Zita Wéber and Judit Brosch: Can cash payment be limited in a modern payment system?*, [1]

Is it acceptable that festivals allow payment by festival cards only but not by cash, and that some airlines will sell you flight tickets only if you use your bank card to purchase online? In connection with the interpretation of the legal tender status of banknotes and coins, different views have been voiced in recent years: whether cash or certain denominations of banknotes and coins (large-denomination banknotes, small-denomination coins) can be rejected as means of payment for products or services; whether it is acceptable that a product or service can be paid only through electronic payment instruments, and whether cash surcharges can be applied. In the opinion of the Magyar Nemzeti Bank as the body responsible for the issuance of forint banknotes and coins, the legal tender status of banknotes and coins does not mean their obligatory acceptance for payment under all circumstances. In this article, we provide an overview of the various approaches to the legal tender status and present the technical arguments which we believe support the position of the MNB.

INTRODUCTION

In the past decade, the advance of modern information technologies has led to the spread of new electronic forms of payment. As with any innovation, new solutions give rise to new questions. It is no different in the case of payment instruments. Because of the widespread use of electronic payment instruments, private persons have approached the MNB as the entity responsible for the issuance of money on several occasions. They complained that they had been unable to purchase certain products or services with cash; they had to use some electronic payment instrument, mostly a bank card. To mention but a few examples: organisers of increasingly popular festivals like to issue festival cards that can be loaded using cash or bank cards at the festival location; this (and only this) card can be used by festival visitors for payments; some airlines allow flight tickets to be paid only through the internet using bank cards; recently a café was opened accepting bank cards but not cash. In all these cases, the question was whether it was legitimate for retailers to refuse cash, so that persons wanting to purchase the product or service concerned need to have a bank card or need to load the card issued by the event organizer for the purpose of payment.

It is no coincidence that the issue of mandatory acceptance of cash has been raised just now. New non-cash payment instruments have become common; in some market segments their use has become so widespread that retailers are no longer afraid that their competitiveness will suffer if they accept only cashless payment. For them, this is safer and cost effective; for their customers, it is safer, cheaper and more convenient.

When cash was the only possible means of payment for daily purchases, the provision of the Central Bank Act governing the legal tender appeared to be self-explanatory.[2] Today we can choose from among several electronic payment methods (deposit card, credit card, pre-paid card, reloadable card, mobile payment, online payment, etc.). This situation has put the provisions of the Central Bank Act on legal tender in a new perspective and raised questions: What does the legal tender status of banknotes and coins mean? Is it compulsory to always accept any denomination of banknotes and coins qualified as legal tender?

The European Commission has also addressed these issues and other questions relating to legal tender and issued a recommendation[3] on this subject in 2010. The position of the MNB on the mandatory acceptance of legal tender is different from the recommendation of the European Commission. The subject is particularly topical as the Commission is expected to follow up on the implementation of the recommendation in the first half

* The views expressed in this article are those of the author(s) and do not necessarily reflect the offical view ot the Magyar Nemzeti Bank.

[1] We would like to thank Dr Ildikó Szeder Gubek for her useful legal comments.

[2] Act CCVIII of 2011 on the National Bank of Hungary, Article 27 (2).

[3] Commission Recommendation of 22 March 2010 on the scope and effects of legal tender of euro banknotes and coins (2010/191/EU).

of 2013 and assess the need for any additional, legally binding legislation.

From a legal aspect, we can establish that the retailer's refusal of cash payment and its practice of accepting electronic payment instruments only does not violate the provisions of the Central Bank Act. In this study, we examine the meaning of legal tender status, review the legislation of various countries to the interpretation of legal tender and present the considerations that led the MNB – as the entity exercising the right of issuer – to adopt its position.

