

# **COMPETITION IN PAYMENT SYSTEMS**

**A response to consultation**

**HM Treasury  
August 2001**

## 1 INTRODUCTION

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**1.1** The Government issued its consultation document “*Competition in Payment Systems*” in December last year in response to recommendations made by Don Cruickshank in his review of competition in UK banking.

**1.2** The Government accepted the basic premise of the Cruickshank report - that there was insufficient competition in the provision of payment services; that this led to poor service and value for customers; and that, due to the nature of the industry, these problems would not be corrected naturally through the operation of market forces. The Government, therefore, proposed that the Office of Fair Trading (OFT) should be given new powers to promote effective competition in payment systems in order to benefit personal and business customers.

**1.3** The consultation document sought comments on a number of key issues related to: the regulator’s objectives; the regulator’s powers and functions; the appeals processes; the roles of other authorities with an interest in payment systems; the scope of the new regime; and the proposed rules.

**1.4** The consultation period closed on 20 March and a total of 43 responses were received, mainly from institutions in the banking sector or from bodies representing the business and personal customers of the banks. The Government wishes to thank all those who took part in the consultation. A detailed feedback statement on the responses received forms an annex to this paper.

**1.5** The responses to the consultation document have confirmed the Government in its view that a new competition regime for payment systems is needed and that the proposals in the December consultation document generally represent the best way forward. However, some changes have been made to the detail of the proposals in the light of consultation responses received.

## 2 BACKGROUND

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**2.1** In November 1998 the Chancellor of the Exchequer asked Don Cruickshank to carry out a review of the banking industry in the UK, with a particular remit to consider levels of innovation, competition and efficiency.

**2.2** Don Cruickshank reported in March 2000. In his report, *Competition in UK Banking*, he noted that it was the banks’ control of money transmission systems that made the level of their innovation and efficiency crucial to the UK economy. As a consequence, this feature of banks’ activities was a focus of his review. The Cruickshank report concluded that there was a profound lack of competition in payment systems. This was caused by the underlying economic characteristics of the industry, where network effects placed a natural limit on the level of competition. This allows inefficiencies to persist for many years. The report further concluded that the existing framework of

competition law was not sufficient to tackle these problems and that the Government should set up a licensing system, administered and supervised by a newly instituted Payment Systems Commission (Paycom), to promote competition.

**2.3** The Government agree with the overall thrust of the Review's recommendations, although it does not fully accept every detail. In his Budget speech on 21 March 2000 the Chancellor said:

*“The money transmission system affects every cheque, every credit card and every debit transaction. It reaches from every local cash dispenser to every corporate inter-bank transfer. Today I am announcing that we will legislate to ensure the UK payments system is open to new competition.”*

### **3 CONSULTATION**

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**3.1** The Government's detailed proposals for implementing the Cruickshank report's recommendations, including its commitment to legislation, were set out in its consultation document published in December 2000. These largely built upon Don Cruickshank's views. However, the Government decided that rather than create a separate Paycom the OFT should be given additional powers in this area. Also, instead of a licensing regime, all participants in payment systems would be obliged to comply with a set of competition-oriented rules.

**3.2** Based on these proposals, the consultation document asked for representations on 29 questions.

**3.3** Responses to consultation showed that, in general, the larger participants in the payment services industry did not agree that there was a need to regulate, but - if regulation was judged necessary - thought that it should be conducted with a light touch. The second tier bodies, whereas they thought that regulation was necessary, shared the view that it should be light touch. Retail and consumer groups generally favoured the proposals.

**3.4** Beyond the issue of principle as to whether or not payment systems should be subject to sector specific regulation there was general acceptance that if such regulation was to be introduced then the proposals in the consultation document seemed to be on the whole satisfactory. There were, of course, areas where particular respondents disagreed with specific proposals:

- some respondents continued to favour the Cruickshank report view that an independent body, rather than the OFT, should regulate the sector;
- many respondents thought that the partial Regulatory Impact Assessment understated the costs of the proposed regime;

- many respondents disagreed with the proposal that the OFT should have a duty to facilitate innovation; and
- the schemes and their members generally objected to the proposal that the OFT should have similar powers to enter premises for investigatory purposes under payment services legislation as it does under the Competition Act 1998.

