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[Via *regs.comments@federalreserve.gov*](mailto:regs.comments@federalreserve.gov)

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

RE: Debit Card Interchange Fees and Routing, Docket No. R-1748, RIN 7100-AG15

Ladies and Gentlemen:

Mastercard International Incorporated (“Mastercard”) submits this comment letter to the Board of Governors of the Federal Reserve System (“Board”) in response to the Board’s request for comment on a proposal to amend Regulation II (the “Proposal”).¹ Mastercard appreciates the opportunity to provide input on the Proposal.

Regulation II implements 15 U.S.C. § 1693o-2 (the “Durbin Amendment”). Among its other requirements, the Durbin Amendment directs the Board to prescribe regulations that require depository institutions that issue debit cards, including prepaid cards, (“Issuers”) to enable at least two unaffiliated payment card networks (“Networks”) on which an electronic debit transaction may be processed. As discussed below, the Proposal imposes obligations on Issuers that exceed the direction of Congress and would harm Issuers and consumers. The Proposal fails to follow the line drawn by the Durbin Amendment between the responsibility of Issuers and Networks to provide merchants with a routing choice and the necessity of merchants to modernize in basic ways to avail themselves of that choice. The Proposal also fails to recognize that e-wallet providers, not Issuers, control the contents of e-wallets, and that Issuers cannot be made responsible for the acts of e-wallet providers.

We comment below on the Board’s approach in the Proposal to card-not-present (“CNP”) transactions and the Board’s proposed treatment of “information stored within an e-wallet . . .” as a means of access, and we recommend changes to the Proposal to address our concerns.

CNP Transactions

The Durbin Amendment requires the Board to:

prescribe regulations providing that an issuer or payment card network shall not directly or through any agent, processor, or licensed member of a payment card network, by contract, requirement, condition, penalty, or otherwise, restrict the number of payment card networks on which an electronic debit transaction may be processed to (i) 1 such network; or (ii) 2 or more such networks which are

¹ 91 *Fed. Reg.* 26,189 (May 13, 2021).

owned, controlled, or otherwise operated by (I) affiliated persons; or (II) networks affiliated with such issuer.²

The Board fulfilled its statutory obligation by including in Regulation II a provision that prohibits an Issuer or Network from restricting the number of Networks on which an electronic debit transaction may be processed “to less than two unaffiliated networks.”³ The Board explained in Regulation II that an Issuer complies with the two-Network requirement only if the Networks it enables do not restrict their operation to a “limited geographic area, specific merchant, or particular type of merchant or transaction” and have taken reasonably designed steps to handle the volume of expected transactions from the Issuer.⁴

The Proposal would revise Regulation II, in pertinent part, so that an Issuer complies with the two-Network requirement only if the Issuer enables at least two unaffiliated Networks on which an electronic debit transaction may be processed “for every geographic area, specific merchant, particular type of merchant, and particular type of transaction for which the issuer’s debit card can be used.”⁵ The Proposal would revise the Official Board Commentary on Regulation II (the “Commentary”) by identifying CNP transactions as a particular type of transaction.⁶

In the Supplementary Information to the Proposal, the Board describes the CNP issue that it intends to address with this proposed change and explains how the proposed change provides the solution. However, the Board’s description is based on misleading information provided to the Board and consequently the Board’s proposed solution is flawed.

The Board asserts that “merchants are often not able to choose from at least two unaffiliated networks when routing card-not-present transactions.”⁷ The Board concludes this based on (1) information from “individual merchants, merchant trade associations, and representatives of single-message networks,” and (2) inferences drawn from data showing that few CNP transactions are routed over a single-message Network despite that most debit cards are enabled with unaffiliated dual-message and single-message Networks.⁸ However, we know from experience that Issuers always enable two unaffiliated Network on their cards.

To resolve this purported issue, the Board proposes the changes to Regulation II and the Commentary described above. The meaning of the changes is not clear without the context

² 15 U.S.C. § 1693o-2(b)(1)(A).