Box 1
Limitation of use of banknotes – Constitutional Court's resolution

With the spread of ticket machines and vending machines accepting only coins, the question of interpretation of the concept of legal tender arose quite some time ago. In this context, the Constitutional Court adopted the following position in response to a complaint from a citizen to the effect that banknotes are also legal tender and that they must also be accepted as payment by operators of parking meters:[4] the "provision[5] [in the Central Bank Act] does not rule out the possibility that the special characteristics of the various payment methods shall prevail, within reasonable limits, when making payment for various goods or services. Instances where payment can be made, alternatively or exclusively, at a machine is a special payment method".

DEFINITION OF CASH AS LEGAL TENDER IN THE CENTRAL BANK ACT AND IN THE VIEW OF THE MNB RESPONSIBLE FOR THE ISSUANCE OF CASH

In Hungary, the MNB has the right and responsibility to issue banknotes and coins. In respect of the issue of cash, the Central Bank Act contains the following key provisions:

> *Article 4 (2) The MNB shall be entitled to issue banknotes and coins. Banknotes and coins – including commemorative banknotes and coins – issued by the MNB shall be legal tender of Hungary.*

> *Article 27 (1) The Governor of the MNB shall declare in a decree the issue of banknotes and coins, their denominations and distinguishing features and their withdrawal from circulation. The banknotes and coins withdrawn from circulation shall lose their function as legal tender as of the date specified in the decree of the Governor of the MNB.*

The Central Bank Act provides the following on the acceptance of cash:

> *Article 27 (2) Each person shall be obliged to accept banknotes and coins issued by the MNB at face value for payments to be made in official Hungarian currency until withdrawal.*

This provision imposes the obligation to accept legal tender at face value, i.e., if the payment is made in cash, banknotes and coins shall not be accepted at a value different from their face value (e.g. a 100-forint coin for the value of 90 forints), while the provision quoted contains no obligation as to the payment method. Nevertheless, in our experience, the private persons complaining to the MNB as issuer about their inability to pay with cash interpret Article 27 (2) of the Central Bank Act as requiring everyone to accept cash for payment, that is, payment with any denomination of banknotes or coins should be possible under all circumstances.

Incidentally, the Central Bank Act itself also contains provisions limiting cash payment to the effect that the acceptance of coins in unlimited quantities is not obligatory when cash payment is accepted. That is, economic agents other than credit institutions and post offices are allowed not to accept more than 50 coins in a single payment.

> *Article 27 (4) For cash payments, including cash payments to a payment account, credit institutions and institutions operating the postal clearing centre shall be obliged to accept more than 50 coins.*

[4] Resolution No. 1063/B/2005. of the Constitutional Court.
[5] Act LVIII of 2001 on the National Bank of Hungary, Article 31 (2) as effective at the time.

CONCEPT OF LEGAL TENDER IN THE LEGISLATION OF DIFFERENT COUNTRIES

Other countries have also given consideration to the interpretation of the concept of legal tender in their acts on the status of central banks or in other financial legislation. In 2010, the European Commission set up an expert group with the participation of the euro-area Member States to discuss this issue. They established that there were only a few Member States that had financial legislation to define the elements of the concept of legal tender, the reason being that national legislation consider this concept to be 'generally accepted'.[6] In contrast, outside the euro area, typically in Anglo-Saxon countries, there are examples where the national legislation on legal tender is more detailed and the central bank of the country provides additional interpretation of the rules, publishing its position on its website as the case may be.[7]

Elements of the concept of legal tender

The comparison of the legislative provisions and interpretations of the countries reviewed concerning legal tender shows that the following three elements of the concept of legal tender are present in the laws of most countries.

Standardised medium of payment protected by the state

Legal tender is a standardised medium of payment issued by the body authorised for this purpose[8] in the denomination structure corresponding to the requirements of cash circulation. The issuer determines its physical appearance and characteristics, issues it as a means of payment for payment transactions, withdraws it from circulation and protects it against counterfeiting with a number of laws and printing processes. In modern economies, a standardised cash system is a precondition for smooth payment transactions.

Acceptance at face value

It is an important feature of the legal tender, that it must be accepted at face value. This is stated in the legislation of several countries.