Further detail on the response to consultation is set out in the feedback statement that forms an annex to this document.

## **4 THE GOVERNMENT'S REVISED PROPOSALS**

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**4.1** The Government confirms that it intends to introduce a new competition regime for the payment systems industry and that it will introduce the necessary legislation as soon as Parliamentary time allows. Set out below is a description of the Government's main proposals, as revised following consultation. The Government will, of course, keep developments in general competition law, in both the UK and the EU, under review as it proceeds with its proposals. In particular the Government will take account, as they develop, of the current proposals put forward by the European Commission for the modernisation of the rules for the implementation of Articles 81 and 82 of the EC Treaty. Once the likely outcome of the modernisation negotiations has become clear the Government will need to reconsider any potential impact on the proposals set out below.

### **Scope and nature of the regime**

**4.2** The Government intends that the new regime should be a rule based regime rather than a licensing regime. It proposes that anyone who falls within the scope of the regime should automatically be subject to the rules, provided that they exceed the threshold for intervention, without needing to be authorised or registered for that purpose.

**4.3** While the Government would expect the OFT to use general competition law whenever appropriate, it is satisfied that competition issues arise in this industry for which general competition law will not provide an appropriate remedy. In view of the importance of the industry to the national economy, the Government therefore proposes to put in place sector specific regulation. This will mean that the industry is bound by specific rules intended to encourage effective competition.

**4.4** The Government believes that the scope of the regime should encompass all those who participate in the provision of payment services. The policy intention is to catch anyone who may present a competition bottleneck in the provision of payment services to the detriment of end users, whether the end users in question are personal customers, small or medium sized businesses or large corporate customers. Payment services comprise activities involved in the end-to-end process of transferring value from one

end user to another. The Government, therefore, will seek to bring a range of participants within the scope of the regime, including:

- Scheme governing boards, the members of those boards, and the administrative organisations which work for those boards;
- Infrastructure providers, whether they are the schemes, scheme members, companies providing a service to the scheme under contract or other participants connected to the scheme perhaps on an agency basis (eg owners or controllers of ATMs, point of sale terminals etc); and
- Firms who participate in making or receiving payments to end users.

**4.5** The consultation document suggested that the Government would exclude those payment systems which are not used to provide retail payment services, such as those involved in securities settlement (eg. CREST). On reflection, it is not clear that this distinction is entirely clear-cut (eg. although individual investors do not have direct access to CREST, they still ultimately bear the cost of transactions through that scheme). Given this, the Government does not wish to exclude any systems or classes of system in primary legislation but intends to make provision for an order making power, conferred on the Treasury, to exclude certain classes of person from most aspects of the regime if it considers that there would be no threat to effective competition as a result of the exclusion. In order to preserve the independence of the regulatory regime from day-to-day political control, the order making power should only be exercisable following a recommendation from the OFT. The Government also proposes that excluded bodies should supply the regulator with such information as the regulator may require to monitor the exclusion. If the regulator concludes, as a result of this monitoring, that there has been a change in circumstances, the exclusion may be revoked.

## **The regulator and its objectives**

**4.6** The Government intends that the new regime for regulating payments systems should be operated by the OFT. Administratively, it expects that responsibility for sector specific regulation will fall on a separate division within the OFT. The Government proposes to set the OFT a specific objective to guide its use of its new powers and functions it will acquire with respect to the payment system sector. This will be designed to promote effective competition, wherever appropriate, in the interests of all consumers and other end users.

**4.7** In the light of representations received, the Government now intends that the “regulatory principles” proposed in the consultation paper should be cast in the form of matters to which the OFT must have regard in carrying out its functions. These matters will include avoiding any material adverse effects of its actions on:

- financial stability;
- efficiency of payment systems;

- payment security; and
- combating financial crime.

**4.8** Furthermore, the Government envisages that the OFT will be required, in carrying out its payment systems functions, to ensure that its actions are consistent with the principle of proportionality in the balance of benefits and costs.

