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<u>BY EMAIL</u>

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Docket No. R-1404 (Debit Card Interchange Fees and Routing)
RIN No. 7100 AD63

Dear Ms. Johnson:

On behalf of the merchant community, the Merchants Payments Coalition (the "MPC")[1] respectfully submits the following comments and proposals in response to the notice of proposed rulemaking published by the Federal Reserve Board ("Board") in the Federal Register on December 28, 2010. *Debit Card Interchange Fees and Routing*, 75 Fed. Reg. 81,722 (proposed Dec. 28, 2010) ("NPRM"). These comments supplement our January 20, 2011 submission relating to the fraud prevention adjustment.

We appreciate the extensive time and effort invested by the Board and its staff in drafting the NPRM, and commend the Board for proposing regulations consistent with the bipartisan compromise reflected in Section 920 of the Electronic Fund Transfer Act ("Section 920"). By addressing market failures and bringing competition and transparency to the debit card industry, these proposed regulations would benefit consumers and industry participants alike by lowering costs, making transactions more secure, and spurring innovation. Highlights of the MPC's comments detailed below include:

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[1] The MPC is a group of retailers, supermarkets, drug stores, convenience stores, fuel stations, on-line merchants and other businesses who are fighting against excessive credit and debit card fees and for a more competitive and transparent card system that works better for consumers and merchants alike. The MPC's member associations collectively represent about 2.7 million stores with approximately 50 million employees.

- With respect to the regulation of interchange fees, Alternative 1 is preferable, but the safe harbor and cap should be much closer to the average per-transaction costs of authorization, clearance, and settlement ("ACS") which issuers themselves report to be no greater than 4 cents and First Annapolis Consulting reports to be 0.33 cents for PIN transactions (and 1.36 cents for signature debit transactions).

- With respect to the prohibitions on network exclusivity, Alternative B (two unaffiliated networks for each type of authorization method on the card) should be fully implemented by April 2012. As a transitional measure, Alternative A (two unaffiliated networks) should be adopted within three months after the Board issues final rules, and network fees charged to merchants should be capped at current levels until Alternative B is fully implemented.

- With respect to merchant routing, the proposal set forth in the NPRM that prohibits networks or issuers from directly or indirectly inhibiting merchants from routing their transactions should be adopted.

- With respect to preventing circumvention and evasion, the MPC proposes an amended version of the net compensation proposal which would include a general anti-circumvention provision and close remaining loopholes.

The MPC believes that final regulations building on the NPRM in a manner consistent with the following comments will be faithful to the statutory mandate, and should be promulgated within the timeframe specified in Section 920. Our detailed comments are set forth below.

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I. Background

Before we address the substance of the NPRM, some background on the market failure that motivated Congress to pass the statute, which should inform the Board's approach to some of the outstanding issues, is warranted.

A. The debit card market has failed for the past twenty years

Interchange is not necessary to motivate banks to issue debit cards and, thus, the proliferation of interchange for debit transactions in the United States is merely a function of market failure. Banks have strong incentives to provide debit cards even without substantial income from interchange. When banks first began to offer PIN debit cards, they did not charge interchange fees. To the contrary, they paid merchants to provide debit services, a practice known as "reverse," "negative," or "issuer-paid" interchange. Under that structure, banks profitably provided debit services using at-par interchange. This model prevailed until the early 1990s, a period that saw widespread expansion of debit card services. *See* Report of Steven C. Salop, Oct. 27, 2010 ("Salop Report") at ¶¶ 21, 45, 136; Report of Stephen Craig Mott, Oct. 29, 2010 ("Mott Report") at ¶¶ 7, 8, 9, 11, 14, 23.[2]

In fact, this model prevailed until Visa and MasterCard conspired with their members to fix prices and leverage their power in the credit card market to dominate the debit market. Beginning in the early 1990s, Visa and MasterCard aggressively began to implement and enforce a strategy to leverage their market power and force merchants to pay higher debit interchange through their "Honor All Cards" rules. This policy forced merchants to accept signature debit cards as a condition of accepting the networks' dominant credit cards. Crucially, Visa and MasterCard set the same or similar interchange for merchants' debit card transactions as they did for credit card transactions, and merchants that had no choice but to accept their dominant credit products had to pay these fees. Visa and MasterCard then used the lucrative interchange stream created by this practice to compete for bank issuance and thereby entrench their dominance in the debit market. As banks became accustomed to receiving high interchange rates for signature debit transactions — rates which bore no relationship to costs — a dynamic of merchants being forced to pay ever-increasing interchange rates to underwrite network competition for issuers became the norm for the industry. Mott Report at ¶¶ 12-14, 16; Salop Report at ¶¶ 4, 11, 24, 33, 43-44, 55, 139, 145. Visa also used its acquisition of the leading PIN debit network, Interlink, to push this dynamic into the PIN debit segment as well. In PIN debit alone,

[2] Because the MPC's White Paper and the attached Salop, Mott, and Morrison reports were submitted to the Board in advance of the NPRM, they have been posted already on the website that the Board has set up for these rulemakings. As such, we are not reproducing them as attachments to these comments and instead request that the Board treat them as incorporated by reference.

for example, merchants faced market-wide effective interchange increases of an estimated 234% between 1998 and 2006.[3] These increases were even more severe for small non-supermarket merchants who have faced a 467% increase in Interlink PIN debit prices since 1998.[4]

This scheme worked because merchants had no choice but to accept the networks' debit cards — as rejecting those cards would severely harm merchants' operations — and thus the networks could raise (collusively-set) interchange prices to merchants with impunity. Against this backdrop, banks had no incentive to compete for merchant acceptance, as cartelizing through Visa and MasterCard (and thereby exercising collective market power over merchants) was far more lucrative than competing for merchants. This market failure has persisted for the past two decades and is expected to remain intact in the foreseeable future, resulting in Congress's decision to regulate debit interchange.

The experience in other G-20 countries reinforces the conclusion that the development of debit in the United States, with a high credit card-style interchange fee, was not inescapable but rather was a function of the market failures in the debit industry in this country. Tellingly, seven of the eight countries with the highest debit usage utilize an at-par pricing model. For example, the Canadian debit system has always been based on an at-par pricing model, and Canada has traditionally had higher per capita debit usage than the United States, as well as higher debit penetration in merchant categories that do not accept PIN debit in the United States. Report of Kenneth J. Morrison, Oct. 27, 2010 ("Morrison Report") at ¶¶ 2, 13-14, 42-43; Salop Report at ¶¶ 48, 64-68.

B. <u>Banks will have strong incentives to issue debit cards at lower interchange rates</u>

Given debit cards' positioning as a key access device to the demand deposit account ("DDA") relationship, debit cards provide numerous benefits to banks that will continue to justify their issuance post-regulation. These benefits include: (i) displacing more costly alternative transactions; (ii) motivating cardholders to maintain greater balances, which banks can then lend; and (iii) helping banks to cross-sell other lucrative services. Moreover, debit cards enhance the "stickiness" of the banks' valuable relationships with their DDA customers. Mott Report at ¶¶ 1, 29-30; Salop Report at ¶¶ 19, 60-63.

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[3] Mott Report at ¶ 24 and Attachment 48. Moreover, the interchange associated with PIN debit has continued to increase since 2006. *Id.* at ¶ 24; Salop Report Exhibits 1a-1d. Even if the 23-cents-per-PIN-debit-transaction figure reported in the NPRM is used to calculate the growth rate after 1998, that growth is still 166%, which likely understates the escalation of PIN debit costs for merchants. NPRM at 81725.

[4] *See* Fumiko Hayashi, Richard J. Sullivan, and Stuart E. Weiner, "A Guide to the ATM and Debit Card Industry – 2006 Update," Federal Reserve Bank of Kansas City, at 13 (Figure 8), and Interlink Interchange Reimbursement Fees, Oct. 16, 2010, at 2, available at http://usa.visa.com/download/merchants/october-2010-interlink-interchange-rate-sheet.pdf (percentage increase based on calculation of interchange fees using default non-supermarket rate on a $50 debit transaction).

It is notable that, while the networks and banks have spared no effort to criticize the NPRM, when they are talking to investors and subject to the securities laws, they have acknowledged that their debit programs will readily adapt and thrive after debit interchange rates are reduced. Examples include the following:

- **MasterCard** (Ajay Banga, President & CEO): "[W]e continue to believe that impacts on our debit business will be manageable. … [W]e continue to anticipate some potential upside to our volumes as a result of the routing non-exclusivity, regardless of how it finally gets sorted out. So from a share perspective, as I said in the past, we have more to gain than to lose." (MasterCard Q4 2010 Earnings Call Transcript, Feb. 3, 2011) (emphasis added).[5]

- **Citigroup Inc.** (Vikram Pandit, CEO): "We don't have much of an impact on debit card interchange or overdraft fees. Those are really small impacts on us." (Citigroup Inc. Q4 2010 Earnings Call Transcript, Jan. 18, 2011) (emphasis added).

- **City National Corporation** (Russell Goldsmith, Chairman & CEO): "The Durbin amendment on debit card interchange fees … its economic impact on City National is not going to be material." (City National Corporation Q4 2010 Earnings Call Transcript, Jan. 20, 2011) (emphasis added).

- **Wells Fargo Company** (Howard I. Atkins, Senior EVP & CFO): "We've been working very hard about strengthening our relationship model. In fact, the relationship model we employ here is probably the best thing — the best anecdote [sic] to what's happening in the regulatory reform arena, because as we deepen relationships, profitability grows exponentially as we add products prophetically. So I think it's a work in progress." (Wells Fargo Company Q4 2010 Earnings Call Transcript, Jan. 19, 2011).

- **Associated Banc-Corp** (Philip B. Flynn, President & CEO): "It's not our intention to replace fee income losses by charging other fees to the same customer base. Our emphasis will be on accelerating our efforts to attract and retain true core households and capturing the organic fee income that comes through deeper relationships with those customers." (Associated Banc-Corp Q4 2010 Earnings Call Transcript, Jan. 20, 2011).

- **Webster Bank and Webster Financial Corporation** (James C. Smith, Chairman & CEO): "[W]e'll have more profitable relationships that we'll bring onboard and our team is very well developed and trained to be able to maximize the value of these relationships as they come onboard. So we see ourselves as building

[5] MasterCard could not possibly see "upside to [its] volumes" if the debit industry were poised to contract.

> broader, deeper relationships with a core set of customers that we've identified as the primary customer for Webster." (Webster Financial Corporation Q4 2010 Earnings Call Transcript, Jan. 14, 2011).

These statements, which are merely a sampling of the network and bank commentary on the impact of Section 920, indicate that debit card issuance will continue to thrive in the United States even after debit interchange is substantially reduced. There are additional examples of bank conduct that run counter to their doomsday predictions about the impact of these regulations. For example, TCF Bank announced on January 5, 2011, after the NPRM was issued, that it intended to reduce minimum balance requirements and eliminate fees for more of its checking account customers, belying the standard bank claim that reduced interchange inevitably results in higher cardholder fees. *See* "TCF Bank Announces Checking Product Enhancements and Introduces Mobile Banking," Business Wire, Jan. 5, 2011. That banks will continue to issue and promote debit cards is hardly surprising given that debit cards were initially profitable with rates much lower than those proposed in the NPRM, and the longstanding rationale for banks to issue debit cards remains unchanged.

C. The small issuer exemption will be maintained after the regulations go into effect

There has been much comment recently about whether the small issuer exemption will be sustainable after the regulations go into effect. Two concerns have been raised. First, some have suggested that networks will decline to set two tiers of interchange rates, one for regulated banks and another for exempt banks. Second, some have said that even if networks establish two rate tiers, merchants will reject or discriminate against the cards from exempt banks and, thus, those banks will end up receiving the same interchange as regulated banks.[6] Neither concern is valid.

On the first issue, several debit networks, including Visa and STAR, have announced their intention to retain higher interchange tiers for exempt banks. *See* Sean Sposito, "Visa Plans Two-Tiered Interchange Rates After Fed Rules," American Banker, Jan. 10, 2011; Kate Fitzgerald, "Two-Tier Debit Interchange Rate Plan OK With First Data," ISO & Agent Weekly, Feb. 10, 2011. This is not surprising given that Visa's earlier claim that configuring two sets of rates is operationally impossible was demonstrably false.[7]

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[6] It is also worth noting that the banking industry is trying to have it both ways on this point. In the context of the Board's regulatory proceeding (including in the media and on Capitol Hill), they argue that small issuers ultimately will receive the same interchange as large issuers. In contrast, in the context of their constitutional challenge to Section 920 filed in federal court, they argue that small issuers will be able to receive significantly higher interchange than large issuers. Indeed, this latter representation to the court is the very basis of their Equal Protection argument. *See* Amended Complaint at ¶¶ 4, 34, 134-139, *TCF Nat'l Bank v. Bernanke*, No. 10-cv-4149(LLP) (D.S.D. Jan. 27, 2011).

[7] A cursory review of Visa's and MasterCard's elaborate and complex interchange rates, which include hundreds of rates that vary by product, card type, and merchant category, among other things, shows that

Moreover, the networks have every incentive to set higher rates for the small banks. In this regard, exempt banks represent a not insubstantial portion of the market, approximately 30% by volume and over 90% of the financial institutions, and they are the institutions that get the most value from highlighting the networks' brands because their own brands generally lack the prominence of the regulated banks' brands. It is also worth noting that, if it is true that exempt banks' debit programs would not be viable at lower interchange, then that reinforces the networks' incentives to set higher rates for them to maintain their volumes.

As for the claim that merchants would reject cards from exempt banks, it, too, is patently false. The statute gives merchants the ability to route between networks, not between issuers. *See* Section 920(b)(1)(B) (prohibits inhibiting "the ability of any person who accepts debit cards for payment to direct the routing of electronic debit transactions for processing <u>over any payment card network</u> that may process such transactions") (emphasis added). That distinction is critical because routing between banks that issue on a network violates all of the networks' Honor All Cards rules that, by network rules, must be included in every merchant contract governing the acceptance of debit cards. Those rules specifically require merchants that agree to accept a network's debit cards to accept all of that network's debit cards, irrespective of the issuer (or its size), without discrimination.[8] As such, those rules would prohibit a merchant that accepts, for example, Visa debit cards from accepting only the Visa debit cards issued by regulated banks. Small banks, therefore, will be protected against the very discrimination that

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setting different debit interchange rates for exempt and regulated banks will be straightforward compared to the rate tiers that already are in effect. *See* Visa U.S.A. Interchange Reimbursement Fees, Oct. 16, 2010, available at http://usa.visa.com/download/merchants/october-2010-visa-usa-interchange-rate-sheet.pdf; MasterCard Worldwide U.S. and Interregional Interchange Rates, Apr. 2010, available at http://www.mastercard.com/us/merchant/pdf/MasterCard_Interchange_Rates_and_Criteria.pdf. The credibility of Visa's claim that two sets of rates is operationally impossible was best summarized by a payments industry consultant, Eric Grover, who said "[t]hat was simply intended to scare credit unions and small banks to keep them lobbying." Sean Sposito, "Visa Plans Two-Tiered Interchange Rates After Fed Rules," American Banker, Jan. 10, 2011.

[8] The Honor All Cards rule that is applicable to MasterCard's Debit Program mandates the following: "Merchants that choose to accept Debit MasterCard Cards must honor all valid Debit MasterCard Cards without discrimination when properly presented for payment. The Merchant must maintain a policy that does not discriminate among customers seeking to make purchases with a Debit MasterCard Card." MasterCard Rules, updated Dec. 10, 2010 (Ch. 15a United States Region Debit-related Rules – 5.8.1 Honor All Cards) at Ch. 15a-3. Visa's Honor All Cards rule similarly stipulates that "A U.S. Merchant that wishes to accept Visa Cards must accept any valid Visa Card in its category of acceptance [*i.e.*, debit and/or credit] that a Cardholder properly presents for payment." Visa International Operating Regulations, Oct. 15, 2010 (Honor All Cards – U.S. Region 5.2.B) at 406. Moreover, both MasterCard and Visa require that these rules be included in all merchant contracts. *See* MasterCard Rules (The Merchant Agreement – 5.1.2 Required Terms) at Ch. 5-1 ("Each Merchant Agreement must contain the substance of each of the Standards set forth in Rules 5.6 through 5.12"); Visa International Operating Regulations (Merchant Agreement Requirements) at 356 ("An acquirer must … [e]nsure that required acceptance provisions are included in its Merchant Agreement"). *See* Attachments A and B for excerpted copies of these rules.

some have incorrectly suggested would undermine the viability of the small issuer exemption.

For these reasons, there is no basis for the concern that exempt banks inevitably will receive the same interchange as regulated banks.

D. Section 920 is a narrowly-tailored response to market failures in the debit card industry

Section 920 does not prohibit any issuer from charging fees directly (*i.e.*, not through a network) to merchants or their acquirers.[9] Such issuer-specific fees (*e.g.*, to recover that issuer's fixed costs or its costs of customer service) are permissible if they are transparent and subject to the discipline of market competition, and are therefore not imposed through or under network rules, including the Honor All Cards rules.

It is those concerns about fees charged through a network for debit issuers that Section 920 addresses. Networks and issuers have contended that fees intended to cover certain costs of a debit transaction — ACS costs — must be set collectively by a network for its issuers. Unfortunately, however, this results in two types of market failure: rival issuers colluding on price and certain networks exercising market power.

Regulation is a standard policy response when either type of market failure exists, regardless of whether the issuers' collusion and certain networks' use of market power technically amount to antitrust violations. *See, e.g.,* James C. Miller III, "Addressing the Debit-Card Industry's Market Failure," Prepared for the Retail Industry Leaders Association, Feb. 2011 ("Miller Report"), at ¶¶ 21-26 ("[T]he case for regulatory intervention is strong. This is truly a case of market failure: networks with monopoly power over merchants are setting prices for merchants' access to their networks on behalf of their (frequently overlapping) card-issuing members, utilizing agreements in which every bank participating in those card networks agrees to charge merchants exactly the same interchange fees, regardless of who issued the card.").[10] It is well-settled among mainstream economists and regulators that limited and targeted regulation is appropriate in situations like this. *See, e.g., id.* ("[S]ometimes a free market does not — or for any number of reasons cannot — correct a divergence from the competitive norm. The persistence of such divergences over time, uncorrected by unencumbered economic

[9] Such issuer competition in the marketplace could take many forms; an issuer simply would be prohibited from utilizing a network's market power or collective price setting to impose such issuer-specific fees because that would violate Section 920. For example, if an issuer sets individual prices and then requires merchants to pay them (directly or through the merchants' acquirers) under a network's "Honor All Cards" rules, merchants would have no choice but to pay whatever the issuer charges because they would have no ability to reject the cards. If an issuer did that, such conduct would merely reinstate the current market failures through another means, and therefore would violate Section 920.

