TESTIMONY OF

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BEFORE THE

U.S. SENATE COMMITTEE ON THE JUDICIARY

HEARING ON

"BREAKING THE VISA-MASTERCARD DUOPOLY: BRINGING COMPETITION AND LOWER FEES TO THE CREDIT CARD SYSTEM"

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Thank you for providing me with the opportunity to testify on the swipe fees that are imposed by the credit card industry on merchants and the Credit Card Competition Act of 2023, among other potential solutions to these vexing issues. Most consumers are not aware of these fees and do not see the effects they create on the cost of goods and services and the U.S. economy, but those effects are dramatic. For merchants, these excessive and ever-increasing fees are a constant source of stress and financial difficulty, and for consumers these fees contribute significantly to inflation. In fact, swipe fees reduce efficiency across the economy.

I am testifying today on behalf of my association, the National Association of Convenience Stores (NACS), as well as a coalition that we helped found to try to address these issues, the Merchants Payments Coalition (MPC). NACS is an international trade association representing the interests of the convenience industry. In the United States, the industry includes more than 150,000 stores employing 2.44 million people. It is truly an industry of small business with a full 60 percent of the industry comprised of single-store operators. The industry handles about 165 million transactions in total each day – a number equivalent to about half of the U.S. population. An efficient and competitive payment system is critical to the health of the industry and its employees.

The MPC is a group of retailers, supermarkets, restaurants, drug stores, convenience stores, gas stations, online merchants, and other businesses focused on reforming the U.S. payment system to make it more transparent and competitive.

I. Executive Summary

The credit and debit card systems in the United States are burdened by anti-competitive conduct that makes the systems less efficient and effective than they should be. Two payment card networks, Visa and Mastercard, dominate the market and bring together thousands of banks across the nation to wield market power in ways that harm competition in the marketplace. Merchants have no realistic options to refuse to take cards controlled by the dominant networks and virtually all the banks that are their members. With very few exceptions, merchants must accept all credit and debit cards that run over those two networks no matter how high the fees the networks charge and no matter how onerous the rules and conditions they impose. The high fees that result from this exercise in market power inflate the costs of goods and services across the nation in a way that harms consumers.

It does not have to be this way. The rates that Americans pay on credit card swipe fees are the highest in the industrialized world – and it's not close. Congress has the opportunity to do something about this. The Credit Card Competition Act (CCCA) provides that opportunity. The changes the CCCA would bring are proven to work and would do nothing more than introduce market competition where there is none today. Competitive markets incentivize innovation on price and service that benefits consumers and the economy alike. Swipe fees desperately need those incentives and lack them today. The CCCA would deliver on that.

As noted by the think tank American Compass, the CCCA is "laser-targeted at creating competition in a market that currently lacks it."[1] Similarly, an editorial in the New York Times has called the CCCA the "best deal" for the "vast majority of Americans."[2]

The problems in this market have developed because Visa and Mastercard each separately set the fee rates for the largest portion of the swipe fees, known as interchange, that all the banks that issue cards with those networks charge to merchants. Because the banks' fees are centrally set in this way, the banks don't compete on price. That leads to problems that are common for anti-competitive arrangements – high and escalating prices and neglect of key aspects of the service (such as protection against fraud). Visa and Mastercard also dictate a complex set of terms (called network rules) that govern how credit card transactions happen. These terms further insulate swipe fees from competitive market pressures and, in most cases, keep the fees confusing for merchants and hidden from consumers.

In particular, by imposing an "honor all cards" rule that requires a merchant to accept all cards issued with a Visa (or Mastercard) logo if the merchant wants to accept any cards carrying those networks' logos, the two largest networks remove the incentives for banks to negotiate with merchants on price or acceptance of their cards – and remove almost all bargaining power that merchants otherwise might have had. This is a central element of the credit and debit card systems in the United States today and creates additional competition policy problems.

The extent of the anticompetitive problems created by this structure was recently highlighted by the U.S. Department of Justice (DOJ) in the lawsuit it filed against Visa.[3] While that case only covered debit cards, a story in the Wall Street Journal made clear that Visa's actions also negatively impacted the credit card market.[4] Because only the debit market today has even a baseline level of network competition, however, the DOJ focused on debit. The CCCA is needed to bring a basic level of competition to credit cards.

The problems caused by all this for consumers, merchants and the economy are immense. Total card swipe fees imposed on merchants were $172 billion in 2023[5]– up from $64 billion in 2010. Of that total, $100.77 billion were fees for Visa and Mastercard branded credit cards and $31.3 billion were fees for Visa and Mastercard branded debit cards.[6] In fact, the fees charged by the two major networks, Visa and Mastercard, that they kept for themselves were $10.9 billion

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[1] Chris Griswold, "The Credit Card Competition Act will help support a stronger, more competitive free market," The Hill (Nov. 13, 2023) (available at The Credit Card Competition Act will help support a stronger, more competitive free market | The Hill).

[2] James Robinson and Emily Holzknecht "Your Rewards Card is Actually Bad for You, And for Everyone Else," New York Times (Nov. 21, 2023) (available at Opinion | Your Rewards Card Isn't as Rewarding as You Think - The New York Times (nytimes.com)).

[3] U.S. v. Visa, Complaint (Sept. 24, 2024) (available at dl).

[4] "Visa Wanted a Vast Empire. First, It Had to Beat Back Its Foes." By Annamaria Andriotis, The Wall Street Journal (Oct. 19, 2024) (available at Visa Wanted a Vast Empire. First, It Had to Beat Back Its Foes. - WSJ).

[5] The Nilson Report, March 2024 (available at 1259 - Nilson Report).

[6] The Nilson Report, March 2024 (available at 1259 - Nilson Report).

on credit cards and $8.3 billion on debit cards.[7] The fees on Visa and Mastercard credit cards alone have nearly quadrupled since 2010 from $26 billion to $100 billion.[8]

The size of the fees and the fact that they are set largely as a percentage of transaction amounts means that they are an inflation multiplier. The United States already pays the highest swipe fees in the industrialized world. The roles played by the two dominant card networks and the fees and terms they set cause other problems as well by reducing incentives for innovation in new payment products and improvements in services such as fraud protection. The United States should have the most efficient, effective and innovative payment system in the world, but we don't. Instead, as revealed by the Justice Department and the Wall Street Journal, we have a dominant payment network -Visa- actively holding back innovation in the market through pay-offs and manipulative fee practices. This market desperately needs changes so that there are competitive market forces that improve payments for everyone.

The CCCA would help address these problems. The bill would inject market competition into these arrangements by ensuring that each credit card issued by banks with more than $100 billion in assets has two network options enabled on those cards. That would provide a competitive option for merchants to seek the network that offers them the best deal on service and price. The competition among networks, in turn, would push each of them to acknowledge Main Street businesses as their customers and offer better services and prices in order to win business. The networks do not have those incentives today because they have no meaningful competition on credit cards. The bill would also close a glaring loophole by blocking China's state-controlled netwok UnionPay from being added on U.S. credit cards. The reforms in the Credit Card Competition Act would mean that fees would be about $16 billion per year less than they would be without reform and it would lead to enhanced security measures.

This testimony will cover a few topics relating to swipe fees. First, it will lay out some background on how credit and debit card payments work. Second, it will address the competition policy problems created by those payment systems. Third, it will discuss how the CCCA will help to solve those problems. Fourth, the testimony will discuss the negative impact these fees have on merchants. Fifth, the testimony will note the negative impact of the fees on consumers. Sixth, it will describe the negative impact of swipe fees on the U.S. economy. Seventh, it will walk through and set the record straight on a number of the myths that the credit card industry regularly espouses in order to distract from the problems with these payments and the need for reform.

II. How Card Payments Work

In order to understand the competition problems with the credit and debit card markets, it helps to have some background on how these payments work. Neither Visa nor Mastercard, the two largest card networks, has a direct relationship with individual cardholders. Financial

[7] CMSPI-IAC State of the Industry Report (Sept. 2024) at 19 (available at State of the Industry Report | CMSPI Global).
[8] *See* The Nilson Report (Nov. 2011) (available at 983 - Nilson Report); The Nilson Report (March 2024) (available at 1259 - Nilson Report).

institutions such as banks and credit unions actually enter into agreements with individuals and issue cards to them. The structure is similarly indirect with merchants. Merchants contract with banks or payment processors to handle the merchants' acceptance of payment cards.

Visa and Mastercard actually started as associations of their bank members.[9] In fact, even after Visa and Mastercard transitioned away from being associations in the mid-2000s (in an attempt to skirt antitrust liability), the "biggest US banks" for many years own restricted shares that, for Visa alone, were worth $96 billion.[10] The banks owned major stakes in Mastercard as well.

The two major networks do a few things to make card payments happen. They maintain data lines that connect the banks that issue cards to consumers with the banks that work with merchants. They also advertise their brands to make the cards more appealing to consumers and businesses. And, they set the prices for the fees that the card issuers charge to merchants as well as the rules that govern how cards are issued and processed. It is this price- and rule-setting role that raises antitrust issues to be addressed below.

A good explanation of the process of a card payment can be found at knowyourpayments.com.[11] In the simplest terms, when an individual dips or swipes a payment card at a store, the information necessary to process that payment goes to the merchant's bank (or processor) who sends the information to a card network (e.g., Visa or Mastercard) and that network sends the information to the card issuer (the bank that gave the consumer that card), then a message authorizing the transaction (or declining it) goes back through each of those entities to the merchant's payment terminal allowing the transaction to take place. The clearance and settlement of the funds takes place later through a similar process. The graphic below depicting this basic process can be found at corporatetools.com.

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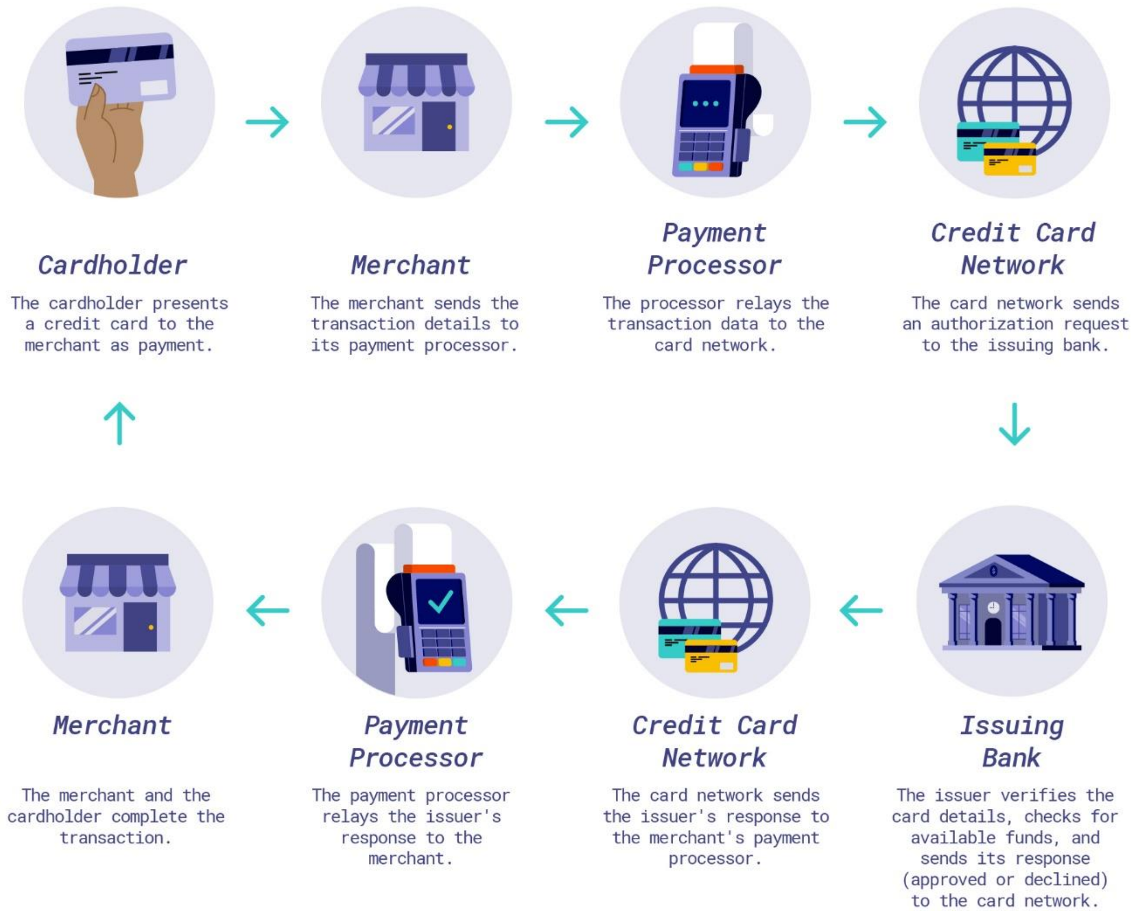
[9] Both companies changed their structures in the 2000s in order to try to insulate themselves from antitrust liability after a court of appeals held in 2003 that Visa and Mastercard "are not single entities; they are consortiums of competitors" and that the rule then challenged by the DOJ was "a horizontal restraint adopted by 20,000 competitors." *United States v. Visa U.S.A. Inc.*, 344 F.3d 229, 242 (2d Cir. 2003). Some major banks still own billions in restricted shares in the companies.

[10] Jenny Surane, "Visa Takes First Step to Let Big Banks Sell $96 Billion of Stock," Bloomberg News (Sept. 13, 2023) (available at News Article — Bloomberg Government (bgov.com)).

[11] *See* Know Your Payments » Transaction Basics.



According to the Federal Reserve Bank of San Francisco's Diary of Consumer Payment Choice, credit cards accounted for 32 percent of consumer transactions in 2023 (up from 31 percent the year before), debit cards accounted for 30 percent, and cash was 16 percent (down from 18 percent).[12] This represented a large jump in credit card payments, which had been 24 percent of payments in 2019.[13]

These changes in the payments mix have profound implications for the costs that Main Street businesses face and the revenues that the credit card industry collects because there are fees that each player involved in the processing of the card deducts out of the amount that the merchant gets paid in the transaction. By far the largest fee is the interchange fee, which goes to

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[12] Berhan Bayeh, Emily Cubides and Shaun O'Brien, "2024 Findings from the Diary of Consumer Payment Choice," Federal Reserve Bank of San Francisco (available at [2024 Findings from the Diary of Consumer Payment Choice]). Credit cards make up a larger percentage of payments in e-commerce.