³ 12 C.F.R. § 235.7(a)(1).

⁴ 12 C.F.R. § 235.7(a)(2).

⁵ 91 *Fed. Reg.* at 26,194.

⁶ *Id.*

⁷ *Id.* at 26,190.

⁸ *Id.* at 26,191.

provided by the Board in the Supplementary Information. In the Supplementary Information, the Board implies that an Issuer would not be deemed to have enabled a single-message network for a CNP transaction unless the Issuer enabled the PINless PIN service of the single-message network. The Board does this through a series of statements that convey this point without expressing it directly: (a) “methods of PIN authentication for card-not-present transactions, such as PIN entry in an online setting, were not well-established” in 2011; (b) “most single-message networks are now capable of processing card-not-present transactions [through PINless PIN services];” (c) “despite the widespread adoption of these innovations [i.e., PINless PIN services], the volume of card-not-present transactions processed over single-message networks remains low;” (d) “some issuers do not make single-message networks *available to process card-not-present transactions* on any of their cards;” and (e) “the Board views these practices by issuers with respect to card-not-present transactions as inconsistent with Regulation II.”⁹ To our knowledge, all Issuers enable two Networks to process all of their debit card transactions, without exception. Thus, we can only infer from the Board’s discussion in the Supplementary Information that the Board means that a single-message Network is not “available to process card-not-present transactions” unless an Issuer is enrolled in the single-message Network’s PINless PIN service.

This characterization of the state of CNP transactions is not accurate. Issuers that enable unaffiliated dual-message and single-message Networks on their debit cards provide merchants a routing choice in CNP transactions *even when Issuers do not participate in the PINless PIN service of the enabled single-message Network*. In the Supplementary Information, the Board reasons backwards from the fact that merchants mostly do not route CNP transactions over single-message Networks to a conclusion that Issuers must not be enabling single-message Networks for CNP transactions in a manner that would give merchants a routing choice.

But this reasoning is flawed. It assumes that merchants are incapable of accessing single-message Networks for CNP transactions and then concludes that this must be because Issuers have not enabled the PINless PIN services of single-message networks. Only one sentence in the Proposal mentions another possible explanation, but dismisses it. In a footnote, the Board states that “[t]echnologies have also been developed to support PIN entry in different transaction environments, such as online purchases. However, the industry has not widely adopted those technologies for PIN entry.”¹⁰ The industry to which the Board refers is the *merchant* industry, and the participants in that industry have been making a conscious decision not to adopt technologies for PIN entry in CNP transactions.

We know this because PIN technology for CNP transactions has existed since at least 2008. A provider of the technology, Acculynk, brought this to the Board’s attention in a

⁹ *Id.* at 26,191. See also Memorandum to Board from Board Staff, April 30, 2021, p. 4 “Because single-message networks primarily processed PIN-authenticated transactions, this technological limitation posed an impediment to the use of those networks for card-not-present transactions. This difficulty, along with the industry practice of enabling only one dual-message network on each card, meant that card-not present transactions could often only be processed on that one dual-message network.”

¹⁰ *Id.* at 26,191 (n. 17).

comment letter submitted to the Board in 2011 during the public comment period for Regulation II:

The technology for encrypting PINs with software has been in the marketplace for more than [a] decade with predecessor companies; since acquiring this technology in 2008, Acculynk has leveraged this experience into a quickly-growing alternative to signature-debit for purchases over the Internet. . . . PIN-debit works very well online, and can work equally well for mobile payments.¹¹

The original appeal to merchants of PIN technology for CNP transactions was that it was a way to lower card acceptance costs. That appeal diminished after Regulation II lowered card acceptance costs by capping interchange on signature and PIN debit transactions.¹² However, the technology still exists and still is viable. Thus, merchants have not widely adopted PIN entry technology for CNP transactions as a business decision, not because merchants are incapable of doing so. Furthermore, it is concerning that the largest merchants in the country, which are technologically savvy and quite capable of adopting PIN entry technology for CNP transactions, have been lobbying the Board for the Proposal.¹³ These merchants, it seems, have determined that it is more cost effective to advocate for Issuer adoption of PINless PIN services than to adopt PIN entry technology for CNP transactions. While this may be a shrewd business strategy for the merchant community, it is a step backwards for cardholder security and the Durbin Amendment does not direct the Board to execute on this strategy.