[10] The Miller Report is appended hereto as Attachment C.

forces, is among the few scenarios in which I believe there is reason for government to examine and possibly correct the underlying cause…. [T]he proposed regulations appear to be consistent with both the limited mandate of [S]ection 920 and the policy prescriptions embodied in that provision.”).

Here, Section 920 requires regulation only of the fees characterized by such market failure. Accordingly, the proposed regulations set forth in the NPRM are consistent both with the limited mandate of Section 920 and the standard policy prescription embodied by that statutory provision.[11]

II. “Reasonable and proportional interchange transaction fees” (Section 235.3 of the proposed regulations)

A. Proposed Alternative 1 is preferable to proposed Alternative 2

Proposed Alternative 1 calls for a safe harbor of 7 cents per transaction for interchange fees, with an upward adjustment up to a cap of 12 cents based upon an issuer’s allowable costs. In contrast, proposed Alternative 2 calls for what is effectively both a safe harbor[12] and a cap of 12 cents per transaction for interchange fees. The former is the better approach because (i) it is more faithful to the statute, (ii) it has a safe harbor closer to average ACS costs, and (iii) its more flexible structure is better designed to reflect the variability in individual issuers’ costs.

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[11] There is continuing evidence that the banks are cartelizing through the dominant networks to extend their ability to fix prices to merchants. For starters, the critical rules that underpin the system — resulting in all issuers complying with a “default” set of interchange rates that are consistently imposed on merchants through the Honor All Cards rules — were maintained verbatim after Visa’s and MasterCard’s Initial Public Offerings. *See, e.g.*, Second Consolidated Amended Class Action Complaint in the *In re Payment Card Interchange Fee and Merchant Discount Antitrust Litig.*, No. 05-md-1720(JG)(JO) (E.D.N.Y.), Jan. 29, 2009, at ¶¶ 150-151, 238-239, 242-243. The banks’ complete control over any settlement by Visa and MasterCard of the *In re Payment Card Interchange Fee* lawsuits provides further evidence of such collusion because the resolution of those lawsuits almost certainly will determine the future of interchange going forward. *See, e.g.,* Visa Retrospective Responsibility Plan (described in Visa Dec. 21, 2007 10-K (Item 3)); Loss Sharing Agreement and Interchange Judgment Sharing Agreement between Visa and banks (attached to Visa July 24, 2007 S-4 (Amendment 1)); MasterCard Settlement and Judgment Sharing Agreement with banks (referenced in MasterCard Incorporated 8-K, Feb. 8, 2011); and Omnibus Agreement Regarding Interchange Litigation Judgment Sharing and Settlement Sharing between Visa, MasterCard and banks (apportioning Visa and MasterCard shares) (referenced in Visa Inc. 8-K, Feb. 8, 2011 and MasterCard 8-K, Feb. 8, 2011). This evidence reinforces the conclusion that the banks have every intention of continuing the collusion that has plagued this industry for as long as they can perpetuate the current system.

[12] Although Alternative 2’s 12-cent cap is not also explicitly labeled a “safe harbor,” it acts as one because — like the 7-cent safe harbor under Alternative 1 — there are no circumstances under which an issuer would fail to qualify for a 12-cent interchange transaction fee under Alternative 2.

1. Alternative 1 is more faithful to the statute, but its safe harbor should be tied to the mean rather than the median

The statute calls for interchange transaction fees to be based upon each issuer's ACS costs. Section 920(a)(2), (a)(4)(B). While any safe harbor technically is inconsistent with this mandate, the MPC recognizes the Board's attempt to ease administrative burdens in Alternative 1. Moreover, Alternative 1 properly requires interchange transaction fees above the safe harbor level to be based upon an individual issuer's costs. There is no such requirement based upon an individual issuer's costs under Alternative 2. Given the plain meaning of the statute, however, even Alternative 1's regulatory accommodation in the name of administrative practicality should be as limited as possible. In the current context, this suggests that any safe harbor should be tied to the lower "mean" level of ACS costs rather than the higher "median" level of ACS costs. NPRM at 81737. This would preserve a substantial reduction in administrative burden across the industry, but limit inconsistencies with the statutory mandate. In addition to greater fidelity to the statute, tying the safe harbor to the lower mean measure of costs also would create greater incentives to decrease costs. *See* Submission of the Merchant Payments Coalition, October 27, 2010 ("White Paper") at 6. These incentives would lead issuers to move from signature debit to the lower-cost (and more secure) PIN debit as well as to adopt even newer technologies and procedures that offer additional cost savings (and security features). Finally, existing federal regulations already utilize safe harbors based upon mean cost levels.[13]

2. Alternative 1's safe harbor is closer to average ACS costs

Both safe harbors greatly exceed the average ACS costs reported by First Annapolis Consulting and the issuers themselves, but Alternative 1's safe harbor (and cap) is closer to these costs than Alternative 2's. Specifically, the interchange fees permissible under the NPRM's two proposed alternatives are 2100% to 3600% of the ACS costs reported by First Annapolis Consulting for PIN debit transactions (and 510% to 880% of costs for signature debit transactions). Mott Report at ¶¶ 33-35 (ACS costs are 0.33 cents for PIN and 1.36 cents for signature).[14] The safe harbor under Alternative 1, however, is at the bottom of this range, slightly closer to average ACS costs than the safe harbor under

[13] For example, the Internal Revenue Service's safe harbor for vehicle mileage deductions is derived from state-by-state calculations that are then combined into a weighted average result for the entire country. *See* Internal Revenue Service, "IRS Announces 2011 Standard Mileage Rates," Press Release, Dec. 3, 2010; Revenue Procedure 2010-51 Section 4-5.

[14] During the November 2, 2010 meeting with the Fed staff, a large merchant reported ACS processing costs consistent with the First Annapolis Consulting figures. The merchant referenced a totally outsourced processing proposal offering to provide full ACS services for an open loop PIN and signature debit product for 0.8 cents per transaction. That figure undoubtedly reflected a profit margin and non-variable costs in addition to incremental ACS costs. Also, costs should have decreased substantially since the 2004 proposal referenced.

Alternative 2. Similarly, Alternative 1's safe harbor is 75% higher than the 4-cent weighted average ACS costs reported by issuers in their rulemaking survey responses, while Alternative 2's safe harbor is 200% higher than these costs. NPRM at 81737. In both cases, Alternative 1's 7-cent safe harbor is closer than Alternative 2's 12-cent safe harbor and cap to average ACS costs.

It is also important to note that the cost estimates based upon the issuers' and networks' survey responses likely reflect a substantial upward bias,[15] which may explain most, if not all, of the difference between them and the lower figures independently calculated by First Annapolis Consulting. Accordingly, even if the final regulations were based upon Alternative 1 and used the 4-cent mean (reported by the issuers), the safe harbor likely would be too high given this likelihood of upward bias and evidence of lower mean ACS costs. Moreover, a cap of 12 cents also would be too high, not only because of the same likelihood of upward bias and evidence of lower mean ACS costs, but also because allowing issuers to recover up to 300% of the industry mean ACS costs does little to incent these highest-cost issuers to do better. Lower safe harbors and caps create economically sound incentives to reduce costs over time.

Lowering Alternative 1's safe harbor and cap to bring them closer to actual ACS costs would pose little risk of adverse consequences. As noted above in Section I., history and current practice both confirm that banks have strong incentives to provide debit cards even without any income from interchange:[16]

- When banks first began to offer PIN debit cards, they actually paid merchants interchange to provide debit services. Salop Report at ¶¶ 21, 45, 136; Mott Report at ¶¶ 7, 8, 9, 11, 14, 23.

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[15] First, it appears that these cost estimates reflect, in part, certain higher-cost prepaid cards that are exempt under Section 920(a)(7). Inclusion of exempt prepaid cards would skew the cost estimates because the variable per-transaction ACS costs for those cards are nearly 4 times the level of signature debit cards and 6 times the level of PIN debit cards. *See, e.g.*, NPRM at 81725 n.26. Second, as the MPC has noted previously, subtle differences in cost definitions, allocations, and internal reporting conventions are among the many potentially complex issues that an interested party may address or interpret differently than would an objective outsider when measuring ACS costs. Obviously, any given issuer's incentives to maximize its reported ACS costs in response to the Board's surveys would be strong, and no third party would be as familiar as that issuer with its cost data. The decision of certain low-cost issuers not to respond to the surveys also could skew upward the Board's ACS cost estimates. While the MPC appreciates the effort the Board put into the issuer and network surveys, and believes they are a sufficient basis upon which to finalize a rule consistent with the statute, there is a likelihood that the survey responses overstate these costs.

[16] Additionally, under an approach like Alternative 1, inefficient issuers would retain a "safety valve" even if both the safe harbor and cap are lowered — issuers with ACS costs above the safe harbor level still would be able to receive higher interchange fees up to the amount of the cap.

- Currently, seven of the eight countries with the highest debit usage utilize an at par pricing model — Canada, Denmark, Finland, Iceland, the Netherlands, New Zealand, and Norway. Salop Report at ¶ 68. This underscores that fact that market failure, not industry economics, is the reason for higher interchange transaction fees in the United States during the past decade.[17]

- Even bankers view the debit card as merely another access device, with the DDA being the true product. Banks profitably offer their customers access devices such as checks (without interchange) and debit cards because of the profits the banks earn on that core product. Tellingly, TCF Chairman and CEO William Cooper admitted that, "<u>[a] debit card is actually just part of a checking account … not a product in and of itself</u>. It's a delivery system for the checking account in a similar way that the checks are … <u>[A] checking account is the core business</u>." Transcript to TCF Financial Corp.'s Conference Call, *TCF Discusses Lawsuit Challenging Durbin Amendment*, Oct. 12, 2010, at 2, 9 (emphasis added).[18]

For all of these reasons, a low safe harbor and cap are desirable. Alternative 1 is preferable to Alternative 2 in this regard, although even Alternative 1 would benefit from a lower safe harbor and cap closer to actual ACS costs.

3. Alternative 1's more flexible structure is better designed to reflect the variability in individual issuers' costs

The issuers' rulemaking survey responses confirmed that ACS costs vary widely among issuers. As noted above, Alternative 1 requires these differences to be taken into account for issuers seeking interchange transaction fees above the safe harbor. There is no such requirement under Alternative 2. Specifically, Alternative 1 permits issuers who have ACS costs up to the safe harbor level to recover them automatically, while issuers with ACS costs above the safe harbor level can recover them up to the cap amount simply by identifying them.

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[17] It is also worth noting that positive interchange has, all else being equal, suppressed merchant acceptance (and therefore consumer usage) of debit in the United States. This is apparent from a comparison between the United States and Canada, where at-par pricing for debit has resulted in PIN debit being virtually ubiquitous, with acceptance comparable to, if not greater than, Visa and MasterCard. The cheaper, safer and more efficient PIN debit product is accepted in Canada in numerous categories that are largely unpenetrated for PIN debit in the United States including the Internet, T&E merchants, restaurants, fast food restaurants, movie theatres, parking meters, and taxis. Morrison Report at ¶ 33.

[18] CEO Cooper explains that <u>talking specifically about the profit on debit cards "would be like saying, what's the profit on the bun at Burger Chef. We don't sell a bun. We sell a hamburger which is a checking account</u> and we've got all the costs associated with that checking account and all of the revenues associated with that. Now if you take all of our revenues and our expenses into consideration, our retail banking system makes a profit. <u>We'll obviously still be profitable</u> [even if the Board promulgates debit card regulations pursuant to Section 920]." *Id*. at 7 (emphasis added).

B. The treatment of network-owned third-party processing fees creates a loophole that networks and issuers can exploit

There is a loophole regarding network-affiliated third-party processors that the MPC believes should be closed. Left unaddressed, this loophole would allow a network to charge merchants 24 cents per transaction (12 cents in interchange fees; 12 cents in other network fees) and pass on that amount to an issuer regardless of how low its ACS costs were.

The problem arises when a network owns a third-party processor (*e.g.*, Visa Debit Processing Service ("Visa DPS")). Even if that third-party processor's costs are 0.33 cents, the network that owns it can charge the issuer 12 cents per transaction. As a result, that issuer can qualify for a 12-cent interchange transaction fee, which that network can impose on merchants and pass through to the issuer. NPRM at 81760 ("any per-transaction fee the third party processor charges is a variable cost for the issuer"). Further, that scenario allows the network to give the issuer an additional 12 cents under the "net compensation" provision of the anti-circumvention rules. This is because of an asymmetry in how costs are treated — the 12 cents paid by an issuer to a network for "network processing" (as well as for "optional services") performed by the third-party processor owned by that network are counted as compensation paid to the network, but interchange transaction fees that reimburse the issuer for that payment are not counted as compensation paid to the issuer. NPRM at 81747. The result of this asymmetry is that the network can effectively pay the issuer another 12 cents. There is no prohibition on a network charging merchants 12 cents per transaction in other network fees to fund this second 12-cent payment to the issuer.

Obviously, such an outcome — merchants being forced to pay 24 cents per transaction to networks who pass it on to issuers — would be inconsistent with Section 920(a). The MPC believes there are two simple steps that would close this loophole. First, under Alternative 1, only the ACS costs of a third-party processor (not the entire fee charged to the issuer) should be considered a variable cost for the issuer.[19] Second, under the "net compensation" provision, either (i) fees paid by an issuer to a network for third-party processing should not be counted as compensation paid to networks or (ii) interchange transaction fees that networks pass through to reimburse issuers for that payment should be counted as compensation paid to issuers. In short, the asymmetry (where one counts and the other does not) should be eliminated.

[19] While the MPC believes it would be best to limit the variable costs to ACS costs for all third-party processors, it is most crucial with respect to network-owned third-party processors because of the loophole discussed above. Accordingly, the Board could consider an approach under which the entire per-transaction fee charged by any third-party processor unaffiliated with a network could be considered a variable cost for the issuer, but for every third-party processor affiliated with a network only the ACS costs of that third-party processor (not the entire fee charged to the issuer) could be considered a variable cost for the issuer.

C. Basing interchange transaction fees on variable ACS costs is consistent with Section 920

As discussed by the MPC in previous submissions, Section 920(a)(4)(B) clearly directs the Board to consider certain costs and not to consider other costs in establishing standards to assess debit interchange fees. Specifically, this provision requires the Board to consider incremental ACS costs incurred by an issuer in a particular debit transaction.[20] Section 920(a)(4)(B) also prohibits the Board from considering any issuer costs that are "not specific to a particular electronic debit transaction."
The legislative history is also clear. As stated by the provision's author, Senator Durbin, on the Senate floor during debate on this legislation:

> [T]he cost to be considered by the Board in conducting its reasonable and proportional analysis is the incremental cost incurred by the issuer for its role in the authorization, clearance, or settlement of a particular electronic debit transaction, as opposed to other costs incurred by an issuer which are not specific to the authorization, clearance, or settlement of a particular electronic debit transaction.

Cong Rec. S. 5925 (July 15, 2010).

Even an issuer of debit cards — TCF National Bank — confirmed this interpretation of the statute in a brief it filed in federal court late last year:

> [Section 920] restricts regulated debit issuing banks to recover only three discrete costs of debit transactions from merchants: the authorization, clearance and settlement of individual electronic debit transactions. The statute explicitly forbids regulated banks from charging retailers for "any cost" of a debit transaction other than those three electronic steps: in other words, it excludes variable costs that are needed to service the customer's account, and all fixed costs that are incurred in order to establish, maintain and operate the system.

Plaintiff's Memorandum of Law in Support of its Motion for a Preliminary Injunction at 2, *TCF Nat'l Bank v. Bernanke*, No. 10-cv-4149(LLP) (D.S.D. Nov. 4, 2010); *see also* Amended Complaint at ¶ 2, *TCF Nat'l Bank v. Bernanke*, No. 10-cv-4149(LLP) (D.S.D. Jan. 27, 2011).

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[20] As noted previously, Bank of America unwittingly highlights the strict limitation that Section 920 places on the types of costs that the Board is permitted to consider by juxtaposing an unrelated statutory provision in which Congress explicitly directs the Board to consider "all direct and indirect costs … including interest[,] overhead, … taxes[, and] return on capital." Letter from Bank of America Deputy General Counsel Stacie E. McGinn to Director Louise L. Roseman, Nov. 12, 2010, at 6 (quoting 12 U.S.C. § 248a(c)(3)).

In short, the Board should not consider any costs other than incremental ACS costs incurred by the issuer for a particular debit transaction.[21] Among others, all fixed costs are non-ACS costs that should be excluded from the calculation. As noted previously, these ACS costs are well-defined in the industry. Mott Report at ¶¶ 33-34. With respect to the definition of "incremental" costs, the MPC appreciates the Board's proposal to use "average variable" costs as a proxy and believes it is a reasonable approximation that could simplify calculation and supervision.

D. Networks and issuers should not be permitted to engage in price discrimination against merchants or authorization methods

1. The "issuer's average cost" approach and the "network's average cost" approach should be rejected

Both the "issuer's average cost" and "network's average cost" approaches on which the Board requested comment would permit issuers and networks to engage in price discrimination that is inconsistent with Section 920 and sound public policy.

a. The approaches are inconsistent with Section 920

As discussed extensively above, Section 920 permits interchange transaction fees based upon certain specified cost considerations. Section 920, however, prohibits networks and issuers from maintaining the status quo in which a network can set different interchange rates for any transaction it pleases based upon factors unrelated to these statutorily-mandated cost considerations. In other words, attempting to inflate certain interchange rates by taking into account factors with no relationship to the issuer's incremental ACS costs or other costs specific to a particular debit transaction is inconsistent with Section 920(a).

The two "interchange averaging" approaches would allow issuers and networks to flout these statutory prohibitions by setting different interchange transaction fees based upon factors that are wholly unrelated to an issuer's specific costs. In arguing for one such approach, Visa conceded that it would permit discrimination based upon merchant size, merchant segment, and/or acceptance channel. Letter from Visa General Counsel Joshua R. Floum to Director Louise L. Roseman, Nov. 8, 2010 ("Visa Letter"), at 11-20. Even more pernicious, these "interchange averaging" approaches would permit issuers and networks to engage in classic price discrimination in which merchants and consumers would be charged based upon the maximum amount each one is willing to pay. As a matter of economics, the amount of these discriminatory fees would be unrelated to the supply curve (reflecting actual marginal costs) altogether and, instead, would be based

[21] Consideration of authorization costs alone may be permitted under the statute given the analogy to checking, but the MPC is not advocating this approach.

entirely on the demand curve (representing what economists refer to as "willingness to pay") that is unrelated to costs.[22] Giving issuers and networks free reign to engage in this type of behavior would be inconsistent with Section 920(a) and must be rejected for that reason alone.

b. The approaches are inconsistent with sound public policy

These "interchange averaging" approaches also should be rejected because they are inconsistent with sound public policy. Issuers and networks would be permitted to continue engaging in naked price discrimination — conduct characteristic of firms exercising market power — and this would enable them to continue appropriating for themselves the consumer surplus that otherwise would go to consumers and merchants in a competitive marketplace.[23] There is no justification for allowing issuers and networks to seize this windfall by transferring this portion of the social surplus to themselves. Under these "interchange averaging" approaches, however, that inequitable result is likely.

