

Bureau of Consumer Financial Protection
1700 G Street NW
Washington, D.C. 20552



August 11, 2021

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551

Dear Ms. Misback,

This letter is submitted in support of the Board of Governors of the Federal Reserve System's (the Board) May 7, 2021 notice inviting public comment on proposed changes to Regulation II regarding network availability for card-not-present debit card transactions.

Summary

The debit card networks facilitate payments between a customer's bank account and a merchant's bank account when consumers use their debit cards. The processing of debit card transactions is largely dominated by just two companies. In 2019, debit network companies collected over \$32 billion in interchange and network fees.¹

The Durbin Amendment to the Dodd-Frank Act (section 1075 of the Act) was intended to bring more competition to the processing of debit card transactions and limit debit card interchange

¹ 2019 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions, Federal Reserve Board, May 2021 at 3.

fees. To implement this section of the Dodd-Frank Act, in 2011 the Board required at least two unaffiliated debit networks to be activated on debit cards issued by issuers of all sizes.

The Board recently released a Notice of Proposed Rulemaking clarifying that for card not present (CNP) transactions, each debit card needs to be able to be processed on two unaffiliated networks. The Consumer Financial Protection Bureau (CFPB) supports this clarification since it likely will increase competition between networks for CNP transactions, benefiting both merchants and ultimately consumers.

Processing on Two Unaffiliated Networks

The Board has proposed to clarify that the requirement in its Regulation II (12 CFR 235) that each debit card must be able to be processed on two unaffiliated networks applies to CNP transactions.² Specifically, the Board has proposed to clarify that CNP transactions are a particular type of transaction for which two unaffiliated payment card networks must be available.³ Requiring a second network for CNP debit transactions is a first step in increasing competition and ensuring the benefits, such as the potential for lower interchange fees for merchants, might occur. Lower merchant interchange fee costs may be passed through in the form of lower prices to consumers.

CNP debit transactions include all payments when a cardholder is not present (e.g., mail orders, phone orders, etc.). Today, online transactions make up the majority of CNP transactions, and the volume of online sales during the COVID-19 pandemic increased online transactions dramatically. Over the last ten years, the market for online debit transactions has been highly concentrated, and the Department of Justice (DOJ) in its 2020 Complaint to the Visa Inc. and Plaid Inc. merger alleged that “Visa is a monopolist in online debit transactions, extracting billions of dollars in fees annually from merchants and consumers”.⁴ According to DOJ, Visa

² Notice of Proposed Rulemaking, Debit Card Interchange Fees and Routing, Board of Governors of the Federal Reserve System, 86 FR 26189, May 13, 2021 (2021 NPRM).

³ 2021 NPRM at 26190.

⁴ Complaint, United States of America, Plaintiff v. Visa Inc. and Plaid Inc., Defendants, United States District Court, Northern District of California, San Francisco Division, November 5, 2020 at 1 (Complaint). According to the Complaint, Plaid was developing a payments platform to challenge VISA’s monopoly and the transaction would

has a market share of approximately 70 percent of the online debit transactions market, and exercises monopoly power.⁵ Since online transactions reflect the majority of CNP debit transactions and given the DOJ's position, there is reason to believe that Visa's monopoly power extends to the entire CNP market.

Further, the CNP market has been growing rapidly over the last ten years from 5.09 billion transactions in 2011 to approximately 18.1 billion in 2019, an increase of over 250 percent.⁶ Technology has developed over the last decade such that CNP debit transactions can now be supported by multiple networks. In 2011 when the Board promulgated Regulation II,⁷ including its provisions requiring two unaffiliated networks on debit cards, solutions for CNP single message networks that processed PIN-authenticated transactions were not as widely established as they are now.⁸ According to the Board, in 2011 about half of the single message debit networks conducted CNP transactions, yet in 2019 nearly all performed this type of transaction.⁹ Although nearly all single message networks conducted CNP transactions, only 6 percent of CNP transactions were processed over single message networks in 2019,¹⁰ an indication that the market did not naturally develop such that two unaffiliated payment networks are available for all CNP transactions. The rules established in 2011 did not directly address whether the rules requiring two unaffiliated networks on debit cards directly applied to CNP transactions, and the 2021 NPRM usefully seeks to clarify this requirement for CNP transactions.

The proposed clarification in the 2021 NPRM related to the number of networks available for debit CNP transactions will provide merchants with a choice of two unaffiliated networks to

have allowed VISA to eliminate the competitive threat. Complaint at 3-5. In January 2021, VISA and Plaid terminated their planned merger. Department of Justice Press Release, "Visa and Plaid Abandon Merger After Antitrust Division's Suit to Block", January 12, 2021, available at <https://www.justice.gov/opa/pr/visa-and-plaid-abandon-merger-after-antitrust-division-s-suit-block>.

⁵ Complaint at 2. DOJ also notes that there are significant barriers to entry and expansion in the online debit market. Complaint at 2.

⁶ Interchange Fee Revenue, Covered Issuer Cost, and Covered Issuer and Merchant Fraud Loss Related to Debit Card Transactions, Data Tables available at, Table 2, available at <https://www.federalreserve.gov/paymentsystems/regii-data-collections.htm>.

⁷ 76 FR 43394, July 20, 2011 (2011 Rule).

⁸ 2021 NPRM at 26191.

⁹ 2021 NPRM at 26191.

¹⁰ 2021 NPRM at 26191.

process these debit transactions, including online debit transactions. This may bring an increase in competition in the processing of CNP transactions and the potential of the benefits from that competition. Such benefits may include merchants paying lower interchange fees, and in some instances, passing these savings on to consumers in the form of lower prices. However, given the concentration level in this market, it is unlikely that there will be a significant reduction in Visa's market power in the CNP market from this regulatory action alone.

Benefits may accrue to the extent that online merchants' ability to select from two unaffiliated networks will result in lower interchange fees due to increased competition. Benefits to consumers of this rule are dependent on the extent online merchant costs are lowered and the pass-through rate of these costs to consumers. Merchants in highly competitive markets with low margins are the likeliest to pass on a high portion of these cost savings.

The cost to issuers to implement two unaffiliated networks for CNP transactions appears to be less significant than when two unaffiliated networks were first required in 2011. The primary cost to issuers to implement the availability for two unaffiliated networks should be to enable the debit card's second unaffiliated network to process CNP transactions. Since all debit cards are required to have two unaffiliated networks with the ability to process card present transactions, and since nearly all single message networks have the ability to process CNP transactions, the costs to issuers should be relatively small. In 2011, the compliance date for the Regulation II transaction-routing provisions was set for a little over eight months after the regulation was published in the *Federal Register*.¹¹ Given that implementation costs for CNP transactions should be relatively small, it would be reasonable to establish an early effective date given the need to increase competition in the processing of CNP transactions as quickly as possible.

¹¹ 12 CFR 235.7(c).

Conclusion

The CFPB supports the clarification that CNP transactions should be able to be processed by two unaffiliated networks, and this clarification will increase competition between networks for CNP transactions.

Sincerely,

David K. Uejio

David K. Uejio
Acting Director