

Appointment of the competent authority and approach to national discretions for the interchange fee regulation

HM Treasury

RPC rating: fit for purpose

Description of proposal

In anticipation of the entry into force of the EU directly applicable regulation on interchange fees (IFR), HM Treasury must designate a competent authority for monitoring and enforcing compliance with the IFR. The department proposes to designate the Payment Systems Regulator (PSR).

Although not required under the better regulation framework, the department has also assessed the directly applicable effects of IFR. The regulation will place a cap on interchange fees charged for the acceptance of credit and debit cards transactions in the UK. These fees are set by card networks (schemes) such as Visa and Mastercard, and paid by merchants' banks (called 'merchant acquirers') to customers' banks (called 'issuing banks'). The regulation will cap interchange fees at 0.2% of the transaction value for debit cards and 0.3% for credit cards.

Impacts of proposal

Domestic changes required by the regulation

The IFR requires the UK to designate a competent authority and the department's proposal designates the Payment Systems Regulator (PSR) as this authority. The PSR estimates that supervising and enforcing the IFR will cost them £1.2 million each year, which is 8% of the PSR's £15 million annual budget, as estimated in the April 2015 Impact Assessment for the establishment of the PSR. As the regulator is funded by industry, these costs are a direct cost to business. The PSR has already budgeted the aforementioned £1.2 million in the current year and expects a similar cost for future annual budgets. The department categorised these costs as an 'IN' with 'zero net cost' at the time given the pro-competition remit of the PSR. On this basis, the department's assessment in this IA that the proposal will not impose any additional costs on the PSR is reasonable.

Directly applicable impacts of the proposal

The department explains that the proposal will be cost neutral to business overall. This is because reduced interchange fee revenue for banks issuing debit or credit cards and processing card payments will be matched by equivalent gains to retailers and other merchants who will pay lower interchange fees. The department states that figures from the European Commission's impact assessment suggest that the potential transfer to retailers

and other merchants from card issuers of the cap on interchange fees could be as much as £1 billion per annum in the UK. During consultation stage, the British Retail Consortium estimated that caps of 0.2% and 0.3% to debit and credit cards, respectively, could save retailers in the UK around £480 million. Following consultation, respondents submitted further evidence supporting an estimate that the saving could be in the region of £700 million a year across all merchants.

The department intends to take advantage of the option to apply a transitional period of up to three years. During this period, schemes in which third parties license banks to issue domestic debit cards will not be subject to the fee cap for a period of three years, providing the market share of the scheme is less than 3% of the total value of annual card transactions in the UK. The department states that a transitional period gives smaller three-party schemes time to adjust their business models to allow for the introduction of the fee cap. The department explains that, given the low number of three party schemes, the transition period is expected have a negligible impact on the PSR's costs and to have a zero net impact on business.

Quality of submission

The department identifies the main impacts on business of the proposal and estimates these using industry consultation evidence and data from the PSR.

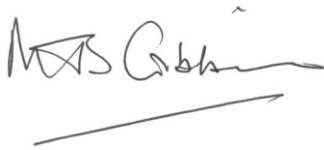
As we requested, the department has carried out benchmarking analysis to estimate the level of savings that would be passed on from merchants to their customers as a result of the proposal. The department explains that similar caps in interchange fees in the US resulted in merchants passing on 69% of savings to consumers. In addition, the IA would have benefitted from an analysis of the extent to which merchant sales volumes might change as a result of the reduction in interchange fees. Nevertheless, the department explains that the IFR obliges the European Commission to review, by 2019, the extent to which European merchants have passed on the reduction in interchange fee levels to consumers. This is expected to reveal the extent of the pass through impact in the UK. However, in any case these effects are considered to be indirect.

Initial departmental assessment

Classification	Out of scope
Equivalent annual net cost to business (EANCB)	£0
Business net present value	£0
Societal net present value	£0

RPC assessment

Classification	Out of scope
EANCB – RPC validated	£0
Small and micro business assessment	Not required



Michael Gibbons CBE, Chairman