ORAL ARGUMENT SCHEDULED FOR JANUARY 17, 2014

No. 13-5270

UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

NACS, ET AL.,
Plaintiffs-Appellees,

v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Defendant-Appellant.

On Appeal from the United States District Court for the District of Columbia
Judge Richard J. Leon, Case No. 11-CV-02075-RJL

BRIEF OF AMICUS CURIAE
UNITED STATES SENATOR RICHARD J. DURBIN
IN SUPPORT OF PLAINTIFFS-APPELLEES

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CERTIFICATE AS TO PARTIES RULINGS, AND RELATED CASES

Parties and Amici

All parties, intervenors, and amici in this case and the case below are listed in the Defendant-Appellant's Certificate as to Parties, Rulings and Related Cases.

Rulings Under Review

Reference to the ruling under review is listed in the Defendant-Appellant's Certificate as to Parties, Rulings, and Related Cases.

Related Cases

This case was not previously before this Court or any court other than the District Court below. Counsel is unaware of any related cases currently pending in this Court or any other court.

Statutory and Regulatory Provisions Involved

Applicable statutes and regulations are contained in the addendum to the Brief for Defendant-Appellant.

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INTEREST OF *AMICUS CURIAE*

Amicus Curiae Senator Richard J. Durbin is the primary author of Section 920 of the Electronic Fund Transfer Act ("EFTA") (15 U.S.C. §1693 *et seq.*) as amended by Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-203, 124 Stat. 1376 (2010)), a provision commonly known as the "Durbin Amendment." In this case, the plaintiff merchants and merchant trade associations ("Merchants") have challenged final regulations issued by the Board of Governors of the Federal Reserve System ("Board") as exceeding the statutory authority given to the Board under the Durbin Amendment. *See Debit Card Interchange Fees and Routing, Final Rule*, 76 Fed. Reg. 43,394 (July 20, 2011) ("Final Rule"). Both the Merchants and the Board extensively cited statements made by Senator Durbin in their respective arguments before the District Court. Senator Durbin submitted an amicus brief before the District Court to ensure that his statements were accurately represented and to highlight how the text, purpose and legislative history of the Durbin Amendment supported the Merchants' position. The District Court granted the Merchants' motion for summary judgment, and the Board appealed. The Board has again extensively cited statements made by Senator Durbin in its brief before this Court. As this Court reviews the Board's interpretation of the statute pursuant to the analysis laid out in *Chevron U.S.A. Inc. v. NRDC*, 467 U.S. 837 (1984), Senator

Durbin submits this brief to assist the Court and to reiterate his view, shared by the Merchants and the court below, that the Board's Final Rule fails to follow the text, purpose and legislative history of the Durbin Amendment in a number of crucial respects.[1]

STATEMENT

A. Background on the Durbin Amendment

In 2010, Congress enacted the Durbin Amendment in order to carefully but firmly rein in interchange fee collusion and other anti-competitive practices in our nation's debit card industry. The Amendment was motivated by years of Congressional hearings, Government Accountability Office reports, Federal Reserve studies, academic articles, and press reports that demonstrated that the interchange fee system was not a properly functioning market.[2] These analyses showed that the interchange system was designed and operated by payment card networks and their card-issuing banks to avoid transparency and competition and

[1] All parties have consented to the filing of this brief. No counsel for a party authored this amicus brief in whole or in part, and no party or counsel for a party made a monetary contribution to fund its preparation or submission to the Court.

[2] A detailed listing of these documents is available in footnotes 3-7 of the amicus brief that Senator Durbin filed before the court below. *See* Amicus Brief of Senator Richard J. Durbin, *NACS et al. v. Board of Governors of the Fed. Reserve Sys.*, No. 11-cv-02075-RJL (D.D.C., May 9, 2012) *available at* http://www.durbin.senate.gov/public/index.cfm/files/serve/?File_id=508ce2b0-f4b0-49ca-bdc9-c15501a986d2.

to generate billions each year in high fees that exceeded what could be sustained in a normal competitive market environment. The enactment of the Durbin Amendment reflected a bipartisan recognition in Congress that reform was needed to bring transparency, competition and choice to a system that lacked it.