2. Interchange transaction fees should be the same for signature, PIN, and prepaid transactions

The approach to setting interchange transaction fees set forth in the NPRM is sufficiently flexible to cover signature, PIN, and prepaid transactions. Moreover, it should be applied consistently in all transactions, including card-present and card-not-present merchant transactions. Consistent with Section 920, the NPRM does not differentiate between or among authorization methods. This uniform approach is not only appropriate, but there would be concerns about circumvention and evasion if there were different standards or approaches. Further, as a matter of economics, regulating signature, PIN, and prepaid transactions uniformly would drive the marketplace over time to gravitate towards the lowest cost, most secure, and best functioning of these (or even other) authorization methods.

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[22] Because this anticompetitive result can exist only when a firm is exercising market power, it is telling that last week Visa appears to have publicly endorsed such pricing based upon "value" instead of "cost." Statement of Joshua R. Floum on behalf of Visa, Inc. before the Subcommittee on Financial Institutions and Consumer Credit of the Committee on Financial Services, United States House of Representatives (Feb. 17, 2011) ("Visa Testimony"), at 6.

[23] Miller Report at ¶ 7 ("Monopoly power is also evidenced by the prices established by the card networks. The pricing schedules of Visa and MasterCard show a pattern of what economists call 'third degree price discrimination' -- which can take place only if there is monopoly power…. [I]n a truly competitive market, sellers are not able to divide the market and charge different prices to different consumers unrelated to differences in costs.").

E. *Ex post* verification by regulators should be required

Under Alternative 1, the Board (or other appropriate regulatory agency) should verify the "allowable costs" of any issuer that has received an interchange transaction fee above the safe harbor amount. Coupled with the other anti-circumvention provisions in Section 235.6 of the proposed regulations, this *ex post* verification will help ensure compliance with Section 920(a).

III. "Limitations on payment card restrictions" (Section 235.7 of the proposed regulations)

A. Prohibition on network exclusivity (Section 235.7(a))

In the NPRM, the Board requested comment on two alternative approaches to Section 235.7(a). Under Alternative A, issuers and payment card networks can comply if "the number of payment card networks on which an electronic debit transaction may be processed is not limited to less than two unaffiliated payment card networks." NPRM at 81749. As the Board acknowledges, issuers and payment card networks can comply with Alternative A by placing one signature and one PIN debit network on debit cards, an ultimate result that the MPC considers problematic for reasons detailed below. By contrast, under Alternative B, issuers and payment card networks are prohibited "from directly or indirectly restricting the number of payment card networks on which an electronic debit transaction may be processed to less than two unaffiliated networks 'for each method of authorization that may be used by the cardholder.'" NPRM at 81750 (citing proposed Section 235.7(a)(1), Alternative B).

For the reasons discussed below, the MPC believes that the following phased implementation of the network non-exclusivity requirements under Alternative B is appropriate:

- During a transition period starting three months after the Board issues final rules, all debit cards must be compliant with Alternative A.[24] Additionally, network fees charged to merchants would be capped at current levels during this transition period. *See* Section IV.A., *infra*.

- By April 2012, Alternative B must be fully implemented. This means that every debit card must permit merchants to route over at least two unaffiliated networks

[24] As discussed below, if the Board concludes that requiring compliance with Alternative A during this transition period would be burdensome with respect to certain healthcare cards as well as debit cards associated with government-administered benefit programs, such cards could be exempted from complying with this regulation until Alternative B is fully implemented in April 2012 under our proposal.

> for each type of debit authorization functionality that the issuer has chosen to enable on that card.

1. Alternative B is the only approach that is faithful to the language and intent of the statute

In our view, only Alternative B is faithful to the letter of the statute as well as to its legislative intent. Section 920(b)(1) prohibits limiting the "number of payment card networks on which an electronic debit transaction may be processed" to only one network (or two or more networks that are affiliated). *See* Section 920(b)(1)(A). The statute does not address how many networks a given card allows. Instead it requires that every transaction must have at least two routing options to create network competition for merchants. Given market realities, to effectuate this provision there must be at least two network options for each authentication method. Some debit cards are limited to signature debit functionality,[25] and the banks and networks have contended that certain debit cards, such as healthcare cards, are not well-suited to PIN debit. If that is true, then that supports the need to interpret Section 920(b)(1)(A) to require at least two signature debit networks on all debit cards that possess that functionality. Otherwise, transactions using such cards will be limited to only one debit network option in clear violation of the statute. Moreover, certain merchants accept only signature debit and, as the Board acknowledged, some merchants cannot readily accept PIN debit and, thus, the marketplace will not receive the benefit of competitive choice and price pressures for entire classes of transactions if Alternative A is adopted.[26] NPRM at 81749 (discussing that T&E merchants cannot accept PIN debit). A result that provides no routing options for millions of transactions cannot be reconciled with the statute. For these reasons, Alternative B is the only approach that is consistent with the letter and spirit of the statute.

Alternative B also is the only option that adheres to Congress's expressed rationale for enacting this provision. As Senator Durbin explained in reference to Section 920(b), "[t]his paragraph is intended to enable each and every electronic debit transaction — no matter whether that transaction is authorized by a signature, PIN or otherwise — to be

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[25] For example, a significant number of signature debit-only cards are issued by banks in the Midwest, such as US Bank, that have chosen to not provide their customers with PIN debit functionality.

[26] We understand that there has been some discussion that networks and issuers could choose to set interchange transaction fees below the "safe harbor" thresholds under either alternative proposed in Section 235.5 in order to attract volumes when merchants can route transactions to lower-cost networks. That scenario is plausible only if the Board selects Alternative B to Section 235.7 because, as discussed, only this alternative will necessarily give all or virtually all merchants the ability to route transactions to lower-cost networks. That said, even with Alternative B in place — which under the NPRM would not be implemented until 2013 (a time frame with which we draw issue below) — it is hard to predict whether network competition would be sufficiently robust, at least in the near term, to motivate networks to reduce prices below the safe harbor level.

run over at least two unaffiliated networks." 156 Cong. Rec. S 5926 (July 15, 2010). Given that some debit cards and some merchants are limited to one authentication technology, this mandate can be accomplished only with Alternative B. Put differently, this provision was enacted to create network competition for merchant acceptance, a dynamic that has long been absent in this industry, that hopefully will have a disciplinary effect on prices. That objective would be frustrated if millions of merchants are deprived of the opportunity to route debit transactions to lower-cost networks.

Additionally, Alternative B is likely to result in new entrants offering signature debit. The signature debit segment of the debit market has been dominated by Visa and MasterCard. In fact, with the exception of Discover's signature debit product, which was launched in 2006 and has achieved limited success to date, Visa and MasterCard collectively have had a complete monopoly on the signature debit portion of this market. That should come to an end under Alternative B. In that regard, it is worth noting that the PIN debit networks almost certainly will jump into this portion of the market if Alternative B is adopted, and that entry could conceivably stimulate vigorous competition in a sector that has seen little competition to date.[27] In fact, working with these networks would be a fast and easy way for issuers to enable multiple signature debit functionalities on their cards given that the PIN debit networks already process signature debit transactions as part of the services they provide their member banks. This is a powerful additional policy reason to select Alternative B.

Finally, it is imperative that Alternative B be selected to ensure that all merchants have some ability to discipline network fees. This conclusion is reinforced by the inescapable fact that, even after the regulations go into effect, the market power that has plagued this industry will remain intact for the foreseeable future. Against that backdrop, the dominant networks will continue to have the ability and incentive to compete for issuers by raising fees to merchants as they have been doing for years. Because Section 920(b) reflects Congress's attempt to provide merchants with some competitive check against that power, that intent would be frustrated if the Board selected Alternative A and millions of merchants had no ready ability to react to increasing network fees via routing.

For these reasons, Alternative B is the only option that is consistent with the letter and purposes of Section 920(b)(1).

2. Alternative A is neither consistent with the statute nor will it enhance network competition for merchants

The conclusion that Alternative B is the only option that is consistent with the statute is reinforced by some of the consequences that might flow from the permanent adoption of

[27] Such entry has been blocked by exclusive deals that Visa and MasterCard have with virtually all of the banks to thwart competition in signature debit. *See, e.g.*, Mott Report at ¶ 26.

Alternative A. Notwithstanding the success of Visa's strategy of entering into exclusive debit deals with large issuers, a not insubstantial portion of the market (estimated to be 35-40%) still has more than one PIN debit bug on the card. Issuers of such cards could comply with Alternative A by removing PIN debit options from their debit cards. If that happens, then the network options available to PIN-capable merchants would be reduced, a result that cannot be reconciled with Section 920(b). We are concerned that this might happen and, if it does, Alternative A will reduce the competitive choices available for many merchants.[28]

Under Alternative A, we can conceive of scenarios in which it would make economic sense for dominant networks to enter into volume-based deals that would give banks incentives to take steps to inhibit merchants' ability to route transactions. In fact, because Alternative A would limit the routing choices of millions of merchants to only one network, we disagree with the Board's conclusion that "issuers will, as a practical matter, be unable to guarantee or otherwise agree to commit a specified volume, percentage share, or dollar amount to a particular debit network" by simply prohibiting network and issuer routing rules or priorities under Section 235.7(b). Even with those restrictions, which as discussed below the MPC supports, networks and issuers could predict with some confidence their signature and PIN debit volumes when they reduce the routing options to one signature and one PIN debit option. As such, Alternative A will require the Board to revisit the question of prohibiting volume commitments under Section 235.7(b), whereas Alternative B would not.

Moreover, Alternative A arguably runs afoul of Section 920(b)(1)(B) because merchants that cannot accept PIN debit currently will be effectively inhibited from directing the routing of debit card transactions if issuers elect to comply with Alternative A, as we expect, by placing one signature and one PIN debit network on their cards. If that happens, many merchants, such as the T&E merchants that the Board acknowledged cannot accept PIN debit, will have no routing options. NPRM at 81749. That result — which would completely inhibit these merchants' ability to route transactions — is inconsistent with the letter and spirit of the statute.

[28] While many merchants could conceivably install PIN pads to take advantage of Alternative A, that does not provide a compelling reason to select Alternative A over Alternative B. In addition to the fact that some merchants, such as T&E merchants, cannot readily accept PIN debit transactions, others, such as card-not-present merchants, have limited PIN debit options as a direct consequence of the perverse incentives created by the current system. Vendors offering PIN-debit-over-the-Internet solutions like Acculynk, for example, have gained limited traction in the marketplace, and other online PIN debit options have garnered no support from the banks that are critical to the success of any PIN debit option over the Internet. Whether that will change as those incentives are eliminated is hard to predict. And we cannot help but note that many merchants have not installed PIN pads because the business case for PIN debit has been distorted and undermined over the years, as Visa (and the banks) engaged in strategies to push signature debit and limit the growth of PIN debit. Against that backdrop, it is unfair to these merchants — many of which are smaller merchants — to essentially require them to install PIN pads to take advantage of Section 920(b).

3. Alternative B can and should be implemented by April 2012

The debit industry has a long history of multiple networks co-residing on debit cards. In the late 1980s, the debit networks, working with processors, acquirers and issuers developed the ISO 8583 message format, which made connecting and routing transactions to multiple networks seamless for acquirers, processors, and issuers. With a common message format, most banks connected to at least two, if not more, debit networks. It also became routine that all of the major processors and acquirers could read those formats and route transactions based on issuer or merchant instructions with ease. In fact, the placement of multiple PIN debit networks on most debit cards was the norm in the industry until the past decade, when Visa's strategy of entering into exclusive deals with larger banks for both signature and PIN debit changed the landscape. Notably, many banks (including many small banks) still link up to at least two PIN debit networks. Salop at ¶ 31 n.21.

Because of this backdrop, most of the infrastructure and experience that would be necessary to implement Alternative B already exists in the industry. Gateway processors —– which can link issuers and merchants to all of the networks — already provide the necessary connections. The industry has decades of experience with revising the bank identification number ("BIN") tables to ensure that the BINs assigned to particular banks can reside in multiple network tables at the same time. Issuers have experience with managing different networks' rules on chargeback and risk management issues. As noted, most banks were members of multiple PIN debit networks in the 1990s. On the signature-based side of the industry, many banks are dual MasterCard and Visa credit card issuers and, thus, they have deep experience managing Visa's and MasterCard's various (and often highly similar) chargeback and risk management rules.[29]

While this infrastructure was developed for PIN debit, it can be replicated to provide the same efficient and seamless technical backdrop for multiple signature debit networks co-residing on debit cards. The required changes are not as extensive or as costly as the Board — based on the NPRM and the January 1, 2013 timeline it has proposed for Alternative B — has been led to believe by the networks and banks.

For example, the NPRM states that "enabling multiple signature debit networks on a debit card could require the replacement or reprogramming of millions of merchant terminals." NPRM at 81749. Multiple signature debit networks can be accomplished without any reprogramming or replacement of terminals and, thus, the industry could

[29] Duality has been a feature of the payments industry since the 1970s. Virtually every issuer of Visa and MasterCard credit cards has simultaneously issued both brands of cards and, thus, has put in place a back-office infrastructure to handle the systems and rules of both organizations. As there is significant overlap between credit and debit issuers — an issue we address in the anti-circumvention discussion — these banks can easily accommodate the back-office changes that co-residency of signature debit functionality may require them to implement.

implement multiple signature debit networks without changes at the terminal level. Having said that, even if such changes are necessary, the vast majority of terminals can be reprogrammed remotely by software that can be downloaded by processors, like First Data, which reach millions of merchants.[30] In short, the suggestion that the need to replace or reprogram merchant terminals should somehow delay the implementation of Alternative B cannot withstand scrutiny.

The NPRM also states that multiple signature debit networks will require "substantial changes to software and hardware for networks, issuers, acquirers and processors," without explaining what those changes might be. NPRM at 81749. We understand that technical changes will need to be made, particularly at the acquirer/processor level, to facilitate the implementation of multiple signature debit networks on debit cards. Such changes can be accomplished within a year, particularly if steps are taken to replicate for signature debit the efficient and seamless routing that exists today with PIN debit. Given that this has been done before with PIN debit and the ready model it provides, this could be accomplished by the end of 2011 and implemented by the time of Visa's and MasterCard's semi-annual interchange adjustments scheduled for April 2012.

4. The Board should implement a transitional approach that requires compliance with Alternative A within three months after the Board issues final rules

To the extent that the Board gives the industry additional time to carry out the changes necessary to implement Alternative B with respect to signature debit, we respectfully suggest that it require issuers to comply with Alternative A as an interim measure. As noted, the infrastructure for both multiple PIN debit functionality and dual signature/PIN functionality on debit cards has long been a feature of this industry since the late 1980s and there is no credible reason why the industry cannot comply with Alternative A for all debit cards within three months of the rules becoming effective. In fact, the Board acknowledged this in the NPRM when it proposed that timeline for Alternative A because that alternative effectively requires the placement of a second PIN debit network on the hundreds of millions of debit cards that currently are exclusive Visa/Interlink or MasterCard/Maestro cards by October 2011.[31] Moreover, the NPRM notes that approximately 70% of debit cards already have dual functionality. NPRM at 81723.

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[30] The MPC understands that a relatively small portion of merchant terminals cannot handle such programming downloads and would need to be replaced. To the extent that merchants gain substantial benefits from the ability to route to lower-cost networks, they likely will be willing to make the necessary investments to take advantage of the new environment.

[31] Notably, Interlink is the exclusive PIN debit network on approximately 89% of the debit cards whose transactions can be routed over that network (which equates to hundreds of millions of debit cards in the United States). Salop Report at ¶¶ 31, 35, 154. Accordingly, even a leading merchant attempting to route away from signature debit and Interlink because of their high interchange fees still ends up routing approximately 42% of its PIN debit transactions over Interlink. *Id*. Against that backdrop, many issuers will be adding a second PIN debit network to comply with Alternative A.

Lastly, it is worth noting that issuers do not need to reissue their cards to meet this timeline. In fact, they can comply by establishing the necessary linkages, perhaps through a gateway, and by ensuring that their BINs are included in the alternative PIN debit network's BIN table.

Accordingly, the MPC respectfully suggests that the Board require that all debit cards comply with Alternative A within three months after the Board issues final rules.[32]

5. The application of practical rules to the at-least-two-unaffiliated-networks requirement is appropriate

The NPRM identifies several circumstances in which the addition of a second unaffiliated network nonetheless would not put the issuer in compliance with Section 235.7. The first involves an issuer linking up to a network that "is accepted in only a limited geographic region of the country." NPRM at 81750. To the extent issuers do that, the MPC agrees with the Board that such practices would not comply with the statute because there would be portions of the country where merchants would be deprived of a viable second debit network option. *Id*. The MPC also agrees with the Board that an issuer could provide a second option across the country by adding networks with limited geographic coverage, provided that those networks cover the vast majority of the country in the aggregate. *Id*. Consistent with that, the MPC further agrees that the geographic reach requirement can be met if there are only "limited areas" that are not served by the network[s] that are added to the cards. *Id*. We also agree that issuers cannot comply with Section 235.7 by linking up with networks that are accepted at only "a limited number of merchant locations or for limited merchant types or transactions." *Id*. The network should have general widespread merchant acceptance that is comparable and close to parity (if not at parity) with the established network or networks on the card.

The Board requested comment on the impact of these proposals on regional PIN debit payment card networks. Given that gateways link the "regional" PIN debit networks to national merchants and thereby provide each of them national reach, we consider the "regional" appellation a misnomer. We, therefore, do not consider these proposals a threat to the viability of so-called "regional" networks that likely will be gaining volume

[32] Some signature debit-only cards are healthcare cards associated with Flexible Spending Arrangements, Health Reimbursement Arrangements, and Health Savings Accounts. As the NPRM correctly notes, Internal Revenue Service rules require the implementation of certain technology at the point-of-sale by merchants to substantiate qualifying transactions, and PIN debit networks "may not" be able to support such transactions at present. NPRM at 81751. While we understand that the PIN debit networks could implement the necessary functionality without too much difficulty, to the extent that the Board is concerned about burdening these programs, it could exempt these cards (and other debit cards associated with government-administered benefit programs that could raise similar issues) from having to comply with a transitional approach within three months after the Board issues final rules, and require them only to be fully compliant with Alternative B by April 2012.

when they are added to debit cards after the regulations go into effect. To the extent the Board is concerned about these impacts, we agree with a standard that requires the implementation of a second unaffiliated network only with respect to the regions (or states) where cardholders generally use the card. This issue could come into play with a regional bank that has the vast majority of its customers' debit transactions occur within 20 miles of where its cardholders live and work (which is the norm in this industry). Such banks, which are likely to be smaller banks, should not be required to put additional networks on the card (or a national network instead of regional networks) to cover portions of the country where its cardholders only sparingly use their cards. This approach will limit the costs and burden on smaller banks.