Unfortunately, we have witnessed this all before. The merchants that supplied the Board with an Issuer-focused explanation for their failure to route CNP transactions over single-message Networks are in the exact same position as the merchants who complained in 2011 that they were denied a routing choice because their manual card swipe machines (a.k.a. knuckle busters) were incapable of receiving a PIN. The Board should adopt the same position now that it adopted then. In 2011, the Board did not require Issuers to accommodate merchants that decided not to install card reader terminals. The Board understood that the Durbin Amendment only requires Issuers to enable two unaffiliated Networks on their debit cards and does not require Issuers to accommodate merchants that decide not to use available technologies to access the Networks enabled by the Issuer.

¹¹ Letter to Jennifer L. Johnson, Secretary, Board, from Acculynk, LLC, February 22, 2011.

¹² See *E-Commerce: A Tangled Web for PIN Debit*, Digital Transaction, February 1, 2013 (“We were all set to roll out programs with several of the top PIN-debit networks, and then Durbin came along. A lot of the merchants that had been interested in PIN debit to lower their transaction costs started to take a second look and they put their programs on hold,” says Ralph Bianco, chief operating officer for Plantation, Fla.-based Adaptive Payments Inc., a company with a unique system that combines online purchases with PIN entry on mobile phones.”)

¹³ Record of Meeting Between Staff of the Federal Reserve Board and Representatives of PIN Debit Networks, Merchants, Merchant Trade Groups, and Counsel (June 11, 2019) (participants included Walmart and Target); Record of Meeting Between Staff of the Federal Reserve Board and Representatives of Merchants and Merchant Trade Associations (September 23, 2020) (participants included Best Buy, Floor & Décor, Foot Locker, The Home Depot, Kroger, Lowes, Walgreens and Walmart).

In reaching its conclusion, the Board explained:

To the extent a merchant has chosen not to accept PIN debit, the merchant, and not the issuer or the payment card network, has restricted the available choices for routing an electronic debit transaction under Alternative A. Similarly, where a consumer selects signature or PIN debit as the method of payment, the consumer, and not the issuer or the payment card network, has restricted the available routing choices.¹⁴

The Board's explanation then is equally applicable now. If a merchant has chosen not to adopt PIN-acceptance technology for a CNP transaction because of the costs associated with doing so or because of the belief that cardholders will not want to use a PIN for a CNP transaction or for some other reason, "the merchant, and not the issuer or the payment card network, has restricted the available choices for routing an electronic debit transaction."¹⁵ The Durbin Amendment does not require Issuers to subsidize the cost of merchants enabling technology that is necessary to avail themselves of the Network routing choice. This is no less true in the case of PIN-acceptance technology for CNP transactions as it is in the case of electronic terminal technology for in-person transactions.

The manner in which the Board ultimately determines to address the CNP issue is of critical importance to Issuers. It is not only that the Durbin Amendment does not direct the Board to force Issuers to accommodate merchants. It is also that the Proposal will impose significant costs on Issuers. PINless PIN services allow Issuers to authorize an electronic debit transaction through a single-message Network without the consumer having to enter a PIN, which is the key anti-fraud protection deployed by single-message Networks. PINless PIN services by single-message networks strip away this protection, making PINless PIN services more expensive for Issuers and less safe for consumers than traditional PIN services.

