



Link Scheme Holdings Ltd

## LINK Interchange Report 2023

6<sup>th</sup> September 2023

### Public

This Report sets out LINK's approach to interchange for 2024, as agreed at a meeting on 6<sup>th</sup> July 2023 of the Board of Link Scheme Holdings Ltd.

This report is in three sections:

1. LINK's Interchange Fee Strategy – How Interchange Fees are Set.
2. Approach to Interchange Transparency.
3. The Annual Interchange Notification for 2024.

In setting Interchange Fees, the Board follows all of the requirements of the Members' Agreement (this is the agreement between LINK and all of its membership on how interchange is set). This report does not seek to amend or vary the Members' Agreement in any way and Network Members should seek their own legal advice in relation to any questions that they may have with regards to the Members' Agreement (or otherwise).

### 1. LINK's Interchange Strategy – How Interchange Fees are Set

The Members' Agreement between LINK and Network Members sets out how Interchange Fees are set. It reflects the collective strategy of LINK and Network Members in relation to interchange, as approved by Network Members and LINK. In setting Interchange Fees, LINK is careful to follow the Members' Agreement. LINK's decision-making powers in relation to Interchange Fees are limited to what is specified in the Members' Agreement.

Interchange Matters are covered in the Rate Card, which is an appendix to the Members' Agreement. The Rate Card does not contain a prescriptive methodology. Rather, it requires the Board to give careful consideration in the round to a number of factors.

In terms of timing, the Board may review and change interchange at any time. This is set out in paragraph 6.5:

- *At any time following the Annual Interchange Notification in respect of the Interchange Fee for a calendar year, HoldCo<sup>1</sup> may, taking account, inter alia, of the Interchange Matters, revise the Interchange Fees for that calendar year by not less than two (2) months' notice to Network Members (such notice being, the Interim Interchange Notification).*

However, the Board is also required to review and set interchange annually. Paragraph 6.4 sets out the procedure for this annual review as follows:

- *Following the completion of the Cost Study, HoldCo shall, taking account, inter alia, of: (i) the Cost Study, (ii) the Objects, (iii) the Regulatory Framework; (iv) the Board's objective of the maintenance of a satisfactory geographical spread of free-to-use ATMs and Counter Terminals in the UK; and (v) the Access to Cash Objectives (together, the*

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<sup>1</sup> HoldCo is Link Scheme Holdings Ltd.



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*"Interchange Matters"), set the Interchange Fees for the next calendar year. Prior to the end of July of each calendar year and following the decision of HoldCo pursuant to this paragraph, SchemeCo<sup>2</sup> shall notify (such notice being, the "Annual Interchange Notification") the Network Members of the Interchange Fees for the next calendar year (as determined by Holdco in accordance with this paragraph).*

Described below are each of the factors set out in paragraph 6.4.

LINK currently carries out this review at the July Board meeting each year. At that meeting, the Board gives careful consideration to the factors specified in paragraph 6.4, together with any other factors that it considers relevant. LINK will also review interchange as it feels necessary at other times, but there are no specific dates or events that will trigger a review. The Board notes that changes in cost will in due course show up in the Cost Study analysis and that this will provide further data for the Board's consideration when it sets Interchange Fees in July.

Past events have sometimes triggered an interim review. For example, LINK has at times considered the effects of changes to Base Rate at interim reviews. It has done this when the Board considers that the Base Rate change could be significant enough to affect achievement of its objectives, typically at times of heightened economic uncertainty. For example, LINK did not reduce Interchange Fees with falls in Base Rate at the start of the pandemic. LINK has, however, sometimes increased Interchange Rates with rises in Base Rate, both the main Rates and Protected Rates. Given the sustained satisfactory position of the ATM footprint, which is reviewed at each Board meeting, LINK sees no case currently for regular interim reviews. Directors can request an additional review at any time, should events require that.

### **The Cost Study**

This is item (i) in the Rate Card extract above. When the changes to setting interchange were introduced in 2018, it was decided to maintain the Cost Study. This is to give LINK insight into the costs of the network, as there is no other ready source of this sort of cost data. This is valuable for a number of reasons including:

1. It allows LINK to judge the effects of market events on average costs periodically.
2. It allows LINK to assess the commercial viability of deployers, which is important for judging resilience of the payment system.
3. It allows LINK to make judgements on the cost effectiveness of alternative mechanisms to deploy ATMs such as Direct Commissioning.