Before concluding, we would like to flag a concern that has to come to our attention as banks and networks in the industry discuss how they might comply with Section 235.7 once it is finalized. We understand that some banks have entered into discussions with a small and capacity-constrained network, Alaska Option, with the expectation that it will not have the capacity to handle their volumes and, as a result, transactions would default to the established network on the card. This circumvention could allow issuers to ensure that the vast majority of their volume is delivered to the dominant networks. We consider the exploitation of a capacity-constrained network such as Alaska Option to be a violation of Section 235.7, as well as conduct that should be captured by the general anti-circumvention rules that we discuss below. We request that the Board make clear that, in addition to geographic reach and comparable merchant acceptance, comparable and sufficient capacity is equally critical to creating effective competition on the cards going forward.[33]

6. Alternative B will not impose undue costs on issuers that are exempt from Section 920(a)

In endorsing Alternative B, we are cognizant that some have argued that this approach will injure the smaller banks and credit unions that are exempt from Section 920(a) of the Act but not from Section 920(b). In evaluating the credibility of these concerns, it is important to emphasize that smaller issuers typically outsource the connectivity function to gateway providers, which greatly ease the operational burden and expense associated with establishing connections to multiple networks. These gateway providers — including, for example, Fiserv, FIS/Metavante, and Jack Henry — already have connections with all of the debit networks, which smaller issuers can utilize to link up with the various networks. Gateway processing is a competitive market in which competition should discipline pricing and hold down the costs to the smaller issuers. As for the costs of connecting to additional debit networks, the PIN debit networks impose

[33] With respect to this at-least-two-unaffiliated-networks requirement, it should also be noted that the MPC believes that Visa and MasterCard must be treated as affiliates under Section 920 and the NPRM. Section 920(b)(1)(A)(ii)(I), (c)(1); NPRM at 81755 (proposed Section 235.2(c)).

nominal connection and/or membership fees ($1,000-$2,000) that they might even waive, as some have done in the past for competitive reasons, to attract more volume. Lastly, processors can add network functionality for debit issuers merely by adding the BIN associated with the card to the BIN table held by the networks without any change to the card itself. As such, banks can add networks without reissuing the card, which further minimizes the costs associated with linking to multiple networks. For these reasons, Alternative B can be implemented without unduly burdening small issuers.

7. Requiring multiple networks will not have adverse effects on cardholders

The NPRM asserts that "from the cardholder perspective … requiring multiple payment card networks could have adverse effects." NPRM at 81748. We disagree. To the extent that certain networks provide consumers valuable benefits, there is no reason to believe that competition will not motivate other networks to provide similar benefits to consumers. In this regard, the main purpose of Section 920(b) is to invigorate debit network competition that has been stagnant for decades due to the market failure that has plagued this industry. If that proves successful, then that dynamic should help consumers along with merchants. Moreover, since issuers do not want to jeopardize their relationships with cardholders by exposing them to situations in which valued benefits are available to them only some of the time, we would anticipate that issuers would ensure that key benefits are available to consumers with all of the network options that they choose to put on the card.

It is also worth noting that these network benefits are of dubious value and have been used to push consumers to signature debit transactions that increase risks of fraud and identity theft. In fact, as pointed out by Georgetown Law Professor Adam Levitin, consumers have no contractual relationship with networks and cannot be sure that they will ever receive any of the network benefits that are sometimes touted.[34]

Lastly, it is worth noting that many of the arguments that have been made about issuers being forced to link to networks that expose cardholders to data breaches and other security issues are based on false assertions that some networks expose consumers to fraud more than others. *See, e.g.*, Visa Letter at 4-5; Visa Testimony at 14-15. There is absolutely no evidence that particular debit networks are more prone to data breaches or fraud. In truth, all of the networks are audited by the FFIEC for various attributes, including security, and all of them maintain basic standards including PCI compliance. As such, these arguments should not be credited by the Board.

[34] Adam Levitin, "Visa's Identity Theft (I Mean Superbowl) For Life Promotion," Jan. 23, 2011, available at http://www.creditslips.org/creditslips/2011/01/visas-identity-theft-i-mean-superbowl-for-life-promotion.html.

8. Alternative B will not harm innovation

The Board has requested comment on whether Section 235.7 will undermine the development of new authentication technologies. NPRM at 81751. As an initial matter, there is no reason why a key fob or mobile phone embedded with a contactless chip could not be developed consistent with a requirement that at least two networks be available for any authentication method that is available. Nor do we see any reason why that requirement would be costly or somehow frustrate the development of these products. The development of these technologies has been based on interactivity with multiple networks to maximize the number of consumers who might use these devices.

Against that backdrop, we propose that there should be a presumption that new authentication technologies shall comply with Section 235.7, which can be rebutted by clear and convincing evidence that a new authentication technique cannot accommodate multiple networks or cannot be cost-effectively developed in a manner compliant with Section 235.7. The Board also could consider creating special rules for pilot programs. We are cognizant of the fact that networks often test new technology in limited pilot programs before deploying it more widely, and such practices should not be discouraged as an unintended consequence of the rules. The Board could monitor such pilots and mandate that this Section shall apply if the technology is widely deployed.

B. Prohibition on merchant routing restrictions (Section 235.7(b))

As an initial matter, we concur with the Board's conclusion that this provision, "[i]n practice, means that merchants, not issuers or networks, must be able to designate preferences for the routing of transactions, and that the merchant's preference must take priority over the issuer's or network's preference." NPRM at 81751. As the Board acknowledged, this principle requires the invalidation of all network and issuer rules, preferences and arrangements, including contracts, which inhibit merchants' ability to direct the routing of transactions. As such, PIN debit network rules or issuer preferences that dictate routing should be prohibited by Section 235.7(b). And the same result should apply to contractual arrangements, including volume commitment deals that might persist in the industry if Alternative A is adopted (as discussed above).

We also concur with the Board's conclusion that Section 235.7(b) should reach issuer or card network rules or requirements that prohibit merchants from "steering" transactions from one authentication method to another (usually from signature to PIN debit). As such, any rules that prohibit such steering or which could inhibit merchants' ability to steer — including anti-discrimination or no-surcharging rules — should be invalidated by Section 235.7(b). Moreover, this section should reach practices that could inhibit steering, including various longstanding practices that issuers have utilized to undermine merchants' ability to steer. Those practices include imposing fees on PIN debit and not signature debit (a practice that would make little sense — if it ever made sense — after the rates for the two products are equalized), and providing consumers with incentives to prefer signature over PIN debit, such as through rewards programs or liability protections that are available only with signature debit.

The NPRM indicates that the Board will not require that merchants gain the ability to route transactions in real time to comply with this requirement. If that is the case, then merchants, either directly or through their processors, should get access to the BIN tables (or other more efficient electronic means) at no cost to the merchant that will give them the ability to direct routing. In addition, networks should be required to provide merchants with the effective weighted average interchange rates that are applicable to each merchant to enable them to make informed decisions as to which networks are lower-cost than others for purposes of determining their routing priorities. Otherwise, the intent of this provision could be frustrated.

IV. "Prohibition on circumvention or evasion" (Section 235.6 of the proposed regulations)

A. Introduction

As the Board acknowledges in the NPRM, Section 920 includes two separate grants of authority to address the myriad ways that the networks and issuers can circumvent the restrictions on interchange fees. First, Section 920(a)(8) authorizes the Board to prescribe rules to ensure that network fees are not used "to directly or indirectly compensate an issuer with respect to an electronic debit transaction" and "to circumvent or evade" the regulation of interchange. Section 920(a)(1) addresses other forms of circumvention and gives the Board the authority to prescribe rules that would prohibit ways, other than network fees, through which the regulations can be evaded. The NPRM addresses both provisions by proposing that circumvention or evasion would occur "if an issuer received net compensation from a payment card network, not considering interchange transaction fees." NPRM at 81746. As we read the proposed Section 235.6, that is the only circumstance under which circumvention or evasion could be found to occur under the NPRM.[35]

Before we address the net compensation proposal in some detail, we have some preliminary observations. Network fees have been increasing in recent years and, in our view, they reflect the market power of the dominant networks and the fact that the smaller networks have been pricing under the umbrella created by the larger networks. *See, e.g.*, Mott Report at ¶¶ 70-72; Salop Report at ¶ 138. Moreover, network fees could

[35] While proposed Section 235.6 starts with a general proscription against circumvention, it then defines circumvention as an issuer receiving net compensation from a network with respect to electronic debit transactions. As drafted, that definition appears to be the only way that a network or an issuer could run afoul of the anti-circumvention rule.

easily substitute for interchange because, absent stringent anti-circumvention rules, networks can simply raise those fees after the regulations go into effect and pass them along to issuers to replace the lost revenue from interchange. Salop Report at ¶¶ 53-54, 140-141. This concern is amplified by the fact that the market failure that resulted in the passage of Section 920 will not be cured in the foreseeable future even with regulations in place regarding debit interchange. *See, e.g.*, Salop Report at ¶ 11-13, 172.

For these reasons, we respectfully reiterate our suggestion that network fees be capped at current levels, at least until non-exclusivity Alternative B is implemented. With non-exclusivity Alternative B in place, we are optimistic that a less regulatory approach to network fees will be necessary because virtually all merchants will have routing options and the ability to discipline network fees by preferring lower-cost networks. For the reasons detailed in our discussion of Section 235.7, many merchants will not have those options prior to the implementation of Alternative B and, in that period, a transitional approach that caps network fees and, thus, eliminates the networks' ability to exploit them to circumvent the regulations is in order. After that, a net compensation approach (amended to reflect our suggestions below) and a general proscription against circumvention (also discussed below), along with provisions that ensure monitoring and enforcement, should be sufficient to protect against circumvention.

B. <u>Because the net compensation approach is inherently underinclusive, the Board should include strong general anti-circumvention language in the regulations</u>

Because the NPRM limits circumvention to circumstances in which issuers receive net compensation from networks regarding the issuer's debit program, the proposal, by definition, would not reach other forms of circumvention. For instance, even though the NPRM acknowledges in another section that issuers could create hybrid credit/debit products to migrate consumers from regulated debit transactions to unregulated credit card transactions, the NPRM proposes no mechanism to address that possibility. *See* NPRM at 81729.[36] This is of particular concern to the MPC because, as we noted to the Board prior to the NPRM, we understand that MasterCard is marketing a product that is specifically designed to migrate consumers from signature debit to credit card transactions.[37] We also understand that TSYS is pushing a hybrid product that it claims will help issuers move debit card transactions covered by Section 920 to credit card transactions that are not.[38]

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[36] The limitation against compulsory use under the EFTA and Regulation E are alone insufficient to protect against the effective development of such products to circumvent the statute.

[37] Because of our concerns regarding the use of such hybrid cards to circumvent the regulations, we support the Board's proposal with respect to deferred and decoupled debit cards. NPRM at 81729.

[38] We are also concerned that credit card interchange rates could be increased to replace lost debit card interchange. *See* Salop Report at ¶ 114-17. That happened after signature debit interchange declined due to the settlements in the *In re Visa Check/MasterMoney Antitrust Litigation*, No. 96-cv-5238(JG) (E.D.N.Y.) (June 4, 2003) and, given that many of the large debit issuers have substantial credit card

Our concerns with the current proposal extend beyond the potential exploitation of hybrid credit/debit products to circumvent the regulations. The NPRM does not indicate whether issuers are currently receiving net compensation with the deals they have in place. As such, we do not have visibility into the extent to which networks can increase network fees to merchants to provide replacement revenue to issuers without contravening the net compensation standard for circumvention. And we are troubled that the NPRM explicitly permits networks to raise their network fees to merchants or decrease them to issuers (or both), even if those increases (or decreases) are designed to circumvent the regulations to the extent that net compensation is not provided. NPRM at 81747.[39] This result expressly contradicts (and thus would "circumvent") the Board's rationale for excluding fees paid to networks from ACS costs allowed to be recovered under the standard: "[T]he Board recognizes that if network processing fees were included in allowable costs, acquirers (and, by extension, merchants) might be in the position of effectively paying all network fees associated with debit card transactions. That is, an acquirer would pay its own network processing fees directly to the network and would indirectly pay the issuer's network processing fees through the allowable costs included in the interchange fee standard." NPRM at 81735.

Given the market failure discussed above, if the Board declines to cap network fees prior to the implementation of Alternative B, we respectfully suggest that it should implement regulations that can be flexibly applied to network fee changes that circumvent the regulation of interchange, even if they do not run afoul of the net compensation standard. Since neither the MPC nor the Board can replicate the creativity of the dominant networks (or their issuing members), it makes no sense to write overly prescriptive rules to cover the virtually limitless ways they could come up with to get around the regulations.[40] As such, we think it would be prudent for the regulations to include general anti-circumvention language that indicates that no person shall circumvent or evade the interchange transaction fee restrictions in Sections 235.3 and 235.4 by providing value that is economically equivalent to an interchange fee or by engaging in any practice that has the purpose or effect of compensating an issuer for its involvement

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portfolios, raising credit card interchange rates would be an easy way to provide them economic benefits in lieu of debit interchange. *See* Salop Report at ¶ 116 n.110 and Exhibits 8a and 8b.

[39] The Board's rationale for permitting increases to merchant fees and decreases to issuer fees is tautological. Even though the Board admits that such fee changes "could have the effect of offsetting reductions in interchange transactions," it defines away the obvious circumvention problem because such changes in network fee may not "necessarily indicate circumvention … absent net payments to the issuer." NPRM at 81747. Once one accepts that there can be circumvention without net payments to the issuer, the NPRM's reasoning collapses.

[40] In highlighting the creativity of the networks, it is worth noting that a general rule against circumvention could protect against some of the circumvention issues that are being discussed in the industry, including the use of general purpose reloadable prepaid cards to replace regulated debit cards, and possibly the exploitation of three-party network structures by banks or networks to charge higher interchange.

in an electronic debit transaction. We also suggest that there be some enforcement mechanism to address those situations.

With respect to enforcement of this general anti-circumvention provision, the MPC believes that the Federal Trade Commission, which will enforce the network aspects of these regulations after they go into effect, is well-positioned as an antitrust and consumer protection agency to handle such enforcement issues under the Electronic Fund Transfer Act ("EFTA").

C. The net compensation proposal has loopholes that need to be addressed

With some modifications, including some mechanism to monitor network arrangements with issuers, the NPRM's net compensation proposal could provide a workable approach to circumvention if applied in tandem with the proposed general anti-circumvention provision. In this regard, we respectfully suggest that signing bonuses, in-kind services, and fees for non-routine transactions (including chargebacks) be included in the calculation.

With respect to signing bonuses, we see no principled reason why they should be excluded from the net compensation calculation. They clearly are an economic benefit that can be provided to issuers, and we understand that Visa and MasterCard have provided massive signing bonuses in the past to the large issuers.[41] If they are excluded, then this loophole likely will undermine the efficacy of the entire approach, as networks will create packages with signing bonuses, which could be funded by network fee increases to merchants, without running afoul of the net compensation approach.[42] Moreover, networks can grow their volume and increase their efficiency without offering lucrative signing bonuses to issuers. If all debit networks are subject to these restrictions, they will compete for issuers based on performance criteria, rather than large signing

[41] *See, e.g.*, *United States v. Visa U.S.A. Inc.*, No. 98-cv-7076(BSJ), 2007 WL 1741885, at *4 (S.D.N.Y. June 15, 2007) ("Visa and MasterCard use so-called 'hard dollar' financial incentives — *e.g.*, signing bonuses, marketing support, and compensation for costs of conversion such as issuing new plastic cards — to persuade issuing banks to switch from one network to the other."); *see also id.* at *5 n.14 (relying on evidence from Visa and finding that "While the bulk of a bank's debit card earnings comes from interchange revenue, Visa and MasterCard do not compete for banks' business by promising higher interchange rates. Banks deem Visa and MasterCard roughly equal in terms of interchange revenue, which represents the fees that issuing banks receive from merchants for completing debit transactions. Visa's own conversion analyses explicitly assume parity with MasterCard in interchange revenue. Even though interchange revenue eclipses hard-dollar financial incentives in size, it is the incentives that drive a bank's brand-switching decision, since most banks deem interchange revenue 'pretty much a wash.'") (internal citations omitted).

[42] As detailed in Section II.B., *supra*, the net compensation calculation should exclude payments to affiliated entities, such as Visa DPS, to the extent that those payments are included in the allowable cost calculation for purposes of interchange.

bonuses funded by merchant fees. We therefore urge the Board to include signing bonuses in the net compensation calculation.

We are equally concerned about the exclusion of fees for chargebacks or violations of network rules from the net compensation calculation. NPRM at 81747. The networks easily can manipulate these rules to circumvent the regulations, and these fees could be used to compensate issuers for network services in lieu of interchange. As such, they should be included in the calculation.

Lastly, we respectfully suggest that the Board ensure that the net compensation calculation cover benefits provided to issuers for non-debit programs, when such benefits are clearly tied to the issuers' debit programs. Similarly, the rules should reach circumstances in which affiliates of issuers, such as acquirers, receive benefits that are clearly tied to the issuers' debit programs. These scenarios should be addressed in the net compensation approach.

V. Fraud prevention adjustment (reserved Section 235.4 of the proposed regulations)

A. Sound approach for fraud prevention adjustment exists based upon the Board's work

The fraud prevention adjustment standards discussed in the MPC's January 20, 2011 comment letter are drawn from the background and analysis in the Board's NPRM, and are consistent with Section 920. Importantly, they would balance the interests of issuers and merchants to motivate the implementation of potentially paradigm-shifting fraud prevention technologies without prescribing any particular one. The resulting reduction in fraud would benefit not just issuers and merchants, but consumers as well. Key aspects of these standards include:

- Each issuer, not the Board, would determine which "low fraud technologies"[43] it wishes to pursue.
- An issuer would receive reimbursement — from merchants who choose to use an eligible "low fraud technology" — for that issuer's initial capital investment necessary to implement the technology. The maximum per-transaction reimbursement would be based upon statistics already calculated by the Board.
- Consistent with both the approach in effect in Canada and recent network proposals to merchants in the United States, as a trade-off for this reimbursement, the issuer would be prohibited from imposing on

[43] Eligibility as a "low fraud technology" would be based upon a performance standard — reducing fraud below that occurring with PIN debit transactions — rather than on a prescriptive model.

merchants who choose to use the issuer's "low fraud technology" both (i) fines or penalties related to any debit card information compromised by a data breach and (ii) any fraud loss costs associated with transactions using the "low fraud technology."[44]

- This approach would be easy to administer because, in lieu of requiring surveys and calculations regarding all merchants' costs, it simply would prohibit the imposition of certain fraud-related costs on merchants who choose to use the issuer's "low fraud technology." Only limited verification of data provided by the parties would be required of the Board.