[13] Laura Kim, Raynil Kumar and Shaun O'Brien, "2020 Findings from the Diary of Consumer Payment Choice," Federal Reserve Bank of San Francisco (July 31, 2020) (available at [2020 Findings from the Diary of Consumer Payment Choice - San Francisco Fed]).

the bank that issued the consumer the card. That fee alone can account for about 80-85 percent of all of the fees involved in the transaction. The networks, such as Visa and Mastercard, impose their own separate fees, called network fees, in addition to the swipe fees. And, the merchant's processor or bank receives a fee for its services. Processing is a reasonably competitive market. Merchants don't always like how much they pay in those processor fees, but they have options to do business with different processors (or negotiate new agreements) and that helps discipline that cost. Merchant concerns about network fees are different than concerns about swipe fees. Networks set their own fee amounts, which is appropriate. Unfortunately, the two major networks have structured and applied their network fees to have certain anti-competitive effects to protect and grow their market power. The networks' market share and the way the networks bring together the card-issuing banks has enabled them to do this. The DOJ lawsuit shines a light on the problem of network market power and actions to deter competition and innovation in the card network market (at least for debit cards). It is worth noting that the CCCA would likely first put competitive market pressure on network fees, which last year amounted to $10.9 billion on Visa and Mastercard credit cards.[14] The concerns about network fees are related to, but different than, the problem created by anti-competitive behavior in the setting of swipe fees by the two major networks on behalf of card-issuing banks, which is discussed below.

Credit card issuing is very concentrated among a small number of very large banks. The ten largest Visa-Mastercard credit card issuers in the United States collectively have more than 80 percent of that credit card issuance market.[15] Those issuers compete to get consumers to sign up for and use their cards. They do this through a complex set of pricing mechanisms that include interest rates, a variety of rewards offerings, and a number of potential penalty fees and related terms. These complex pricing mechanisms can be difficult for consumers to evaluate and may lead consumers to choose offers that are less favorable than other offers.[16] And, the enticement of credit card offers can lead consumers to create financial problems for themselves that are challenging to fix.

Because credit card issuers receive fees from merchants every time one of their cards is used, they have a strong incentive to push for those cards to be used as many times as possible. They have been particularly aggressive in trying to get consumers to use their cards for small, everyday purchases. Using credit for everyday purchases, of course, can create financial problems for consumers if they are not careful. Unfortunately, card issuers can be less concerned about individuals' financial problems due to the revenue those issuers earn from merchants.

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[14] CMSPI-IAC State of the Industry Report (Sept. 2024) at 19 (available at State of the Industry Report | CMSPI Global).

[15]The Nilson Report, Feb. 2024 (available at 1258 - Nilson Report); See also Bianca Peter, "Credit Card Market Share by Issuer," (Feb. 24, 2022) available at https://wallethub.com/edu/cc/market-share-by-credit-card-issuer/25530.

[16] For an explanation of some of these confusing prices and terms, *see* Consumer Reports, "What Credit Card Offers and Rewards are Best for you?" (November 2012) available at https://www.consumerreports.org/cro/magazine/2012/11/the-best-credit-card-for-you/index.htm; and Adam Levitin, "Testimony Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs," (July 19, 2011) available at https://www.banking.senate.gov/imo/media/doc/LevitinTestimony71911.pdf.

Though there are problems, consumers at least have the benefit of competition among different credit card issuers that try to get their business. That can lead to helpful offers. Merchants, however, do not have that benefit due to the way that the two dominant card networks bring together card issuers from across the country into their two networks.

III. The Credit Card Industry's Anti-Competitive Activity

The central problem with credit cards in the United States is that the two largest networks, Visa and Mastercard, set the amounts of the swipe fees that the card-issuing banks charge for each transaction and they set the terms governing how these transactions happen. All of those card-issuing banks – particularly the largest ones which have the vast majority of credit card market share – could set their own prices and compete with each other for merchants' business. Those card issuers all compete that way for consumers' business. But, they refuse to compete for merchants' business. One hundred percent of the banks and credit unions that issue cards with Visa logos agree to charge merchants the same schedule of network-fixed fees. The same is true for the banks and credit unions that issue cards with Mastercard logos on them.

There is no avoiding the destructiveness of these agreements not to compete on price. Merchants on the whole have no realistic ability to refuse accepting payment from virtually all the banking institutions across the nation. That is in part because retail is incredibly competitive in the United States. There are many different types of merchants trying to out-compete each other on price and service for the business of the American consumer. If one of them stops taking these credit cards, the competitor across the street will take some of their business. So, merchants take the cards and the fees keep growing at dramatic rates. In fact, economists with the Kansas City Federal Reserve Bank have studied these fees and found that, in light of the centralized fee-setting structure and the competitiveness of U.S. retail, swipe fees will increase to the point that retailers may go out of business.[17] That is the only effective brake on the steep rise in these fees.

It is also important to note that the swipe fees banks charge merchants to accept their cards (the ones set by Visa and Mastercard) are not the same on every transaction. In fact, they can vary dramatically. Visa and Mastercard set complex schedules of fee rates, and the fees vary based on the level of rewards associated with the card, the type of merchant accepting the card, the manner in which the card is accepted (online versus in-person and other aspects of acceptance) as well as, in some sectors, the card network's view of the merchant's level of security.[18] Both Visa and Mastercard also systematically disadvantage many small businesses by building higher fees for those businesses into their fee schedules.[19] The fees for the most expensive cards can be about triple the amount of the fees for the least expensive cards for some merchants.

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[17] Fumiko Hayashi, "A Puzzle of Card Payment Pricing: Why Are Merchants Still Accepting Card Payments?" Federal Reserve Bank of Kansas City (2004) available at https://ideas.repec.org/p/fip/fedkpw/psrwp04-02.html.

[18] There are other factors that can change the economics as well such as other services (including tokenization, fraud detection, and other services) that the networks have tried to control.

[19] This is more fully explained in section IV below. The Visa and Mastercard swipe fee rate schedules can be found at Visa USA Interchange Reimbursement Fees and U.S. Region Interchange Bulletin (mastercard.us).

In addition to the fee-setting, however, Visa and Mastercard impose a set of terms that further insulate those prices from the possibility of any competitive market forces keeping the fees in check. There are hundreds of pages of these terms and problems with them are detailed well in ongoing antitrust litigation that is pending in the U.S. District Court for the Eastern District of New York.[20]

A few of these terms merit particular attention. One is the central price-setting engaged in by Visa and Mastercard noted above. Another is the so-called "honor all cards rule." This "rule" is imposed by both Visa and Mastercard on merchants. It creates an all-or-nothing proposition for every merchant across the country and says that if a merchant wants to accept any Visa- (or Mastercard-) branded credit card, that merchant must take every credit card with that brand (and the same with debit cards). "Honor all cards" removes any possibility for a merchant to negotiate prices or terms with any bank – and completely removes the incentive for any bank to try to negotiate prices or terms with any merchant.

Removing those normal market incentives for price competition and negotiated deals is very significant. Because the fees are so much higher for some cards than for others, merchants very sensibly might want to accept some of them but not others (for fear of going out of business). But, they can't make that choice. If they could, of course, banks issuing the most expensive cards might be inclined to cut their prices, but they don't need to worry about that because Visa and Mastercard have removed the normal market dynamics from the playing field.

Visa and Mastercard also put restrictions on banks to stop competition from creeping into the picture. They both prohibit banks from enabling any network that competes with them to work on those banks' credit cards.[21] That way, one hundred percent of the transactions on credit cards that have Visa enabled on them go through the Visa network (and the same is true for Mastercard).

These prohibitions are very similar to rules that were the subject of litigation the U.S. Department of Justice filed against Visa and Mastercard in 1998. The rule in question was known as the exclusionary rule. It prohibited banks that issued cards under Visa's or Mastercard's brands from issuing cards from any of their competitors (including companies such as American Express and Discover). The U.S. Circuit Court of Appeals for the Second Circuit ruled in favor of the Department of Justice in that case and the exclusionary rule is no longer permitted.[22] NACS filed comments with the Federal Trade Commission discussing how Visa and

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[20] A redacted version of the complaint filed in the case by NACS and others can be found at: https://constantinecannon.com/wp-content/uploads/2022/04/13-cv-5746-Doc.-183-6th-Amd.-Complaint-Redacted.pdf.

[21] Federal Reserve Regulation II prohibits these types of exclusivity requirements on debit cards.

[22] *United States v. Visa* U.S.A., Inc., 344 F.3d 229 (2d Cir. 2003), cert denied, 543 U.S. 811 (2004), available at Second Circuit Decision in U.S. v. Visa (02-6074) | ATR | Department of Justice. American Express and Discover each sued for the damages they suffered due to the rule and reached settlements with Visa and Mastercard. Discover, Visa and MasterCard settle antitrust suit | Reuters.

Mastercard's prohibitions against banks issuing credit cards with other networks on them violates the antitrust laws and harms competition.[23]

Visa and Mastercard also have a long history of restricting how merchants price their products to their customers. These restrictions formed a veil of secrecy around swipe fees that further insulated the fees from competitive market pressures. Some of those restrictive terms have been eroded through legal challenges over time. For example, the Department of Justice and seventeen states entered into a consent decree with Visa and Mastercard that became final in 2011 which prohibited those two networks from preventing merchants from offering their customers discounts for using less expensive payments.[24] Prohibiting merchants from giving American customers discounts strikes directly at the heart of how competitive markets should work. But, that is just one in the long line of actions the two largest networks have taken to undercut competition in the credit card market.

In fact, Visa and Mastercard's fee- and term-setting have turned competition on its head. While competition normally causes businesses to try to keep prices low in order to attract market share, Visa and Mastercard don't compete for merchants' business. The honor all cards rule and lock-up of all the banks takes care of that. Instead, Visa and Mastercard only compete to attract banks to issue more of their cards. They do that by trying to push the swipe fees they set on behalf of those banks higher and higher.[25] It is the opposite of what real competition does and demonstrates how the market is broken.

The major card networks have also taken actions that erode competition from any other potential competitors. These actions have been described in the complaint filed by the U.S. Department of Justice in September against Visa as well as in a recent Wall Street Journal expose.[26] These sources show that Visa has used punitive "cliff-pricing", deals to buy-off competitors, and targeted acquisitions to create a "moat" around its monopoly position.

For example, the DOJ has alleged, "Visa's efforts have not only reduced innovation from other companies that would benefit consumers and businesses today, but also its own incentives to innovate: Visa admitted that it has not materially invested in innovation in the last decade other than its tokenization efforts."[27] "Visa's strategy has been to align its incentives with Apple,

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[23] NACS-Comments-to-FTC-on-Unfair-Contract-Clauses-Fi.pdf (convenience.org).

[24] Final Judgment as to Defendants Mastercard International Incorporated and Visa Inc. | ATR | Department of Justice. The states that joined the action and consent decree were: Arizona, Connecticut, Idaho, Illinois, Iowa, Maryland, Michigan, Missouri, Montana, Nebraska, New Hampshire, Ohio, Rhode Island, Tennessee, Texas, Utah, and Vermont.

[25] Andrew Martin, "How Visa, Using Card Fees, Dominates a Market," New York Times (Jan. 4, 2010) available at https://www.nytimes.com/2010/01/05/your-money/credit-and-debit-cards/05visa.html ("Competition, of course, usually forces prices lower. But for payment networks like Visa and MasterCard, competition in the card business is more about winning over banks that actually issue the cards than consumers who use them. Visa and MasterCard set the fees that merchants must pay the cardholder's bank. And higher fees mean higher profits for banks, even if it means that merchants shift the cost to consumers.")

[26] U.S. v. Visa, Complaint (Sept. 24, 2024) (available at dl); "Visa Wanted a Vast Empire. First, It Had to Beat Back Its Foes." By Annamaria Andriotis, The Wall Street Journal (Oct. 19, 2024) (available at Visa Wanted a Vast Empire. First, It Had to Beat Back Its Foes. - WSJ).

[27] U.S. v. Visa, Complaint at 53.

which Visa refers to as a 'mutually assured destruction principle.'"[28] "Visa would continue to work with Apple as long as Apple didn't become a competitor, the DOJ said."[29]

The DOJ complaint only addresses the debit card market, but the Wall Street Journal shows that the same actions (if not more troubling practices) also take place in the credit card market. Only debit cards have any semblance of competition between networks because Congress in 2010 required that two networks be enabled on each debit card. The absence of a similar requirement for credit left DOJ in a much more difficult position to bring a case against Visa for its credit card practices. The DOJ case is a clear indication of how strongly legislation is needed to bring a modest baseline of competition to the credit card market.

Another example of the anti-competitive reality of payment cards was the subject of an opinion by the U.S. Fifth Circuit Court of Appeals in litigation brought by Pulse, a debit network, against Visa. In that case, the Fifth Circuit found that Pulse's claims that Visa had violated antitrust laws to squeeze Pulse out of the debit market should be decided by a jury, "And a reasonable jury could find that some of Visa's volume-based agreements amount to exclusive-dealing contracts designed to squeeze Pulse out of the PIN-less transaction market."[30] That was just one legal action raising troubling concerns about what the largest payment networks do to harm competition.

Visa has also sought to bolster its hold on the market and keep out innovative competitors through acquisition. Its attempt to acquire Plaid – a potential competitor in the debit market – led to a lawsuit from the Department of Justice to block the deal during the Trump Administration.[31] Plaid offers a potential alternative technology for consumers to access funds in their bank accounts to pay for things which "likely would drive down prices for online debit transactions, chipping away at Visa's monopoly and resulting in substantial savings to consumers."[32] Visa wanted to block the innovation and cost savings that Plaid could bring to the market by acquiring it – similar to Visa's past pattern of trying to block competition.[33] Acquisitions, exclusivity contracts and other moves have been used by Visa to protect its market power and block potential competition. All of this has been a detriment to the market, merchants, consumers, and the economy.

One of the clearest ways to see just how anti-competitive the credit card system is from a competition policy perspective is to compare it to a paradigm that is generally agreed to be highly problematic. The Organization of the Petroleum Exporting Countries (OPEC) provides just such an illuminating example. OPEC, for example, shares a similar structural foundation to Visa and Mastercard. OPEC was formed by five oil-producing nations that ought to have been competing with each other.[34] Similarly, competing credit card issuing banks joined together to

[28] U.S. v. Visa, Complaint at 50.
[29] Andriotis, WSJ (Oct. 19, 2024).
[30] *Pulse Network, LLC v. Visa, Inc.*, No. 18-20669, 18 (5th Cir. Apr. 5, 2022).
[31] Complaint, *U.S. v. Visa, Inc. and Plaid, Inc*. (Nov. 5, 2020).
[32] *Id*. at ¶ 8.
[33] *Id*. at ¶¶ 44-45.
[34] See OPEC : Member Countries.

form both Visa and Mastercard.[35] OPEC sets a target price for crude oil and influences the market price indirectly through production quotas.[36] Visa and Mastercard, however, directly set the prices that the competitors who founded them (and those added since) charge in the market.[37] By that measure, credit card pricing is less competitive and more constrained than the pricing regime set by OPEC.