**4.9** The addition of a requirement to avoid material adverse effects on the security of payment systems reflects the importance of ensuring that these matters are taken fully into account by the OFT. However, reflecting on representations received, the Government accepts that it would not be appropriate to make facilitating innovation a formal matter to which the OFT should have regard. It has been persuaded that innovation is a matter for the industry and should come about naturally as a result of more effective competition. The other regulatory principles mentioned in the consultation paper (competitive neutrality, transparency, flexibility and accountability) are general requirements to be taken account of in setting up the framework for the new regime rather than issues needing specific mention in legislation.

## **Powers and functions**

**4.10** The Government intends that the OFT should have the powers and functions set out in the consultation document. It envisages that the OFT will be able, with regard to its work in the payment systems sector to:

- conduct competition investigations into the provision of payment services;
- investigate complaints about competition in payment services;
- collect information in relation to payment services;
- enforce rules, make determinations and impose financial penalties;
- publish information and advice;
- publish information on its payment systems work in its annual report;
- establish advisory bodies; and
- exchange information with other regulators and government bodies.

**4.11** In general, the Government's intention is that the OFT's enforcement powers in relation to payment systems should be similar to those it enjoys under general competition law. This is to ensure that differences in enforcement powers will not be a consideration for the OFT when deciding which set of powers to use. The Government would expect the OFT to use general competition law whenever possible and only use its sector specific powers when, in the OFT's opinion, it is more appropriate to do so.

**4.12** The Government thus intends giving the OFT powers, similar to those it enjoys under the Competition Act 1998, to enter premises under the payment systems regime. The OFT will also be given powers to impose financial penalties where it is satisfied that the infringement giving rise to the financial penalty had been committed intentionally or negligently.

## Role of the Bank of England and the Financial Services Authority

**4.13** The Government intends that the Bank of England should have a right, enshrined within the legislation, to be consulted on decisions or actions which could have an effect on the smooth running of payment systems or which might have a material adverse impact on financial stability. The Government intends that the Financial Services Authority (FSA) should have a right, enshrined within the legislation, to be consulted on decisions or actions in relation to the performance of its public functions. The Government's intention is that the OFT should be obliged to consult these bodies in respect of the exercise of the following specific functions:

- any proposals to modify the rules; and
- relevant individual enforcement decisions.

**4.14** The OFT will be under a duty to take account of the advice of the Bank and the FSA.

**4.15** There will also be a requirement for advice from the Bank and the FSA to be published by the OFT, where it takes action, except on grounds of, for example, commercial confidentiality. If the OFT publishes Bank and/or FSA advice, it will also be required to publish alongside this a statement of the extent to which that advice has been taken into account, and reasons for any divergence from that advice, in the decision that it has reached.

**4.16** The Government is grateful that the Financial Ombudsman Service (FOS) has indicated its willingness to deal with consumer complaints regarding payment services.

## Rules

**4.17** The Government proposes to introduce a set of competition-oriented rules to govern participants in the provision of payment services. These are likely to include rules which will aim to ensure:

- retail price transparency;
- efficient wholesale pricing;
- fair, reasonable and non-discriminatory access;
- co-operation in the development of payment services; and
- good governance.

**4.18** The rule on retail price transparency will apply to all participants in the provision of payment services. In the case of the other rules there will be a minimum threshold before they apply.

**4.19** The Government intends to seek legislative powers to enable the Treasury to make the initial set of rules by means of a Statutory Instrument. Thereafter, all changes to the rules will be made by the OFT.

**4.20** The Government intends that the OFT should have the power to propose and make modifications to the rules including:

- amending an existing rule;
- introducing a new rule;
- withdrawing a rule; and
- providing that particular rules may apply to particular categories of participants.

**4.21** The Government proposes that the OFT will be required to make publicly available a draft of any proposed modifications. In addition to this general consultation the OFT must specifically consult the Bank and the FSA.