We believe that by marrying the best of the two proposals set forth in the NPRM, this new approach is the best of the three because it avoids dictating any specific technology, while providing a balanced and administrable structure likely to incent all parties to implement paradigm-shifting fraud prevention technology. In detailing this proposal, we believe that the comment letter also addresses the Board's requests for comment in the NPRM. For all of the reasons mentioned, regulations based upon this approach should lead to substantially reduced fraud that will benefit all parties, including consumers.

B. New technologies, including some currently in use in other nations, have demonstrated an ability to substantially reduce fraud

Networks and issuers could dramatically reduce debit card fraud in the United States simply by adopting new payment card technology. Different technologies to do this exist today and some are already in use in every other G-20 country. International comparisons show that the United States has the highest fraud rates, with the gap growing in recent years and probably understated. Counterfeit Fraud Migration, European Payments Council (June 29-30, 2010) at 5-7 (United States not among top ten countries with the most counterfeit fraud in 2004 but, by early 2010, it accounted for 85% of total counterfeit fraud of all top ten countries combined); Richard J. Sullivan, "The Changing Nature of U.S. Card Payment Fraud: Industry and Public Policy Options," Federal Reserve Bank of Kansas City Economic Review (2d. Quarter 2010) ("Sullivan") at 112-15.

Paradigm-shifting technology was proven in these other nations long ago, and even newer technology has been developed since. European Payments Council presentation (June 29, 2010) at 6 (United States last of 19 nations in adoption rate for one such technology); Sullivan at 114-15; Mott Report at ¶¶ 64-68. Technology options have been ready for the networks and issuers to adopt in the United States for some time. If they did, then this would make payment card transactions fundamentally more secure and, at

[44] In Canada, merchants that implemented EMV readers received protection against fraud-related chargebacks for <u>all</u> transactions, including those completed with legacy magnetic stripe systems.

the same time, eliminate most of the fraud-related liability that merchants face, while obviating the need for most of the data security expenditures currently required of merchants and processors.

Unfortunately, despite the availability of truly game-changing technology to reduce fraud, the networks and issuers have no incentive to adopt it under the current system in the United States because they can shift fraud-related costs to merchants.[45] Visa highlighted this point less than two weeks ago when it launched a new fraud prevention initiative based upon the "growing global … adoption" of such a technology. Visa Inc. Press Release, "Visa Program Encourages Merchant Adoption of EMV Chip as A Path Toward Dynamic Authentication," Feb. 9, 2011. Tellingly, however, Visa decreed that even though "[a]ll merchants outside the United States are eligible," it refuses to make this new initiative available in the United States. *Id*.

Networks and issuers currently like to argue that the passage of Section 920 approximately eight months ago is the excuse for not adopting proven fraud reduction technology in the United States. While they may find that excuse to be a useful rhetorical flourish in their massive lobbying campaign, it does not comport with reality. Certain types of this new technology were available — indeed, were adopted globally outside the United States by these very same banks and networks — well before the passage of Section 920. *See, e.g.*, European Payments Council presentation (June 29, 2010) at 6; Sullivan at 114-16. The networks and issuers simply chose not to implement them here.[46]

VI. Comments on other issues addressed in the NPRM

A. <u>"Exemptions" (Section 235.5 of the proposed regulations)</u>

1. Non-exempt debit cards

a. Healthcare cards (FSA, HSA, and HRA)

In our view, there is no credible argument that Flexible Spending Arrangement, Health Savings Account, and Health Reimbursement Arrangement cards are exempt from Section 920(a). They simply are not among the exemptions set forth in Section

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[45] As a matter of economics and policy, the party best able to control fraud should bear the costs. *See generally* Salop Report at ¶¶ 129-136. This creates the right incentives to reduce fraud. *Id*. Unfortunately, this is not the current state of affairs with respect to the current debit card system in the United States.

[46] The Chairwoman of the House Subcommittee on Emerging Threats, Cybersecurity, and Science and Technology concluded nearly two years ago that "[m]agnetic stripe-based technology is outmoded and inherently less secure … [and] the payment card industry and issuing banks should be ashamed about the current state of play and doing everything possible to immediately institute improvements in infrastructure." Statement of Subcommittee Chairwoman Yvette D. Clarke, "Do the Payment Card Industry Data Standards Reduce Cybercrime?," Mar. 31, 2009.

920(a)(7). First, these cards are not government-administered programs under Section 920(a)(7)(A)(i). To the contrary, they are cards issued to consumers as part of benefits packages that they receive from programs administered by their employer, benefits manager, or insurance company. As such, they are unlike a benefit program that is managed by a government agency, where the agency nonetheless outsources the administration of the program to a third-party that "act[s] on behalf of the government agency." *See* NPRM at 81744. Further, these cards access accounts that are typically held by the employer for the benefit of the cardholder (the employee) or are held by the cardholder himself, which disqualifies them under Section 920(a)(7)(A)(ii)(II). In addition, these cards typically are not "reloadable," as the cardholder designates his/her contribution prior to the year and cannot reload the card if the account is depleted during that year, creating another reason why they do not qualify for the prepaid card exemption. *See* Section 920(a)(7)(A)(ii)(V).

b. Certain prepaid cards

Section 920(a)(7) exempts certain reloadable general purpose prepaid cards from Section 920(a). Whether the underlying funds are subject to FDIC insurance determines the line between prepaid cards subject to Section 920, on the one hand, and general purpose reloadable prepaid cards exempt from Section 920, on the other.[47]

Specifically, Section 920(a)(7) exempts from Section 920(a) reloadable cards or devices "linked to funds, monetary value, or assets which are purchased or loaded on a prepaid basis." In order to fall within this exemption, the card may not be used to "access or debit any account held by or for the benefit of the card holder (other than a subaccount or other method of recording or tracking funds purchased or loaded on the card on a prepaid basis)." Section 920(a)(7)(A)(ii)(II). That is, if the funds are in an account "held for the benefit of the card holder," then the interchange fee standard applies, but if the "account" is a mere bookkeeping device, then the exemption applies.

The FDIC general counsel has issued an opinion which makes clear that for FDIC insurance coverage to extend on a "pass-through basis" to each cardholder's prepaid balance, the cardholder — not just the custodian of the overall account into which funds may be pooled — must actually "own" the prepaid funds. 73 Fed. Reg. 67155, 67157 (Nov. 13, 2008).[48] If a cardholder "owns" the account balance, then those funds are clearly being "held for the benefit" of the cardholder and Section 920(a)(7) cannot apply.

[47] This dichotomy applies even if the funds are held in a pooled general account, so whether the issuer holds the funds in a general account or a cardholder-specific account will not be determinative.

[48] The General Counsel of the FDIC also has classified funds placed in pooled accounts as "deposits" for purpose of the FDIC's mandate because such funds are no different than the funds underlying "traditional access mechanisms" to the deposit accounts. *See* General Counsel's Opinion No. 8.

Accordingly, the exemption for prepaid cards under Section 920(a)(7) must be limited to reloadable general purpose prepaid cards where the cardholder is not extended the benefit of FDIC coverage for the funds that are loaded with respect to the card. Applying this bright line rule[49] would be faithful to the statute and should limit the potential use of prepaid cards as a circumvention device.[50]

2. Certification

The Board requested comment on whether it should implement a certification process for the issuers and products that are exempt from Section 920(a)(1). NPRM at 81743-46. With respect to the exemption for small issuers, the MPC supports a process whereby issuers would notify the Board and payment networks within 90 days of the end of the preceding calendar year in order to be eligible for an exemption for the next rate period.

As for the exemption for certain general purpose reloadable prepaid cards, the MPC respectfully suggests that the Board establish general guidelines and a certification process whereby networks or issuers have to certify compliance with the exemption to the Board. Because of our concerns that such cards may be used to circumvent the statute, the MPC does not support permitting the networks to develop their own certification processes for these cards. The Board could require such certification to occur no later than three months before each calendar year. Even though they present a lower circumvention risk, for administrative simplicity, the same rules could be applied to debit cards associated with government-administered benefit programs.

B. "Definitions" (Section 235.2 of the proposed regulations)

1. Definition of "payment card network"

The proposed definition of "payment card network" in Section 235.2(m) can and should be applied to mobile phone networks that link issuers and merchants and thereby perform all of the network functions that traditional networks handle. This definition would not apply to PayPal, however, unless and until it opens up its platform to third-party issuers.

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[49] Because the set of exempt prepaid cards may be even narrower, a secondary test to identify additional non-exempt cards could be used. As an initial sorting device, however, this bright line rule is appropriate and easily administered.

[50] Earlier this month, the Consumers Union, the National ACH Association (NACHA), and the American Payroll Association, among other groups, jointly issued 10 "core principles" for payroll cards. Principle 7 states that "[e]mployers must select a program that maintains payroll funds in an FDIC- or NCUA-insured account on a pass-through basis to the individual cardholder." To be eligible for pass-through insurance status, as noted above, the FDIC requires that the cardholder must "own" the funds. Hence, at a minimum, cards issued under a payroll card program meeting these guidelines voluntarily, or as may be required by state law, are not exempt from Section 920(a).

The definition of "payment card network" should be sufficiently flexible such that it could be applied to products, such as eBillme, where issuers could use an alternative platform that has the capability of linking them to merchants to facilitate debit transactions. If that happens, any interchange associated with those transactions should be regulated for covered issuers. Moreover, if the definition of "payment card network" is not sufficiently flexible to cover such situations, general anti-circumvention language should be in place to reach such conduct. We are concerned that the Board's departure from the explicit language of the statute, by adding "that establishes the rules, standards, or guidelines" could reduce the flexibility to adapt to such circumstances.

2. Definition of "interchange transaction fee"

The proposed definition of "interchange transaction fee" in Section 235.2(j) tracks the statutory definition as "any fee established, charged, or received by a payment card network and paid by a merchant or acquirer for the purpose of compensating an issuer for its involvement in an electronic debit transaction." The proposed rule simply adds "paid by a merchant or acquirer" to clarify where the burden of interchange fees lies. Proposed comment 2(j) emphasizes that such fees are only those paid to an issuer, and not those that may be charged by a payment card network for its own activities in connection with a debit transaction.

The MPC believes that one issue merits clarification. The rule should ensure that the term "established" is construed broadly in scope to include any fees "established, allowed, or permitted" by a payment card network, and not narrowly to those fees expressly "set" by the network. In particular, the Board should clarify that the definition incorporates any fee that merchants are forced to pay under the umbrella created by network Honor All Cards rules. As we have stated elsewhere, if networks "permitted" the imposition of such fees that would, in effect, reinstate the collective fixing of interchange fees through another means, the collective imposition of Honor All Cards rules. This issue should be addressed in the definition of "interchange transaction fee" as well as through the general anti-circumvention regulations.

3. Definition of "issuer"

The proposed definition of "issuer" in Section 235.2(k) simply states that the term means "any person that issues a debit card." In so doing, the rule eliminates the statutory phrase "or the agent of such person as with respect to the card" (Section 920(c)(9)), because in the Board's view, "as a matter of law," agents are held to the same restrictions as their principles." NPRM at 81731. The MPC believes more clarity is required, particularly with respect to the impact of the definition of an "issuer" on the scope of "interchange transactions fees," which is definitionally limited to fees that "compensate an issuer." Such matters should not be left to the dictates of the law of agency in a particular state.

C. Administrative issues

1. Reporting requirements

Section 920(a)(3)(B) allows the Board to collect information "as may be necessary" from issuers and networks, and also requires the Board to disclose certain cost and interchange transaction fee information "on at least a bi-annual basis." In other words, the statute requires disclosure at least twice a year. In contrast, Section 235.8(c) of the proposed regulations requires issuers and networks to report this information to the Board "biennially." In other words, the proposed regulations appear to contemplate disclosures only every two years.

The MPC believes that biennial data collection and disclosure would be too infrequent, especially during the first several years that the regulations promulgated pursuant to Section 920 are in effect. During the early years of implementation, all interested parties should have more regular visibility into the relevant costs and fees. While the MPC believes annual data collection and disclosure would be appropriate, the statute requires it even more frequently.

Frequency aside, validation of this cost and fee information that issuers and networks will have to provide is critical to assessing compliance with Section 920. As mentioned in note 15, *supra*, the nuanced complexity of accounting for ACS costs means that it would be unrealistic to expect anyone not participating in the industry on a daily basis to be able to audit and validate this information thoroughly. Accordingly, the Board should permit a limited number of representatives from the merchant community to review this information (pursuant to a confidentiality agreement) in order to provide regulators additional expertise upon which they can draw to conduct a thorough assessment.

2. Compliance

Monitoring compliance with these regulations is necessary, particularly with respect to the anti-circumvention rules (Section IV., *supra*), verification of allowable costs above the safe harbor level (Section II.E., *supra*), verification of compliance with each merchant's routing instructions (White Paper at 16), and certification of exempted issuers and debit cards (Section VI.A.2., *supra*). Additionally, because deterrence is a function of both the probability of getting caught and the punishment imposed if one is caught, it is also important for there to be consequences associated with engaging in such prohibited behavior.

While Section 235.9 of the proposed regulations identifies the regulatory agencies responsible for enforcement, the MPC believes that the Board should assess whether the types of (and standards for assessing) penalties set forth in the authorizing statute for each of those agencies are appropriate for enforcement of these particular regulations. It may be useful to complement any such general penalty provisions with enforcement options internal to these regulations themselves. For example, with respect to misconduct involving issuers, they could be temporarily denied the opportunity to recover any costs above the safe harbor or to benefit from any fraud adjustment. With respect to misconduct involving networks, the punishment need not be imposed directly on them, but instead could be in the form of temporarily prohibiting issuers from issuing new debit cards with that network as a routing option. This would be analogous to a temporary debarment under federal contracting law. Making these additional options available to the relevant regulatory agencies could result in more streamlined and appropriate enforcement that would further dissuade parties from evading or circumventing these regulations.

VII. Conclusion

Thank you for the opportunity to submit comments regarding this important regulatory proceeding. The MPC commends the Board and its staff on their thorough review and analysis of these issues to date, and hopes the Board will take the views set forth in this letter into consideration in drafting the final regulations required under Section 920.

Please do not hesitate to contact us if you would like to discuss any of these issues further.

Sincerely,

Jeffrey I. Shinder /MP

Jeffrey I. Shinder

Todd Anderson /MP

Todd Anderson

Attachment A

MasterCard Rules

29 October 2010
Updated 10 December 2010

5.1 The Merchant Agreement

Each Member in its capacity as an Acquirer must directly enter into a written Merchant Agreement with each Merchant from which it acquires Transactions, whether such Transactions are submitted to the Member directly by the Merchant or through a Member Service Provider acting for or on behalf of such Member.

An Acquirer shall not submit into interchange any Transaction resulting from the acceptance of a Card by an entity or person except pursuant to a Merchant Agreement then in effect between the Acquirer and the entity or person.

The Merchant Agreement must reflect the Acquirer's primary responsibility for the Merchant relationship and must otherwise comply with the Standards.

5.1.1 Verify Bona Fide Business Operation

Before entering into, extending, or renewing a Merchant Agreement, an Acquirer must verify that the Merchant from which it intends to acquire Transactions is a bona fide business, has sufficient safeguards in place to protect from unauthorized disclosure or use such Cardholder and Transaction information as the Standards permit to be captured, and complies with applicable laws, and that each Transaction will reflect bona fide business between the Merchant or Sub-merchant and a Cardholder. Procedures for verifying that a Merchant is a bona fide business are set forth in section 7.1 of the *Security Rules and Procedures* manual.

5.1.2 Required Terms

Each Merchant Agreement must contain the substance of each of the Standards set forth in Rules 5.6 through 5.12. Furthermore, each Merchant Agreement with a gambling Merchant must incorporate the requirements set forth in section 2.5.4 of the *Chargeback Guide*. The failure to include the substance of any one or more of such Standards in the Merchant Agreement or the grant of a variance by the Corporation with respect to any one or more such Standards does not relieve an Acquirer from responsibility for chargebacks or compliance.

Each Merchant Agreement may contain only such terms agreed to by the Acquirer and the Merchant, provided that no such term conflicts with any Standard.

Each Merchant Agreement with a Merchant registered as a Payment Facilitator must additionally contain the substance of Rule 5.5 and a provision stating that the Payment Facilitator accepts financial liability for all Transactions entered into interchange on behalf of its Sub-merchants and will be responsible for the handling of all disputed Transactions, credits, and customer service-related expenses. The Merchant Agreement must provide for:

1. The Acquirer's right to terminate the Payment Facilitator, and
2. The Payment Facilitator's obligation to ensure the ongoing compliance of each of its Sub-merchants with the Standards and
3. The Payment Facilitator's obligation to terminate the written agreement with a Sub-merchant for the conduct of activity deemed by the Payment Facilitator, its Acquirer, or the Corporation to be in violation of the Standards.

Note **Additions to this Rule appear in Chapter 10a, "New Zealand Rules"; Chapter 12, "Europe Region Rules"; Chapter 14a, "South Africa Rules"; and Chapter 15a, "United States Region Debit-related Rules."**

5.1.3 Assessments for Merchant Agreement Noncompliance

An Acquirer in violation of Rule 5.1 may be assessed up to USD 2,500 per day with respect to each entity or person on whose behalf the Acquirer submits Transactions into interchange with no Merchant Agreement being in effect between the Acquirer and the entity or person, retroactive to the first day of such noncompliant practice.

5.2 Acquirer Obligations

An Acquirer must satisfy all of the obligations set forth in this Rule 5.2.

5.2.1 Acquiring Transactions

Each Acquirer must acquire all Transactions properly presented to it from each of its Merchants on such terms as set forth in the Merchant Agreement.

4. the following disclaimer must appear in close proximity to the mark on the same page and in an equal size and type of print:

"MasterCard International Incorporated is not affiliated in any way with [Merchant] and has not endorsed or sponsored this offer."

"Merchant further agrees to submit its first direct mail solicitation(s), prior to mailing, to the MasterCard Law Department, to be reviewed only for compliance with this Corporation's trademark rules and shall furthermore not distribute in any manner such solicitations until Merchant shall have obtained this Corporation's written approval of the manner in which it uses MasterCard mark and logo on such solicitations. Merchant shall likewise, upon request, submit to the Corporation any amended solicitations prior to mailing."

5.8 Card Acceptance Requirements

An Acquirer must ensure that each of its Merchants complies with the Card acceptance requirements set forth in this Rule 5.8 and in section 2.1 of the *Chargeback Guide*.

5.8.1 Honor All Cards

A Merchant must honor all valid Cards without discrimination when properly presented for payment. A Merchant must maintain a policy that does not discriminate among customers seeking to make purchases with a Card. A Merchant that does not deal with the public at large (for example, a private club) is considered to comply with this rule if it honors all valid and properly presented Cards of Cardholders that have purchasing privileges with the Merchant.

