

# Congress Should Repeal the Durbin Amendment

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U.S. District Judge Richard Leon's decision rebuking the Federal Reserve for ignoring the plain language of and not faithfully implementing the Durbin amendment was a victory for the rule of law and, therefore, for all Americans, whatever one thinks of the legislation's merits. Rogue regulators are more dangerous than bad laws, the remedy for which is Congress amending or repealing them.

Leon's ruling, however, should remind the payments industry just how harmful the Durbin amendment is.

In a 2011 [BankThink column](#), I argued merchants' suit against the Fed was righteous, not because I was a fan of Sen. Richard Durbin's (D-Ill.) punitive legislation, but because the Fed's job is to implement, not make policy.

Many have assumed Leon must harbor animus to the Fed, because he wrapped their knuckles, and to banks as his decision will hurt their economics. The judge's personal sentiments about banks, merchants, networks and the Fed should have been and appear to have been irrelevant to his decision-making. Leon rightly looked to the Durbin amendment's text as the best gauge of Congress's intent, not to its author's declarations or what the Fed thought reasonable and fair. He noted the central bank does not have "[the authority to ignore the expressed will of Congress](#)." Congress's intent was patently clear.

Days before Leon's decision, implacable payments-industry foes Durbin and Rep. Peter Welch (D-Vt.) sent a [letter](#) to Fed Chairman Ben Bernanke urging him to heed the [European Commission's proposal](#) to cap debit interchange at 20 basis points. Brussels regulatory mandarins' views, however, are irrelevant to the Fed's task. Congress gave the central bank

express instructions intended to produce debit interchange well below 20 basis points.

The Fed is not going to give up arrogating itself above the law without a fight and plans to appeal. The central bank likely will argue the Chevron standard defining regulator latitude implementing laws wasn't met. The standard was spelled out by now-retired Justice John Paul Stevens who for a unanimous Supreme Court wrote "if the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of congress." So, while the outcome would seem a foregone conclusion, the legal battle isn't over.

However, Congress created the problem. Congress needs to fix it.

The law requires debit interchange reasonable and proportional to issuers' incremental processing costs, which for large issuers aren't more than a couple cents, if that. Absent Congressional action, debit interchange is therefore likely to come down to between a couple cents and the Fed's original 7-cent-per-transaction safe-harbor cap.

[The unbanked population has been increasing and free checking accounts declining](#) as a result of a gelded implementation of the Durbin amendment. Issuers with more \$10 billion in assets such as Bank of America, JPMorgan Chase, Wells Fargo and U.S. Bancorp face the specter of losing billions more in interchange revenue. Consequently, more consumers will be pushed out of the banking system and lose free checking. Cardholders, the constituency with no seat at the table, will suffer higher fees and reduced benefits.

Unlike in the U.S., interchange regulation abroad has been uniform. The European Commission didn't propose 20 basis points for out-of-favor banks and 145 basis points for favored banks. In contrast, in the U.S. to paraphrase George Orwell, all banks are equal but some banks are more equal under the law than others, which is profoundly un-American. Politically sympathetic small banks are exempt from Durbin's punitive price caps.

Leon's ruling requires merchants have routing choice for every debit payment – the Fed's original "alternative B" mandating at least two signature and two PIN debit networks for every card. As such, it will also upend debit-network competition.

The temptation and slippery slope of lowering interchange to win transactions would be strong. While regulated and unregulated interchange will be squeezed, issuers can threaten to drop networks cutting interchange to win transactions, particularly for PIN.

Changes to signature-debit network competition will be more momentous. If every issuer has to align with Visa and MasterCard, which [collectively have 99.9% market share](#), the networks could raise fees on issuers, who would no longer influence network share.

How it plays out, however, depends not only on Visa's and MasterCard's actions, but whether Discover with de minimis share today decides to compete and Star, NYCE and other traditional PIN-networks invest to offer sig-authentication and widen acceptance.

Historical distinctions between sig and PIN debit networks will blur.

While European regulators have stymied retail network competition, the U.S. payments market is relatively lightly regulated, and has become more competitive, innovative and open. This has enabled an unprecedented wave of new entrants, challenging the status quo, including scores of payments service providers and digital wallets, none of which were hatched in Washington. America's leading retail payment systems – Visa, MasterCard, American Express, Discover, PayPal, Star, NYCE and Accel – are commercial and independent of banks.

Washington, Brussels and Canberra central planners mandating lower fees at one point in the value chain rather than letting the market set prices and decide value, suppresses competition, knowledge acquisition and innovation, and thereby hurts consumers and merchants.

Regulators gloss over in free markets consumer payment preferences trumping merchants'. Higher interchange up to a point, fuels issuer innovation and enriches cardholder value, spurring greater use. The issue is not what the right interchange price is, but rather should it be set by the state, litigation or the interplay of networks, financial institutions, merchants and consumers in the market.

The payments industry should mount an all-out campaign to repeal the Durbin amendment. The argument should be framed in the public arena in terms of defending markets and cardholders across the socioeconomic

spectrum, against Washington central planning. For the sake of payments innovation, competition and consumers, Congress should repeal Durbin's price controls.

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