**4.22** The Government has decided, on reflection, against requiring the OFT to provide a cost-benefit analysis for any rule modification proposal. There is no such requirement in other areas of competition law. Instead, the OFT will be required to publish an explanation of the reasons for proposing a rule modification and to produce a Regulatory Impact Assessment, whenever appropriate, in accordance with Cabinet Office guidelines.

**4.23** Following consultation, the OFT will be required to publish a statement of whether it intends to proceed with a particular rule modification or with a revised version of the modification reflecting comments received. Such a statement should include the OFT's reasons for its decision, the effect of any amendments made and its response to the advice of the Bank and the FSA. The OFT will have the power to make the proposed rule modification if those affected by the change raise no objection to it, or if – in the opinion of the OFT - the revised form of the rule modification adequately meets the objections raised against the original proposal. If those affected by the proposed rule modification object to the change, but the OFT still wishes to proceed, it will have the power to refer the proposed rule modification, or a revised version of it, to the reporting arm of the Competition Commission for a decision on whether the change is an appropriate remedy to any adverse public interest that would otherwise exist. If the reporting arm rules that there would otherwise be an adverse public interest, and that the change – or a modification of it - is an appropriate remedy, then the OFT will have the power to make the rule modification even if those affected have not withdrawn their objections.

**4.24** The Government proposes that the OFT should be responsible for assessing whether someone meets the test of sufficient interest in a rule modification. However, a decision by the OFT that someone did not have sufficient interest should be appealable by that person to the Appeal Tribunals. It is, however, proposed that a decision that someone did have sufficient interest should not be appealable by third parties.

## Appeals

**4.25** The Government intends that the OFT's decisions should be capable of being appealed in the first instance to the Competition Commission Appeal Tribunals:

- a decision on whether a rule has been breached;
- a direction following a rule breach;
- a decision to impose a financial penalty or the size of a penalty;
- an interim direction;
- a decision that a party did not have sufficient interest to require a rule modification to be referred; and
- a decision that a party did not have sufficient interest to appeal a decision.

**4.26** It is further intended that appeals may be made from the Appeal Tribunals to the relevant court on points of law or on the amount of a financial penalty.

## **5 CONCLUSION**

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**5.1** As noted earlier, the Government is committed to legislate as soon as Parliamentary time permits. While some representations received during consultation have queried the precise allowance made for regulatory costs in the draft Regulatory Impact Assessment, the Government remains convinced that more effective competition in payment systems will deliver substantial net benefits to end users, and believes that the proposals set out above best deliver that outcome.

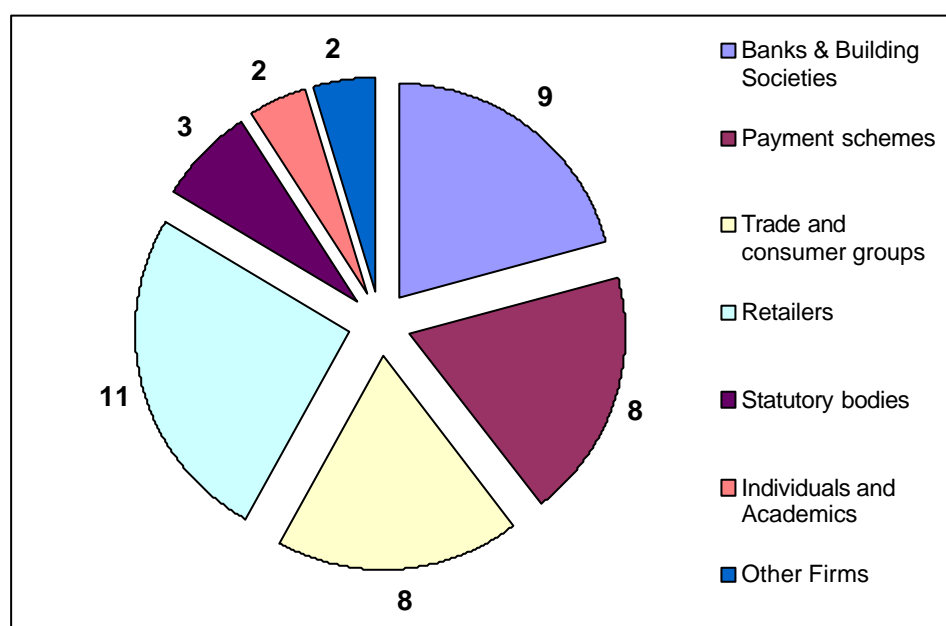
## ANNEX: RESPONSES TO CONSULTATION

### Introduction

**A1.** The consultation document sought comments on a number of key issues related to: the regulator's objectives, the regulator's powers and functions, the appeals processes, the roles of other authorities with an interest in payment systems, the scope of the new regime, and the proposed rules. This annex summarises the responses received.