Note **Variations to this Rule appear in Chapter 10a, "New Zealand Rules"; Chapter 11a, "Canada Region Code of Conduct Related Rules'; Chapter 12a, "Europe Region Debit-related Rules"; Chapter 14a, "South Africa Rules"; and Chapter 15a, "United States Region Debit-related Rules."** *chg*

5.8.2 Merchant Acceptance

Note **A Rule on this topic appears in Chapter 10a, "New Zealand Rules"; Chapter 12, "Europe Region Rules"; Chapter 14a, "South Africa Rules"; and Chapter 15a, "United States Region Debit-related Rules." A variation to the Europe Region Rule appears in Chapter 12a, "Europe Region Debit-related Rules."**

5.8.3 Obtain an Authorization

When required by the Standards or by the Acquirer, the Merchant must obtain an authorization before completing a Transaction.

For specific Merchant authorization requirements, refer to sections 2.1.2 through 2.1.5 of the *Chargeback Guide*. *chg*

5.8.4 Additional Cardholder Identification

A Merchant must not refuse to complete a Transaction solely because a Cardholder who has complied with the conditions for presentment of a Card at the POI refuses to provide additional identification information, except as specifically permitted or required by the Standards. A Merchant may require additional identification from the Cardholder if the information is required to complete the Transaction, such as for shipping purposes. A Merchant in a country or region that supports use of the MasterCard Address Verification Service (AVS) may require the Cardholder's ZIP or postal code to complete a Cardholder-Activated Terminal (CAT) Transaction, or the Cardholder's address and ZIP or postal code to complete a mail order, phone order, or e-commerce Transaction.

5.8.5 E-Commerce Transactions

A Merchant must not refuse to complete an e-commerce Transaction solely because the Cardholder does not have a digital certificate or other secured protocol.

5.8.6 Purchase With Cash Back Transactions

Refer to sections 2.1.12 and 2.4 of the *Chargeback Guide* for purchase with cash back Transaction requirements.

15a United States Region Debit-related Rules

This chapter contains debit-related Rules that apply only in the United States Region.

Organization of this Chapter

The Rules in this Chapter 15a are variances and additions to the "global" Rules resulting from the settlement of In Re Visa Check/MasterMoney Antitrust Litigation. These Rules apply to Debit MasterCard Cards and Other Cards issued in the U.S. Region by U.S. Region Members and presented for payment at Merchant locations in the U.S. Region. Members and Merchants in the U.S. Region must continue to comply with the global Rules for Cards issued by Members outside of the U.S. Region and presented for payment at Merchant locations in the Region.

With respect to Debit MasterCard Cards, these Rules apply where signature is used as the Cardholder verification method (CVM) or where no CVM is required. For Rules applicable to Debit MasterCard Cards where PIN is used as the CVM, refer to Chapter 15b.

Definitions

Solely for the purposes of this Chapter 15a, the following terms have the meanings set forth below.

1. "Debit" or "Debit MasterCard Card" or "Debit Card" shall mean any Access Device, Program, or Card issued in the Region, by a Regional Member, that when presented for payment in the United States, accesses, debits, holds, or settles funds from a consumer's demand deposit or asset account. "Debit" or "Debit MasterCard Card" shall include consumer signature debit Programs, stored value Programs, prepaid Cards, payroll Cards, electronic benefit transfer Cards, and deferred debit Cards that access, debit, hold, or settle funds from the user's demand deposit or asset account less than fourteen days after the date of purchase. "Debit" shall not include any point-of-sale device that accesses, debits, hold, or settles funds from the user's demand deposit or asset account fourteen or more days after the date of the purchase.
2. "Other Card" shall mean any Access Device, Program, or Card that is not defined as "debit" or "Debit MasterCard Card".

2.7 Liability for Assigned ICAs and BINs

Rule 2.7 of Chapter 2, "Licensing and Licensed Activities," is modified to include the following:

Transaction/BIN Identification. Members must use specific and unique bank identification numbers (BINs) for Debit MasterCard Cards.

2.20 Risk of Loss

In addition to the Rules in Chapter 2, "Licensing and Licensed Activities," the following applies:

The Risk of Loss Rule applies with respect to affiliate debit Licensees in the same manner as it applies to Members.

4.2 General Rules for Use of the Marks

4.2.6 Particular Use of a Mark

4.2.6.6 Use on Cards

Rule 4.2.6.6 of Chapter 4, "Trademarks and Service Marks," is modified to include the following:

Clear and Conspicuous Debit Identifier. Members must display

1. the Debit MasterCard Hologram instead of the MasterCard Global Hologram on the front of all Debit MasterCard Cards issued in the United States, in the position required for the MasterCard Global Hologram, or
2. the "Debit" word mark on the Card front if the Debit MasterCard Hologram is on the Card back. Debit MasterCard Cards must conform to the Standards set forth in the *Security Rules and Procedures* manual and the Card Design Standards System.

5.1 The Merchant Agreement

5.1.2 Required Terms

Rule 5.1.2 of Chapter 5, "Merchants and Sales Transactions," is modified to include the following:

In addition to the Standards set forth in Chapter 5, Merchant Agreements must provide the Merchant with the option, and the applicable Merchant discount rate for each option, to elect to accept Debit MasterCard Cards only, Other Cards only, or both Debit MasterCard Cards and Other Cards. With respect to any contract existing on or before 1 January 2004, under which a Merchant accepts Cards, a Merchant may choose to stop accepting Debit MasterCard Cards or Other Cards by providing no less than 30 days advance written notice to its Acquirer.

5.8 Card Acceptance Requirements

5.8.1 Honor All Cards

Rule 5.8.1 of Chapter 5, "Merchants and Sales Transactions," is replaced with the following:

Honor All Debit MasterCard Cards. Merchants that choose to accept Debit MasterCard Cards must honor all valid Debit MasterCard Cards without discrimination when properly presented for payment. The Merchant must maintain a policy that does not discriminate among customers seeking to make purchases with a Debit MasterCard Card.

Honor All Other MasterCard Cards. Merchants that choose to accept Other Cards must honor all Other Cards without discrimination when properly presented for payment. The Merchant must maintain a policy that does not discriminate among customers seeking to make purchases with another Card.

5.8.2 Merchant Acceptance

Merchants that accept Cards may choose to accept Debit MasterCard Cards only, Other Cards only, or both Debit MasterCard Cards and Other Cards. Acquirers must advise the Corporation when a Merchant in the Region chooses not to accept either Debit MasterCard Cards or Other Cards.

Merchants that request signage for the purpose of indicating their acceptance of Debit MasterCard Cards must display such signage for a minimum of three months. The signage may be requested at www.mastercardweacceptdebit.com.

Acquirers must provide a complete list of the BINs that apply to Debit MasterCard Cards to Merchants upon any form of reasonable request.

15b United States Region PIN-based Debit Transaction Rules

This chapter contains Rules that apply only to PIN-based Debit MasterCard Transactions occurring in the United States Region.

Organization of this Chapter

Rules in this Chapter 15b are variances and additions to the "global" Rules that apply in the U.S. Region. These Rules relate to Debit MasterCard Cards where a PIN is used as the Cardholder verification method.

Definitions

Solely for the purposes of this Chapter 15b, the following terms have the meanings set forth below.

1. "Debit" or "Debit MasterCard Card" shall mean any Access Device or Card that, when presented for payment in the United States, accesses, debits, holds, or settles funds from a demand deposit or asset account and where PIN is used as the Cardholder verification method.
2. "Service Marks" shall mean (i) from an issuing perspective, the MasterCard Word Mark and/or the MasterCard Brand Marks as those terms are defined in the Definitions chapter of this manual, and (ii) from an acquiring perspective, the MasterCard Word Mark and/or the MasterCard Brand Marks as those terms are defined in the Definitions chapter of this manual and the MAESTRO trademarks, trade names, service marks, logotypes, and trade designations made available for use pursuant to License by the Corporation.
3. "Maestro Service Marks" shall mean the MAESTRO trademarks, trade names, service marks, logotypes, and trade designations made available for use pursuant to license by the Corporation.
4. "Cirrus Service Marks" shall mean the CIRRUS trademarks, trade names, service marks, logotypes, and trade designations made available for use pursuant to license by the Corporation.

3.9 Transaction Requirements

3.9.6 PIN-based Debit Transactions

Members may choose to issue Debit MasterCard Cards where a PIN is used as the Cardholder verification method and/or acquire Transactions effected with such Cards as defined in this Chapter 15b. If Members so choose, the rules contained in the *Maestro Global Rules* will apply to such Transactions except

1. for the requirements contained in sections 1.2 Membership, 1.3.1 License Application Process (as those requirements relate to issuing Activity), 1.7 Termination from the Organization, 4.3 Display on Cards, and 6.1.1 b.1. Eligible Cards, of that rulebook, and
2. that when the term "Member" appears in the text of the *Maestro Global Rules*, the definition of that term contained in the Definitions chapter of this manual applies, and
3. that when the term "Service Marks" appears in the text of the *Maestro Global Rules*, the definition of that term contained in part 2 of the Definitions section in this Chapter 15b applies.

4.2 General Rules for Use of the Marks

4.2.6 Particular Use of a Mark

4.2.6.6 Use on Cards

Rule 4.2.6.6 of Chapter 4, "Trademarks and Service Marks," is modified to include the following:

1. The Maestro and/or Cirrus Service Marks must not appear on Debit MasterCard Cards issued on or after 1 June 2006. Effective 1 June 2007, the Maestro and/or Cirrus Service Marks must not appear on Debit MasterCard Cards.
2. Issuers that display regional debit brands on their Debit MasterCard Cards must place the MasterCard Brand Mark on the back (in equal size and prominence with those regional debit brands) as well as on the front of the Card. Refer to the Card Design Standards System for additional information.

Attachment B

Visa International Operating Regulations

15 October 2010

Chapter 6: Payment Acceptance

Core Principle 6.1

Display of Marks

Accepting Visa Products for Payment

Visa merchants displaying Visa acceptance marks at payment locations agree to accept corresponding Visa-branded products for payment. If the customer indicates that he or she wants to pay with a Visa product, a merchant must complete and process the Visa transaction as defined in the Visa Operating Regulations.

ID#: 160210-150210-0007777

Core Principle 6.2

Honor All Cards Properly Presented

Honoring All Visa Cards

Visa merchants may not refuse to accept a Visa product that is properly presented for payment, for example, on the basis that the card is foreign-issued, or co-branded with a competitor's mark. Merchants may steer customers to an alternative method of payment, such as providing discounts for cash, but may not do so in a confusing manner that denies consumer choice. Merchants may decline to accept a Visa product that is not covered by their acceptance contract, and may also consider whether present circumstances create undue risk.

Footnote: In the US, Canada, and Australia, merchants may decline to accept certain categories of Visa products for domestically issued cards.

ID#: 160210-150210-0007778

ID#: 010410-010410-0008478

Inspection

An Acquirer must conduct a physical inspection of the business premises of a prospective Merchant. For Mail/Phone Order and Electronic Commerce Merchants, the Acquirer must also obtain a detailed business description.

ID#: 010410-010410-0005251

Merchant Agreement Requirements

An Acquirer must:

- Have a Merchant Agreement with each of its Merchants
- Include language in the Merchant Agreement that obligates its Merchant to:
  - Perform its obligations under the Merchant Agreement in compliance with applicable laws
  - Comply with the *Visa International Operating Regulations* regarding use of the Visa-Owned Marks
- Ensure that its Merchant complies with the *Visa International Operating Regulations* regarding payment acceptance
- Ensure that required acceptance provisions are included in its Merchant Agreement or as a separate addendum
- Only accept Transaction Receipts from a Merchant with which it has a valid Merchant Agreement

Refer to the *Visa International Operating Regulations* for further information regarding Member compliance with applicable laws, requirements for certain Merchant segments, and Visa rights to monitor, audit, inspect, and investigate Members.

ID#: 081010-010410-0003356

Electron

A Merchant must have a Merchant Agreement with its Acquirer to accept Visa Cards or Visa Electron Cards. The same contract may cover Visa Cards and Visa Electron Cards.

ID#: 010410-010410-0005107

Right to Terminate

The right of Visa to limit or terminate a Member's agreement with a Merchant must be specified in each Merchant, Sponsored Merchant, and agent agreement.

ID#: 010410-010410-0008473

- Query the Terminated Merchant File to determine if the prospective Merchant has been terminated for cause
- Whenever feasible, conduct a physical inspection of the business premises of a prospective Merchant
- For Mail/Phone Order Merchants, obtain a detailed business description

ID#: 010410-010410-0003474

Merchant Agreement Specifications and Options - U.S. Region

In the U.S. Region, for each new Merchant, a Merchant Agreement must clearly:

- Specify the Limited Acceptance options and the Merchant's election, if any, of one of those options
- Distinguish all Card acceptance-related fees, such as discount rates or other pricing methodology, associated with each Limited Acceptance category

An existing Merchant Agreement must be revised to include the Limited Acceptance options and distinguish all Card acceptance-related fees when either:

- The existing Merchant Agreement is renewed
- The Merchant indicates to its Acquirer that it wants Limited Acceptance

ID#: 031209-150210-0008510

Specification of Merchant Fees - U.S. Region

In the Merchant Agreement, a U.S. Acquirer must clearly distinguish fees associated with Visa Transactions from fees associated with other card transactions.

ID#: 010410-010410-0003361

Terminal Processing by Competitors - U.S. Region

A U.S. Acquirer must **not** prohibit a Merchant from using terminal processing services offered by competitors for the direct delivery of Visa Transactions captured at the Point-of-Transaction to VisaNet for Clearing and Settlement.

ID#: 010410-010410-0003362

Merchant Agreement Form - U.S. Region

In the U.S. Region, most of the form, content, and appearance of a Merchant Agreement is at the discretion of the Acquirer. However, each Merchant Agreement must contain at least the requirements for Merchant Card acceptance specified in the *Visa International Operating Regulations* to the extent permitted under applicable law. An Acquirer may include other provisions in its Merchant Agreement if they are consistent with the *Visa International Operating Regulations.*

Each Merchant Agreement must:

ID#: 010410-010410-0005323

Point-of-Transaction - Display of Marks

Display of Marks at the Point of Sale

Merchant Standards for Card Acceptance

An Acquirer contracting with a Merchant to accept Cards must ensure that the Merchant meets the standards specified in the table below.[2]

Merchant Acceptance Standards

Symbols Displayed at Merchant	Cards Accepted by Merchant	Electronic Capability	Cash-Back
Visa Brand Mark	Visa Cards[1]	Optional	For Domestic Transactions only, at the option of Visa
Visa Brand Mark with the Electron Identifier	Visa Electron Cards	Required	For Domestic Transactions only, at the option of Visa

1. A variance to this requirement applies in the U.S. Region.
2. A variance applies to this requirement in the Canada Region.

ID#: 010410-010410-0003658

Display of Appropriate Marks

A Member or Merchant must display the appropriate Marks to indicate which Cards it accepts for payment, as specified in the *Visa Product Brand Standards.*

ID#: 010410-010410-0008496

Display of Marks Exclusion VIOR 5.1.A.1.d, USOR 5.2.A.1.a

A Merchant is **not** required to display the Visa-Owned Marks if it does not deal with the general public (e.g., a private club, or if prohibited by trade association rules).

ID#: 010410-010410-0002643

Honoring Cards

General Acceptance Requirements

Valid Acceptance

A Merchant must accept all Cards properly presented for payment as specified in the "Merchant Acceptance Standards" table.

A variance to this requirement applies in the U.S. and Canada Regions.

If a Merchant does not deal with the public (e.g., a private club), it complies with this requirement if it accepts Cards from its Members.

ID#: 081010-150210-0008591

Transaction Processing Requirement - CEMEA Region

Subject to local law, a CEMEA Acquirer must process all valid Transactions originating from its Merchants.

ID#: 010410-010410-0005242

Acceptance of Visa Electron Cards - CEMEA Region

In the CEMEA Region, the following requirements apply to all Visa Electron Card Transactions at Merchant Outlets or Point-of-Transaction Terminals, including ATMs, whether or not a Merchant Outlet has specifically contracted with the Acquirer to accept Visa Electron Cards:

- An Authorization Request must **not** be systematically rejected or declined by an Acquirer if a Point-of-Transaction Terminal, including an ATM, has sent the Transaction Online for Authorization
- An Authorization Request involving a Visa Electron Card Transaction must be forwarded to the Issuer or to the Issuer's Processor for an Authorization Response
- A Visa Electron Card Transaction is subject to the conditions specified in the *Visa International Operating Regulations* and "Dispute Resolution"

ID#: 010410-010410-0005243

Visa Electron Card Transactions - CEMEA Region

In the CEMEA Region, a Visa Electron Merchant must accept valid Visa Electron Cards when presented for payment. A Visa ATM must accept all Visa Electron Cards, subject to the same local restrictions allowed for Proprietary Cards bearing the Plus Symbol.

ID#: 010410-010410-0004747

Discount at the Point of Sale

Discount Offer - U.S. Region 5.2.D.2

In the U.S. Region, any purchase price advertised or otherwise disclosed by the Merchant must be the price associated with the use of a Visa Card or Visa Electron Card.

A U.S. Merchant may offer a discount as an inducement for a Cardholder to use a means of payment that the Merchant prefers, provided that the discount is:

- Clearly disclosed as a discount from the standard price
- Non-discriminatory, as between a Cardholder who pays with a Visa Card and a cardholder who pays with a "comparable card"

A "comparable card" for purposes of this rule is any other branded, general purpose payment card that uses the cardholder's signature as the primary means of cardholder authorization (e.g., MasterCard, Discover, American Express). Any discount made available to cardholders who pay with "comparable cards" must also be made available to Cardholders who wish to pay with Visa Cards. Any discount made available to a Cardholder who pays with a Visa Card is **not** required to be offered to cardholders who pay with "comparable cards."

ID#: 010410-010410-0008590

Discounts on Purchases Made with Affinity Cards - U.S. Region

When presented with an Affinity Card, a U.S. Merchant or Affiliated-merchant must **not** provide a discount to the Cardholder, unless either the:

- Discount, such as a credit on the Cardholder statement, rebate, etc., is provided subsequent to the time of the Transaction
- Cardholder presents a coupon or voucher in addition to the Affinity Card

A Merchant or Affiliated-merchant must **not** promote at the Point-of-Transaction the availability of discounts on purchases made with an Affinity Card.

ID#: 010410-010410-0003034

Cardholder Choice

Honor All Cards - Canada Region

Effective 20 February 2009, in the Canada Region, unless a Merchant has elected to not be a Visa Debit Acceptor, a Merchant that accepts Visa Cards must accept any valid Visa Card that a Cardholder properly presents for payment. This means that the Merchant must permit the Cardholder to choose whether to pay for a transaction with that Visa Card or with some other means of payment accepted by the Merchant.