Relative share of the market is also an important measure of the ability to constrain competition. OPEC has 37.9% of the market for the production of crude oil and 80% of the world's known reserves.[38] Visa and Mastercard, however, have 83% of the credit cards in circulation in the United States.[39]

If anything, then, the Visa and Mastercard duopoly has a larger share of the market and more tightly controls competitors' pricing than does OPEC. The most eye-opening factor, however, may be the remarkably similar excuses that each organization peddles to try to justify the anti-competitive moves they make.

- OPEC claims: "In order to secure fair and stable oil prices for petroleum producers; an efficient, economic and regular supply of petroleum to consuming nations; and a fair return on capital to those investing in the industry."[40]
- Visa asserts: "Visa uses these fees to balance and grow the payment system for the benefit of all participants."[41]
- Mastercard claims: ". . . we strive to maximize the value of the Mastercard system (including the dollars spent on Mastercard cards, the number and types of cards in circulation, and the number and types of merchants accepting Mastercard cards) by setting default interchange rates at levels that balance the benefits and costs to both cardholders and merchants."[42]

In other words, each of these organizations justifies their actions by claiming that they are helping the public and increasing value to everyone. Unfortunately, it's not true. Instead, they control the market to maximize profits for their members who should be competing with one another. We all know markets where competitors need to compete to win business are what is actually best for everyone. Monopolized markets with centralized price-setting simply are not the best system for anyone other than those jointly controlling the market. This should be an obvious

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[35] See Visa Inc. - Wikipedia (formed by "BankAmericard, Barclaycard, Carte Bleue, Chargex, Sumitomo Card, and all other licensees" in 1976) and Mastercard - Wikipedia ("created by an alliance of several banks and regional bankcard associations").

[36] "What is OPEC+ and How Does It Impact Prices?" Reuters (Nov. 20, 2023) (available at What is OPEC+ and how does it impact oil prices? | Reuters).

[37] Interchange fee - Wikipedia

[38] OPEC - statistics & facts | Statista

[39] Credit Card Market Share Statistics | Bankrate

[40] OPEC : Brief History

[41] Credit Card Processing Fees & Interchange Rates | Visa

[42] Mastercard Interchange Fees & Rates 2022 Explained

point and we should not be fooled by the claims of Visa and Mastercard (or OPEC) that they are actually just acting in a public interest capacity.

IV. The Credit Card Competition Act Would Help

The Credit Card Competition Act would narrowly and specifically address the competition policy problems with the current market in a way that, as noted above, American Compass has referred to as "laser-targeted." The CCCA would only apply to the less than 30 banks that have more than $100 billion in assets. Some of those banks do not issue any significant volume of credit cards. But, of those that do, they would need to enable at least two networks on each card that could handle the payments on those cards. This is what Congress has already required them to do on debit cards, and there are numerous networks that can handle those payments and have been doing so on debit and automated teller machine (ATM) transactions for decades.[43] Similar dual-network systems exist for credit cards in several other countries as well.[44] In fact, JP Morgan Chase notably trumpeted its issuance of credit cards with dual networks in France earlier this year.[45]

They noted the major advantages of such a system including, in particular, "By doing so, the U.S. bank aims to 'provide competitive transaction costs' to its clients, it said, without elaborating."[46]

Under the CCCA, just like JP Morgan Chase in France, the large banks subject to the Credit Card Competition Act would be responsible for selecting which two of the dozen or so network options would be enabled on the credit cards they issue. The banks already have existing relationships with multiple networks through their debit card programs and could make those choices in any way that they want. Presumably, they would both push those networks to set swipe fee rates high and deliver other services such as lower costs to the banks, better security and the like. When those cards were used to pay merchants, in turn, merchants would be able to work with their processors to select which of the two networks on a particular card that the merchant preferred. Similar to the bank, the merchant would make its preferences on the basis of things like the reliability and security of the network as well as the cost to the merchant of using that network (such as the swipe fee pricing of that network).

All of this happens millions of times per day, every day, in the United States on debit cards and works quite well. Consumers aren't even aware that it is happening. In fact, not only are the smaller competitors to Visa and Mastercard on debit often cheaper for merchants to accept than the big incumbents, they have better track records for security. According to the most

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[43] There are more than a dozen current networks including: Star, Pulse, Shazam, ATH, Accel and others. See Federal Reserve Board - Regulation II - Average Debit Card Interchange Fee by Payment Card Network. Some of these networks were processing transactions before Visa and Mastercard ever entered the debit market.

[44] CMSPI State of the Industry Report (Sept. 2024) at 105-106 (available at State of the Industry Report | CMSPI Global).

[45] "JPMorgan joins France's payments network CB to skirt Visa, Mastercard," Reuters (March 5, 2024) (available at JPMorgan joins France's payments network CB to skirt Visa, Mastercard | Reuters).

[46] *Id*.

recent data from the Federal Reserve, the competitive networks have one-eighth of the incidence of fraud per transaction that Visa and Mastercard have.[47]

And, competition for credit card market share will push all of the networks, including Visa and Mastercard, to improve their services and find innovations to attract more business from banks and merchants. That is exactly what happened when regulations requiring two networks on debit cards came into effect more than a decade ago. When those regulations came into place, the Star network quickly announced that it would encrypt all debit transactions from end-to-end – a level of service that had not previously been made available. Because there was competition among networks, that led all of the other networks in the market (including the two largest) to announce they would provide such encryption as well. Competition incentivized the entire market to improve security.

The CCCA would also provide a back-up for times when technology fails or is hacked. Every network has periodic outages. Visa and Mastercard have already had several this year alone within the United States, including:

- June 20, 2024: Visa network
- April 15, 2024: Mastercard network
- February 28, 2024: Visa network
- February 17, 2024: Visa network
- January 3, 2024: Interlink (Visa debit) network

While these episodes may only last a few minutes, they can be disruptive. When a customer's card is declined, they have no way of knowing what the cause was and can be left with no option but to go home without food for that night's dinner, or diapers for their child. Having a second network on credit cards would allow us to mitigate those effects. When this happens with credit cards today, those cards are denied and cannot be used until the outage is resolved. This means the U.S. credit card system has a "single point of failure" incorporated into each card. When Visa or Mastercard goes down, the cards cannot be used. But, the debit card system is not nearly as vulnerable because every card can operate over two networks. That means every debit card can be used even when one network has an outage. We should have that level of reliability for credit cards as well.

Frankly, if the security benefits of switching some of the credit card market from Visa and Mastercard to competitive card networks was the only benefit of the CCCA, it would be well worth passing.

Of course, security is not the only benefit. Competition would also spur all of the network providers in the market to be more efficient and compete on prices. Competition is a central element of improvements in efficiency across the U.S. economy. Analysis of the CCCA predicts that passage would result in swipe fees that are $16 billion lower per year than they would be

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[47] Board of Governors of the Federal Reserve System, "2021 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions" at 36, Table 10 (Oct. 2023) (available at Federal Reserve Board Publication).

without the CCCA.[48] That would mean more than $100 per American family in annual savings. As noted on the New York Times opinion page referencing the CCCA, "The truth is for the vast majority of Americans, the best deal might not come in the form of a new piece of plastic but instead a new piece of legislation."[49] The New York Times piece also noted that the CCCA would use competition to drive down the price of the fees and help deal with the fact that, as the Federal Reserve found, the "average American at every income level loses more to swipe fee prices hikes than they earn in rewards," and the lowest-income Americans "pay five times more in price mark-ups than they'll ever receive in rewards."[50]

As noted, price pressure would not just be in one direction. Networks would continue to compete to provide banks with higher fixed swipe fees, and lower processing costs, so that banks would enable those networks on their cards. The CCCA would just balance this already-existing pressure with a countervailing market pressure to lower fees so merchants would choose one of the card's networks over the other. That is part of why savings would not be nearly as significant under the CCCA as the savings in many nations around the world that have taken more aggressive regulatory action on their fees.

The CCCA would also give banks an opportunity to play the networks against each other to bargain down bank costs. That is exactly what has happened on debit cards. In fact, credit unions have been one of the biggest beneficiaries of network competition on debit cards. A number of them formed a group called Co-op Pay to negotiate with different debit networks and drive down their own costs. They struck a deal with the Star network to do just that.[51] None of that would have been possible without competition among debit networks and the ability of credit unions to put two different competing networks on their debit cards. And, it is worth recognizing that the credit unions did not just negotiate for lower costs, they also bargained for better security services including "predictive fraud scores" from the Star network.[52] Co-op Pay is a good example of the benefits of debit network competition and how credit card competition under the CCCA would similarly help the economy on cost and fraud.

The CCCA would also protect the U.S. credit card market from incursions by China's dominant payment network, China UnionPay, which is a Chinese state-owned financial services corporation. There are legitimate concerns about the way that Visa and Mastercard have brought China UnionPay into the U.S. card security system. Specifically, China UnionPay is a member of the two bodies that govern the security of U.S. payments – the Payments Card Industry Security Standards Council (PCI) and EMVCo. The governing boards of those entities are limited to a

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[48] "Credit Card Competition Act Could Result in Annual Savings Upward of $16.4 Billion" CMSPI (Oct. 18, 2024) (available at Credit Card Competition Act Could Result in Annual Savings Upward of $16.4 Billion | CMSPI Global).
[49] James Robinson and Emily Holzknecht "Your Rewards Card is Actually Bad for You, And for Everyone Else," New York Times (Nov. 21, 2023) (available at Opinion | Your Rewards Card Isn't as Rewarding as You Think - The New York Times (nytimes.com)).
[50] *Id*.
[51] John Adams, "Credit Unions Join Forces to Keep Debit Card Costs Under Control," American Banker (March 13, 2023) (available at Credit unions join forces to keep debit card costs under control | Credit Union Journal | American Banker).
[52] *Id*.

handful of companies and Visa and Mastercard have welcomed China Union Pay to both small governing boards.

In fact, when China Union Pay joined EMVCo's governing board, Visa executive Joe Cunningham said in discussing the entity's work on payment card security, "We are delighted to welcome UnionPay as a member and active contributor to this work."[53]

In 2017, when China Union Pay joined the decision-making body of PCI, PCI executive (and former Mastercard executive) Stephen Orfei said, "Today we welcome [Beijing Unionpay Card Technology Co.] BCTC to the PCI family. This is a world-class facility with outstanding staff expertise. China is a critical market for global commerce and a strategic priority for PCI."[54]

PCI and EMVCo not only set security standards in a closed process but also dictate their implementation. Today, no U.S. bank nor any retailer may sit on the boards of nor vote on the standards set by PCI and EMVCo. Ultimately, a small handful of the dominant U.S. card networks plus Japan's JCB and China Union Pay have complete control over the creation and implementation of payment card security standards that impact all U.S. businesses and consumers. That is a mistake.

Those moves and statements, combined with Mastercard's recent move into the market in China,[55] make us concerned that the dominant networks in the United States are paving the way for China to have an increased role in the U.S. credit card market. There is no law currently on the books that prevents that from happening. The only legislation of which we are aware that creates a legal barrier to that shift is the CCCA. The CCCA would prohibit any U.S. issuer of credit cards from enabling China UnionPay as a network on its credit cards. With no law on the books, any U.S. issuer could do that today. The CCCA would stop China UnionPay before it finds a way onto U.S. credit cards.

[53] "China UnionPay joins EMVCo," Finextra (May 20, 2013) (available at China UnionPay joins EMVCo (finextra.com)).

[54] "Payment card industry security standards council welcomes beijing unionpay card technology co. As pci recognized laboratory," (Feb. 6, 2017) (available at HEADLINE (pcisecuritystandards.org)).

[55] Mastercard Incorporated - Mastercard JV Approved to Begin Domestic Payments Processing in China

V. Swipe Fees Hurt Merchants

Credit and debit card swipe fees are huge business and are growing at an alarming rate. Collectively, U.S. merchants paid $172 billion in fees to accept card payments in 2023.[56] That was a huge jump from the $110 billion that merchants paid in 2020.[57] That is on top of the fees nearly doubling in the decade between 2010 (when the fees were $64 billion) and 2020.[58] And, it followed the decade between 2001 and 2010 when the fees more than tripled from $16 billion to $64 billion.[59]

Perhaps most telling, the fees on Visa and MasterCard credit cards have grown at the fastest pace. Those fees were $26 billion in 2010.[60] By 2023, the fees totaled more than $100 billion.[61] That near quadrupling is a staggering fact and contributes to higher costs and prices throughout the U.S. economy during that time span. The huge multiples by which the fees have grown seem hard to believe, but that is what happens when there is price-fixing in place of competition.

In the convenience industry, recent swipe fee increases have been even more dramatic. In 2022, the total amount of the fees paid by convenience retailers to accept payment cards jumped by more than 40 percent.[62] And, that was before the October 2023 increases pushed through by Visa and Mastercard.[63] These increases are completely unsustainable.

Even before these dramatic jumps, swipe fees, on average, were convenience retailers' second-largest operating cost after labor. In fact, that is true for retailers in nearly every sector. That means swipe fees are more than the average retailer pays for rent or utilities or for any other operating cost. Some convenience retailers have even reported that the fees are approaching their labor costs.

One reason for these dramatic increases is the destructive interaction between swipe fees and inflation. The majority of the amount of credit card swipe fees is set as a percentage of the total amount of each transaction (for example, a fee may be set at 2.30% of the transaction amount plus $0.10). That means swipe fees increase along with every dollar of inflation. And, those swipe fees act as an inflation multiplier, with spiraling fees contributing to higher retail prices which then further increases the fee amounts.

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[56] The Nilson Report (March 2024) (available at 1259 - Nilson Report).
[57] Nilson Report (July 2021) available at Nilson Report – Merchant Processing Fees in the United States—2020.
[58] Stephen Mott, "Industry Facts Concerning Debit Card Regulation Under Section 920," (Oct. 27, 2010) at 14, available at http://www.federalreserve.gov/newsevents/files/merchants_payment_coalition_meeting_20101102.pdf.
[59] *Id*.
[60] The Nilson Report (Nov. 2011) (available at 983 - Nilson Report).
[61] The Nilson Report (March 2024) (available at 1259 - Nilson Report).
[62] NACS State of the Industry (April 2023).
[63] Angel Au-Yeung, "Visa, Mastercard Prepare to Raise Credit-Card Fees," Wall Street Journal (Aug. 30, 2023) (available at Visa, Mastercard Prepare to Raise Credit-Card Fees - WSJ).

During two earnings calls at the height of the inflationary cycle in 2022, in fact, Visa executives made clear that Visa is "a beneficiary of inflation," and that inflation is "a positive for us."[64] Most Americans and American businesses would not say the same of themselves.

