

ATFS Bulletin January 2021 – Mastercard Interchange Increase

The News

Some of you will have seen the reports on the BBC website, in the FT and elsewhere this week. For those that haven't picked this up, Mastercard announced that from October, it will treat the UK as outside the EEA and will apply the same consumer card interchange rates to the UK that it does to the rest of the world. Currently, the UK is considered 'intra-regional', as opposed to 'inter-regional' going forward. For those that thought 'here we go again', you can rest easy. These increases only apply where a UK card is used to buy goods or services from a European Company. For once, the impact on the Higher Education is negligible; if buying using a card, Universities will typically be using a corporate card provided by their bank.

Some of the terms used above may be new to you, so it's worth explaining the basis. This will also be of interest to those of you looking to review or tender your card acquiring in 2021. Last year's WPM acquirer survey results showed that nearly half of the sector hadn't changed their acquirer in the last 5+ years, but also found that one-third of institutions said they plan to review their acquirer in the next twelve months. If you are one of those, any colleagues likely to be involved will find this bulletin useful as the survey also found that transaction costs and achieving "Value for Money" was the most important factor when choosing an acquirer.

Card Acquiring Basics

Different regions were referred to above. In terms of differences in pricing, for us here in the UK, the following apply:

- **Domestic:** Cards issued in the UK
- **Intra-Regional:** Cards issued in the EEA
- **Inter-Regional:** Cards issued anywhere in the rest of the world

Interchange is one of the three elements of the cost of a card transaction:

- **Interchange:** This is the fee that your acquirer will pay to the issuing bank; it is the same, regardless of who your acquirer is. Its level depends on the card type, how it is processed (including how securely) and where it was issued. Since 2015, this fee has been almost entirely based on the value of the transaction.
- **Scheme/Assessment Fees:** This fee is paid to the scheme to which the card belongs - primarily Visa and MasterCard. It is charged both on the value of the transaction and as a pence per transaction fee (PPT). Both elements vary considerably, depending on the broad card group e.g., Visa Debit, where the card was issued and how it is processed. Scheme fees across the acquirers are broadly similar, but the differences should not be ignored.
- **Processing Fee:** This third element is kept by the acquirer; it is the only element they have complete control over. It can also be charged on an ad valorem basis or by PPT and of course covers all acquirer costs.

These three pricing elements can be combined into three different pricing models:

- **Blended:** This combines the three elements into a price for each card or group of cards, sometimes including across all three regions of issuance and acceptance methods. With blending, the acquirer will earn a larger processing fee from some cards over others; this is hidden in the blend, so whilst blended allows for easy identification of individual card cost, it is the least transparent pricing model.
- **Interchange Plus (IC+):** This model combines the processing and scheme fees into a single fee, with interchange applied separately. This is clearly more transparent than blended, but some blending can still occur if a fee is charged across a group of cards where the individual levels of scheme fees are different, due to where the card was issued or how it is processed.

- **Interchange Plus Plus (IC++):** This is the most transparent form of pricing and the three elements are shown separately in the merchant statement. The lack of blending ensures the acquirer charges the same processing fee for every card transaction. Whilst transparent, the complexity of the merchant statement makes it more difficult to understand the cost of an individual transaction or card type.

There is a multitude of further charges when taking card payments, some will apply regardless of the pricing model you are being charged by and some only apply to blended pricing. Charges like, terminals, PSP costs for online payments, PCI-DSS and minimum monthly fees will apply regardless of the pricing model, but additional fees, depending on where the card was issued and how it is processed, can be applied to blended pricing as can additional charges for non-secure transactions.

How can we Minimise our Costs?

Pricing Model: The last six years has seen a significant shift across the sector. Some acquirers (not all, unfortunately) have been promoting IC++ as the preferred pricing model for the sector and to a lesser extent, IC+. ATFS (nee Finalysis) has also played a part; we have now competed over 100 reviews and tenders across the sector, working closely with Finance and Procurement Teams. The 2020 WPM acquirer survey also showed the pricing model split: IC++ at 62%, IC+ 12% and blended 26%. This is much improved, but there is still work to be done.

Introduce Dynamic Currency Conversion (DCC): For the uninitiated, in simple terms, DCC is the process that allows the cardholder to pay in their own currency, as opposed to Sterling. From the University's perspective, this is a process that allows it to reduce its acquiring costs through benefiting from the foreign exchange transaction that takes place when it receives Sterling, but the cardholder has paid in their own currency. The transaction involves a foreign exchange transaction and the DCC process allows the university to receive a proportion of the value of the foreign exchange spread built into the transaction. All Universities can benefit from DCC; this enables acquiring costs to be reduced as well as allowing the student to pay in their own currency. The largest Universities we've worked with receive a rebate of over £100k – a significant reduction to their costs.

There are several points worth noting. Firstly, for the cardholder the DCC process is voluntary; forcing it is against card scheme rules and there are several points within the payment process where the cardholder can decline. Secondly, the reader should note the foreign exchange deal occurs regardless of the choice made by the student at the time of the transaction. With DCC, the cardholder has some control over the process and will know at the time of the transaction what exchange rate is applied. If Sterling is chosen, the rate will only be known when the card statement is received, or the account viewed online.

There is a range of factors affecting the financial benefit of DCC, including the student nationality mix and the different approach of each acquirer. Further detail on this may be the subject of another bulletin later in the year.

Many Universities already benefit from the provision of DCC, but we have found multiple instances where the conversion level has been below the sector average. Reasons can include turnover of staff, poor staff training or lack of online visibility to the cardholder. Accordingly, it is just as important to ensure that the DCC uptake keeps at the expected level as it is to introduce it in the first place.

Summary

Whether to review and negotiate or test the market through a tender process will depend on the current situation at your institution, the level of service from the existing acquirer and the preference of Procurement. A tender process is often preferred if there is dissatisfaction with the level of service, whereas reviews are seen where the relationship is fine, but there is uncertainty over the pricing. Regardless of which side your institution sits, doing nothing is not really an option.

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