### **The Objects**

Item (ii) LSHL's Objects are contained in its Articles of Association. While they do not refer to interchange, they broadly support the orderly running of LINK and are set out below for reference:

- *to promote adherence to and compliance with such agreements forming part of the Link Scheme as may be in force from time to time;*
- *to maintain the operation of the LINK Network in the United Kingdom in an efficient, accessible, competitive, innovative and sustainable manner;*

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<sup>2</sup> SchemeCo is Link Scheme Ltd.



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- *to promote continuous improvement and updating of the LINK Network within the United Kingdom;*
- *to put in place and oversee the appropriate infrastructure and other resources to deliver the LINK Scheme and to ensure the resilience of the infrastructure;*
- *to facilitate the operation of a wide range of business models in the provision of access to cash through the LINK Network in the United Kingdom;*
- *to support the stability of the financial system in the United Kingdom with due regard to the CPSS-IOSCO Principles for Financial Market Infrastructures or such equivalents as may be recognised in future;*
- *to carry out detailed research in furtherance of the Objects;*
- *to promulgate, develop and protect the LINK Scheme brand or such other brands as may in future complement or replace it;*
- *to improve public, government and industry understanding of the role and contribution of the LINK Network within the United Kingdom financial sector and the United Kingdom economy;*
- *to represent the LINK Network in the United Kingdom to government, regulators, policy makers, industry and the public;*
- *to promote innovation and competition in the provision of payment services for the benefit of end-users;*
- *to carry on business as a general commercial company; and*
- *to do all things necessary for and incidental to the advancement of the above Objects, having always due regard to the public interest.*

They allow the Board to consider an extensive range of relevant factors when setting interchange. For example, there are references to maintaining stability, resilience and sustainability that directly support arguments that interchange needs to attract and sustain a broad membership.

### **The Regulatory Framework**

This is item (iii). As well as considering general regulatory requirements, relevant here are LINK's responsibilities under the PSR's Specific Direction 12. This requires LINK to take effective measures to meet its voluntary access to cash commitments. LINK has committed to maintain the geographic footprint of free-to-use ATMs in line with the position as at 1<sup>st</sup> February 2018 when interchange was reformed (referred to in this paper as the "reform changes" or the "reform"). These commitments are set out in the next section of the note. LINK reviews how it is achieving its commitment through its Footprint Review, which is currently part of every Board meeting.

### **Access to Cash**

A very important factor when setting interchange is whether it is helping LINK achieve its access to cash objectives. Items (iv) and (v) build in LINK's access to cash objective into the setting of interchange.

Item (iv) brings in the concept of "geographic spread" (the Board more often uses the term "Footprint"). It also sets out that the Board will consider Counter Terminals as well as ATMs as potentially acceptable sources of cash access. Although LINK does not treat Counter



Terminals as an alternative to ATMs at the moment, this wording would support that should it ever be desired.

Item (v) brings in explicitly the “Access to Cash Objectives” concept which are defined in the Members Agreement (in the Definitions section) as:

- *to maintain the broad geographic spread of ATMs as at 1 February 2018 and/or as the Board otherwise considers appropriate to enable free access-to-cash across the Home Territories; and*
- *to maintain and, in some instances, improve free access to cash in the most deprived areas of the Home Territories; and*
- *such other objectives as the Board may consider are in the pursuit of the public interest in relation to access to cash.*

## 2. Approach to Interchange Transparency

### **LINK’s Access to Cash Commitments**

In terms of access to cash, LINK has chosen to make a number of commitments that form part of the access to cash objectives referenced above. Although LINK may change these commitments at any time, it is committed to full transparency. For example, the material is available on LINK’s public website. These commitments are also within the scope of the PSR’s Specific Direction 12, which places a number of constraints on their reporting and development. The commitments are as follows<sup>3</sup>:

- *“In LINK’s Final Decision and Impact Assessment on the results of its Interchange Consultation, published on 31<sup>st</sup> January 2018, the Board of LINK set out its commitment to maintain free access to cash for many years to come through an extensive footprint of ATMs with the same coverage as now.*
- *The date of this commitment started from 1<sup>st</sup> February 2018. This included a commitment to leave interchange unchanged for all existing free ATMs 1 kilometre or more away from another free ATM, to ensure that LINK’s reduction in interchange would not give a reason for closure.*
- *These ATMs are known as Protected ATMs. This also initially included a commitment to apply at LINK’s discretion a premium of up to 30 pence to deal with specific problems with free coverage of ATMs caused by loss of a Protected ATM. On 1<sup>st</sup> April 2019, LINK introduced additional premiums that can significantly increase payments to ATM operators by up to £2.75 per cash withdrawal. Premiums will be made available to all eligible Protected machines; these measures are aimed at safeguarding free-to-use ATMs in remote and rural areas.*
- *Should these premiums not deal with a particular situation, then LINK has the ability to directly commission ATMs to provide free access.*
- *The Board has decided to publish the total number of Protected ATMs and the number where free access has been removed through closure or by being turned into charging ATMs. Reports will be provided on a regular basis.*
- *The reports will set out an analysis of the number of Protected ATMs no longer transacting and, after identifying where there is alternative access to cash provision (such as a Post Office counter providing free cash access), and where there is no public impact*

<sup>3</sup> This text is taken from the “LINK Scheme ATM Footprint Reports” that are published on LINK’s website each month and that meet requirements under the PSR’s Specific Direction 12.



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*(for example, because the site was not accessible to the general public, e.g. it was within a closed company site), it shows the resultant number of sites that will be targeted for replacement with premiums.*

- *Note that where the loss is due to a security reason such as a raid, and there are no willing site owners, LINK will not plan a replacement until the security situation is judged safe again by local site retailers and ATM operators.*
- *In addition to this, LINK also publishes on its website the number of free and charging ATMs by parliamentary constituency.”*

The reform changes also set out the need to consider the competitive position of LINK in relation to other schemes, and the need to manage the risk of ATMs becoming concentrated in parts of the country.

Each Board meeting currently considers a Footprint Report that is designed to answer the question “*is LINK meeting its commitments*”. A similar report is provided to the PSR each month as a requirement of Specific Direction 12. This is also published on LINK’s website. The position has been satisfactory since LINK’s reforms were introduced in 2018.

This is a historic view, so LINK also looks forward with a forecast that is publicly available in our Strategic Plan. LINK uses the Cash Usage Forecasts published by UK Finance in its UK Payment Markets report to derive its forecast. LINK forecasts out to 2031 and estimates that there will be around 13,000 free remote ATMs at this point. We also estimate that the lower limit needed to meet our commitments is about 10,000. The aim of this analysis is to assure the Board that overall coverage will not drop below the number of machines necessary to cover the UK satisfactorily and in line with LINK’s commitments. The forecast is not a target, rather an analysis to understand the forward shape of the Footprint and whether it is consistent with LINK’s objectives.

As part of considering Interchange Fees, the Board decides the appropriate levels of interchange for other relevant channels, including the Counter Terminal channel. As this is still an establishing service, the Board’s decision has been to set the various types of Counter Terminal interchange at the same levels as for ATMs. This will help allow the channel to develop before deciding if to diverge from ATM interchange levels or not.

### **The Cost Study**

The Cost Study shows average costs. The Board does not have a target for the gap between Interchange Fees and average costs.

However, at the time of the 2018 interchange reforms, LINK’s analysis was that a 20% gap was needed to correct “*that free ATMs will continue unnecessarily to be concentrated in busy urban centres but become less viable in less busy communities, hence reducing geographic access to cash*”<sup>4</sup>. LINK bears this in mind when considering the Cost Study, in the assessment of Interchange Fees.

The table below compares the actual Interchange Rates compared to the comparable average costs as calculated by Cost Studies (excluding Protected Interchange, as the Cost Study does not calculate average costs for Protected ATMs given the small numbers).