Power to discharge monetary debt or obligation

The legal tender is the instrument for the payment of monetary debt and obligations. Creditors may not refuse the settlement of debt or obligations in cash except where the parties agreed on other means of payment. A debtor discharges a debt by transferring a means of payment with legal tender status to creditor.

Acceptance of legal tender – can cash be rejected for payments?

There is also general consensus that the choice of the payment method or instrument to be used for payment depends primarily on the agreement between the parties, just as the specification of other terms of payment (time, location, etc.).

This follows from the principle of contractual freedom, which means that the contractual parties are free to decide whether to enter into contract and agree on all material terms. In the scope of transactions between economic entities (B2B transactions), the primacy of contractual freedom is easy to understand as agreeing on the terms and payment method is part of the bargaining process.

By contrast: in a retail transaction, would a retailer be obliged to accept cash payment when a customer insists on paying in cash or based on contractual freedom may the retailer decide not to make a deal (informing customers in advance that only cards are accepted at the shop)? In other words: does legal tender mean that it must be accepted at all times, except where the parties agreed upon the use of a different payment method or payment instrument in advance? On this issue, the position of the Anglo-Saxon countries and four euro-area Member States (Finland, the Netherlands, Ireland and Germany) is different from the view of the majority of euro-area countries.

The U.S. legislation defines legal tender as follows: "United States coins and currency are legal tender for all debts, public charges, taxes, and dues."[9] In other words, the legal tender status means obligatory acceptance only in respect of payments under contracts already concluded, discharging existing debt or obligations (naturally except in cases where parties had previously agreed to use some other payment method or payment instrument). The relevant British

[6] ELTEG (2010).

[7] http://www.federalreserve.gov/faqs/currency_12772.htm, http://banknotes.rba.gov.au/legaltender.html, http://www.royalmint.com/aboutus/policies-and-guidelines/legal-tender-guidelines

[8] Central banks are authorised to issue banknotes, while in a number of countries the Ministry of Finance has the right to issue coins.

[9] Article 31 U.S.C. 5103 of Coinage Act of 1965.

legislation also contains a similar provision in respect of the discharge of debt in legal tender.[10]

Based on these rules, the central banks of Anglo-Saxon countries have clearly taken the view that retailers may not be obliged to accept cash unless debt has been incurred. "There is, however, no Federal statute mandating that a private business, a person, or an organisation must accept currency or coins as payment for goods or services" – the Fed interprets the legal tender provisions of the Coinage Act on its website.[11] On the website of the Australian central bank a similar position is stated.[12]

Four of the euro-area Member States (Finland, the Netherlands, Ireland and Germany) are also of the opinion that the legal tender provision applies to contracts already concluded; therefore, the retailer is not obliged to accept cash as payment for products or services.[13] Under the regulations effective in the Netherlands, a retailer may refuse the use of cash for making payment if it is clearly posted at the entrance of the shop that only cards are accepted for payment.

According to the majority of euro-area Member States (with the exception of the four countries mentioned previously), however, the retailer is obliged to accept cash if the customer wants to pay in cash. This view is reflected in the Commission recommendation referred to above, which states in point 2: "The acceptance of euro banknotes and coins as means of payments in retail transactions should be the rule. A refusal thereof should be possible only if grounded on reasons related to the 'good faith principle' (for example the retailer has no change available)".[14] They explained their position arguing that while in B2B transactions the parties are deemed to have an equivalent negotiation power, therefore the choice of the payment method and payment instrument may be based on contractual freedom, in business to consumer (B2C) relationships the bargaining positions of the parties are not equivalent, therefore the principle of contractual freedom can be limited. In other words, retailers cannot decide at their discretion and they must accept cash if the customer insists on paying in cash.

As the introduction stated, the MNB as issuer has adopted a position close to the views of Anglo-Saxon countries and the four aforementioned Member States[15] in considering that the acceptance by a retailer of only electronic payment instruments to pay for a product or service is not against the Central Bank Act. Even though the exclusive acceptance of electronic payment methods may be constrained by civil law or consumer protection considerations in certain cases, the examination of those considerations is beyond the competence of the MNB.