Ironically, the Board characterizes PINless PIN as an innovation, but it is the exact opposite. Rather, it is essentially the degradation of a technology in an effort to meet the desires of merchants. While merchants tend to characterize the adoption of PINless PIN services of single-message Networks by Issuers as a no-cost way for Issuers to make it easy for merchants to route transactions to single-message Networks, the cost to Issuers will be substantial in the form of higher fraud losses, costs associated with Network dispute resolution processes (as there are likely to be many transaction disputes associated with PINless PIN transactions) and Network integration costs. Unsurprisingly, small Issuers will be the most significantly impacted because they generally have fewer resources to bear the costs of PINless PIN services than large Issuers. After adoption of Regulation II, many banks stopped offering free checking, to the detriment of consumers, in order to mitigate the loss of interchange revenue.¹⁶ If the Board finalizes the

¹⁴ 76 Fed. Reg. 43,394, 43,448 (July 20, 2011).

¹⁵ *Id.*

¹⁶ "The Impact of Debit Card Regulation on Checking Account Fees," by Rick Sullivan, Federal Reserve Bank of Kansas City, published in *Economic Review* (Fourth Quarter (2013)) ("In 2010, when Congress authorized the Federal Reserve to cap the fees paid to banks for debit card transactions, some news reports predicted the banks might react by increasing checking account fees. The cap on debit card fees reduced revenue significantly for some

Proposal as drafted, we expect that consumers will be harmed again because banks, particularly smaller banks, will eliminate services on which consumers rely in order to mitigate the increase in costs that will result from the Board's action. Also, we expect that some debit card programs that operate on particularly thin margins, such as government benefits programs, may be imperiled by the increased costs Issuers will bear if required to use the PINless PIN services of single-message Networks.

If the Board adopts a final rule that requires Issuers to enable two unaffiliated Networks for every "particular type of transaction for which the issuer's debit card can be used," then the Board also should clarify in the final rule that an Issuer meets this standard when the Issuer contracts with two unaffiliated Networks and each Network uses a cardholder authentication technology that merchants are capable of adopting. Such technologies, of course, include PIN technology and signature technology.¹⁷ The Board should not adopt a final rule that requires an Issuer to use the PINless PIN services of a single-message network it has enabled on its debit cards.

Means of Access

The Board proposes to revise the Commentary discussion of form factors. But the proposed changes drastically expand the scope of Issuers' responsibility, requiring Issuers to be responsible for actions of e-wallet providers outside of Issuers' control.

Currently, the form factor paragraph explains that the two-Network requirement applies to all debit cards of an Issuer "regardless of whether the debit card *is issued* in card form."¹⁸ It goes on to say that this requirement "applies to any supplemental device, such as a fob or token, or chip or application in a mobile phone, that *is issued* in connection with a plastic card, even if that plastic card fully complies with the rule."¹⁹ The Commentary also notes that an example of a practice that would inhibit a merchant's routing choice is "requiring a specific payment card network based on the type of access device *provided to the cardholder by the issuer.*"²⁰ The above-quoted language refers to debit cards and access devices issued or provided by an Issuer. Limiting the Commentary in this way is logical because debit cards and access devices that are issued or provided by an Issuer are within the control of Issuer. Also, this approach is consistent

banks, and the concern was that they might seek to offset their losses by raising more revenue from checking accounts. In fact, in recent years, many of the large banks bound by the new debit card regulations have raised their checking account fees.")

¹⁷ Our comment also is relevant to the "every . . . specific merchant" language in the Proposal. For all of the reasons discussed above, the Durbin Amendment does not require an Issuer to develop technologies that each merchant might demand to lower its cost of accepting debit cards, and it would be absurd to impose this obligation on Issuers. But, the Board's explanation in the Proposal of what it means for an Issuer to enable two Networks for "every . . . particular type of transaction" suggests that this is what the Board would require of Issuers.

¹⁸ 12 C.F.R. Pt. 235, App. A, ¶ 235.7(a)-7 (emphasis added).

¹⁹ *Id.*

²⁰ *Id.* at ¶ 235.7(b)-2(iii) (emphasis added).

with the Durbin Amendment two-Network requirement because that requirement applies to Issuers (and Networks) but not to other parties.