When retailers raise their prices, customers notice and often blame them for it even though retailers typically raise prices more slowly than their own costs rise. But, the credit card industry pretends that its swipe fee price increases don't happen. Because card networks set much of their swipe fee prices as percentages, they automatically increase their prices when merchants' prices rise. This automatic price increase mechanism is why the card industry repeatedly pretends they don't increase their fees. But, of course they do increase the fee rates in their schedules and have increased their own fees repeatedly over the last few years.

It is worth noting that swipe fees give credit card issuers a favored claim on businesses' revenue in a way that even business owners do not have. Swipe fees are taken as a percentage of revenue, before expenses. Even business owners must pay their expenses before they can earn a percentage of profits (not revenues). The fact that the card industry pretends that taking more and more dollars out of U.S. businesses magically is not a price increase offends Main Street and our sense of basic decency. The card networks should at least admit the truth.

An area that has among the largest impacts for the convenience industry and for American consumers are gas prices. This industry sells about 80 percent of the gasoline used across the nation. Retailers, similar to their customers, like an ample supply of gasoline and low prices. That is because as gas prices rise, the margins retailers make actually get smaller. Competition in the market means that retailers cannot pass along their own increased wholesale costs as quickly as they pay those costs. At the same time that retailers' margins are getting squeezed, however, their credit card fees are rising because they are a percentage of the total transaction amount. That means there were many times during the 2022 inflationary cycle when retailers were paying more in swipe fees (often about 10 cents per gallon) than they were ultimately making on those sales. That makes no sense given the costs retailers incur and risks they take to maintain a site with underground storage tanks, transport fuel, and sell it to customers (often staying open 24 hours per day in the midst of a labor shortage and, not long ago, a pandemic). Processing those transactions should not cost more than the profits that can be made after all of that effort.

What is particularly troubling for many businesses, however, is that they are powerless to plan for, or deal with, these rising costs. They can take measures to keep other costs in check – installing more energy-efficient equipment, using a different supplier, and the like. But there is no dealing with swipe fees because of the competition problem noted above and the unpredictability of the increases. Businesses just don't know how much the fees will go up. Even after new rates are announced it is difficult to predict how those rates will impact a merchant's fees because the card networks have made the system so complex. GAO reported

[64] *See* Logan Kane, "Visa: A Great Business, But Wait for a Pullback," Seeking Alpha (April 26, 2022) available at https://seekingalpha.com/article/4503588-visa-great-business-wait-for-pullback; "Visa (V) Q2 Earnings Call Transcript," Motley Fool Transcribing (April 27, 2022) available at https://www.fool.com/earnings/call-transcripts/2022/04/27/visa-v-q2-2022-earnings-call-transcript/.

that Visa and MasterCard each had four credit card rate categories in 1991, but by 2009 Visa had 60 rate categories and MasterCard had 243.[65] The numbers have grown since that time and that complexity helps obscure the consistent, large fee increases that merchants must bear.

In fact, Visa is increasing its fees again this January. That is unusual. The two networks typically increase fees only in April and October. We are still investigating the extent of these fee increases, but the dominance of the two networks means that even increases which seem small on a per transaction basis can be massive due to the large number of transactions the networks handle.

Before now, Visa and Mastercard most recently increased their fees in October of 2023. Those changes are adding about $500 million per year in additional costs for merchants.[66] To give you a sense of how the credit card networks operate, both networks issued statements denying that they were increasing fees. But, if you read their statements carefully, you can see that they admit they are creating new fees.[67] And they also increased some fee categories. The denials fit a pattern of misleading Congress and public about what is actually going on. The card networks rely on the complexity of the fees and the difficulty people have sorting out the facts to obscure what they are really doing. The big dollar increases in what merchants pay year after year, however, tell the story that the networks try to deny.

Swipe fees also increase even when Visa and Mastercard do not "raise" them by changing the fee schedules. As noted, inflation is one reason that happens. Another reason is that the banks issuing cards simply push more higher fee cards into the market. That is true for their new and existing customers. Many cardholders receive notification from their bank that they now have a different level of rewards or other perks. It might not be clear to the cardholder why that is, but it is not a mystery to merchants – it means the merchant must pay higher swipe fees. By systematically moving cardholders to more expensive cards, banks can drive up swipe fees without Visa and Mastercard changing their rate schedules at all.

Of course, merchants do not have visibility into the card issuing decisions that drive up their fees. For example, no merchants were provided direct notice by Visa of its price increases scheduled for this January. Frankly, merchants have very little visibility into the price-setting engaged in by Visa and Mastercard. Merchants don't receive direct communications of these changes from Visa and Mastercard. Those notifications go to banks and processors. Typically, when sent, those notifications are deemed confidential so that they cannot be passed along to merchants. The price changes that can so dramatically impact merchants' bottom lines become rumors in the marketplace until they are sprung on merchants with very little notice. The lack of clarity is just another sign of how broken this market is.

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[65] Government Accountability Office, "Credit Cards: Rising Interchange Fees Have Increased Costs for Merchants, but Options for Reducing Fees Pose Challenges," (2009) at Credit Cards: Rising Interchange Fees Have Increased Costs for Merchants, but Options for Reducing Fees Pose Challenges | U.S. GAO.

[66] Angel Au-Yeung, "Visa, Mastercard Prepare to Raise Credit-Card Fees," Wall Street Journal (Aug. 30, 2023) (available at Visa, Mastercard Prepare to Raise Credit-Card Fees - WSJ).

[67] See Setting the record straight – Clarifying recent headlines | Mastercard Newsroom and Sometimes headlines don't tell the whole story | Visa.

Visa and Mastercard also systematically set higher rates for small businesses than they do for large businesses. This can be seen directly in the Visa and Mastercard rate schedules.[68] Visa's rates stratify supermarkets, for example, across multiple tiers based on their transaction volumes. Those with the fewest transactions pay about 42% more per $100 transaction than their larger competitors to accept Signature Preferred cards, for example.[69] According to Visa's rates, supermarkets with less than 16.5 million transactions or $950 million in Visa sales get in the "other" category and pay the highest rates while supermarkets above 370 million transactions and $19.6 billion in Visa volume get into "Tier 0" and pay the lowest rates.[70] Visa sets similar volume tiers that disadvantage small businesses for the general retail category as well.

Mastercard disadvantages small supermarkets even more than Visa. According to its rates, supermarkets with less than $750 million in transactions pay 2.10% plus $0.10 for World Elite cards while the largest ones with more than $6 billion in transactions pay 1.32% plus $0.05.[71] That is a 60% penalty for small businesses on a $100 purchase. Mastercard sets volume tiers that hurt small businesses not only for supermarkets but for general retail, convenience stores, unregulated debit cards, and commercial credit cards.

Visa and Mastercard pricing, then, ensures that every bank across the nation hits small businesses overall with higher fees than larger businesses pay. There is no justification for this unfair disparity and it demonstrates why legislation to reform the credit card system is needed by small businesses even more than it is needed by large businesses across the nation.

VI. Swipe Fees Hurt Consumers

Ultimately, all of us pay for these overinflated swipe fees in the prices of the goods and services we buy. The fierce price competition in retail ensures this. Retail profit margins are notoriously low. As of January 2024, for example, net profit margins for general retailers were 3.09 percent.[72] For grocers and other food retailers, those margins were even narrower – 1.18 percent.[73] With those margins, which are around or below the level of swipe fees these businesses pay, those fees must be passed on to consumers or the retailers would go out of business.

It is worth noting that while retailers' margins are notoriously thin, banks' and credit card networks' margins are very large. The money center and regional banks that dominate credit card

[68] The Visa rate schedule is available at Visa USA Interchange Reimbursement Fees and the Mastercard rate schedule is available at U.S. Region Interchange Bulletin (mastercard.us).
[69] Visa USA Interchange Reimbursements Fees at 7. The smallest supermarkets pay 2% plus $0.07 for Signature Preferred cards while the largest pay 1.4% plus $0.05 for the same cards.
[70] *Id*. at 10.
[71] U.S. Region Interchange Bulletin (mastercard.us) at 2-3.
[72] New York University, "Margins by Sector (US)," at Operating and Net Margins).
[73] New York University, "Margins by Sector (US)."

issuing have net profit margins of 30.89 and 29.67 percent, respectively.[74] Visa's net profit margin as of September 30, 2024 was 54.96 percent and Mastercard's was 45.26 percent.[75] All of those margins are instructive as to the relative competitiveness of these sectors. No other industry sector reported on by NYU had net profit margins higher than those card-issuing banks, and it is likely that none would dare dream of margins at the level of Visa's and Mastercard's.

The current system fools consumers by hiding the large interchange fees that are built into the cost of their purchases. According to the consumer group U.S. PIRG, "Interchange fees are hidden charges paid by all Americans, regardless of whether they use credit, debit, checks or cash. These fees impose the greatest hardship on the most vulnerable consumers – the millions of American consumers without credit cards or banking relationships. These consumers basically subsidize credit card usage by paying inflated prices – prices inflated by the billions of dollars of anticompetitive interchange fees. And unfortunately, those credit card interchange fees continue to accelerate, because there is nothing to restrain Visa and MasterCard from charging consumers and merchants more."[76]

In addition, a number of consumer, public interest and union groups have endorsed the Credit Card Competition Act and quite a few have established a broad coalition to support the bill, the Lower Credit Card Fees Coalition.[77] Members of the coalition include the International Brotherhood of Teamsters, Service Employees International Union, Americans for Financial Reform, American Economic Liberties Project, Accountable.US, U.S. PIRG, National Community Reinvestment Coalition and others.

The European Commission has extensively studied this subject and has found that interchange fees harm consumers. In December 2007, the Commission deemed MasterCard's multilateral interchange fee illegal and Competition Commissioner Neelie Kroes said that interchange "inflated the cost of card acceptance by retailers without leading to any advantage for consumers or retailers. On the contrary, consumers foot the bill, as they risk paying twice for payment cards. Once through annual fees to their bank. And a second time through inflated retail prices . . ."[78] Kroes concluded that MasterCard's interchange "acts like a 'tax on consumption' paid not only on card users but also by consumers using cash and cheques."

One of the most troubling aspects of the high swipe fees imposed by the broken credit card market is the way they impact low-income Americans. The fees get baked into the prices of goods and services with very few exceptions in part due to the longtime pricing constraints imposed by Visa and Mastercard. So, those who do not have or cannot qualify for credit cards

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[74] *Id*.

[75] *See* Visa Profit Margin 2010-2024 | V | MacroTrends and Mastercard Profit Margin 2010-2024 | MA | MacroTrends.

[76] "Testimony of Ed Mierzwinski before the House Judiciary Committee Antitrust Task Force," (May 15, 2008).

[77] See Lower Credit Card Fees.

[78] "Commission Prohibits MasterCard's intra-EEA Multilateral Interchange Fees: Introductory remarks at press conference," available at https://www.parlement.com/id/vhqtky3qp9z8/nieuws/toespraak_eurocommissaris_kroes_over.

pay the cost of these fees as well – as do cardholders with basic cards that don't carry rewards. In 2009, the Hispanic Institute published a paper showing how payment card swipe fees and rewards systematically transferred wealth from low income to high income individuals.[79]

A working paper published by Boston Federal Reserve economists came to the same conclusion: that swipe fees combined with rewards programs amount to a regressive system in which low-income Americans subsidize high-income Americans.[80] This disproportionate negative effect on low-income consumers is particularly unfair.

Another study was released by the Hispanic Leadership Fund in 2022. That study found that because of swipe fees:[81]

1) "Lower income Americans are losing money to higher income individuals.
   - American families earning less than $75,000 per year send a total of $3.5 billion to families earning more than $75,000 per year.
   - More than $1.9 billion of that money goes into the pockets of those making more than $150,000 per year.
   - Families making less than $20,000 per year pay more than $1.2 billion of the $3.5 billion that gets transferred to higher income people."

2) "Black families are disproportionately harmed by today's credit card schemes.
   - The average American Black family pays nearly $60 per year to subsidize higher income people's rewards through these fees.
   - Black families in the United States lose more than $1 billion each year from these transfers."

3) "The current swipe fee structure drives up shelf prices for all Americans regardless of how you pay.
   - The study found that swipe fees cost some retailers between 17 and 19 percent of annual profit.
   - Annual variation in interchange costs drives profit up and down by about 4.5 percent for smaller stores. This added risk generates economic inefficiency, and the entire economy suffers from this unneeded risk."

In addition, in December 2022, Federal Reserve economists published a report that looked at the combination of income and credit scores in this context. They concluded: "We

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[79] Hispanic Institute, "Trickle-Up Wealth Transfer: Cross-subsidization in the payment card market," by Efraim Berkovich (Nov. 2009) available at Trickle-Up Wealth Transfer: (thehispanicinstitute.net).
[80] Marie-Helene Felt, Fumiko Hayashi, Joanna Stavins, and Angelika Welte, "Distributional Effects of Payment Card Pricing and Merchant Cost Pass-through in the United States and Canada," Federal Reserve Bank of Boston (Dec. 2020) at 4, available at https://www.bostonfed.org/publications/research-department-working-paper/2020/distributional-effects-payment-card-pricing-merchant-cost-pass-through-united-states-canada.aspx.
[81] Efraim Berkovich and Zheli He, "Rewarding the Rich: Cross-Subsidies from Interchange Fees," Hispanic Leadership Fund (May 2022) available at https://hispanicleadershipfund.org/.

estimate an aggregate annual redistribution of $15 billion from less to more educated, poorer to richer, and high to low minority areas, widening existing disparities."[82]

Those findings are staggering. Low-income Americans should not be forced to pay for their wealthy neighbors' airline tickets, but that is precisely what Visa and Mastercard's anti-competitive practices cause. According to the New York Times, "So this rewards card, it's really a screw-over-poor-people card."[83] Of course, the Times also made clear, "You're probably not benefitting from rewards as much as you thought. In 2020, the Federal Reserve found that the average American at every income level loses more to swipe fee price hikes than they earn in rewards."[84]

Not only have fees increased dramatically and moved money from low-income to high-income Americans, but these fees change the nature of the credit card business in a way that hurts consumers. As Georgetown Law professor Adam Levitin observed in testimony before the House Judiciary Committee, the huge fee revenue the banks earn from credit card transactions taking place has created bad incentives. He testified, "The card industry's business model is the heart of the problem and needs to change. Just as with subprime mortgages, the credit card business model creates a perverse incentive to lend indiscriminately and let people get into so much debt they can't pay it back."[85]

Others have clearly observed this trend as well. For example, Acting Comptroller of the Currency Julie Williams said in March 2005, "Today the focus for lenders is not so much on consumer loans being repaid, but on the loan as a perpetual earning asset . . . it's not repayment of the amount of the debt that is the focus, but rather the income the credit relationship generates through periodic payments on the loan, associated fees, and cross-selling opportunities."[86] These changes mean that banks are less worried than they should be about consumers' welfare. It should be in the interest of banks for consumers to do well and be able to pay back credit card loans. But the huge fee income the banks generate through interchange and other fees gives them another incentive – milk consumers for all they are worth and don't worry about the money getting paid back.