B. Structure of the Durbin Amendment

The Durbin Amendment as enacted by Congress consists of two main parts. The first part, contained in EFTA Section 920(a), places constraints on the debit interchange fee-fixing that the nation's largest card-issuing banks permit networks like Visa to perform on their behalf. Senator Durbin explained in his Comment Letter to the Board[3] the concerns that motivated Congress to apply these constraints:

> Network setting of interchange fees has negative implications for the efficiency of issuers' card operations and also prevents fee rates from being tempered by competitive market forces. In network-established interchange fee systems, there is no competition between issuing banks over the fees they receive, and each bank that issues the network's cards receives exactly the same network-established fee no matter how efficiently or inefficiently that bank processes transactions or prevents fraud. Also, it has often been observed that competition between networks does not lead to downward pressure on interchange rates because networks compete to attract issuers and do so by raising interchange fees.
>
> It is obvious why the current interchange fee system was set up by the banks and the dominant debit card networks Visa and MasterCard.

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[3] Comment Letter of Senator Richard J. Durbin (February 22, 2011), at JA 430-445. Note that the Board has repeatedly cited this Letter in its own brief. *See, e.g.*, Appellant's Br. at 26, 34, 37, and 39.

> The system is lucrative for issuing banks, who receive tens of billions per year in high fees that are not tempered by competitive market forces and that are not linked to any particular bank's actual costs. It also benefits the card networks, because they are paid each time a card is swiped and high interchange fees mean banks will issue more cards. But the system is unfair to consumers, who pay tens of billions per year in hidden fees passed on to them in the form of higher retail prices. And it is unfair to merchants, who cannot negotiate interchange fees and who can no longer realistically refuse to accept the dominant card networks despite constant fee increases.

Joint Appendix ("JA") 434 (internal citations omitted).

Prompted by these concerns, Congress established the mandate in Section 920(a)(2) that "[t]he amount of any interchange transaction fee that an issuer may receive or charge with respect to an electronic debit transaction shall be reasonable and proportional to the cost incurred by the issuer with respect to the transaction." After laying out 920(a)(2)'s mandate, Congress then directed the Board in 920(a)(3)(A) to prescribe implementing regulations for the mandate and also gave the Board the authority in 920(a)(3)(B) to compel the provision of information so the Board would be able to access cost information that had previously only been known to the issuers and networks and use this information in crafting the regulations as Congress directed.[4]

[4] The financial services industry had historically refused to share information about its actual costs of card operations, even with the Government Accountability Office. *See* U.S. Gov't Accountability Office, *Rising Interchange Fees Have Increased Costs for Merchants, but Options for Reducing Fees Pose Challenges*, GAO-10-45 at 23 (Nov. 2009).

Congress next gave two clear and specific considerations in Section 920(a)(4) for the Board to take into account when carrying out 920(a)(3)(A). First, in 920(a)(4)(A), Congress instructed the Board to "consider the functional similarity between (i) electronic debit transactions; and (ii) checking transactions that are required within the Federal Reserve bank system to clear at par."[5] Second, in 920(a)(4)(B), Congress authorized the Board to "distinguish between (i) the incremental cost incurred by an issuer for the role of the issuer in the authorization, clearance, or settlement of a particular electronic debit transaction, which cost shall be considered under paragraph (2); and (ii) other costs incurred by an issuer which are not specific to a particular electronic debit transaction, which costs shall not be considered under paragraph (2)…" The legislative intent behind Section 920(a)(4)

[5] Senator Durbin explained the rationale for 920(a)(4)(A)'s requirement for the Board to include this consideration in its standards as follows: "Debit card transactions are fundamentally different from credit card transactions. All that happens in a debit card transaction is you deduct money from your bank account. It is akin to writing a check. That is why debit cards are advertised as check cards. Right now in the United States there are zero transaction fees deducted when you use a check. The Federal Reserve does not allow transaction fees to be charged for checks. But when it comes to debit cards, Visa and MasterCard charge high interchange fees just as they do for credit. Why? Because they can get away with it. There is no regulation, there is no law, there is no one holding them accountable." 156 Cong. Rec. S3696 (daily ed. May 13, 2010) (statement of Sen. Richard Durbin).

was summarized in Senator Durbin's Comment Letter as follows:

> In determining the appropriate cost considerations for the Board to keep in mind when crafting its standards, Congress limited the Board's consideration to "the incremental cost incurred by an issuer for the role of the issuer in the authorization, clearance, or settlement of a particular electronic debit transaction" because Congress intended to create a closer equivalency between the debit card system and the checking system in which transactions are regulated to clear at par. In so limiting network-established debit interchange fees to those incremental authorization, clearance and settlement costs, the new law will incentivize issuers to manage all other costs of their debit card operations efficiently. This stands in stark contrast to the current system of unregulated network-established fees, in which inefficient and efficient issuers receive the same high fees.[6]

JA 435 (internal citations omitted).