The Proposal would (a) replace “form factor” with “means of access;” (b) define “means of access” to include “information stored inside an e-wallet on a mobile phone or other device;” and (c) change the example to “requiring a specific payment card network based on the means of access *presented by the cardholder to the merchant.*”²¹ In the Supplementary Information, the Board characterizes the first change as aligning the Commentary terminology with current industry technology, explains the second change as capturing recent technological developments, and does not explain the third change.

Taken together, these proposed changes to the Commentary would radically alter the scope of an Issuer’s obligations under the Durbin Amendment, going far beyond the statutory mandate. This is because the proposed changes would make Issuers responsible for the actions of e-wallet providers that (a) operate outside the control of Issuers, (b) are not subject to Section 235.7 of Regulation II, and (c) contract directly with consumers to load debit cards to their e-wallet products. It is not hyperbole to describe the proposed changes as creating a regulatory requirement that Issuers are incapable of satisfying.

Independent e-wallet providers that load debit cards to their product without the consent or assistance of Issuers should be treated by the Board the same as consumers. Just as a consumer’s refusal to type a PIN may thwart a merchant’s routing choice but does not constitute a violation of Regulation II by an Issuer, an e-wallet provider that acts independently of an Issuer to store debit card information in a manner that cannot be routed over two networks may thwart a merchant’s routing choice but should not constitute a violation of Regulation II by an Issuer. The Durbin Amendment does not require Issuers to protect merchants from the acts of consumers or independent e-wallet providers, and Issuers have no ability to do so.

Also, irrespective of whether an e-wallet provider loads a debit card with the consent or assistance of an Issuer, merchants do not need the protection provided by the Durbin Amendment with respect to e-wallets that are used in CNP transactions because merchants can negotiate directly with e-wallet providers for these transactions.²² To accept a CNP transaction payment made by an e-wallet, a merchant needs to technologically integrate with the e-wallet provider either directly or through its processor or its acquirer, and thus a merchant has an opportunity to determine whether to allow payments by e-wallet and, if so, on what terms. In other words, merchants control the interaction with e-wallet providers in the case of CNP transactions. Also, merchants that choose not to allow cardholders to initiate CNP transactions with e-wallets can receive those transactions by requiring cardholders to type in a debit card

²¹ 91 *Fed. Reg.* at 26,195.

²² Senator Durbin articulated his concerns about Networks establishing default interchange rates for debit card transactions in a letter to the American Bankers Association in 2011. He asserted that Network-established default interchange rates are “unfair to merchants, who cannot negotiate interchange fees and who can no longer refuse to accept the dominant card networks.” Letter from Senator Durbin to the American Bankers Association (February 14, 2011). Neither of these two concerns is relevant to merchant relationships with e-wallet providers.

number, by using a debit card stored by the merchant, or by any other payment initiation technology.

Any final rule based on the Proposal that makes changes to the Commentary should exclude certain e-wallets from the Commentary discussion of a “means of access.” In particular, e-wallets provided by companies that operate independent of, and load a debit card without the consent or assistance of, the Issuer of the debit card should be excluded. Also, any final rule based on the Proposal should clarify in the Commentary that the term “means of access” does not refer to an e-wallet that a merchant allows a cardholder to use to initiate a CNP transaction at that merchant. These changes would maintain the original intent of the Commentary discussion of form factors – to clarify that Issuers are responsible for all types of debit cards that they issue or provide to a cardholder, while addressing the Board’s desire to update the Commentary to address recent and future innovations in debit card technology. By making the changes we suggest, the Board will achieve this result without creating a condition in which Issuers cannot control their compliance with Regulation II. Finally, the Board should explain clearly in the Supplementary Information to any final rule what any changes to the Commentary are designed to accomplish.

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Mastercard appreciates the opportunity to provide comments on the Proposal. If you have any questions regarding our comments, please do not hesitate to contact the undersigned at (914) 249-1582 or Tina.Woo@mastercard.com, or our counsel at Sidley Austin LLP in this matter, Joel Feinberg, at (202) 736-8473.

Sincerely,



Tina Woo
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cc: Joel Feinberg