The bottom line is that abuse of consumers by banks will continue as long as banks have the incentive to treat people that way. Interchange fees are the key incentive with which Congress has not yet dealt. Abuses of consumers and using credit cards as predatory lending vehicles will continue until something is done about interchange fees.

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[82] Sumit Agarwal, Andrea Presbitero, Andr´e F. Silva, Carlo Wix, "Who pays for your rewards? Redistribution in the credit card market," December 2022 (available at [Who Pays For Your Rewards? Redistribution in the Credit Card Market (federalreserve.gov)]).

[83] "Your Rewards Card Is Actually Bad for You, and for Everyone Else," New York Times (Nov. 21, 2023) (available at [Opinion | Your Rewards Card Isn't as Rewarding as You Think - The New York Times]).

[84] *Id*.

[85] Adam J. Levitin, Testimony before the House Judiciary Subcommittee on Commercial and Administrative Law, "Consumer Debt – Are Credit Cards Bankrupting Americans?" (April 2, 2009).

[86] Remarks by Julie L. Williams, Acting Comptroller of the Currency, Before the BAI National Loan Review Conference, New Orleans, LA, (March 21, 2005) available at http://www.occ.treas.gov/ftp/release/2005-34a.pdf.

The credit card industry strenuously argues that if anything at all happens to reduce swipe fees, then other fees paid by consumers will increase and consumers will be in a worse position than they are today. This is false. In fact, the European Commission's Directorates for Competition and Financial Services jointly conducted a comprehensive study into the European payment card industry in general, and Visa and MasterCard in particular. The Commission found no evidence to support the card systems' arguments that the high fee levels associated with the existing interchange system benefit consumers. In particular, the Commission rejected arguments that lower interchange fees to merchants would result in higher fees to consumers:

> "There is no economic evidence for such a claim. Firstly, the inquiry's data suggests that in most cases card issuers would remain profitable with very low levels of interchange fees or even without any interchange fees at all. Secondly, the international card networks have failed to substantiate the argument that lower interchange fee would have to be compensated with higher cardholder fees. The evidence gathered during the inquiry rather suggests that the pass-through of higher interchange fees to lower cardholder fees is small. Consumers already pay the cost of the interchange fee without knowing it. This cost is now hidden in the final retail price and is therefore non-transparent."[87]

University of Utah economist Hal Singer has written that this argument stems from a fallacy put forth by the financial services industry.[88] He notes that there is no economic basis for this industry-backed myth. Instead, the myth exists as a shield against any type of reform. Essentially, the financial services industry claims that, should any legislation pass that it does not like, the industry will hurt consumers – and that therefore it is futile to try to do anything to deal with problems in the industry. They came up with the myth simply to hold off any effective oversight of their practices.

Federal Reserve economists' have made similar findings. They found that in fact banks collect higher interest and fee payments from people who use cards with higher swipe fees rates.[89] The opposite would be true if there was any merit to the credit card industry's claims.

The truth, as noted above by Professor Levitin and others, is that the industry will hurt consumers regardless of whether any legislation is passed because there is an incentive for them to continue to do so.

Experience in the United States confirms the findings of the European Commission's Directorates for Competition and Financial Services that unchecked, anticompetitive fees do not

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[87] European Commission, Directorates on Competition and Financial Services, *Competition: Final report on retail banking inquiry – frequently asked questions*, Jan. 31, 2007, *available at* http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/07/40&format=HTML&aged=0&language=EN&guiLanguage=en.

[88] "The Lie Banks Use To Protect Their Late-Fee Profits," by Hal Singer, The Lever (March 20, 2024) (available at The Lie Banks Use To Protect Their Late-Fee Profits).

[89] Sumit Agarwal, Andrea Presbitero, Andre Silva, and Carlo Wix, "Who Pays For Your Rewards? Redistribution in the Credit Card Market," Federal Reserve Board, Finance and Economics Discussion Series (Dec. 2022) at 11, 16-17 (available at Who Pays For Your Rewards? Redistribution in the Credit Card Market)

provide any redeeming value to consumers. As swipe fees have skyrocketed over the past few years, consumer interest rates on credit cards have moved in the same direction. For example, average interest rates that banks charge consumers on credit cards grew to 27.82% at the end of last year.[90] In fact, more than one in three credit cards had interest rates of 30% or more.[91] This is while financial institutions across the nation paid average interest rates on savings accounts that consumers had at those institutions of . . . 0.46%.[92] That is obviously far out of balance and shows that the more than $1,000 per year in swipe fees that the credit card industry brings in from the average American family is doing nothing to help prevent those same financial institutions from taking every penny they can directly from consumers.

In short, the evidence could not be clearer that higher swipe fees do not help reduce consumer fees at all. That is because rewards cardholders, whose cards generally result in higher swipe fees, actually pay higher average interest rates than many other categories of cardholders.[93] That is in addition to the $6.4 billion in annual fees (often paid by rewards cardholders) that banks collected.[94] If there were any truth to the credit card industry's claims, they would at the very least give rewards cardholders a break on their interest rates compared to other consumers. The unfortunate fact is that the credit card industry will take as much as it can in fees and interest payments from anyone it can – regardless of how greatly it profits from the broken market for swipe fees. Without competition to constrain its actions, everyone will just continue to pay more.

VII. Swipe Fees Hurt the U.S. Economy

Payments should not cause all these negative outcomes. The purpose of having money (as opposed to just bartering for goods and services) is to reduce transaction costs and make buying and selling things more efficient. Our credit card system unfortunately does the opposite. The comparison to our hundred-year-old system of paper checks is instructive. It was not that long ago that the originals of those checks had to be transported around the country to the proper banking institutions in order to clear payments. That was an expensive way to do things. But, remarkably, the Federal Reserve prohibited the equivalent of swipe fees (known as exchange fees) from being charged on checks. There were (and are) still costs to processing checks, but the system works efficiently and those who accept and handle checks are able to make decisions about how to conduct business and how best to keep their costs under control.

Electronic payments should be much more efficient than paper payments. The actual costs of handling electronic payments are indeed lower. But, the prices paid by all of society are

[90] Michelle Black and Robin Saks Frankel, "What is the Average Credit Card Interest Rate This Week? December 18, 2023," Forbes Advisor (Dec. 18, 2023) (available at What Is The Average Credit Card Interest Rate? – Forbes Advisor).

[91] "Average Credit Card Interest Rates in America Today," Lendingtree (Dec. 14, 2023) (available at Average Credit Card Interest Rate in America Today | LendingTree).

[92] Casey Bond, "Good News: The average savings account interest rate is still on the rise," Fortune (Dec. 18, 2023) (available at What's the average savings account interest rate for 2023? | Fortune Recommends).

[93] See "Average Credit Card Interest Rates in America Today," Dec. 14, 2023 , supra.

[94] "The Consumer Credit Card Market," Consumer Financial Protection Bureau (Oct. 2023) at 63 (available at 2023 Consumer Credit Card Market Report).

much, much higher on electronic payments due to competition problems inflating the associated fees.

An economist with the Federal Reserve Bank of Kansas City has illustrated this problem by showing that even U.S. debit cards, which are subject to some regulation of their swipe fees, are more expensive for merchants to accept than cash.[95] The study found:

- Credit cards are the most expensive payment method to accept[96] – which is why the interesting thing to look at was debit versus cash.
- Debit cards are 2.5 times more expensive for merchants to accept than cash.[97]
- Debit fees alone are more than all of the costs of accepting cash before even getting into other costs of accepting debit cards (like card readers, PIN pads, handling receipts, etc.).[98]
- In the other countries studied, cash is more expensive than debit cards in significant part because debit fees are much lower in other countries than in the United States, even with the debit regulations that are in place in the United States.[99]

The United States is an outlier in the world in this area – and not in a good way. Credit swipe fee rates are higher in the United States than anywhere in the industrialized world.[100] This harms American retailers and consumers – disadvantaging them compared to the rest of the world. Just to take one example, merchants and consumers in China pay much lower rates than their American counterparts.[101]

These fees are stunting business growth and hurting efforts to hire more workers and expand operations. One study of this impact in 2010 concluded that without the higher prices caused by fees above and beyond costs plus a reasonable rate of return, consumers would have an additional $26.9 billion to spend (due to lower retail prices) and the economy could add 242,000 jobs.[102] Of course, the fees have tripled since that report was written. The lost economic growth during that time period is likely immense.

The Department of Justice complaint against Visa points to additional ways in which the credit card industry's actions harm the economy. That is because – through buying off competitors and blocking others through pricing power and other means – Visa has kept new potential innovations from coming to market. Those types of innovations bring immense value to the economy. They drive efficiency and productivity and make consumers' lives better. Unfortunately, while the rest of the world has left the United States in the dust on mobile

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[95] Fumiko Hayashi, "Cash or Debit Cards? Payment Acceptance Costs for Merchants," Federal Reserve Bank of Kansas City, Economic Review, Third Quarter 2021 (available at Cash or Debit Cards? Payment Acceptance Costs for Merchants (kansascityfed.org)).
[96] *Id*. at 46.
[97] *Id*. at 52.
[98] *Id*. at 59.
[99] *Id*. at 59.
[100] *See* Kansas City Federal Reserve, "Credit and Debit Interchange Rates in Various Countries August 2021 Update," CreditDebitCardInterchangeFeesVariousCountries_August2021Update.pdf (kansascityfed.org).
[101] *Id*.
[102] Robert J. Shapiro and Jiwon Vellucci, *The Costs of Charging It in America: Assessing the Economic Impact of Interchange Fees for Credit Card and Debit Card Transactions*, Feb. 2010, at 2.

payments and innovative services interacting with their banks, Visa and its stranglehold on the market has held us all back.

Overinflated swipe fee rates cause other economic problems as well. The U.S. credit card system has the most fraud in the world.[103] The United States accounted for 25% of global card volume but 41% of global fraud in 2022.[104] These problems are related. The high fees reduce the economic incentives for the credit card industry to fight fraud – because they make money even with relatively high fraud rates and would have to spend money to make the system safer for all of us. And, not incidentally, much of the fraud on credit cards gets charged back to merchants so the credit card industry does not lose those funds – the merchants do.

Rather than taking straightforward actions that have proven to be effective in fighting fraud, like requiring the entry of personal identification numbers (PINs) or using other means of authenticating the person making the transaction, the card networks have pushed most of the costs of fighting fraud onto merchants. The switch to chip cards in the United States is a primary example. While the vast majority of the world required PINs as part of that switch, Visa and Mastercard not only did not do that here, but they threatened retailers that tried to require PINs with fines.[105] Instead of the common-sense chip-and-PIN measure that had been successful around the world, merchants were forced to spend $30 billion to upgrade their point-of-sale equipment and software to make the transition to chips without the protection of PIN usage. And, for their trouble, many merchants were still required to pay more to cover fraud.

In fact, a 2019 analyst report found that the card networks use their positions in setting card security standards to entrench their own market share at the expense of focusing on card security and fraud protection. They do this through their control of the standard-setting body called EMVCo.[106] According to the report, "Our research reveals an insidious pattern in which the card companies use EMVCo as a tool to maximize their share of transaction volumes: when the card companies feel threatened by competitive pressures or economic challenges, they — or EMVCo supporting their strategies — assume responsibility for the definition of a standard, which results in technical specifications that only benefit the card companies, not the U.S. payments industry at large."[107] Security standards should be made to protect against fraud, not to secure market share for already-dominant companies.

Foreign influence on EMVCo and the Payment Card Industry Data Security Standards Council (PCI) raises additional concerns and provides more evidence that Visa and Mastercard prioritize their market share over card security. Both EMVCo and PCI are primarily controlled

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[103] "Credit Card Fraud Statistics," Shift Processing (Sept. 2021) available at Credit Card Fraud Statistics [Updated September 2021] Shift Processing.

[104] The Nilson Report (December 2023) (available at 1254 - Nilson Report).

[105] Robin Sidel, "Kroger Sues Visa Over PIN Debit Transactions," Wall Street Journal (June 27, 2016) at Kroger Sues Visa Over PIN Debit Transactions - WSJ.

[106] RPCG Group, "Payment Insecurity: How Visa and Mastercard use standard setting to restrict competition and thwart payments innovation," (Dec. 2019) available at https://securepaymentspartnership.com/paper.pdf. EMVCo was started by Visa, Mastercard and Europay but the governing body now includes American Express, Discover, Japan's JCB and China's Union Pay.

[107] *Id*. at 8.

by Visa and Mastercard, yet both bodies brought China's dominant payment network, China UnionPay, onto their decision-making bodies. The timeline makes it appear that this was done to enhance Visa's and Mastercard's business interests with Chinese entities in China, not to improve payment card security. The sequence includes:

- In 2010, Mastercard entered into a Memorandum of Understanding with China UnionPay to "explore business cooperation."[108]
- Then, in 2013, EMVCo – the security standards body controlled by Visa and Mastercard – made China UnionPay a member of its governing body.
- Visa executive Joe Cunningham said at the time of EMVCo's work on payment card security, "We are delighted to welcome UnionPay as a member and active contributor to this work."[109]
- Then, in 2017, the Payment Card Industry (PCI) Security Standards Council, also controlled by Visa and Mastercard, welcomed China UnionPay into its decision-making body on payment security.[110]
- Then PCI executive (and former Mastercard executive) Stephen Orfei said at the time, "Today we welcome [Beijing Unionpay Card Technology Co.] BCTC to the PCI family. This is a world-class facility with outstanding staff expertise. China is a critical market for global commerce and a strategic priority for PCI."[111]
- In 2023, Mastercard was approved to do business through a joint venture in China.[112]

The threat is even clearer in light of China's data practices overall. For example: "Elaine Dezenski, senior director and head of the Center on Economic and Financial Power at the Foundation for Defense of Democracies, said fears of UnionPay are part of a broader concern over Chinese companies operating in the U.S. as part of Beijing's military and intelligence apparatus. China's national intelligence law requires all Chinese businesses and citizens operating overseas to gather sensitive information from host countries and provide that data to the government."[113]

The large amounts of fraud on U.S. credit cards add costs to the economy, nearly $14 billion in 2022.[114] All of us must pay for that as well as swipe fees. And, those swipe fees are inhibiting rather than helping the effort to reduce fraud in the United States. The collective price

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[108] The Memorandum of Understanding between Mastercard and China UnionPay has been removed from Mastercard's website but can be found here: China UnionPay and MasterCard Sign MOU to Explore Business Cooperation | MasterCard Social Media Newsroom.