### The responses

**A2.** The Treasury received 43 responses to consultation. A list of these is in the appendix. Nine responses came from banks and building societies, eight from payment schemes, eight from trade associations and consumer groups, eleven from retailers, three from statutory bodies, one from an academic, one from an individual and two from other firms. The chart below shows a breakdown of the responses received.



Responses to 'Competition in Payment Systems'

### The new regime

**A3.** The responses largely recognised the need for a new competition regime for payment services. The retail sector, led by the British Retail Consortium, expressed their support for the introduction of a new competition regime. A number of respondents, including some banks, expressed their support for moves towards improving competition but noted that regulation should not be so onerous as to stifle innovation. Some respondents, including several payment schemes, felt that a new regime was not necessary, arguing that Cruickshank's concerns about competition in payment services were

unfounded or that the OFT's current powers under the Competition Act 1998 would be broadly sufficient.

## The role of the Office of Fair Trading

**A4.** Respondents were broadly in favour of the Government's proposal to give new powers to promote competition in payment services to the OFT.

**A5.** The consultation document suggested that the OFT's primary objective should be aimed at protecting a broad range of consumers wherever appropriate by promoting effective competition in payment systems. There were a variety of responses commenting on this. Some argued that the OFT should aim to protect consumers, while others argued that the OFT's aim should be limited to promoting competition, noting that this is the best way to deliver benefits for consumers. Some respondents argued that consumers would benefit most if the OFT aimed to promote efficiency instead of competition, while one argued that the OFT's primary objective should be to facilitate innovation.

**A6.** The consultation document also suggested that the OFT should aim to avoid any material adverse effects of its actions on financial stability. This proposal was widely supported, with many respondents noting the importance of financial stability. The Royal Bank of Scotland noted the importance of financial stability in protecting consumers. However, the British Retail Consortium were concerned that safeguarding financial stability should not become an excuse for failing to tackle competition problems.

**A7.** The consultation document asked whether the OFT should be subject to a principle aimed at facilitating innovation and promoting efficiency. Responses to this question were mixed, with many respondents arguing that innovation and efficiency should result naturally from competition and that the OFT should have no explicit role. Other respondents stressed the importance of efficiency in payment systems. The British Bankers' Association argued that the OFT should be careful to not create barriers to innovation or efficiency and should aim to reduce or eliminate them.

**A8.** Many respondents noted the importance of the OFT acting proportionately. Most of the banks supported the introduction of a regulatory principle of proportionality and argued that the OFT should look carefully at the costs and benefits of its actions. Some respondents, including the retailers, questioned the necessity of such a principle, noting that the OFT is already subject to a general principle of proportionality. The Consumers' Association argued that it may be unnecessarily cumbersome to place a statutory duty on the OFT to do something it is, as a Government department, already required to do.

## OFT's powers and functions

**A9.** Responses were mixed as to whether the OFT's information gathering powers should include the power to enter premises. Several banks and

payment schemes argued that these powers would be excessive and would not be needed. Other banks and payment schemes, the retailers and the Consumers' Association argued that there is no reason why the OFT's powers should be different from those in the Competition Act 1998.

**A10.** Respondents held a wide variety of views about the OFT's ability to impose financial penalties. One respondent argued that the power to impose financial penalties was not necessary. Several respondents, including some banks, felt that the penalties relating to total turnover would be excessive and that they should instead be based on turnover deriving from payment system activities. Many respondents, including the British Bankers' Association, argued that the OFT should publish guidance on the appropriate level of penalties. The retailers argued that the OFT should be able to impose financial penalties high enough to act as a real deterrent to anti-competitive behaviour.