Effective 16 August 2010, in the Canada Region, Merchants who have elected to be a Visa Debit Acceptor may choose whether or not to accept domestic Visa Credit Cards. Similarly, Merchants who have elected to be a Visa Credit Acceptor may choose whether or not to accept domestic Visa Debit Cards.

ID#: 081010-200209-0008392

Selection of Payment System - Canada Region

Effective 20 February 2009, in the Canada Region, if a Cardholder presents a Visa Card that bears a Mark representing another payment service:

- **Effective through 15 August 2010,** the Merchant must honor the Cardholder's request if the Cardholder indicates that the transaction is to be processed as a Visa Transaction
- **Effective through 15 August 2010,** the Merchant may process the transaction as something other than a Visa Transaction despite an initial indication by the Cardholder that the transaction is to be processed as a Visa Transaction, but **only** if the Cardholder agrees that the transaction may be processed as something other than a Visa Transaction. The Merchant may **not** mislead the Cardholder concerning what payment service or system will be used. If the Merchant provides any information regarding the customer's rights related to various transaction choices, that information must be accurate.
- **Effective 16 August 2010,** the Merchant may **not** intentionally mislead the Cardholder concerning what payment service or system will be used. If the Merchant provides any information regarding the customer's rights related to various transaction choices, that information must be accurate.

ID#: 081010-200209-0008393

Honor All Cards - U.S. Region 5.2.B

A U.S. Merchant that wishes to accept Visa Cards must accept any valid Visa Card in its category of acceptance that a Cardholder properly presents for payment. This means that the Merchant must permit the Cardholder to choose whether to pay for a transaction with that Visa Card or with some other means of payment accepted by the Merchant. The Merchant may request or encourage a Cardholder to use a means of payment other than a Visa Card.

ID#: 010410-010410-0002867

Selection of Payment System - U.S. Region

In the U.S. Region, if a Cardholder presents a Visa Card that is in the Merchant's category of acceptance and that bears a Mark representing another payment service:

- The Merchant must honor the Cardholder's request if the Cardholder indicates that the transaction is to be processed as a Visa Transaction
- The Merchant may process the transaction as something other than a Visa Transaction despite an initial indication by the Cardholder that the transaction is to be processed as a Visa Transaction, but only if the Cardholder agrees that the transaction may be processed as something other than a Visa Transaction. The Merchant may **not** mislead the Cardholder concerning what payment service or system will be used. If the Merchant provides any information regarding the customer's rights related to various transaction choices, that information must be accurate.

ID#: 010410-010410-0002868

Incentive to Use Other Payment Method - U.S. Region

A U.S. Merchant may offer a non-monetary benefit to a Cardholder as an inducement for the Cardholder to use a means of payment other than a Visa Card. A Merchant may offer a monetary benefit in the form of a discount, as provided in "Discount Offer - U.S. Region," as an inducement for the Cardholder to use a means of payment other than a Visa Card.

ID#: 010410-010410-0002870

Limited Acceptance

Limited Acceptance - U.S. Region

A U.S. Merchant that accepts Visa Cards may choose Limited Acceptance.

A U.S. Merchant that accepts all Visa Cards, or a Limited Acceptance category of Visa Cards, must accept any valid Visa Card issued by a non-U.S. Issuer, as specified in the *Visa International Operating Regulations*.

ID#: 010410-010410-0008680

Limited Acceptance Notification Requirements - U.S. Region

A U.S. Acquirer must register with Visa and provide reporting on each of its Merchants that has selected Limited Acceptance.

ID#: 010410-010410-0005609

Limited Acceptance Merchant Signage - U.S. Region

A U.S. Acquirer must ensure that each of its Limited Acceptance Merchants is provided with Visa-approved signage representing the Limited Acceptance Category it has selected, in accordance with its Merchant Agreement. Specifications for appropriate signage are available from Visa.

ID#: 010410-010410-0005110

Card Acceptance Canada Region

Merchant Display of Marks and Acceptance Signage - Canada Region

Effective 20 February 2009, a Canada Acquirer must ensure that:

- Each of its Merchants that accepts all Visa Cards displays the appropriate Visa-Owned Marks to indicate which Cards it accepts for payment
- Where required by Visa, Visa Debit Acceptors display Visa-approved signage

Liability

As specified in the *Visa International Operating Regulations* , any liability under any theory or form of action whatsoever, in law or in equity, including, without limitation, contract or tort, including negligence, even if the responsible party has been notified of the possibility of such damages. The term also includes liability for infringement of others' intellectual property rights or any liability for Claims of third parties.

ID#: 010410-010410-0024779

Licensee

An entity licensed to participate in the Visa or Visa Electron Program that is neither a:

- Member
- Member or owner of a Group Member

ID#: 010410-010410-0024780

Limited Acceptance - U.S. Region

A term describing a Merchant's option to accept one category of Visa Cards and not another. Categories consist of:

- Visa Credit and Business Category
- Visa Debit Category

ID#: 010410-010410-0024784

Limited Acceptance Merchant - U.S. Region

A category of Merchant that accepts either, but not both, of the following:

- Visa Credit and Business Category Cards
- Visa Debit Category Cards

ID#: 010410-010410-0024785

Limited-Amount Terminal

See Unattended Acceptance Terminal and Cardholder-Activated Transaction Type A.

ID#: 010410-010410-0024781

Limited-Amount Terminal - U.S. Region

A Cardholder-Activated Terminal that has Data Capture-Only Capability, and accepts payment for items such as:

Attachment C

Addressing the Debit-Card Industry's Market Failure

James C. Miller III

Prepared for the Retail Industry Leaders Association

February 2011

REPORT OF JAMES C. MILLER III

A. Background and Expertise

1. I have been asked by the Retail Industry Leaders Association to offer my opinion regarding the Federal Reserve Board's ("Board's") proposed rules implementing the "Durbin Amendment" to the Dodd-Frank Wall Street Reform and Consumer Protection Act -- adding section 920 to the Electronic Fund Transfer Act ("EFTA Act") -- from the perspective of their appropriateness as a regulatory intervention in the market for electronic payments. In particular, I have focused on the appropriate policy response to collusive or otherwise parallel conduct by the major firms in an industry where there is asymmetry between the competitiveness of buyers and sellers.

2. As set out more fully in my *curriculum vitae* (Exhibit 1), this assessment is based on my extensive academic and governmental experience in the field of government regulation (and deregulation). After a career in university teaching and research, I served in the Reagan Administration as the first Administrator of the Office of Information and Regulatory Affairs at the Office of Management and Budget (1981), as Chairman of the Federal Trade Commission (1981-1985), and as Director of OMB and Member of the President's Cabinet (1985-1988). Presently, I serve on the boards of several mutual funds and corporations, such as Clean Energy Fuels Corp., as well as the Board of Governors of the U.S. Postal Service. I hold a Ph. D. in economics from the University of Virginia and am the author or co-author of over 100 articles in professional journals and nine books, including *Economic Regulation of Domestic Air Transport: Theory and*

Policy (Brookings Institution, 1974), *Reforming Regulation* (American Enterprise Institute, 1980), *The Economist as Reformer: Revamping the FTC, 1981-1985* (American Enterprise Institute, 1989), and *Monopoly Politics* (Hoover Institution, 1999).

B. The Debit Card Industry

The existence of market power

3. The major card networks have monopoly power over merchants. In today's marketplace, merchants have no rational choice but to accept debit cards when presented by their customers, since the use of debit cards is so large and growing. Of the over $7 trillion in consumer expenditures for goods and services in 2009, approximately $1.6 trillion was transacted with debit and prepaid cards (for comparison, $1.8 trillion was transacted with credit cards and $1.6 trillion with cash.)[1] Because of their dominance of the card market, Visa and MasterCard control the costs merchants pay to accept debit cards as a means of payment.

4. There are several reasons for this conclusion. First is the history of development of the two major networks. Both Visa and MasterCard were organized by large banks and controlled by them. As they grew, it became increasingly worthwhile for major banks to issue both networks' cards to their customers. And since the banks controlled both systems -- their representatives sat on the boards of both -- it was only natural that the two card networks would establish schedules of services and prices that are nearly identical. By 2009, Visa accounted for 61 percent of all debit-card transactions, MasterCard for 23

[1] *Nilson Report,* Issue 962 (December, 2010), pp. 1 and 10-11.

percent, and a handful of regional networks for the rest.[2] Merchants have little choice but to accept cards from at least one of these two giant networks, and for survival reasons they usually sign with both. Accordingly, the market for debit card transactions -- vigorously competing merchants on the one side and monopolistic card networks on the other -- is quite asymmetric.

5. It is my understanding that over time the two card networks have charged consistent and increasingly higher interchange fees to merchants, all of whom are captive and have no countervailing pressure available to apply. In short, while banks have faced competition in many lines of their businesses, they have had no difficulty in monopolizing the market for card acceptance.

6. Moreover, I understand that debit cards were initially provided by regional networks using PIN authentication and the processing infrastructure of ATM-networks. These networks charged either zero (at-par) interchange fees or paid interchange fees *to* merchants to compensate them for their investment in PIN pads. After 1990, Visa and MasterCard began to promote their "signature" debit cards, processed over their credit-card networks. Signature debit interchange fees were set at the much-higher rates paid for credit-card interchange. I also understand that, around 1990, Visa purchased Interlink, which was among the leading PIN debit networks in the United States, and began to increase its interchange fees. As Visa continued to drive up Interlink interchange rates, the competing PIN debit networks raised their rates to maintain levels of issuance under the pricing umbrella created by Visa. The result has been a convergence

[2] *Nilson Report,* Issue 961 (December, 2010). p. 10.

of PIN and signature debit rates. Thus, the level of interchange fees charged for Visa's and MasterCard's PIN products, and those of the regional PIN networks, followed an upwards path, despite little evidence of increasing costs in making such transactions.

7. Monopoly power is also evidenced by the prices established by the card networks. The pricing schedules of Visa and MasterCard show a pattern of what economists call "third degree price discrimination" -- which can take place only if there is monopoly power.[3] While the cost of a transaction hardly varies by type of merchant or size of a sale, the interchange fee does. Grocery stores, for example, typically pay a low base fee, whereas restaurants and airlines pay much higher interchange fees.[4] And the fee increases with the amount of the sale. It is easy to see that the card networks are establishing relatively low fees for merchants with relatively high (price-) elasticities of demand for payment cards, and higher fees for those with less elastic demands. The same is true with respect to size of sale: the larger the sale, the less elastic the demand. Again, in a truly competitive market, sellers are not able to divide the market and charge different prices to different consumers unrelated to differences in costs.

8. That this form of discriminatory (monopolistic) pricing is the norm was spelled out recently in Congressional testimony by Visa's General Counsel: "Products and services in this economy should be *fairly priced based on the value provided*, not some limited concept of cost, and certainly not on some

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[3] See, for example, D. Salvatore, Microeconomics: Theory and Applications (2003), p. 334.

[4] See, for example, Visa USA Interchange Reimbursement Fees (October 16, 2010), p. 2; and (Visa) Interlink Interchange Reimbursement Fees (October 16, 2010), p. 2.

artificially selected portion of those costs."[5] Again, in a competitive market, prices are related to costs, not to the benefits derived.

9. While debit-card networks establish very high, monopolistic fees for merchants, the issuing banks compete strongly for new card holders – which, of course, leads to more debit-card purchases and more interchange fee revenue. This competition for new card holders (or retention of current card holders) takes a peculiar form, however. The various issuing banks (in alliance with, and incentivized by, the card networks' schedule of charges) offer cards with extensive benefits. "Points" are the ubiquitous benefit -- a sort of currency that can be traded for travel, goods, and even redemptions in cash. I also understand that special favoritism in the form exclusive offers on goods is also common.

10. The very existence of this extensive non-price competition is itself an indication that the debit-card market is not fully competitive. If the banks and the card networks were not charging the merchants monopolistic rates, and instead were charging them truly competitive rates, the extent of such non-price competition for cardholders would be much less. That is, such supra-competitive margins, built into the current interchange fee schedules, lead to marketing efforts that tend to "compete away" those very margins.

The setting of monopolistic interchange fees

11. The cards networks' rules and procedures make clear that each card system is the contractual "hub" through which their interchange fees are set --

[5] Prepared Statement of Joshua R. Floum before the Subcommittee on Financial Institutions and Consumer Credit of the House Committee on Financial Services (February 17, 2011), p. 6; emphasis added.

nominally in the best interests of all participants in the payment system, but actually on behalf of their card issuers.

12. Indeed, Visa's General Counsel has advised the Board that interchange fees should *not* reflect the costs of any particular card issuer, because the networks set fees for all of their issuers. "We believe that this approach [implementing the rate model at the network level] is the most practical and efficient for a number of reasons, including *the fact that the payment card networks currently set the interchange rates for debit transactions over those networks. . . .*[and that]. . . *issuers do not in practice set interchange fees; rather, these fees are set by networks* and issuers accept transactions from different networks."[6]

13. In turn, once interchange fees are set, under the Visa and MasterCard rules – which are binding contracts between each network and its issuers and acquirers—the networks' members use those rates in their payment card transactions.[7]

14. Finally, the networks' "honor all cards" rules bind merchants to this result. Once a merchant decides to accept Visa or MasterCard debit cards, for example, it must accept all debit cards of that type bearing the network's logo. There is no need for each bank to negotiate with individual merchants to accept its debit

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[6] See letter from Joshua R. Floum to Louise Roseman, Director, Division of Reserve Bank Operations and Payment Systems, Federal Reserve Board (November 8, 2010), pp. 13 and 17; emphasis added.

[7] See, for example, Visa International Operating Regulations (Public Version, April 1, 2010), pp. 57 and 961-62; Visa, Inc. SEC Form 10-K (November 19, 2010), p. 13; and MasterCard Rules, Section 9.4 (October 29, 2010). The rules technically permit issuers and acquiring banks to enter into bilateral interchange arrangements, but as noted in paragraph 12, such bilateral arrangements have not occurred in practice.

cards. Thus, networks' current rules enable each debit-card-issuing bank to take advantage of the network's monopoly power to obtain excessive interchange fees.

15. Deposit accounts are not offered in isolation, but as a means of generating funds that enable banks to make loans -- which, in turn, provide interest revenue. For example, in the case of checks, the customer's bank absorbs *all* the cost of the transaction (except for fees that may be charged by the merchant’s bank for depositing a check). Banks have traditionally done so precisely because demand deposits enable the bank to make loans, on which the bank earns interest, and because the relationship opens opportunities for the bank to provide other (remunerative) services to the customer.

C. EFTA Act, Section 920

16. I have reviewed Section 920 of the EFTA Act, the Board's proposed rulemaking implementing that section,[8] and major submissions to the Board pursuant to that proceeding. Section 920(a) requires the Board to establish standards governing debit-card interchange fees. The statute defines those fees as “any fee established, charged, or received by a payment card network for the purpose of compensating an issuer for its involvement in an electronic debit transaction.”

17. The scope of price intervention required by the statute is narrow: it does not address prices charged by an acquiring bank for its role in processing the merchant’s debit-card transactions, nor does it restrict the fees that a card

[8] Federal Reserve Board, *Notice of Proposed Rulemaking,* 75 *Federal Register* (December, 28, 2010), pp. 88722 *et seq*.

network may charge acquiring and issuing banks for its role in processing such transactions (except to prevent evasion of the interchange fee standards). As I will discuss below, this limitation on the Board's regulatory power is appropriate, as such additional constraints are not needed to accomplish the objective of making the card market more competitive. By its terms, the statute does not address independent action by a debit-card issuer to charge transactions fees directly to merchants (possibly through the merchant's acquiring bank) when one of the issuer's cardholders purchases goods or services from the merchant, leaving such transactions to the ordinary forces of competition. This competition could take many forms and would be based on rivalry among individual card issuers (without reliance on networks or honor-all-cards rules) to gain acceptance of that card as a payment mechanism at individual merchants. There would be no need for regulation to limit fees that might be charged as a result of interaction between individual merchants and individual issuers, as long as those fees are transparent and are subject to the discipline of market competition. Thus, in such a competitive environment, there would be no need for regulators to specify what costs such fees might or might not recover.

18. In contrast, section 920(a) addresses fees collected by debit-card issuers when those fees are charged by or through a network, thus enabling an issuer to utilize the network's market power. In this regard, while subsection 920(b)(2) gives merchants the right to provide discounts and other incentives for differing forms of payment -- cash, checks, debit cards, or credit cards -- it is my understanding that the "honor-all-cards" requirements of Visa and MasterCard,

for example, will continue to require non-discriminatory acceptance of cards from every issuer of the relevant type of card offered by the card network.

19. Section 920(a) simply ensures that when debit-card issuers rely on card networks' market position to obtain compensation from merchants as a result of card acceptance, the level of those fees are not set at a supracompetitive level but are “reasonable and proportional” to the card issuers' incremental costs for authorization, clearance, and settlement of those transactions.

20. Importantly, Section 920(b)(1) sets in motion potential longer-term structural reform by (a) ensuring that card issuers offer multiple networks for the routing of debit-card transactions for each type of card authorization method, and (b) giving each merchant the ability to direct and/or prioritize the choice of network to be used in a debit-card transaction. To the extent that these provisions are implemented in an effective and timely manner, networks may, arguably for the first time, compete on price for merchants’ business.

D. An Appropriate Response to Market Failure

21. Throughout my career I have been a consistent skeptic about the ability of government intervention to improve the functioning of the marketplace. But sometimes a free market does not – or for any number of reasons cannot – correct a divergence from the competitive norm. The persistence of such divergences over time, uncorrected by unencumbered economic forces, is among the few scenarios in which I believe there is reason for government to examine and possibly correct the underlying cause.

22. In the case of interchange fees -- and debit interchange fees in particular -- the case for regulatory intervention is strong. This is truly a case of market failure: networks with monopoly power over merchants are setting prices for merchants' access to their networks on behalf of their (frequently overlapping) card-issuing members, utilizing agreements in which every bank participating in those card networks agrees to charge merchants exactly the same interchange fees, regardless of who issued the card. Thus, regulatory intervention is warranted to provide the catalyst to return this market to the competitive norm and thus increase the market's overall efficiency.

23. The pricing solution chosen by section 920(a) and the Board's proposed interchange fee standard approximates the pricing outcome that would obtain in a fully competitive market – that is, prices based on costs, not demand. Further, the relevant costs identified in the statute and incorporated by the Board in its notice are those costs that I understand are directly incurred in processing each transaction: the costs of authorization, clearance, and settlement.[9]

24. Most significantly, section 920(a) requires regulation only of debit-card interchange fees established by payment card networks. Issuers are free to charge fees for card acceptance negotiated directly with merchants as long as the imposition of these fees is not characterized by market failure, including network honor-all-cards rules. Thus, the proposed regulations appear to be

[9] See Federal Reserve Board *Notice, ibid.*, pp. 88722 and 88735. I realize that the Board is undertaking a separate rulemaking regarding an adjustment for issuer-specific fraud prevention costs using the statutory considerations for such an adjustment, but that is beyond the scope of my report.

consistent with both the limited mandate of section 920 and the policy prescriptions embodied in that provision.