[109] "China UnionPay joins EMVCo" (May 20, 2013) (available at China UnionPay joins EMVCo).

[110] "Payment Card Industry Security Standards Council Welcomes Beijing UnionPay Card Technology Co. as PCI Recognized Laboratory," (Feb. 6, 2017) (available at HEADLINE).

[111] *Id*.

[112] "Mastercard will soon be widely accepted in China," by Michelle Toh, CNN (Nov. 21, 2023) (available at Mastercard will soon be widely accepted in China | CNN Business).

[113] "Bill aimed at reducing credit card 'swipe fees' puts Chinese company in crosshairs," Jeff Mordock, The Washington Times (May 13, 2024) (available at Bill aimed at reducing credit-card 'swipe fees' puts Chinese company in crosshairs - Washington Times).

[114] The Nilson Report (December 2023) (available at 1254 - Nilson Report).

tag for all of these inefficiencies is far higher than it should be. The United States has the largest economy in the world and should have the most effective and cost-efficient payment system. It doesn't. That should change.

VIII. Dispelling Myths the Card Industry Uses to Distract From Its Anti-Competitive Behavior

As noted, anti-competitive behavior on the part of the major card networks causes serious problems for merchants, consumers, and the U.S. economy. Because the card networks cannot justify their actions and struggle to defend them, they typically try to distract any focus on their activities with complaints about any potential reform. As Senator Mark Warner said prior to a Senate Banking Committee hearing last year, "The banking community always says, anytime there's new regulation, the sky is falling."[115] When the topic is swipe fees, not only does the industry raise false claims about the Credit Card Competition Act (and any other proposal), but it also criticizes the reforms Congress and the Federal Reserve put in place more than a decade ago to deal with anti-competitive activity in the debit card market. These arguments are a distraction, as well as factually wrong, and the Committee should not let the card networks try to distract its attention with those points – particularly when legislative attempts to derail those reforms have repeatedly failed over many years.

It should also be noted that the bank industry sources they use to criticize debit reform all focus attention on the regulation of debit fees imposed by those reforms, a form of regulation that does not exist in the Credit Card Competition Act. The dual network competition aspects of debit reform have not been the subject of study or criticism because they have worked well – at least when Visa and Mastercard haven't broken the law to evade those reforms, such as through the actions detailed by the Department of Justice complaint against Visa.

Nonetheless, the section below addresses many of the myths that the credit card industry raises in order to set the record straight on these claims.

- <u>Consumers and Businesses Have Benefitted from Debit Reform By Saving</u>

Debit reform authored by Chairman Durbin, which was enacted in 2010 and took effect in 2011, has been helpful in curtailing debit swipe fee rates and providing competition among networks.[116] One report showed that debit reform saved consumers $5.86 billion in 2012 alone - the first year the reforms were in effect.[117] That was nearly 70 percent of the overall savings from debit reform that year with merchants saving an additional $2.64 billion.[118] Collectively, these savings supported more than 37,000 jobs[119] – a significant economic stimulus.

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115 Brendan Pederson, "What Top Bank CEOs Will Say to the Senate Today," Punchbowl News (Dec. 6, 2023) (available at AM: Washington, boxed in (punchbowl.news)).

116 While reform has been beneficial, the rates paid by merchants remain higher than they should be. Costs have declined over the past decade and the rates are not proportional to costs.

117 Robert Shapiro, "The Costs and Benefits of Half a Loaf: The Economic Effects of Recent Regulation of Debit Card Interchange Fees," (Oct. 2013) available here.

118 *Id*. at

119 *Id*. at

In addition, *Moody's Investor Service* has reported that debit reform savings have shielded consumers from higher prices that would have resulted from increases in other operating costs for businesses such as transportation and fuel costs. The report says, "As merchant acquirers pass on debit fee savings to retailers, we believe retailers will use them to help shield customers from the impact of these other rising costs."[120] The report also noted, "While on the surface it would be easy to presume that retailers would benefit from a reduced debit interchange fee, we do not expect retailers to see a material improvement in their earnings due to the Durbin Amendment."

The Moody's report is supported by analysis of how pricing moved following the implementation of debit reform. The data shows that there was inflation in the U.S. economy in the years after debit reform was implemented. Cost increases, as reflected in the Producer Price Index for retail trade industries, rose 9.4 percent from the time reform went into effect in October 2011 through the end of 2016, while price increases to consumers, reflected in the Consumer Price Index, increased only 4.3 percent.[121] That is a large spread between the higher costs that merchants had to pay for the goods they sold and the prices that they charged consumers. Those numbers demonstrate clearly that merchants shielded their customers from the majority of the cost increases the merchants themselves faced. And, that experience has held true even during the recent increased inflation. During 2021, for example, the Producer Price Index rose by 9.7 percent while the Consumer Price Index rose by 7 percent.[122]

Retail profit margins show the same pattern. Those margins did not grow following debit reform. In fact, in the grocery industry, pretax profit margins in the two years prior to debit reform were 2.3 percent – and following debit reform those margins fell to 2.1 percent (in 2012) and 1.9 percent (in 2013).[123]

This data reconfirms the intensely competitive nature of U.S. retail. It is very clear that savings from debit reform (and more) have been consistently passed along from merchants to consumers in the form of prices that are significantly lower than what consumers would have been forced to pay in the absence of those reforms.

Anyone who believes free markets work would need to recognize that cost savings to retail businesses help hold down prices to consumers – unless they believe that there is a market failure in the retail sector of the economy. Of course, there is not. Retail is one of the most competitive sectors of the U.S. economy and has been for decades. Without a market failure, there is no question that reduced costs pass through into lower prices. By arguing otherwise, it

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[120] "New Debit Rules Hurt Banks and Reshape the Payment Processor Market," Moody's Investor Service (June 20, 2012) at 10.

[121] Producer price index figures from the St. Louis Fed can be found here: https://fred.stlouisfed.org/series/PCUARETTRARETTR and consumer price index figures from the Minneapolis Fed can be found here: https://www.minneapolisfed.org/community/teaching-aids/cpi-calculator-information/consumer-price-index-and-inflation-rates-1913.

[122] The U.S. Bureau of Labor Statistics' release on the producer price index can be found here: Producer Price Index News Release summary - 2021 M12 Results (bls.gov) and the 2021 increase in the consumer price index can be found here: CPI Home : U.S. Bureau of Labor Statistics (bls.gov).

[123] "Grocery Store Chains Net Profit," FMI available at FMI | Grocery Store Chains Net Profit.

makes it sound as though the credit card industry has lived with centralized price-setting so long that they have forgotten how real competitive markets work.

The leading report the credit card industry uses to try to say that merchants did not pass-through savings in fact proves the opposite. The report says, "Relative to the average savings per gallon that we estimate in Table 6 ($.0076/gallon) this represents only a 53 percent pass-through of gas retailers' Durbin savings."[124] They also noted that in fact their estimate is low due to some of their results being "noisy" – that is, there were other factors impacting price too. The report states: "Further work on Durbin's impact on gas margins is necessary and these are rough and preliminary estimates. We find it more likely that the upper bound on passthrough we estimate for high-debit zipcodes reflects Durbin's impact than the estimate for low-debit zipcodes, where results are noisy."[125] So, the leading report cited by the credit card industry, which the industry claims shows consumers don't save, actually shows that 53 percent of savings goes directly to consumers and that savings are likely higher than the paper estimates.

And, the report explains "This is consistent with the observation of Wang et al. (2014) that many merchants do not know that their interchange expense decreases following Durbin's enactment. However, in zipcodes where Durbin looms large—**where interchange expense falls significantly—retailers do revise prices quickly**."[126] So, in an industry with 60 percent single-store operators, they found that those who didn't have much debit volume and didn't necessarily realize they had saved were less likely to pass-through savings, but that those with significant savings changed their prices quickly to react to it. This shows that the statements made by the credit card industry denying consumer savings are contradicted by the information that they themselves promote.

The credit card industry also likes to point to a report released by the Richmond Federal Reserve to try to disprove consumers' clear benefits from debit reform. The problem is that, in talking about that report, they never mention the cautionary notes that the study's authors themselves included in the report – which make clear it should not be used to prove the point for which the credit card industry tried to use it. First, the report made clear they did not look at actual costs and prices - it was just an opinion survey.[127] Second, the survey sample was small and could have been biased by getting responses primarily from those dissatisfied with the way the Fed wrote its regulation. Finally, it is worth noting what may be obvious given today's economic environment: inflation is always present and matters. The actual data shows that merchants held prices down as their costs increased. That is real consumer savings. But a survey that asks whether prices were reduced would not get that information. What it would and did get

[124] Vladimir Mukharlyamov and Natash Sarin, "The Impact of the Durbin Amendment on Banks, Merchants, and Consumers," Penn Carey Law: Legal Scholarship Repository (Jan. 31, 2019) (available at The Impact of the Durbin Amendment on Banks, Merchants, and Consumers (upenn.edu)).
[125] *Id*. at 31.
[126] *Id*. at 32.
[127] Renee Haltom and Zhu Wang, "Did the Durbin Amendment Reduce Merchant Costs?" (Dec. 2015) at 4, available here.

is that the vast majority of merchants held their prices in check even though there was inflation and overall costs were rising. If anything, the survey reinforces the point that consumers saved.

- Rewards Will Not End (and the Sky Will Not Fall) if Congress Passes the Credit Card Competition Act

The credit card industry consistently argues that any reforms to the current credit card market will end credit card rewards. In fact, they have spread false advertisements all over television and the Internet alleging that Senators Durbin and Marshall want to end credit card rewards.

It is worth noting that these advertisements started running long before there was any legislation proposed by Senator Durbin or anyone else on this topic. You might think that the credit card industry would want to review any such proposal and analyze its effects before giving a reasoned evaluation of its impact – but you would be wrong. The credit card industry doesn't let details such as facts get in the way of its talking points. That's right, the huge, multimillion dollar campaign scaring people about rewards programs was invented before legislation was even written. It wasn't based on any proposal at all.

It should not be surprising then that these ads have been fact-checked as "False."[128] While the United States has the highest credit card swipe fees in the industrialized world, the rest of the world still has credit card rewards. The one study actually quantifying rewards in other nations—and how they were impacted by much more strict reforms than the Credit Card Competition Act—found that the legislation would reduce rewards in the United States by less than one-tenth of one percent.[129]

The credit card industry resorts to these tactics because the facts are not on its side. Simple math shows that the card industry makes multiples of its rewards costs directly from credit card consumers – without ever counting a single dime earned from merchants through swipe fees. Here are the numbers:

- Annual Fees – many rewards cards carry annual fees that are paid for by cardholders
  - Annual fees can run individual cardholders hundreds of dollars per year
  - Total annual fees collected by big banks in 2022: $6.4 billion[130]
- Late fees and other fees
  - Banks collected $14.5 billion in credit card late fees in 2022[131]
  - Banks also collected more than $4 billion in non-sufficient funds and other fees in 2022[132]

[128] Credit Card Competition Act in Congress doesn't ban card rewards | verifythis.com
[129] Rewards Margins are High Enough to Withstand Competition | CMSPI Global
[130] "The Consumer Credit Card Market," Consumer Financial Protection Bureau (Oct. 2023) at 63 (available at 2023 Consumer Credit Card Market Report).
[131] *Id*. at 5
[132] *Id*. at 67

- Interest payments – consumers paid a record amount of interest on credit card balances in 2022
    - The more than $100 billion in interest payments covered rewards completely and provided huge profits on top of that[133]
- Rewards as a profit center
    - Total rewards earned by cardholders in 2022 were $41.1 billion[134]
    - The total credit card revenues directly from consumers noted above was **$125 billion** (without a single dollar in swipe fees)
    - The result is $84 billion in gross profit margin above rewards

Of course, that extra $84 billion of margin understates how much more the card industry makes from consumers than it provides in rewards. For example, many rewards never get used. Cardholders had $33 billion in unused rewards in 2022.[135] And, rewards consistently get devalued so they are worth less than when they were given out in the first place.[136] The rewards' dollar value is as much of a myth as their revenue source.

Those numbers make clear that rewards will not be negatively impacted in any significant way no matter what happens with swipe fees.

Facts around the world prove this as well. The nation with the longest track record of credit card fee reforms is Australia. After more than a decade under reforms there, the Reserve Bank of Australia found, "The existence of significant credit card rewards programs suggests that credit card interchange fees are currently materially higher than is necessary for banks to provide payment cards with credit functionality. The Bank's 2013 Payments Cost Study shows that – for the average-size transaction for each payment method – the existence of the interest-free period and rewards means that the effective price paid by a cardholder to use a credit card is lower than that for a debit card, even though the resource costs are substantially higher."[137]

When Australia acted, MasterCard said it would mean the end of the credit card system in that nation – arguing that there would be a "death spiral."[138] They were wrong. More consumers used more cards than before in Australia. In fact, rather than Visa and MasterCard competing to raise interchange fees so that banks would issue more of their cards, they had to give consumers what they really wanted – lower interest rates on their cards. This interest rate competition benefitted consumers immensely. The only ones who don't like it are Visa and MasterCard (and their member banks) because they don't make as much on interchange fees and must now

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133 *Id*. at 52
134 *Id*. at 69
135 *Id*. at 100
136 "Credit Card Rewards: Issue Spotlight" Consumer Financial Protection Bureau at 3 (May 2024) (available at Credit Card Rewards Issue Spotlight).
137 Reserve Bank of Australia, "Review of Card Payments Regulation," at sec. 3, available at https://www.rba.gov.au/payments-and-infrastructure/review-of-card-payments-regulation/conclusions-paper-may2016/interchange-fees-and-transparency-of-card-payments.html.
138 *See* Alan S. Frankel, "Toward a Competitive Card Payments Marketplace," at 40, available at https://www.rba.gov.au/payments-and-infrastructure/resources/publications/payments-au/paymts-sys-rev-conf/2007/5-compet-card-payment.pdf.

compete more thoroughly on the value they deliver to consumers. The Reserve Bank of Australia reviewed the interchange reforms instituted there and concluded, "Overall, consumers are benefiting from this greater competition and lower merchant costs . . . one group of consumers clearly better off are those who regularly borrow on their credit cards. They are now able to obtain a card with an interest rate of 10 to 13 per cent, rather than the 16 to 18 per cent payable on traditional cards. For many consumers the resulting savings can run into hundreds of dollars per year . . . Consumers who do not use credit cards at all are also benefiting from the reforms as they are paying lower prices for goods and services than would otherwise have been the case. For many years, these consumers have helped subsidise the generous reward points of the credit card issuers through paying higher prices for goods and services. The reforms have helped unwind some of this subsidy."[139]

In fact, despite Australia capping swipe fees in that country at less than one-fourth of the U.S. average rates, they still have so many rewards programs that they have services to give consumers advice and guidance on their rewards – it's called Point Hacks.[140] Similarly, Great Britain and Canada, which both have more regulation and lower fees than the United States, have their own websites dedicated to giving consumers tips about all of the many rewards programs available in those countries.[141]

Lower fees, competition, and other reforms in other countries have not stopped Visa and Mastercard from aggressively marketing their networks to banks around the world. It is clear that there is plenty of revenue in nations with far lower fees for the credit card business to be very profitable.