**A11.** The consultation document asked with which bodies the OFT should be permitted to share information. Many respondents, including some banks and payment schemes, agreed with the list of bodies proposed in the consultation document (the Bank of England, the FSA, the FOS, the Competition Commission, the European Commission, and other authorities who regulate those who provide payment services in the UK). Most banks argued that information should only be disclosed to other bodies in relation to their statutory functions. The Consumers' Association were concerned that any definition of commercial confidentiality should be carefully drawn to ensure that information is not unnecessarily withheld from the public domain.

## **Appeals process**

**A12.** Almost every respondent supported the proposal in the consultation document that the Competition Commission's Appeal Tribunals should be the first line of appeal from the OFT's enforcement decisions. Some respondents, including the Royal Bank of Scotland, noted that specialist staff with a good knowledge of payment issues would be needed. Some retailers were concerned that the appeals process should not become an excuse for failing to tackle the competition problems in payment systems.

## **The role of the Bank of England, the Financial Services Authority and the Financial Ombudsman Service**

**A13.** The consultation document asked in what circumstances the Bank of England should have a right to be consulted in relation to financial stability. It also asked whether the Bank's advice and/or the OFT's response should be published where publication would have no material adverse effect on financial stability. Several of the banks and payment schemes were keen for the Bank to be consulted in all circumstances. Others were content with the list of circumstances proposed in the consultation document. Both the British Bankers' Association and the Consumers' Association agreed with the list in the consultation document. The majority of respondents were content for the Bank's advice and the OFT's response to be published. Some respondents

noted the importance of not disclosing commercially confidential material, while others noted the importance of publication not threatening financial stability.

**A14.** The consultation document asked in what circumstances the FSA should have a right to be consulted and whether the FSA's advice and/or the OFT's response should be published. Many respondents agreed with the circumstances proposed in the consultation document. Some banks suggested that the FSA should be consulted in all circumstances. Some retailers argued that too onerous a consultation process may dilute the effectiveness of the new regime. The majority of respondents were content for the FSA's advice and/or the OFT's response to be published, although some mentioned that commercial confidentiality should not be breached. The FSA noted that they would expect to formulate their advice to the OFT in such a way that it could be published, and to pass any protected information relevant to this advice through a separate route not for publication.

**A15.** There was widespread support for the FOS introducing a voluntary regime for payment service providers from banks, payment schemes, consumer groups and retailers. The FOS responded noting its desire to expand its remit to provide comprehensive coverage of the financial services industry for the benefit of consumers.

### **Scope of the regime**

**A16.** The consultation document asked which participants in the provision of payment services should be subject to the regime, and whether it would be appropriate to include those who control access to point-of-sale terminal equipment. Almost every bank, several payment schemes, the retailers and the consumer groups argued that all participants in the provision of payment services should be subject to the regime. Some respondents noted the possibility that an exclusion could lead to payment services developing outside of the scope of the regime causing a distortion to competition. Many respondents, including the retailers, the Consumers' Association and some banks supported the inclusion of those who control access to point-of-sale terminal equipment.

**A17.** The consultation document also asked whether the aim in defining a payment service should be to include those services which have a primary purpose of facilitating the circulation of money or the transfer of funds. Most respondents, including banks, payment schemes and consumer groups, argued that the definition must be wide enough to allow for innovation and shouldn't be limited to a particular concept of payment.

**A18.** Responses were mixed about whether systems which are not used to provide retail payment services to end-users should be excluded from the scope of the new regime. Some respondents, including some banks and payment schemes, argued that systems not used to provide retail payment services to end-users should be excluded. CREST argued that there is no public interest requirement to include such systems in the scope of the

regime. Other respondents, including some banks and payment schemes, argued against explicitly excluding such schemes. Some noted that any payment service provider that has a material impact on end-users should be included. The Consumers' Association noted the logic in excluding systems operating within the wholesale market, while questioning the clarity of the dividing line with operations in the retail market. They suggested the inclusion of such systems in the regime, but on the limited basis of reporting and information gathering.