In the following, we look at the considerations behind the MNB's decision to promote electronic payment instruments and not to prohibit their exclusive use.

BENEFITS OF ELECTRONIC PAYMENT INSTRUMENTS FOR THE NATIONAL ECONOMY

Electronic payment methods have a number of benefits over cash payment; in the following, we highlight three of these. The traceability of transactions, efficiency and security are the key reasons that electronic payments are more beneficial for society than cash payments. Using these three dimensions, we present the features of cash that lead to restrictions on the acceptance of cash in European countries including Hungary. We also discuss cases where the rule applied does not limit the use of cash payment generally, only the acceptance of certain denominations of coins or banknotes.

Restriction of the use of cash to combat the shadow economy

Cash is anonymous; this is why it is the ideal means of payment in the black economy. In recent years, the MNB has published several studies analysing the causes of the high cash usage in Hungary in international comparison,[16] concluding that the high cash intensity of the Hungarian economy was partly due to the shadow economy as cash transactions are easier to conceal from the tax authority. For reasons of whitening the economy and combating illegal activities, the MNB has urged the restriction of the use of

[10] Legal tender has, however, a very narrow technical meaning in relation to the settlement of debt. If a debtor pays in legal tender the exact amount he/she owes under the terms of a contract (and in accordance with its terms), or pays this amount into court, he/she has good defence in law if he/she is sued for non-payment of the debt. http://www.bankofengland.co.uk/banknotes/Pages/about/faqs.aspx.

[11] „There is, however, no Federal statute mandating that a private business, a person, or an organization must accept currency or coins as payment for goods or services." http://www.federalreserve.gov/faqs/currency_12772.htm, http://www.richmondfed.org/faqs/currency/

[12] http://banknotes.rba.gov.au/legaltender.html

[13] See ELTEG (2010).

[14] Commission Recommendation of 22 March 2010 on the scope and effects of legal tender of euro banknotes and coins (2010/191/EU).

[15] In addition to Germany, Finland, Ireland and the Netherlands, Scandinavian countries are also pioneers of the use of electronic payments, which is reflected in their legislation (e.g. Leo Van Hove, 2003).

[16] Odorán and Sisak (2008), Bódi-Schubert (2010).

cash through the promotion of electronic payment instruments in its publications as well as in government forums.

Even though the majority of euro-area countries considers the acceptance of cash mandatory for both the settlement of monetary obligations and the execution of retail payments, according to recital (19) of Council Regulation (EC) No 974/98 on the introduction of the euro, the use of cash can be restricted for public reasons: "limitations on payments in notes and coins, established by Member States for public reasons, are not incompatible with the status of legal tender of euro banknotes and coins, provided that other lawful means for the settlement of monetary debts are available."

A number of the Member States have enacted rules limiting payment in cash above a certain ceiling in transactions between businesses and/or private persons and requiring the use of electronic payment methods.[17] Furthermore, some countries require taxes to be paid by bank transfer, and public sector payments and transfers are also made exclusively through electronic means of payment.[18] In Denmark, in addition to electronic payment being compulsory above DKK 10,000 (approx. HUF 400,000), both providers and purchasers are incentivised to comply as both are held jointly and severally liable for any VAT or other tax fraud.[19] In Italy, incentives additional to the limitation of cash payments have been enacted to promote the spread of electronic payments. Since October 2012, public administration bodies and public service providers have been required to accept electronic payment methods and from 2014 on every economic entity offering products or services will be obliged to accept payment by debit card.

The regulation entered into force on 1 January 2013 limits cash payments above HUF 1.5 million in Hungary as well, but only between persons regularly engaging in economic activities.[20]

There are also regulations[21] or practices restricting cash payments to or from the Hungarian government:

1. The Act on the Rules of Taxation requires entities regularly engaging in economic activities to make cashless payments.[22]

2. The overwhelming majority of the remuneration of public servants and government officials is paid into payment accounts.[23]

3. Some public institutions limit the cash payments of households; some universities, for instance, only accept payments from students electronically and they pay scholarships exclusively into bank accounts.