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<sup>4</sup> [h-documents uploads - link-interchange-decision-31-january-2018.pdf](#)





Difference between actual interchange rates and rates from the previous year's Cost Study 2020-24

Category of interchange	2020	2021	2022 Jan - Aug	2022 Aug - Dec	2023	2024
Branch cash	-15%	-24%	-46%	-43%	-45%	-41%
Branch non-cash	-22%	-32%	-51%	-51%	-53%	-44%
Non-branch cash	-10%	-11%	-18%	-16%	-8%	-15%
Non-branch non-cash	-9%	-10%	-18%	-18%	-9%	-5%

It shows that actual interchange has been lower than average costs across all of the main categories for the last few years. This is as expected, as the reduction in interchange against the average cost at the time was one of the building blocks of the reform.

Actual branch Interchange Rates are far lower than average costs because volumes have fallen significantly but operators' costs have remained broadly the same. By contrast, at remote sites, while volumes have also fallen there have also been significant reductions in costs. This in part reflects the strong incentive for remote deployers to reduce costs to drive profitability, while branch ATMs are part of an overall package of overhead costs and have less scope for cost reduction.

Weighted rates are useful as they reflect the overall effect of the various components of Interchange Fees. This is shown in the next table. Weighted rates blend standard interchange with Protected Rates and Premiums on a weighted basis. The data is taken for January each year, as this is when LINK's annual review of Interchange Fees comes into effect. For example, when compared to weighted Remote Cash, the current difference with average costs is -9%.

Weighted average interchange rates, 2020-2024

	Remote Cash Interchange Rates				
	Standard pence	Weighted Average pence	Cost Study pence	Standard is less than Cost Study by	Weighted Average is less than Cost Study by
January 2020	25.9	26.8	28.7	-10%	-7%
January 2021	25.9	27.6	29.2	-11%	-6%
January 2022	25.9	27.5	31.6	-18%	-13%
January 2023	26.5	28.4	28.8	-8%	-2%
January 2024	26.5	28.4	31.0	-15%	-9%

**How Specific Cost Categories are Changing**

The following tables are taken from the Cost Study, comparing remote cost categories and how they have changed from 2019 to 2023. Occupancy and rates, including market rent, had the largest drop at 3.4p. LINK's view at the time of the reform of interchange was that the excessive deployment encouraged by the original approach to focus solely on the Cost Study was driving up market rents for the benefit of retailers rather than IADs. This data is evidence that LINK's view was correct. Other costs have generally shown increases and the overall change is an increase in average cost from 28.7p to 31.0p (8%).



Interchange figures, Remote ATMs, 2019 and 2023 Cost Studies

Cost per transaction (pence)	Remote ATMs		
	2019	2023	Variance (p)
ATM purchase and installation	2.0	2.3	0.3
Occupancy and rates, including market rent	8.5	5.1	-3.4
Repairs and maintenance	2.6	3.4	0.8
Communication costs	0.4	0.6	0.2
Daily operational support, IT and central support	3.3	4.6	1.3
Cost of capital	1.3	1.2	-0.1
Group overhead adjustment	0.2	0.5	0.3
<b>Total non-cash cost</b>	<b>18.4</b>	<b>17.7</b>	<b>-0.7</b>
Cash purchase, delivery, handling, management, insurance and theft	8.8	10.7	1.9
Opportunity cost of cash	1.5	2.6	1.1
<b>Total cost</b>	<b>28.7</b>	<b>31.0</b>	<b>2.3</b>

**Interchange Rates**

The tables below show the rates (including Protected rates) applied to LINK transactions. The final column of the first table compared the current figures to those in early 2018 when the previous year's Cost Study was still being used. All of the rates have reduced between 3% and 10% since 2018.

However, a number of Protected ATM rates have increased. As well as Protected rates, a number of machines receive volume Premiums of up to £2.75. Although the numbers of machines involved are small (about 3,500 out of 25,000 remote ATMs) there is a material increase in weighted average interchange.