Further, the Credit Card Competition Act would only apply to less than thirty out of the thousands of banks and credit unions in the nation, meaning that banks that fall outside its scope would be able to continue doing business exactly as they do today. If a handful of the largest banks were tempted to reduce rewards, they would create market opportunities for the vast majority of banks that are exempt from the Credit Card Competition Act. That, in turn, would mean those large banks would quickly increase their rewards in order to compete and keep market share.

And, it's worth noting that merchants offer many rewards programs to loyal customers with profit margins that are less than one-tenth the banks' profit margins.[142] Nothing in the Credit Card Competition Act would dent banks' profits to bring them in line with most competitive market profits (and certainly not down to the level of merchant profits). There is simply no reason or evidence to show that those banks would significantly cut back on rewards programs if there were some modicum of price competition around swipe fees.

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[139] Payments System Board Annual Report, *Reserve Bank of Australia*, 2005 at 14.

[140] See Find The Best Frequent Flyer Credit Cards | Point Hacks.

[141] See What are the top UK travel credit card sign-up deals? (headforpoints.com) and Canada's Premier Credit Card, Points and Miles Resource | Rewards Canada

[142] A few examples of the many, many merchant rewards programs can be found at 20 Retail Brands with the Best Customer Loyalty Programs.

- Consumers Will Continue to Have Credit Card Options

Federal Reserve economists have made a number of findings that demonstrate how the economics of credit cards actually work. Specifically, banks earn more from interest payments from consumers on credit cards than they earn from interchange fees.[143] The paper makes clear that economic rationale for banks to offer credit cards exists at every income level due to the large revenues earned from consumers in the form of interest payments and fees. Arguments that credit options (particularly for low income people) will be negatively affected are wrong and unsupported by the evidence. This is simply another form of the debunked 'lump of profits' argument that Hal Singer addressed. The $125 billion in credit card industry revenue directly from cardholders demonstrates that the market is much too lucrative for swipe fee reform to have any appreciable negative impact on the appetite for banks to issue more credit cards to consumers.

- Free Checking Increased Following Debit Reform

The credit card industry likes to claim that consumers had fewer options for free checking accounts following debit reform, but their claims are demonstrably wrong. At the outset, it should be noted that the banking industry has admitted that "free" checking is a fallacy, with a Bank of America spokesperson admitting that "Customers never had free checking accounts. They always paid for it in other ways, sometimes with penalty fees."[144]

In addition to Bank of America's doubts about free checking ever having existed, it should be noted that the banking industry rapidly got rid of many free checking account offerings in the years *before* debit reform ever took effect. First, the banking industry blamed the financial crisis as the reason why they had to take away free checking and charge consumers higher fees.[145] Then, the industry pivoted and started blaming overdraft regulations for their decisions to

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[143] Sumit Agarwal, Andrea Presbitero, Andre Silva, and Carlo Wix, "Who Pays For Your Rewards? Redistribution in the Credit Card Market," Federal Reserve Board, Finance and Economics Discussion Series (Dec. 2022) at 9 (available at Who Pays For Your Rewards? Redistribution in the Credit Card Market)

[144] Bank of America spokeswoman, Anne Pace, quoted in "Bank Accounts: Free Checking Fading Fast," The Christian Science Monitor (Oct. 19, 2010), available at http://www.csmonitor.com/Business/Latest-News-Wires/2010/1019/Bank-accounts-Free-checking-fading-fast

[145] *Rising Bank Fees are Setting Records,* USA Today (Oct. 27, 2008), available at http://www.usatoday.com/money/industries/banking/2008-10-26-atms-fees-checks-banks_N.htm ("The high fees come at a time when banks are struggling to unload bad mortgage loans."); *Banks Boost Customer Fees to Record Highs,* Wall Street Journal (Nov. 12, 2008), available at http://online.wsj.com/article/SB122645109077719219.html ("Banks are responding to the troubled economy by jacking up fees on their checking accounts to record amounts."); *Banks Find Ways to Boost Fees; Checking Accounts Latest Target,* USA Today (May 28, 2009), available at http://www.usatoday.com/money/industries/banking/2009-05-27-checks-fees-banks_N.htm ("Banks defend their policies, saying that as unemployment rises, consumers have become riskier, and the higher fees reflect that risk. Banks may also be raising some account fees to compensate for higher borrowing costs and to keep prices in line with other financial institutions, says Scott Talbott of the Financial Services Roundtable, which represents the nation's largest banks."); *Bank Fees Rise as Lenders Try to Offset Losses*, New York Times (July 2, 2009), available at http://www.nytimes.com/2009/07/02/business/02fees.html?_r=1 ("Scott E. Talbott, a lobbyist for the Financial Services Roundtable, said that the banks' fees reflect the cost of providing those services and the

increase checking account fees.[146] In fact, some even had the temerity to suggest that they had to increase checking fees because they couldn't make the same money from risky mortgages anymore.[147]

All of these various excuses for the steep drop in free checking offerings were made long before debit reform came into being. The litany of excuses was summed up well in a 2011 article written when banks were blaming debit reform for their increases in checking fees – remarkably, doing this even before debit reform had ever taken effect – "The pattern is getting old and weary. Banks will raise checking fees whenever and wherever they think they can get away with it. And they will blame any convenient development for their choices."[148]

This background matters because the credit card industry typically relies on two fatally flawed studies to try to show that reductions in free checking that came before debit reform –

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rise in overdraft charges reflects increased risk. 'There is an increased riskiness around repayment because of the recession, he added.'").

146 *Is Free Checking on its Way Out?* CNNMoney.com (July 2, 2009), available at http://moremoney.blogs.money.cnn.com/2009/07/02/is-free-checking-on-its-way-out/ ("Bank customers used to the perks of free checking accounts -- unlimited check writing, online banking, debit card use and ATM access, to name a few -- might have to recalibrate their expectations soon. That's because overdraft fees, which banks use to subsidize the expense of free checking accounts, have been under fire by consumer advocacy groups."); *Banking Expert: Free Checking Accounts aren't Long for this World,* WalletPop.com (Aug. 31, 2009), available at http://www.walletpop.com/2009/08/31/banking-expert-free-checking-accounts-arent-long-for-this-worl/ (Following the Credit Card Accountability Responsibility and Disclosure Act and overdraft regulations, "banks are already trying to think of new ways to make their profits."); *Banks' Struggle May Mean End of Free Checking,* msnbc.com (Nov. 10, 2009), available at http://www.msnbc.msn.com/id/33840681/ns/business-consumer_news/ ("The change by Citi comes as Congress considers legislation that would limit banks' ability to levy overdraft fees on checking accounts."); *The End of Free Checking?* MoneyTalksNews.com (Dec. 30, 2009), available at http://www.moneytalksnews.com/2009/12/30/the-end-of-free-checking/ ("[N]ew Congressional regulations like the CARD Act have limited the amount of money banks can make from credit cards. The Federal Reserve also has plans to address the highly lucrative "overdraft fee industry", estimated to be worth $38.5 billion in 2009 by industry consultants Moebs Services. In other words, free checking accounts may soon be going the way of the dinosaur."); *The End of Free Checking,* NPR Planet Money (June 17, 2010), available at http://www.npr.org/blogs/money/2010/06/17/127899418/you-may-have-to-pay-for-that-checking-account ("It costs banks a few hundred bucks a year to maintain a customer's checking account. Banks have been able to make that up (and more) largely by charging overdraft fees. But new federal rules mean banks can only charge those fees to customers who sign up for overdraft protection."); *The End of Free Checking,* The Atlantic (June 21, 2010), available at http://www.theatlantic.com/business/archive/2010/06/the-end-of-free-checking/58444/ ("Free checking is on life support. . . . The main reason why, of course, is the imminent prohibition of overdraft fees, which had been a boon for banks."); *End of Free Checking a Financial Squeeze: How Employers Can Help*, The Huffington Post (June 28, 2010), available at http://www.huffingtonpost.com/clare-j-morgan/end-of-free-checking-a-fi_b_627540.html ("The free checking accounts many Americans enjoy will soon be a thing of the past as banks scramble to find new ways to recoup overdraft charges and other fees they're no longer allowed to impose.").

147 *The End of Free Checking? Not at Credit Unions!* Credit Unions Online (June 17, 2010), available at http://www.creditunionsonline.com/news/2010/The-End-of-Free-Checking-Not-at-Credit-Unions.html ("Since banks can no longer charge many credit card fees of the past and high risk (high fee) mortgages are gone, banks are finding themselves short of revenue. . . . Now the banks are coming after your checking account to make up the difference.")

148 David Balto "The Bankers' New Goat," HuffPost (May 25, 2011) available at https://www.huffpost.com/entry/the-bankers-new-goat_b_834615.

reductions they blamed on the financial crisis and limits on overdraft fees – were actually caused by debit reform. These studies take January 2009 as the measuring point for free checking prior to debit reform even though those reforms did not come into effect until October 2011, more than two full years later. And, they pushed these studies onto the Government Accountability Office which cited them in a report without recognizing that the timing of the studies meant that the studies were blaming debit reform for things that happened prior to reform coming into effect.[149]

The number of checking accounts without monthly fees fell by 11 percentage points just from 2009 to 2010 – still a year before debit reform.[150] But, by counting the remarkably swift and steep reduction in the number of free checking accounts that occurred during the financial crisis and blaming that on debit reform (which came later), these studies magically claim that debit reform reduced free checking. It didn't.

Banking industry data demonstrates that free checking actually <u>increased</u> from the time debit reform went into effect at least for its first few years in operation. The American Bankers Association reported that 61 percent of banks had free checking in 2014 after debit reform had been in effect for several years, which compares favorably to the 50 percent of banks with free checking that the ABA reported in 2010 and the 39 percent of large banks that Moebs Services reported offered free checking two months prior to debit reform taking effect.[151]

- <u>Debit Reform Has Helped Small Banks and Credit Unions Compete</u>

Currently, the way that credit card swipe fees are fixed disadvantages small banks and credit unions. Those institutions typically have higher costs than do large institutions (which, unlike small banks, often pay nothing to the credit card networks). Credit union representative John Blum, for example, testified on behalf of the National Association of Federal Credit Unions

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[149] *See* "Banking Services," Government Accountability Office (Feb. 2022) available at https://www.gao.gov/assets/gao-22-104468.pdf.

[150] *Region Banks Refrain from Raising Checking Account Fees,* Nwi.com (Nov. 9, 2010), available at http://www.nwitimes.com/business/local/article_337b378b-3f74-5a00-9d86-b9e6b3d58799.html ("Bucking a national trend, the region's community banks aren't raising fees or putting the breaks on free, non-minimum-balance checking accounts, yet. A recent Bankrate.com national survey on checking accounts indicates the percentage of checking accounts with no monthly service charges and no minimum balance fell to 65 percent in 2010 from 76 percent in the 2009 study.")

[151] Cadence Bank, "ABA: Most Americans Pay Nothing for Bank Services," formerly available at https://cadencebank.com/about/resources/aba-survey---most-americans-pay-nothing-for-bank-services (this and other traces of the American Bankers Association's press release showing more free checking after debit reform have been removed from the ABA's website and others, but the link above is one of the places where that release was previously available and the original text of the ABA press release can be viewed by entering the weblink into the Internet Archive tool at Wayback Machine); American Bankers Association, "ABA Survey Shows Majority of Bank Customers Pay Nothing for Monthly Bank Services," available at http://www.prnewswire.com/news-releases/aba-survey-shows-majority-of-bank-customers-pay-nothing-for-monthly-bank-services-104516904.html; Ismat Sarah Mangla and Tali Yahalom "Bank Accounts: Get a Fair Shake, not a Shake-Down," CNN Money (Aug. 31, 2011) available at https://money.cnn.com/2011/08/31/pf/bank_accounts.moneymag/index.htm ("This was backed by data from Moebs Services, which found that 39% of big banks offered free checking in 2011, down from 64% in 2010").

in 2010 and told the House Judiciary Committee: "Credit unions have a higher per-transaction cost for processing card payments."[152] Community banks have similar disadvantages because of their relatively small size resulting, in many instances, in the need to outsource card operations.[153] Because card networks fix fees for all banks at the same level, however, large banks have for years been guaranteed higher profit margins than their smaller competitors. Those large banks have used their advantage to aggressively market themselves to consumers. That is one of the reasons why the credit card market is more concentrated than the debit card market. Many consumers who have accounts and debit cards at small banks and credit unions receive credit card and other offers from large banks. The large banks take the small banks' customers in this way on a regular basis – paid for by their excess interchange earnings. The result is that large banks have a bigger share of both the credit and debit card markets than their share of deposits.[154]

Debit reforms have helped to level the playing field. The Philadelphia Federal Reserve published a study on the impact of debit reform on small financial institutions in February 2016. The study found that after reform, "the volume of transactions conducted with cards issued by exempt banks *grew faster* than it did for large banks."[155] The study concluded that "the evidence does not support the claim that competitive forces have effectively imposed the interchange fee ceiling on small banks."[156]

The Credit Union Times has reported that debit reform created "a powerful way for credit unions to accumulate market share" and "what some say is a huge opportunity for credit unions."[157] According to Texas Trust President and CEO Jim Minge, debit reforms created "…a huge opportunity for credit unions like the Mansfield, Texas Trust Credit Union and everybody else below the $10 billion threshold…" Debit swipe fee reform "applies only to financial

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[152] John Blum, Hearing before the Task Force on Competition Policy and Antitrust Laws, House Judiciary Committee, May 15, 2008, House Report No. 110-179, at 80.
[153] Dave Carpenter, Hearing before the House Judiciary Committee on the Credit Card Fair Fee Act of 2009, Apr. 28, 2010.
[154] *See* Adam J. Levitin, *Interchange Regulation: Implications for Credit Unions*, 2010, at 39 (noting that 10 banks alone account for almost 90 percent of the credit card market and 51 percent of the debit card market, even though those 10 banks hold only 36 percent of insured deposits), *available at* http://www.federalreserve.gov/newsevents/files/levitin_filene_paper.pdf.
[155] James Disalvo and Ryan Johnston, "How Dodd-Frank Affects Small Bank Costs," Economic Insights: Federal Reserve Bank of Philadelphia (Feb. 2016) available at https://www.philadelphiafed.org/-/media/frbp/assets/economy/articles/economic-insights/2016/q1/eiq116.pdf.
[156] *Id*.
[157] "Credit Unions Revive Debit Rewards" (Jan. 22, 2016) available at http://www.cutimes.com/2016/01/22/credit-unions-revive-debit-rewards; "Credit Unions Pile Into Debit Rewards" (Jan. 20, 2016) available at http://www.cutimes.com/2016/01/20/credit-unions-pile-into-debit-rewards?page=1&slreturn=1453333652.

institutions with more than $10 billion in assets, which has created a huge opportunity for credit unions – especially those that want to attract millennials."[158]

As noted above, a number of credit unions also formed Co-Op Pay to negotiate a better deal with the Star debit network on the fees they pay to complete those transactions. That was only possible because of the competition that exists among debit networks. Similar competition among credit networks would improve the bargaining power of smaller banks and credit unions as well.

