Durbin Amendment's Gray and Not-So-Gray Areas

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Cashiers trying in any systematic way to filter out use of debit cards with unregulated interchange issued by banks with under $10 billion in assets is unlikely. But, whether Andrew Kahr's punchy commentary ["Durbin Hurts Small Banks? Nonsense," March 7] arguing that the Durbin amendment's interchange-price-cap exemption for small banks will be effective and competitively advantage them against Goliath retail banks is correct depends on how the network exclusivity ban is implemented. Kahr cavalierly dismissed as "impossible" the notion that the network exclusivity ban, and the requirement merchants that have routing choice, would weaken the exemption's effectiveness. That's not certain.

Interchange flows to the party(ies) choosing the payment transaction, irrespective of cost. The Fed's implementation of the debit network exclusivity ban could affect whose payment network choice is dispositive and therefore the effectiveness of small banks' exemption from interchange price controls.

The Fed requested comment on several implementation approaches. Under the relatively benign and easy to implement alternative A small banks' exemption would probably be effective. It would require debit issuers align with at least two unaffiliated networks. Issuers would align with a single signature and a single PIN debit network. Issuer and cardholder payment scheme and processing preference would therefore generally continue to reign.

The Fed's alternative B, however, could render small banks' carve-out meaningless. It would require issuers offer two networks for each authorization type — signature, PIN and other keys. If merchants only picked transaction routing, but not the rules and interchange, which narrowly read is what the legislation requires, then small banks' exemption ought to be effective. If, however, for every payment merchants or merchant processors on their behalf choose the bundled payment scheme (rules and interchange) and routing, then small banks' exemption would be of little value. Regulated and unregulated interchange and network fees paid by merchants would be subject to a powerful downward ratchet: merchants picking the cheaper network transaction by transaction.

That said, the idea that government should decide interchange is fair for one set of politically favored businesses, while it needs to be punitively capped for another group of politically unsympathetic businesses, is noxious.

Eric Grover
Partner
Intrepid Ventures
Minden, Nev.