It should be noted, though, that one third of the payments by and to the government, some 100 million transactions a year, continue to be carried out in cash rather than electronically.

The examples above indicate that states, including Hungary, limit cash payment to combat the shadow economy, and this effort is supported if the government promotes the wide-spread use of electronic payment instruments in the retail sectors.

The costs of cash payment are high

According the MNB's survey of the social costs of payment instruments,[24] the Hungarian society could save some HUF 100 billion annually if cash payments were replaced by electronic transactions and similar usage ratios of payment methods were reached as in the Northern European countries. At first sight, cash payment has no cost if regarded from the aspect of the customer and only the costs incurred at the time of payment are taken into account. However, the study also assessed all social costs of the electronic payment methods and cash payment and demonstrated that the costs of cash payment exceed the costs of electronic payment.

The fix costs of cash payment are lower than those of electronic payment but the costs relating to cash payment increase proportionately with the volume of cash transactions (production, transportation, storage, control)

[17] For more detail, see Turján et al. (2011), Odorán and Sisak (2008).

[18] MNB (2012b).

[19] If the customer is unable to pay electronically, he is relieved from the joint and several liability as long as he notifies the tax authority of the cash transaction. See: Opinion of the European Central Bank on limitations on cash payments (CON/2012/37) Denmark, 10.5.2012, pdf

[20] Subsection (3a) of Article 38 of Act XCII of 2003 on the Rules of Taxation.

[21] Pursuant to Article 63 (3) of Act LXXXV of 2009 on the Pursuit of the Business of Payment Services, the mandatory use of any payment method can be prescribed only in an Act of Parliament or government decree.

[22] Article 38 (1) of Act XCII of 2003 on the Rules of Taxation.

[23] Article 79/A of Act XXXIII of 1992 on the Legal Status of Public Servants, Article 143 of Act CXCIX of 2011 on Public Service Officials.

[24] Turján et al. (2011).

while the unit cost of electronic payments on the level of the national economy decreases with the increase in the number of payment transactions. When choosing a payment method or payment instrument, cost efficiency is an important aspect for economic agents. Consequently, in the future it is expected that more retailers will refuse payment in cash. In recent years, the card acquiring network has expanded dynamically but it is still considerably below the level seen in most EU countries.[25]

The high cost of using large volumes of coins for payment has been evident for quite some time. Consequently, regulations issued by most central banks allow the limitation of payment with coins. In the euro area Member States[26] and also pursuant to the Hungarian Central Bank Act,[27] parties are not obliged to accept more than 50 coins in cash payment transactions with the exception of the issuing bodies and certain designated institutions with a key role in cash distribution (in Hungary: credit institutions and post offices). The regulations in Australia, Canada and the UK also limit the mandatory acceptance of certain coin denominations, setting different ceilings for payment with the different denomination coins[28] (e.g. in the UK, 50p coins can be used to settle payment up to 10 pounds).

The use and distribution of small-denomination coins is very costly for economic agents in almost every country. Consequently, the possibility of ceasing the issuance of or withdrawing from circulation small-denomination coins not circulating any more in the economy arises time and time again (for more details, see Box 2).

Box 2
Small-value coins

The issue of the use of small-denomination coins is also linked to the high cost of cash payment. Because of changes in price levels and price structures, the problem every country encounters from time to time is that the purchasing power of small-denomination coins drops too low, they no longer take part in cash circulation due to their low value, they are hoarded in jars, customers do not re-introduce them into circulation: they increasingly become 'single-use'. They are used mostly for the exact settlement of small-value purchases. Consequently, the volume of issue of these denominations is by far more than that of larger denomination coins and the cost of their production, distribution, processing and storage is very substantial. This process led the MNB to withdraw 1- and 2-forint coins from circulation in 2008. Retailers did not re-price their products after the withdrawal of these coins; instead, they rounded the final sum payable on goods in line with the rules laid down in the Act on Rounding.[29] After withdrawal, the MNB carefully examined the potential inflation effects of this measure, but no demonstrable price increasing effect was found. According to household surveys, the overwhelming majority of the population supported the withdrawal of the inconvenient and costly small denominations that made purses heavy. Small denomination coins were withdrawn in a number of countries in a similar manner.[30]