Standard interchange rates 2018-2024

Interchange Standard pence	2018 Jan - Jun	2018 July - Oct	2018 Oct- Dec	2019	2020	2021	2022 Jan - Aug	2022 Aug - Dec	2023	2024	Variance to 2018 %
Branch cash	25.1	23.8	24.3	23.1	23.1	23.1	23.1	24.4	24.4	24.4	-3%
Branch non-cash	13.9	13.2	13.2	12.5	12.5	12.5	12.5	12.6	12.6	12.6	-9%
Non-branch cash	28.3	26.9	27.3	25.9	25.9	25.9	25.9	26.5	26.5	26.5	-6%
Non-branch non-cash	18.7	17.8	17.8	16.8	16.8	16.8	16.8	16.8	16.8	16.8	-10%

Protected interchange rates 2018-2024

Protected - from (Pence)	2018 Jan	2018 Oct	2022 Oct	2022 Dec	2023 Feb	2024 Jan
Branch cash	25.1	25.6	26.2	26.8	27.4	27.4
Branch non-cash	13.9	13.9	13.9	13.9	13.9	13.9
Non-branch cash	28.3	28.7	29.3	29.9	30.5	30.5
Non-branch non-cash	18.7	18.7	18.7	18.7	18.7	18.7



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### **Summary of Main Data Taken into Account in Setting Interchange Fees for 2024**

LINK is committed to protecting free access to cash for consumers. It will do whatever it takes to maintain satisfactory national access and uses a range of data to regularly check the position. A summary of this data is set out below:

- The Board considers the Footprint satisfactory and that it is expected to remain so. By April 2023, Protected ATMs had increased to 3,374 (8.7% of the total number of free machines). The cost of Protected Interchange and Premiums was £15.6m or 4.4% of all interchange in 2022.
- Only 51 of the Protected ATMs in scope for replacement had not been replaced by Direct Commissioning. These are explained through factors such as poor site availability and security issues, and are consistent with LINK's Policies.
- The current rate of decline in free ATM numbers is not a cause for concern. In 2022, total free ATM numbers fell from 40,942 at the start of the year to 39,429 (-3.7%), free remote ATMs fell from 27,287 and 26,888 (-1.5%) and branch ATMs from 13,655 to 12,541 (-8.2%), driven by bank branch closures. By May 2023, the total number of free ATMs at 38,766 evidences a similar rate and is not a cause for concern.
- LINK has forecast a reduction in free ATM numbers out to 2031 and this estimates there will be around 19,500 free ATMs at this point and that this can provide satisfactory coverage.
- LINK takes a multichannel approach to cash access and currently counts Post Office Counters as an alternative to a free-to-use ATM. The extension of the Banking Framework to support this service gives LINK confidence in this strategy. In addition, cash at the till is now available through LINK, and through other card schemes whose members are also offering a cashback without purchase service. LINK therefore sees evidence of the resilience of the cash supply network being maintained.
- The Cost Study tracks the average cost per transaction. LINK notes that the difference between average cost and interchange for remote cash and non-cash in 2023 is 15% and 5% respectively. The differences have not been more than 18% since the reforms in 2018 (when LINK assessed that a 20% reduction from average costs was required, although subsequently only two 5% reductions were made).
- For Remote Cash, the difference between average costs and weighted interchange (this blends the standard, Protected and Premium rates) is currently smaller than the unweighted equivalent. The current difference is -9%.





### 3. The Annual Interchange Notification for 2024

The following table summarises the Interchange Notification for 2024 that is sent to Network Members.

**Interchange Rates – Table 1**

	Rate Effective 1 <sup>st</sup> January 2024	
	<i>ATMs (other than Protected ATMs) and Counter Terminals</i>	<i>Protected ATMs</i>
<b>Branch ATMs</b>		
<i>Sterling Cash Withdrawals</i>	24.4	27.4
<i>Enquiry</i>	12.6	13.9
<b>Non-Branch ATMs</b>		
<i>Sterling Cash Withdrawal</i>	26.5	30.5
<i>Enquiry</i>	16.8	18.7

#### Premiums

#### LINK Policy on Financial Inclusion ATMs – Deprived Areas and Low Volume Premiums – Tables 2a and 2b

Monthly Cash Withdrawal Transactions Volumes	Premium Awarded (pence)
0 – 199	£2.75
200 – 399	£0.81
400 – 599	£0.43
600 – 1,500	£0.30
1,501 – 3,000	£0.20
3,001 – 4,500	£0.10
4,501+	No Premium

#### LINK Policy on Protected ATMs – Protected ATM Premiums – Table 2c

Monthly Cash Withdrawal Transactions Volumes	Premium Awarded (pence)
0 – 1,500	£0.30
1,501 – 3,000	£0.20
3,001 – 4,500	£0.10
4,501+	No premium