**A19.** Most respondents, including banks, payment schemes, consumer groups and retailers argued that payment systems which are used to pay a limited number of recipients should be included within the scope of the regime. Many respondents were concerned that an explicit exclusion could distort competition. Some respondents argued that there are currently no legitimate competition concerns about such systems, while others noted the possibility of the significance of such systems growing.

## **The new rules and their modification**

**A20.** The consultation document asked in what circumstances should the OFT be able to proceed with rule modifications without the consent of those subject to the rules. Most respondents, including some banks and payment schemes pointed to a reference to the reporting arm of the Competition Commission as the most suitable method for dealing with disputed rule modifications. Other respondents argued that the OFT should obtain consensus from all the affected parties before modifying a rule. Some retailers argued that the OFT should be able to unilaterally modify rules without the consent of those affected.

**A21.** The consultation document asked whether the threshold for application of the rules, apart from the price transparency rule, should be one based on the concept of material effect on competition. It also asked what should constitute materiality. There were a large variety of responses to these questions. Some banks and payment schemes argued that the thresholds for intervention should be the same as those under the Competition Act 1998. Other respondents, including some of the smaller banks, agreed with the materiality threshold, but noted that guidance on the application of the principle in practice would be needed. Some retailers suggested a threshold of 10 per cent, noting it would be simpler if the rules applied across the board. The Consumers' Association agreed that the threshold should be based on material effect on competition and argued that the definition of materiality should emerge through the development of guidelines.

## **Retail price transparency**

**A22.** Some respondents, including some banks, argued that for the sake of consistency the requirements for price transparency should extend not just to charges for payment services themselves but to other charges that are directly associated with the provision of the payment service. Other respondents argued that price transparency is unnecessary as the Banking

Code already mandates the provision of such information. The retailers and consumer groups were keen for all price information to be clear to end-users.

**A23.** The consultation document asked whether the rule on price transparency should be aimed at promoting price transparency by requiring the provision on a regular basis of the details for all payment services and other charges directly associated with those services. Many respondents, including some banks and consumer groups, noted the importance of providing consumers with enough information to make informed choices. Some responses also noted the importance of ensuring that transparency does not create confusion. Some banks and payment schemes argued that there is no need for more transparency as the area is already covered by the Banking Code. The Consumers' Association argued that the industry is unlikely to provide adequate information to consumers without some form of regulatory oversight.

**A24.** There was general support for the OFT being given the power to approve an industry code which could set out detailed price transparency requirements. Some respondents, including many banks, argued that the Banking Code would lead the way. Others, including some retailers, had little confidence that the industry would draw up an effective code.

## Publication of prices

**A25.** Many respondents supported the OFT having a power, but not a duty, to publish the terms and conditions, including prices, of retail payment services. Some pointed out the benefits of avoiding potential duplication in not giving the OFT a duty to publish such information. Some banks argued that the power was not necessary as such information is already in the public domain. Some of the retailers and consumer groups argued that the importance of information on payment services being available merits giving the OFT a duty to publish.

**A26.** The consultation document asked whether the OFT should be required to publish information on wholesale prices and/or how those prices are set where that would promote effective competition for the benefit of consumers. Responses to this question were mixed. Most of the larger banks and payment schemes argued that the publication of wholesale prices would not benefit consumers. Some of the smaller banks and the retailers argued that the publication of wholesale prices would help promote competition. The Consumers' Association argued there was no good reason not to require publication of wholesale prices.

## Efficient wholesale pricing

**A27.** The consultation document asked whether the rule dealing with efficient wholesale pricing should be aimed at requiring wholesale charges:

- to be derived through a published methodology based on legitimate costs

- to anticipate achievable cost reductions

where a failure to set prices on such a basis would have a material effect on competition.

**A28.** Most of the larger banks and payment schemes had reservations about this rule. Some argued that it is not clear how the setting of wholesale prices is damaging competition and had concerns that such a rule may dull incentives to innovate. Others argued that there is a range of economically justifiable wholesale pricing structures in any scheme and that identifying legitimate costs may prove very difficult. The retailers, led by the British Retail Consortium, strongly supported the proposed rule, and argued that it should not be hedged with the ‘material effect on competition’ condition.

