necessary, including (but not limited to):
- (a) a New Processor building its own network connectivity, and demonstrating it is a credible competitor by winning the LINK tender outright;
 - (b) a New Processor using the Network Access Remedy to facilitate entry to the market by winning a LINK tender, and subsequently builds its own network connectivity so as to remove VocaLink from its supply chain during the lifetime of the contract;
 - (c) changes in the market (eg through technological innovation) removing or reducing the reliance of a New Processor on pre-existing network connectivity;
 - (d) LSL having been able to implement changes to its tendering process to allow potential New Processors to compete more effectively (eg using a layered architecture to separate the provision of connectivity from the provision of processing, as appears to be under consideration for other payment systems);⁸⁹ or

⁸⁹ Payment Strategy Forum, 'A Payments Strategy for the 21st Century', November 2016.

- (e) the PSR's ongoing work in the market resulting in greater levels of competition, introducing competitive constraints equivalent to those imposed by the UILs.
121. In such circumstances, the UILs may no longer be appropriate, and so should be removed either through automatically lapsing, or following the CMA review which will take place no later than two years prior to the end of the first tender cycle.
122. In order to ensure the effectiveness of the UILs in addressing the SLC, safeguards regarding the duration of the Network Access Remedy form part of this remedy package. Therefore, where necessary, the duration of the UILs extend to cover a second tender cycle, as described in paragraph 25. This ensures that LSL has sufficient time to fully implement any necessary changes to its procurement approach to enable a competitive bidding process for the supply of CIS to LINK.
123. The use of long-stop dates limits the risk from any long-term intervention beyond the foreseeable future, for the supply of CIS to LINK. The inclusion of the up-front date for the CMA to review the ongoing necessity of the undertakings provides a further safeguard against the risk of market distortion.

Workability of assessment, implementation and monitoring

124. As set out above, the UILs Guidance states that, for an undertaking to be clear-cut, it must not be of such magnitude and complexity that its assessment and implementation would require unworkable resources at Phase 1. In taking this decision, the CMA has, with the resources available to it and in the timeframe provided under section 73A of the Act (and drawing on the expertise of the PSR in its capacity as the sectoral regulator), been able to carry out a detailed assessment of the Undertakings.
125. The CMA believes that the UILs are capable of ready implementation, in particular because:
- (a) the LIS5 Remedy is structural, with a pre-defined acquirer (ie LSL) similar in nature to situations which include an identified, suitable upfront buyer;⁹⁰
 - (b) the implementation timelines (as described in paragraphs 36-38 above) have been defined, with the majority completing within 6 months of any CMA acceptance of the UILs. Furthermore, these timings allow LINK to

⁹⁰ *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance (OFT1122)*, December 2010, paragraphs 5.31–5.37. This guidance was adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure (CMA2)*, January 2014, Annex D).

provide sufficient clarity about the specific terms on which network access will be granted to potential bidders during its next tender. The Parties are required to ensure that the necessary actions to implement the UILs are undertaken. To the extent that there were any implementation delays, such delays are subject to both dispute resolution through the Monitoring Trustee and/or intervention by the CMA as a result of potential breaches of the UILs;

- (c) the primary customer (LSL) has stated its support of this approach; and
- (d) the Framework Agreement and changes to VocaLink's existing contract with LINK were approved by LINK's Network's Members Council with a very large majority ([X]%).

- *Monitoring Trustee and the PSR*

126. As well as monitoring the ongoing compliance of the Parties with the UILs, the Monitoring Trustee role includes a function to act as an independent arbiter, and dispute resolution mechanism.
127. The inclusion of a Monitoring Trustee provides additional assurance to the CMA in this case as to the practicality and enforceability of the remedy. The CMA recognises that aspects of the UILs may result in future disagreement between the Parties and any New Processor, for example, about the level of cost associated with the Network Access Remedy which can be charged to the New Processor. Having an independent body in place, in advance, to provide verification and a dispute resolution mechanism in relation to these costs ensures a more effective and efficient process.
128. As regards monitoring compliance with the UILs, the CMA also notes that the UILs will be capable of ready and effective monitoring to ensure that there are no breaches. In this case, there is a particularly high level of scrutiny of the Parties' behaviour which would be expected to identify any breaches or potential breaches. The CMA's own compliance monitoring function will be supplemented by:
- (a) the Monitoring Trustee, which has the specific role of monitoring compliance;
 - (b) the existence of a highly engaged sectoral regulator (the PSR), with explicit competition duties and powers which would inform the CMA, as appropriate, if it identifies any concerns around possible breaches of the undertakings in the exercise of its regulatory functions.

- (c) the New Processor, which may be relying on inputs provided by the Parties as part of its critical supply chain;
- (d) LSL, the single customer for the LINK tender, which has very strong incentives to closely monitor the behaviour of one of its key supplier; and
- (e) LINK members who rely on these services and have good visibility of the performance of the underlying infrastructure (eg around availability of services).

129. Taking into account the particular facts and circumstances of this case, the CMA therefore believes that the UILs do not require unworkable resources at Phase 1 and are capable of ready assessment, implementation and monitoring.

Conclusion

130. As discussed in paragraphs 103-129 above, the CMA considers that the UILs will effectively address the competition concerns raised as a result of the Merger, while being practically implementable in a Phase 1 process.
131. The CMA also considers that, in addition to being effective, the UILs conform with the principles of proportionality, as laid out in paragraphs 101-102 above.
132. The CMA therefore concludes that the UILs offered by the Parties are clear-cut and appropriate to remedy, mitigate or prevent the competition concerns identified in the SLC Decision.

Decision

133. The CMA believes that the UILs provided by the Parties are as comprehensive a solution as is reasonable and practicable and remedy, mitigate or prevent the SLC and any adverse effects resulting from it. The CMA has therefore decided to accept the UILs offered by the Parties pursuant to section 73 of the Act. The Merger will therefore not be referred for a phase 2 investigation.
134. The undertakings, which have been signed by the Parties and will be published on the CMA website,⁹¹ will come into effect from the date of this decision.

⁹¹ See <https://www.gov.uk/cma-cases/mastercard-vocalink-merger-inquiry>.

Andrea Coscelli
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Competition and Markets Authority
11 April 2017