In some of the euro -area Member States the role of 1- and 2-cent coins is very similar to that of the 1- and 2-forint coins in Hungary. Therefore, before introducing the euro, two euro-area Member States (Finland and the Netherlands) decided not to issue small-denomination coins and to use rounding rules for payments. This does not mean, however, that 1- and 2-cent coins are not legal tender. All it means is that the Finnish and Dutch central banks do not issue 1- and 2-cent coins, cashiers are not obliged to give change of 1 and 2 cents when they apply the rounding rules; however, if somebody (particularly a foreigner) wants to pay with those denominations, the coins are accepted.

As small-denomination coins are responsible for a very substantial part of the cost of coin distribution, other countries in the euro area also consider from time to time the possibility of withdrawing these denominations from circulation and introducing rounding rules. However, in the expert group of euro-area Member States[31] the majority was of the opinion that all remaining euro-area Member States should refrain from withdrawing small denominations and introducing rounding rules. The main argument was that rounding rules

[25] MNB (2012a).

[26] Pursuant to Article 11 of Council Regulation 974/98/EC.

[27] Article 27 (4) of the Central Bank Act.

[28] http://laws-lois.justice.gc.ca/eng/acts/C-52/page-1.html

[29] Act III of 2008 on the Rules of Rounding Required as a Consequence of the Withdrawal of 1- and 2-forint Coins from Circulation.

[30] For more detail see Leszkó (2009).

[31] See ELTEG (2010): This is also the opinion of experts of countries with high per-capita GDP where the purchasing power of 1 and 2 eurocent coins is so low that these denominations have effectively become 'single-use'.

contradict the notion of legal tender of 1- and 2-cent coins. In its aforementioned recommendation of 2010, the European Commission reflected the majority position. In view of the high social cost saving that would result from the withdrawal from circulation of small-denomination coins, and the fact that rounding had no inflation effect in the countries that opted for it, the Commission will hopefully change its position in this matter.

Security

Security considerations may also motivate retailers to refuse payment in cash. In addition to the personal safety of persons working in the shops, the safekeeping, handling and transportation of cash requires special security equipment due to the risk of robbery. These investments are not necessary when electronic payments are used. The insurance premium is also lower for the business if no cash is handled.

In the case of payment of large amounts in cash and in respect of businesses operating at a large distance from any credit institution or other deposit facility (post office) that are unable to deposit cash receipts in their bank account on the same day, refusal of cash payment is allowed based on the 'good faith principle' even in the countries where the refusal of cash is not acceptable in different circumstances.[32]

For a business, holding cash for the sole purpose of having change for cash payments is a security risk. This consideration is appreciated by the French regulations, which make the acceptance of cash mandatory only if the payer discharges his obligation by paying the exact amount due.[33]

Sometimes customers find it difficult to pay with large-denomination banknotes because retailers refuse to accept them for security and/or efficiency reasons. Based on the proportionality principle, the refusal of payment in large-denomination banknotes is allowed in the jurisprudence of most countries (for more details, see Box 3).

Box 3
Acceptance of high-denomination banknotes

Serving customers who want to buy small-value goods using high-denomination banknotes, particularly early in the morning, is difficult for retailers as they have already deposited their previous day's receipts in their bank account for security and financial management reasons and hold only change at the opening of the day. Therefore in most countries' laws, based on the proportionality principle, retailers are not obliged to accept large-denomination banknotes if their value is not in proportion to the amount to be paid.[34]

When withdrawing cash from an ATM, the withdrawer has no control over the denomination structure of the cash dispensed. Consequently, the MNB requires in its decree credit institutions and post offices to exchange on one occasion a maximum of 50 pieces of banknotes or coins into different denomination banknotes and coins, to make sure that economic agents have the appropriate denomination of banknotes and coins necessary for their cash transactions.[35] Most credit institutions and post offices offer this service free of charge to their clients.