25. It is also notable that the regulatory scope of Section 920 is narrow. It does not regulate any fees that a debit issuer imposes individually and directly (rather than through a network) on merchants or other parties. There should be no market failure associated with such issuer-specific fees as long as they are subject to the discipline of market competition. It is appropriate, therefore, that Section 920 was drafted to leave such fees unregulated under those conditions.

26. Finally, the rules proposed by the Board to implement subsection 920(b)(1) to provide multiple network options on a card and to mandate merchant selection of network routings, promise a longer-term marketplace solution. If implemented to require at least two network choices for each PIN and signature method of authorization, there should be a meaningful increase in competition among issuers. By choosing the lower-cost option, merchants could force issuers and card networks to reduce their interchange and network fees -- perhaps making the regulation of fees no longer necessary, once competition were firmly in place.

EXHIBIT 1

James C. Miller III

Curriculum Vitae
January 2011

Education and Professional Activities

Degrees:	Ph.D. (Economics), University of Virginia, 1969
	B.B.A. (Economics), University of Georgia, 1964
Current Positions:	Senior Advisor, Husch Blackwell Sanders, LLC, since June, 2006
	Senior Fellow (by courtesy), Hoover Institution (Stanford University), since December 1988
	Distinguished Fellow, Center for Study of Public Choice, George Mason University, since October 1988
	Member, Board of Governors, U.S. Postal Service, since April 2003 (elected chairman 2005, 2006, and 2007))
	Member, Board of Directors, Washington Mutual Investors Fund, since October 1992 (Member of Advisory Board, November 1989 – October 1992)
	Member, Board Directors, The Tax Exempt Fund of Maryland, since April 2000
	Member, Board of Directors, The Tax Exempt Fund of Virginia, since April 2000
	Member, Board of Directors, The J.P. Morgan Value Opportunities Fund, since December 2001
	Member, Board of Directors, Clean Energy Fuels, Corp., since May 2006
	Member, Board of Directors, Americans for Prosperity, since February 2004

Member, Board of Directors-Emeritus (previously Co-Chairman or Counselor), The Tax Foundation, since October 1989

Chairman of the Executive Committee, International Tax and Investment Center, since September 2009

Previous Positions: 2010

Member, Board of Directors -Emeritus (previously Member of Board), Progress & Freedom Foundation, April 1994 – March

Chairman of an Independent Commission to address the fiscal challenges of Cayman Island Government; established by Cayman Islands Government; October 2009 – February 2010

Chairman (or Chairman Emeritus), The CapAnalysis Group (of Howrey, L.L.P.), April 2002 – January 2006

Chairman (or Chiarman Emeritus), The CapAnalysis Group)of Howrey, L.L.P.), April 2002 – January 2006

Member, Board of Directors, Independence Air (formerly Atlantic Coast Airlines d.b.a. "United Express" and “Delta Connection”), March 1995 – January 2006

Member, Board of Visitors, George Mason University, June 1998 – June 2002

Distinguished Fellow, Mercatus Center, George Mason University, August 1997 – April 2003

Director, LECG – Economics-Finance, November 2002 – April 2003

Senior Advisor, Hagler Bailly, January 2000 – November 2002.

Member, Board of Directors and/or Counselor), Citizens for a Sound Economy, January 1989 – April 2003

Member, Board of Directors, The Tax Foundation, October 1989 – April 2003

Member, Board of Visitors, U.S. Air Force Academy, November 1988 – November 1990.

Director, U.S. Office of Management and Budget, Member of President's Cabinet, and Member of National Security Council, October 1985 – October 1988

Vice Chairman, Administrative Conference of the United States, December 1987 – October 1988 (Member of Council, November 1981 – December 1987)

Chairman, U.S. Federal Trade Commission, September 1981 – October 1985

Administrator, Office of Information and Regulatory Affairs, U.S. Office of Management and Budget; and Executive Director, Presidential Task Force on Regulatory Relief, January 1981 – September 1981

Resident Scholar, Center for the Study of Government Regulation, The American Enterprise Institute for Public Policy Research, January 1977 – January 1988; Co-Director of the Center, March 1977 – January 1981; Member, Board of Editors, Regulation, July 1977 – January 1981; and Member, Board of Editorial Advisors, The AEI Economist, September 1977 – January 1981

Consultant, National Science Foundation, July 1977 – January 1981

Lecturer (in Economics), George Washington University, September 1971 – May 1972, September 1975 – May 1976, and September 1978 – December 1980

Assistant Director (for Government Operations and Research), U.S. Council on Wage and Price Stability, October 1975 – January 1977

Adjunct Scholar, The American Enterprise Institute for Public Policy Research, May 1975 – January 1977

Senior Staff Economist, U.S. Council of Economic Advisers, July 1974 – October 1975

Associate Professor of Economics, Texas A&M University, August 1972 – May 1974

Consultant, U.S. Department of Transportation, March 1972 – July 1974

Consultant, National Bureau of Standards, January 1974 – June 1974

Research Associate, The American Enterprise Institute for Public Policy Research, May 1972 – July 1972

	Associate Staff, The Brookings Institution, August 1972 – May 1974
	Senior Staff Economist, U.S. Department of Transportation, December 1969 – February 1972
	Assistant Professor of Economics, Georgia State University, September 1968 – December 1969
Affiliations:	American Economic Association
	Public Choice Society
	Southern Economic Association (Vice President, 1990 – 1991; Member of Executive Committee, 1980 – 1982)

Selected Publications and Presentations

Books:	Monopoly Politics (Stanford: Hoover Institution Press, 1999)
	Fix the U.S. Budget!: Urgings of an "Abominable No-Man" (Stanford: Hoover Institution Press, 1994)
	The Economist as Reformer: Revamping the FTC, 1981-1985 (Washington: American Enterprise Institute, 1989)
	The Federal Trade Commission: The Political Economy of Regulation (co-editor and contributor, with Robert J. Mackay and Bruce Yandle; Stanford: Hoover Institution Press, 1987)
	Reforming Regulation (co-editor and contributor, with Timothy B. Clark and Marvin H. Kosters; Washington: American Enterprise Institute, 1980)
	Benefit-Cost Analyses of Social Regulation: Case Studies from the Council on Wage and Price Stability (co-editor with Bruce Yandle; Washington: American Enterprise Institute, 1979)
	Perspectives on Federal Transportation Policy (editor and contributor; Washington: American Enterprise Institute, 1975)

Economic Regulation of Domestic Air Transport: Theory and Policy (with George W. Douglas; Washington: Brookings Institution, 1974)

Why the Draft?: The Case for a Volunteer Army (editor and contributor; Baltimore: Penguin Books, 1968)

Monographs:

The Economics of the Military Draft (with Ryan C. Amacher et al.; Morristown: General Learning Press, 1973)

Transportation Legislation (published anonymously; Washington: American Enterprise Institute, 1972)

Articles:

"Public Choice Theory and Antitrust Policy: Comment," Public Choice (March 2010).

"Economics and the All-Volunteer Military Force" (and with Beth J. Asch and John T. Warner), in John Siegfried, ed., Better Living Through Economics (Cambridge: Harvard University Press, 2010)

"An Event Analysis Study of the Economic Implications of the FCC's UNE Decision: Backdrop for Current Network Sharing Proposals" (with Jeffrey A. Eisenach and Paul S. Lowengrub), 17 Commonlaw Conspectus 33 (2008)

"Monopoly Politics and Its Unsurprising Effects," in Roger Koppl, ed., Money and Markets : Essays in Honor of Leland B. Yeager (London : Routledge, 2006)

"The Tyranny of Budget Forecasts" (with J.D. Foster), Journal of Economic Perspectives (Summer 2000)

"Incumbents' Advantage," George Mason University, Working Papers in Economics (December, 1997)

"Suggestions for a Leaner, Meaner Budget," Jobs & Capital (Spring 1995)

"Budget Process and Spending Growth" (with Mark Crain), William and Mary Law Review (Spring 1990)

"Independent Agencies -- Independent from Whom?," Administrative Law Review (Fall 1989)

"A Reflection on the Independence of Independent Agencies," Duke Law Journal (1988)

"It's Time to Free the Mails," Cato Journal (Spring/Summer 1988)

"Spending and Deficits" (with an introduction by Robert D. Tollison), G. Warren Nutter Lecture in Political Economy, The American Enterprise Institute for Public Policy Research, 1987; reprinted in Thomas Jefferson Center Foundation, Ideas, Their Origins, and Their Consequences (Washington: American Enterprise Institute, 1988)

"Predation: The Changing View in Economics and the Law" (with Paul Pautler), Journal of Law and Economics (May 1985)

"Comments on Baumol and Ordover," Journal of Law and Economics (May 1985)

"Industrial Policy: Reindustrialization through Competition or Coordinated Action?" (with Thomas F. Walton, William E. Kovacic, and Jeremy A. Rabkin), Yale Journal on Regulation (1984)

"The Case Against Industrial Policy," Cato Journal (Fall 1984)

"Report from Official Washington," Antitrust Law Journal (1984)

"Reindustrialization Policy: Atari Mercantilism?," in Richard B. McKenzie (ed.), Plant Closings: Public or Private Choice? (revised edition; Washington: CATO Institute, 1984)

"Resale Price Maintenance: An Analytical Framework," Regulation (January/February 1984)

"Is Organized Labor Rational in Supporting OSHA?," Southern Economic Journal (January 1984)

"A Note on Centralized Regulatory Review" (with William F. Shughart II and Robert D. Tollison), Public Choice (January 1984)

"Comparative Data on Life-Threatening Risks," Toxic Substances Journal (Summer 1983)

"Report from Official Washington," Antitrust Law Journal (1983)

"Occupational Exposure to Acrylonitrile: A Benefit/Cost Analysis," Toxic Substances Journal (Winter, 1982/1983)

"Report from Official Washington," Antitrust Law Journal (1982)

"Regulatory Relief under President Reagan," Jurimetric Journal (Summer 1982)

"The (Nader-) Green-Waitzman Report," Toxic Substances Journal (Winter 1980/1981)

"Has the 1970 Act Been Fair to Mailers?" (with Roger Sherman), in Roger Sherman (ed.), Perspectives on Postal Service Issues (Washington: American Enterprise Institute, 1980)

"Collective Ratemaking Reconsidered: A Rebuttal," Transportation Law Journal (1980)

"Regulation and the Prospect of Reform," in Charles F. Phillips, Jr. (ed.), Regulation, Competition and Deregulation -- an Economic Grab Bag (Lexington: Washington and Lee University, 1979)

"Airline Market Shares vs. Capacity Shares and the Possibility of Short-Run Loss Equilibria," Research in Law and Economics (1979)

"An Economic Analysis of Airline Fare Deregulation: The Civil Aeronautics Board's Proposal," Transportation Law Journal (1978)

"Regulators and Experts: A Modest Proposal," Regulation (November/December 1977)

"Regulatory Reform: Some Problems and Approaches," American Enterprise Institute Reprint No. 72 (August 1977)

"Lessons of the Economic Impact Statement Program," Regulation (July/August 1977)

"The New 'Social Regulation'" (with William Lilley III), Public Interest (Spring 1977); reprinted extensively

"Effects of the Administration's Proposed Aviation Act of 1975 on Air Carrier Finances," Transportation Journal (Spring 1976); reprinted in Paul W. MacAvoy and John W. Snow (eds.), Regulation of Passenger Fares and Competition Among the Airlines (Washington: American Enterprise Institute, 1977)

"Environmental Protection: The Need to Consider Costs and Benefits" (with Robert L. Greene), Highway Users Quarterly (1976)

"A Perspective on Airline Regulatory Reform," Journal of Air Law and Commerce (Autumn 1975)

"Rates of Publication Per Faculty Member in Forty-five 'Rated' Economics Departments" (with Robert D. Tollison), Economic Inquiry (March 1975)

"Government Regulation" (principal author), Chapter 5 in Economic Report of the President, 1975

"Quality Competition, Industry Equilibrium, and Efficiency in the Price-Constrained Airline Market" (with George W. Douglas), American Economic Review (September 1974)

"The CAB's Domestic Passenger Fare Investigation" (with George W. Douglas), Bell Journal of Economics and Management Science (Spring, 1974); reprinted by the Brookings Institution (Technical Series Reprint T-008

"The Optimal Pricing of Freight in Combination Aircraft," Journal of Transport Economics and Policy (September 1973)

“A Time of Day Model for Aircraft Scheduling," Transportation Science (August 1972)

"Marginal Revenue and Pigouvian Second Degree Price Discrimination" (with Richard A. Bilas and Fred A. Massey), Metroeconomica (August 1971)

"The Implicit Tax on Reluctant Military Recruits" (with Robert D. Tollison), Social Science Quarterly (March 1971)

"A Note on Profits, Entry, and Scale of Plant in the Purely Competitive Model," Revista Internazionale de Scienze Economiche e Commerciali (February 1971)

"Pigou's Three Degrees of Price Discrimination" (with Richard A. Bilas), Revista Internazionale de Scienze Economiche e Commerciali (February 1971)

"A Program for Direct and Proxy Voting in the Legislative Process," Public Choice (Fall 1969); reprinted in Ryan C. Amacher, Robert D. Tollison, and Thomas D. Willett (eds.), The Economic Approach to Public Policy: Selected Readings (Ithaca: Cornell University Press, 1976)

"Short-run Solutions to Airport Congestion," Atlanta Economic Review (October 1969); reprinted in Cambell R. McConnell (ed.), Economic Issues: A Book of Readings (4th ed.; McGraw-Hill Book Company, 1972)

"A Paradox on Profits and Factor Prices: Comment," American Economic Review (September 1968)

"Marginal Criteria and Draft Deferment Policy" (with Robert D. Tollison and Thomas D. Willett), Quarterly Review of Economics and Business (Summer 1968)

"An Army of Volunteers," Forensic Quarterly (May 1968)

"An Aircraft Routing Model for the Airline Firm," American Economist (Spring 1968)

"A Critique of Joan Robinson's Economic Philosophy," Western Politica (Autumn 1967)

Presentations before Regulatory Agencies:

Co-authorship of and responsibility for approximately 60 Council on Wage and Price Stability filings and/or testimony before U.S. Government agencies, including the U.S. Departments of Agriculture, Commerce, Health, Education and Welfare, Housing and Urban Development, Interior, and Transportation; the Civil Aeronautics Board, the Coast Guard, the Consumer Product Safety Commission, the Environmental Protection Agency, the Federal Aviation Administration, the Federal Deposit Insurance Corporation, the Federal Energy Administration, the Federal Power Commission, the Federal Reserve Board, the Federal Trade Commission, the Food and Drug Administration, the International Trade Commission, the Interstate Commerce Commission, the National Highway Traffic Safety Commission, the Occupational Safety and Health Administration, the Postal Rate Commission, and the Securities and Exchange Commission (October 1975 January 1977)

Other testimony before the Department of Energy, the Civil Aeronautics Board, the Interstate Commerce Commission, the

Postal Rate Commission, the National Commission for the Review of Antitrust Laws and Procedures, and the California and Pennsylvania public utilities commissions (1970-1979)

Presentations before Committees of the U.S. House of Representatives:	U.S. House of Representatives Committee on Appropriations; U.S. House of Representatives Committee on the Budget; U.S. House of Representatives Committee on the Judiciary; U.S. House of Representatives Committee on Public Works and Transportation; U.S. House of Representatives Republican Study Committee; U.S. House of Representatives Rules Committee; U.S. House of Representatives Subcommittee on Administrative Law & Governmental Relations, Committee on the Judiciary; U.S. House of Representatives Subcommittee on Aviation, Committee on Public Works and Transportation; U.S. House of Representatives Subcommittee on Commerce, Consumer and Monetary Affairs, Committee on Government Operations; U.S. House of Representatives Subcommittee on Commerce, Justice, State, the Judiciary and Related Agencies, Committee on Appropriations; U.S. House of Representatives Subcommittee on Commerce, Transportation and Tourism, Committee on Energy & Commerce; U.S. House of Representatives Subcommittee on Consumer Protection and Finance, Committee on Oversight and Investigations; U.S. House of Representatives Subcommittee on Economic Stabilization, Committee on Banking, Finance and Urban Affairs; U.S. House of Representatives Subcommittee on Legislation and National Security, Committee on Government Operations; U.S. House of Representatives Subcommittee on Monopolies & Commercial Law, Committee on Judiciary; U.S. House of Representatives Subcommittee on Oversight and Investigations, Committee on Energy and Commerce; U.S. House of Representatives Subcommittee on Science, Research and Technology, Committee on Science and Technology; U.S. House of Representatives Subcommittee on Small Business Problems, Committee on Small Business; U.S. House of Representatives Subcommittee on Transportation and Commerce, Committee on Interstate and Foreign Commerce; and U.S. House of Representatives Subcommittee on Treasury, Postal Service and General Government Appropriations
Presentations before Committees of the	U.S. Senate Committee on Appropriations; U.S. Senate Committee on the Budget; U.S. Senate Committee on Commerce, Science, and Transportation; U.S. Senate Subcommittee on the Constitution, Committee on the Judiciary; U.S. Senate Committee

U.S. Senate:	on Governmental Affairs; U.S. Senate Committee on the Judiciary; U.S. Senate Committee on Small Business; U.S. Senate Subcommittee on Administrative Practice and Procedure, Committee on the Judiciary; U.S. Senate Subcommittee on Antitrust and Monopoly, Committee on the Judiciary; U.S. Senate Subcommittee on Alcoholism and Drug Abuse, Committee on Labor and Human Resources; U.S. Senate Subcommittee on Aviation, Committee on Commerce, Science and Transportation; U.S. Senate Subcommittee on Commerce, Justice, State and Judiciary, Committee on Appropriations; U.S. Senate Subcommittee on Consumer, Committee on Commerce, Science and Transportation; U.S. Senate Subcommittee on Federal Expenditures, Research and Rules, Committee on Government Affairs; U.S. Senate Subcommittee on Intergovernmental Relations, Committee on Governmental Affairs; U.S. Senate Subcommittee on Productivity and Competition, Committee on Small Business; U.S. Senate Subcommittee on Regulatory Reform, Committee on the Judiciary; U.S. Senate Subcommittee on Treasury, Postal Service, and General Government Appropriations; and U.S. Senate Special Committee on Aging
Presentations before Joint Congressional Committees:	U.S. Joint Economic Comm. Subcommittee on Economic Goals and Intergovernmental Policy, U.S. Joint Economic Committee; Subcommittee on Trade, Productivity and Economic Growth, U.S. Joint Economic Committee; Congressional Grace Caucus; and Motor Carrier Ratemaking Study Commission
Expert Reports:	Various