Centralized price-setting of credit card swipe fees harms smaller financial institutions. More competition in the market would help give them additional levers to try to compete with the largest banks including by allowing them to negotiate among the different networks.[159]

- Debit Reform and Network Competition Enhanced Fraud Protection

Competition pushes businesses to provide lower prices and better service. That has been the impact that debit reform brought to payments a decade ago. By prohibiting exclusivity arrangements so that more than one network had to be available to handle debit card transactions, the market changed so that networks needed to find a way to improve their offerings. One way they did that was with enhanced protections against fraud. As soon as the debit reforms came into effect, the networks started introducing full end-to-end encryption of data.[160] They also accelerated the transition to chip cards in the United States.[161]

The credit card industry sometimes argues that high swipe fees are needed to cover fraud costs, but this is not the case – as is clear from the fact that fraud is much lower in nations with much lower swipe fee rates. Economists with the Federal Reserve Bank of Kansas City have found that fraud costs are not a justification for over-inflated interchange fees. They wrote, "Card organizations have often argued that the reason why they impose proportional fees stems from the cost they bear from their 'payment guarantee' service which insures merchants against customers who pay with cards without having sufficient funds. We argue that the cost of fraud and insufficient funding is negligible compared with fees at the range of 1% to 3% commonly imposed by brand name cards. For example, industry studies show that the average net fraud

[158] "6 Winning Credit Union Payments Strategies" (Apr. 15, 2016) available at http://www.cutimes.com/2016/04/15/6-winning-credit-union-payments-strategies?slreturn=1487974414&page=2.
[159] The two largest networks favor larger financial institutions in the terms of their deals. *See* "2019 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions," Board of Governors of the Federal Reserve System (May 2021) at 15, available at https://www.federalreserve.gov/paymentsystems/files/debitfees_costs_2019.pdf.
[160] *See*, e.g., Tracy Kitten, "Visa's New End-to-End Encryption Service," Bankinfo Security (Sept. 12, 2012) available at https://www.bankinfosecurity.com/interviews/visas-new-end-to-end-encryption-service-i-1650.
[161] *See* Visa presentation to Federal Reserve (Jan. 8, 2014) at 2, available at http://www.federalreserve.gov/newsevents/rr-commpublic/visa-meeting-20140108.pdf.

losses are around 0.05% for signature debit cards, which do not extend credit to card users."[162] And, as noted above, the majority of fraud is paid by merchants, not banks.

The swipe fee system on debit cards prior to reforms created disincentives to the card industry taking fraud protection more seriously. Because the fees were much higher than losses from fraud, financial institutions were not highly motivated to make changes to cut down that fraud. A June 2011 Consumer Reports article pointed out these problems. It noted that thieves could "easily and cheaply" copy U.S. debit card data that is usually stored unencrypted in a magnetic stripe on the back of the card. According to the article, "The U.S. and some non-industrialized countries in Africa are among the only nations still relying on magstripe payment cards, which came into wide use in the 1970's."[163]

A representative from the New York Police Department explained in the Consumer Reports piece that the NYPD had "recommended to several of the large financial institutions that the biggest deterrent to skimming would be using the kind of cards that are issued in Europe and Canada with a chip that makes them pretty much impossible to skim."[164] The article noted that financial institutions had been reluctant to do that due to their large card revenues. After debit reform, however, the card industry had newfound motivation to reduce fraud and pushed the transition to chip cards – though, unfortunately, they failed to push PIN usage as they had in other parts of the world.

And, as noted above, there is no question that credit card competition among networks would help reduce fraud. This would be true even if there were not competition but instead smaller networks simply replaced Visa and Mastercard. Once again, the Federal Reserve reported just last year that the smaller networks have one-eighth of the incidence of fraud per transaction that Visa and Mastercard have.[165] Having networks with lower fraud rates on credit cards will improve fraud protection.

- <u>Merchants Absorb More Card Fraud Than Banks</u>

While the card industry often talks about a "payment guarantee," merchants are not guaranteed payment on credit or debit card transactions. In fact, merchants are forced to absorb the majority of the cost of fraudulent card transactions. When the merchant is forced to pay for the fraud, this is called a "chargeback." It means that the money the merchant was supposed to

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[162] Oz Shy and Zhu Wang, "Why Do Card Issuers Charge Proportional Fees?" The Federal Reserve Bank of Kansas City Economic Research Department, (December 2008) at 3 available at https://www.kansascityfed.org/documents/5325/pdf-rwp08-13.pdf.

[163] "House of cards: Why your accounts are vulnerable to thieves," Consumer Reports Magazine (June 2011).

[164] *Id*.

[165] Board of Governors of the Federal Reserve System, "2021 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions" at 36, Table 10 (Oct. 2023) (available at Federal Reserve Board Publication).

receive on the transaction is taken away (in other words, charged back). This can happen to a merchant without notice even months after the transaction takes place.

The Federal Reserve has collected data on debit card fraud every two years since debit reform was passed. Its 2019 data showed that merchants covered 56.3 percent of debit card fraud while card issuing banks only covered 35.4 percent.[166] The Fed's most recent data is similar but shows an alarming anti-consumer trend. Based on 2021 data, the Fed determined that merchants covered 47 percent of debit card fraud and card issuing banks covered 33.5 percent.[167] The most significant change, however, was that the largest card networks and banks made consumers foot a much larger proportion of fraud. While in 2019, consumers paid for 8 percent of debit card fraud, by 2021 they had to pay 19.5 percent.[168] Swipe fees, of course, jumped by billions of dollars per year during that same time period. The idea that the card industry needed higher swipe fees to make consumers pay more than double the share of fraud that they had previously paid is, of course, wrongheaded. The overinflated fees and the anti-competitive way they are set make fraud worse, not better.

The picture is similar for credit cards as merchants absorb most fraud losses – particularly since Visa and Mastercard implemented a liability shift to push chip card usage which pushed a significant share of fraud onto merchants. In fact, the Federal Reserve reported that the merchant share of fraud on dual message debit cards in 2021 (which are processed in similar fashion to credit cards) was more than 60 percent.[169]

Of course, all of the fraud chargebacks that merchants must pay are on top of the swipe fees they pay. Those swipe fees amount to a prepayment of all fraud charges (and much more) to card-issuing banks. Merchants should not have to prepay for fraud and they should not have to pay when the fraud happens in addition to prepaying for it. They also shouldn't have to hear about the great "payment guarantee" they receive on credit and debit cards when the merchants pay for fraud multiple times.

It is worth noting that even with debit reform, merchants prepay all the fraud that banks otherwise cover. Federal Reserve Regulation II, which implements debit reform, includes 5 basis points as part of the regulated debit swipe fee to cover fraud losses by banks. That number was pegged to 100 percent of the fraud losses on debit cards paid by the average bank covered by the regulation. Of course, that means that fraud is a profit center for many of the banks covered by the regulation (those with below average fraud losses). And, the vast majority of banks across the

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[166] "2019 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions," Board of Governors of the Federal Reserve System (May 2021) at 4, available at https://www.federalreserve.gov/paymentsystems/files/debitfees_costs_2019.pdf.
[167] "2021 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions," Board of Governors of the Federal Reserve System (Oct. 2023) at 3, available at Federal Reserve Board Publication.
[168] *Id*.
[169] *Id*. at 23 (Figure 17).

nation are not subject to the Fed's fee regulation. They charge even higher fees that exceed their fraud losses on debit cards. Why merchants must pay chargebacks to cover the majority of fraud that they have already prepaid (and then some) to the banks is inexplicable.

- Visa and Mastercard Do Not Need to Set Prices for Large Banks

One of the few ways that the credit card industry has tried to justify the centralized setting of prices by the networks for the banks that issue cards is by citing the large number of banks on each side of a credit card transaction. With thousands of banks issuing cards and thousands of banks and processors handling the merchant side of processing, they argue that it is too complicated and difficult for the prices of all those combinations to be negotiated in a free market.

But, the research has found that the card industry's claims don't fit the facts. Nicholas Economides of New York University has studied this and found that credit card issuing and, on the other side, acquiring/processing of credit card transactions is very concentrated among small numbers of banks and processors with large market shares. As a result, in 2009, he found that a mere 90 negotiated agreements would cover a full 72 percent of all Visa and Mastercard transaction volume.[170] That, of course, is very doable – and there has been significant additional concentration in both markets since then.[171] There is no reason why the largest banks couldn't do business like other companies operating throughout the economy and negotiate their own pricing.

- The Combination of Thousands of Banks Under the Visa and Mastercard Umbrellas Means that Merchants Can't Just Stop Taking Credit Cards

Economists have found that due to the market power of Visa and MasterCard, merchants have no real choice but to accept credit cards. While the credit card industry likes to say merchants have a choice, this argument would be like AT&T claiming in the 1980s that no one should worry about its monopoly because people could choose not to have a telephone. Accepting cards is essential for most businesses – as the U.S. Department of Justice has concluded.[172]

In fact, the Kansas City Federal Reserve studied this and determined, "Only monopoly merchants who are facing an inelastic consumer demand may deny cards when the fee exceeds its transactional benefit. . . Merchant competition allows the network to set higher merchant fees. The network can always set higher merchant fees in more competitive markets. Moreover, in competitive markets the merchant fees in the long run may exceed the sum of the merchant's initial margin and the merchant's transactional benefit. . . . As long as the merchant fee does not

[170] Nicholas Economides, "Competition Policy Issues in the Consumer Payments Industry," at 122 In R. Litan & M. Baily, Moving Money: The Future of Consumer Payment, Brookings Institution (2009) available at 06-0277-1 CH 06 (nyu.edu).
[171] The top 5 Visa/Mastercard issuing banks accounted for more than 70% of purchase volume in 2021, and the top 10 banks comprised more than 80%. *See* Nilson Report, Issue No. 1214 at 8-9 (Feb. 2022).
[172] *See* Complaint, U.S. v. Visa, Inc. and Plaid, Inc. (Nov. 5, 2020) at ¶3.

exceed the level that gives merchants negative profits, merchants may have no choice but to continue accepting cards."[173] The courts also agree that Visa and MasterCard both have market power which means they have the ability to raise their prices above what would be sustained in a competitive market.[174]

- Most Credit Card Issuers Are Exempt From the CCCA; Card Networks Are Not

The CCCA applies to financial institutions that issue credit cards. If they follow centrally fixed swipe fees from a credit card network for their cards, then they need to make two networks available on the cards so that there is some price competition. Financial institutions with less than $100 billion in assets are exempt from the bill's requirement. While Visa and Mastercard like to pretend that this exempts American Express and Discover, it does not. Both of those networks have some cards issued by separate financial institutions. The CCCA applies to those credit cards branded with American Express and Discover just like it does to credit cards branded with Visa and Mastercard. Any prices that American Express and Discover set for credit card issuers get the same treatment and both of those networks have cards issued by banks. Those cards are covered – subject only to the $100 billion asset threshold so that the bill applies exclusively to the largest banks.

Visa and Mastercard could certainly issue their own cards, thereby not setting prices for any banks, but they don't. The reason they don't is that they were established for the purpose of wielding the collective pricing power of banks across the nation, and they still do. That is the central problem with credit card swipe fees today and the element to which the CCCA will bring competition. Any argument that targeting the relief in the bill specifically to the competition policy problem in the market is some kind of exemption is merely an attempt to mislead people about what the problem is in the first place. All centralized network price-fixing on behalf of the largest banks is covered by the CCCA.

- Visa and Mastercard Do Not Provide a Meaningful Break on Swipe Fees at Gas Pumps

Swipe fees jumped by enormous amounts on motor fuel purchases during the heights of the inflationary cycle. During that time, the convenience industry saw its fees rise by 84 percent from 2020 to 2023 alone – jumping from $10.7 billion to $19.7 billion.[175] These large increases added a significant economic pressure to increase gas prices at the worst possible times. The card industry tried to defend itself from criticism for these rapidly rising fees by saying that it capped swipe fees at $1.10 per fill-up. But they know that cap is largely ineffectual. The average amount

[173] Fumiko Hayashi, "A Puzzle of Card Payment Pricing: Why Are Merchants Still Accepting Card Payments?" Federal Reserve Bank of Kansas City (2004) available at https://ideas.repec.org/p/fip/fedkpw/psrwp04-02.html.
[174] *U.S. v. Visa U.S.A., Inc.*, 344 F. 3d 229 (2d Cir. 2003).
[175] NACS State of the Industry Report 2021; NACS State of the Industry Report 2024; see also "Congress Must Rein in Swipe Fees to Help Consumers," Boston Herald (Brennan: Congress must rein in swipe fees to help consumers (bostonherald.com)).

of gas put in a car during a fill-up is 11.7 gallons.[176] So, using the average credit card interchange rate of 2.22 percent, a cap of $1.10 does not impact what the merchant pays for that fill up until gas costs about $4.25 per gallon. As of November 6, 2024, the average price across the nation for regular gasoline was $3.10.[177] And, other than in California, recent gas prices have only rarely reached a point at which $1.10 per fill-up would give retailers any meaningful break.

Swipe fees often approach 10 cents per gallon on a fill-up. That is simply too much for local retailers or their customers to bear.

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The harm done to merchants, consumers and the U.S. economy due to the anti-competitive actions of the card industry is far too large and should end. Market competition improves economic efficiency, innovation, and price competition. Bringing competition to the credit card market through passage of the CCCA would produce real economic benefits across the spectrum. It is time for that to happen.

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[176] https://www.statista.com/statistics/1143194/average-fuel-transaction-volume-us-gas-stations/#:~:text=Average%20quantity%20of%20fuel%20purchased%20per%20transaction%20in%20the%20U.S.%202019%2D2020&text=Americans%20bought%2011.7%20gallons%20of,the%20gas%20pump%20in%202020.

[177] See AAA Gas Prices.