The denomination structure of euro banknotes includes two large denominations, 200 and 500 euro banknotes, the value of which far exceeds the customary value of everyday payments. According to the ECB survey on the use of cash, over half of the population of euro-area Member States have never seen a 500 euro banknote, and 44 per cent have never held a 200 euro banknote in their hands.[36] As the public very rarely if ever sees such banknotes, their acceptance is uncertain. Consequently, the euro area Member States started

[32] See ELTEG (2010).

[33] Art L112-5 du Code Monétaire et Financier: En cas de paiement en billets et pièces, il appartient au débiteur de faire l'appoint. The French financial laws contain no definition of legal tender status. In the case of payment with banknotes or coins, the Act quoted above requires the debtor to pay the exact amount due. French criminal law provides for the offence of refusal to accept payment in cash, but this provision is enforced only if the debtor would pay the exact amount in cash and the merchant refuses to accept it. Such a court case is described at the following link: http://www.avocat-lingibe.com/question-reponse-juridique/entreprise/consomation-25.html.

[34] See ELTEG (2010).

[35] Decree No. 11/2011. (IX. 6.) of the Governor of the MNB on the processing and distribution of banknotes and on technical tasks relating to the protection of banknotes against counterfeiting.

[36] For more detail see ECB (2011).

to consider whether retailers could refuse to accept payment with these banknotes. In the Netherlands, for instance, retailers are not required to accept large denomination banknotes if this fact is clearly indicated by means of a sticker at the entrance to the shop or filling station.[37] The US has adopted a similar practice in respect of large-denomination banknotes.[38] The majority of euro-area Member States, however, reject this practice and accept the refusal of large-denomination banknotes only on an occasional basis under the proportionality principle.[39]

The above examples show that to some extent the authorities of each country reviewed acknowledge the attempts of businesses to restrict the acceptance of cash as long as it is justified by security or efficiency reasons. Within the euro area the majority of Member States consider that the acceptance of cash should be restricted solely on grounds of security. In addition, based on the principle of good faith, they consider it legitimate to refuse cash payment because the seller is temporarily short of the required change.[40] Nevertheless, endeavours by the government to limit cash payments to combat the grey and black economy have become more pronounced in the past one year or two in almost every Member State.

ARE CASH SURCHARGES ACCEPTABLE?

The payment services directive[41] (hereinafter referred to as the 'Directive') provides that in order to encourage competition and the use of efficient payment instruments, Member States may decide at their discretion to forbid or limit the levying of charges for the use of a certain payment instrument by retailers.

The survey conducted in 2011 on the transposition of the Directive by the Member States[42] reveals a mixed picture on whether Member States made use of the possibility to forbid or limit the levying of charges in legislation. Half of the Member States excluding Hungary (e.g. Austria, Denmark, France, Italy, Sweden) specifically prohibited such surcharges, two of them did so only in respect of payment by card though. Thirteen other Member States (e.g. Belgium, the Netherlands, Germany, Spain, the United Kingdom), however, did not make use of this option provided in the Directive, while some of them allow such charges to be imposed in proportion to the actual costs incurred by the use of the payment instrument concerned.

At the time of its entry into force on 1 November 2009, the Act on Payment Services[43] transposing the Directive into Hungarian law was lenient on the imposition of charges and costs. However, in the amendment of the Act effective as of 1 January 2011 the legislator prohibited the imposition of charges or costs in order to promote the use of cash-substitute payment instruments.

Article 36 (4) The payee may not impose any charges, costs or other payment obligations for the use of a cash-substitute payment instrument.

However, the Directive does not discuss whether charges may be imposed in the case of cash payment.