### **Non-discriminatory access**

**A29.** Many respondents supported the rule dealing with non-discriminatory access being aimed at requiring participants to provide access on fair, reasonable and non-discriminatory terms where failure to do so would have a material effect on competition. Many of the banks and payments schemes noted the importance of financial stability concerns in access to payment schemes. The retailers argued for the importance of non-discriminatory access in opening the systems to competitive pressures but had some concerns about the requirement to provide access being limited to circumstances where failure to provide access would have a material effect on competition.

### **Good governance**

**A30.** The consultation document asked whether the rule dealing with good governance should be aimed at prohibiting the abuse of control, either individually or collectively, of a payment scheme where there was a material effect on competition. There was support for this from most of the banks, who expressed their preference for a rule prohibiting abuse of control rather than a prohibition of control itself. Some banks and payment schemes argued against the introduction of such a rule, considering it unnecessary. Both the retailers and the consumers’ groups supported the proposal in the consultation document. However, both also argued that the possibility of instituting a structural solution to the governance concerns identified in the Cruickshank report should be kept as an alternative in case the proposed behavioural solution does not deliver the desired result.

### **Co-operation in the development of payment services**

**A31.** The consultation document asked whether the rule dealing with co-operation should be aimed at requiring participants to co-operate in the development of payment services where:

- a) a failure to co-operate would have a material effect on competition;
- and

b) it is reasonable to require such co-operation.

It also asked in what circumstances it would be reasonable to require co-operation.

**A32.** Responses to these questions were mixed. Many respondents identified problems of developments in payment services being blocked by the players within payment schemes. Many banks and payment schemes were concerned about the OFT becoming too involved in regulating innovation in the payments industry, pointing out that while it may be reasonable to stop individual players blocking developments that would open competition bottlenecks, it would not be reasonable to force firms to incur irrecoverable expenditure. Many banks and payment schemes were also concerned that defining 'reasonable' co-operation would be difficult, and that the OFT should provide clear guidance on the rule's application. The Consumers' Association supported the proposed rule and argued that a definition of what is 'reasonable' should be arrived at by a combination of guidelines and the operation of the rule in practice. The retailers, led by the British Retail Consortium, were keen for the rule to develop in the light of experience of the new regime.

### Other rules

**A33.** None of the banks or payment schemes suggested any additional rules. One retailer predicted that the OFT will have to create new rules in reaction to manoeuvres in the market over the coming years.

### Regulatory Impact Assessment

**A34.** A number of respondents offered comments on the costs and benefits of the Government's proposals as estimated in the partial Regulatory Impact Assessment. Some banks questioned whether it would cost the payments industry 'appreciably less' to deal with the existing competition regulator, the OFT, rather than a new free-standing body. Some banks also questioned the analysis in the Cruickshank report upon which the partial Regulatory Impact Assessment drew. Some payment schemes questioned whether the benefits in the partial Regulatory Impact Assessment had been overstated and the costs understated.

## Appendix: List of responses received\*

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Abbey National  
Alistair Milne  
Alliance & Leicester  
Allpay.Net  
American Express  
Association for Payment Clearing Services  
Arcadia  
Bank of Scotland  
Banking Liaison Group  
Barclays  
British Bankers' Association  
British Cheque Cashers Association  
British Midland  
British Retail Consortium  
British Shops and Stores Association  
Campaign For Community Banking Services  
CLS  
Consumers' Association  
Credit Card Research Group  
Crest  
Dixons  
Financial Ombudsman Service  
Financial Services Authority  
Halifax  
HMV  
HSBC  
John Lewis  
Kingfisher  
Logica  
Marks & Spencer  
Nationwide  
PayPoint  
Peter Mair  
Post Office  
Royal Bank of Scotland Group  
Safeway  
Sainsbury's  
Selfridges  
Tesco  
VISA

\*3 responses were labelled confidential in their entirety and have not been included in the list.