The issue of cash surcharges divided the experts of euro-area Member States. Some considered that surcharging cash is not compatible with the concept of legal tender (obligation of acceptance at face value) as set out in the Treaty on the Functioning of the European Union. Another group of the Member States consider, however, that the mandatory acceptance of legal tender only concerns the payment of a debt under a contract, and thus it has no bearing on the formation of the contract whereby all material conditions (including the price, with the possibility of a surcharge for a cash payment) are agreed.[44]

The use of electronic payment methods can be efficiently promoted by allowing the payee to charge a fee corresponding to its direct costs relating to the cash payment as long as there are other payment methods (such as credit transfer) available as well. It would also be desirable in the relationship of payment service providers and their customers if every customer bore the costs and charges of their own payment service provider, including customers making cash payments to payment accounts

[37] http://www.dnb.nl/en/news/news-and-archive/nieuws-2010/dnb235121.jsp
[38] http://www.richmondfed.org/faqs/currency/
[39] See ELTEG (2010).
[40] See ELTEG (2010).
[41] Directive 2007/64/EC of the European Parliament and of the Council on payment services in the internal market.
[42] http://ec.europa.eu/internal_market/payments/framework/psd_study_en.htm
[43] Act LXXXV of 2009 on the Pursuit of the Business of Payment Services.
[44] See ELTEG (2010).

using postal inpayment money orders (yellow cheques). However, officially there is no uniform position on the issue of bearing the costs and charges of cash payment. For instance, the Act on Consumer Protection prohibits public utility companies from charging a separate fee for the payment of bills through postal inpayment money orders as of 29 July 2012,[45] and the Act on Electronic Communications imposes the same prohibition on electronic communications service providers as of 17 November 2012.[46] The law only allow service providers to give discounts to clients who choose a method for paying their bills that is less costly for the service provider. Because of this restriction, utility companies incorporate the cost of cash management into their rates and make all clients pay for it, including the ones using cheaper electronic payment methods.

The evolution of a more efficient payment structure requires that consumers choosing between payment methods are aware of their respective costs. The prices of different payment methods must provide incentives to users to choose the effective payment structure. This in turn requires that, on the one hand, the fee structures of payment service providers reflect costs and are not distorted through cross-subsidisation between products and services. On the other hand, the costs of cash payment should be borne by those who make use of that means of payment.

SUMMARY

Limiting cash usage is reasonable in the current economic environment and possible under Hungarian law. The MNB is in support of the broader use of electronic payment instruments with an eye to combating the grey and black economy, promoting efficient payment instruments and enhancing security. Consequently, the MNB as the issuer of forint cash is not against retailers accepting exclusively electronic payment instruments.

In respect of payments to and from the government and the regulation of B2B cash transactions Hungary has already taken steps in this direction, but the cash intensity of the economy is still high in a European comparison. This is why further measures are needed to promote the spread of electronic payments. For instance, payees should be allowed to charge a fee corresponding to their direct costs relating to the cash payment if there are other payment methods available as well. Furthermore, in our opinion consideration should be given to rewording Article 27 (2) of the Central Bank Act, which regulates the acceptance of banknotes and coins, so that the rule unambiguously pertains to the obligatory acceptance of banknotes and coins at face value rather than the acceptance of cash in all circumstances.

We do not think that cash as a payment instrument will disappear in the foreseeable future. Cash has qualities that remain important for society. For instance, at this point many people find it easier to manage their monthly expenditures if the cash in their purse limits overspending while others find the anonymity of cash important to protect their privacy. This may be one of the reasons that even though the overwhelming majority of Hungarian households have bank accounts, many people still withdraw their regular income received on the bank account and settle their utility bills and pay for their daily purchases in cash.[47] Households that have no bank accounts obviously cannot obtain any regular or occasional income except in cash. There is yet another consideration that will keep cash usage necessary and legitimate in the longer term: in Hungary there are substantial differences between communities, depending on their population size and region, in terms of their access to the infrastructure required for cashless payment (bank branches, POS terminals).[48]

Based on the experience of other countries, however, the spread of electronic payment methods is a clear tendency, particularly because they are more efficient and cheaper. The role of cash is likely to decrease in payments in Hungary as well, if not in terms of volume, but in terms of proportion.

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