The second part of the Durbin Amendment, contained in EFTA Section 920(b), prohibits several anti-competitive practices that were commonly used by card networks and issuing banks, including (b)(1)(A)'s prohibition on efforts by networks and their issuers to restrict the number of networks on which an electronic debit transaction may be processed to one exclusive network (or to two networks which are affiliated with each other). As Senator Durbin stated in his Comment Letter, "[t]he intent behind this provision was to inhibit the continued consolidation of the dominant debit networks' market power and to ensure

[6] Senator Durbin pointed out in his Comment Letter that Section 920(a)(2) and (a)(3)(A) only regulate interchange transaction fees and that "issuing banks can, do, and will continue to charge many other types of fees which are not regulated by the amendment, although unlike interchange fees those other fees are currently set in a competitive market environment." JA 435.

competition and choice in the debit network market." JA 440. Section 920(b)(1)(B) then directs the Board to prescribe regulations providing that a network or issuer cannot inhibit the ability of a person who accepts debit cards to direct the routing of electronic debit transactions over any network that may process such transactions.

SUMMARY OF ARGUMENT

The enactment of the Durbin Amendment in July 2010 represented a landmark reform of the interchange fee system. Through the Durbin Amendment, Congress established a mandate that conditioned the legality of regulated interchange transaction fees upon a reasonable and proportional relationship to the cost incurred by the issuer with respect to the electronic debit transaction for which the fee was charged or received. Congress then carefully crafted a limited set of directives authorizing the Board to effectuate this mandate. This mandate and the directives Congress gave to the Board were clearly articulated in the Durbin Amendment's text and were reinforced by Senator Durbin's statements of legislative intent. Recognizing this, the Board issued a draft rulemaking[7] in December 2010 that proposed to implement the Durbin Amendment's directives in ways that were largely consistent with the Amendment's plain text as well as its

[7] *Debit Card Interchange Fees and Routing, Notice of Proposed Rulemaking*, 75 Fed. Reg. 81,722 (Dec. 28, 2010) ("NPRM").

expressed purpose. The Board's draft rulemaking was centered around a proposed 12 cent debit interchange fee cap for issuers with over $10 billion in assets, a standard the Board based on an issuer's per-transaction variable costs of authorization, clearance and settlement ("ACS"). JA 170.

The nation's financial services industry expressed outrage with the Board's draft rulemaking and launched an aggressive lobbying campaign to weaken the draft rule and secure a final rule that preserved more of the industry's interchange revenue stream (estimated at $16.2 billion for 2009[8]). Even though a bipartisan majority in Congress had already considered and rejected the arguments of the financial services industry in voting to enact the Durbin Amendment, the industry's campaign succeeded in influencing the Board to issue a Final Rule in June 2011 that deviated from the plain text and intent of the statute that Congress had enacted.[9] The Board appears to have shaped its Final Rule in an effort to accomplish two of the Board's own policy goals: (1) making the Final Rule

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[8] JA 143.

[9] *See* Statement of Frank Keating, President and CEO of the American Bankers Association, *Who won and who lost with the Federal Reserve's final debit interchange rule?*, Am. Bankers Ass'n Washington Perspective, July 1, 2011, *available at* http://durbin.senate.gov/public/index.cfm/files/serve?File_id=68d6ba0d-0238-4d5f-b9a8-a38f782a24fb (stating "I am pleased that the Fed took what action it could to ease the rule's impact on banks. . . . It's clear to me that the aggressive six-month campaign that ABA, state bankers associations and bankers waged on this issue had a real bottom-line impact . . . the Fed heard enough concerns and credible arguments from banks that they practically doubled their originally proposed 12-cent cap.").

significantly more generous to issuing banks than the draft rulemaking, which it accomplished by permitting regulated issuers to receive an interchange fee amounting to 21 cents plus an *ad valorem* component of 5 basis points plus a one cent fraud prevention adjustment on each debit transaction; and (2) splitting the baby between banks and merchants, which it accomplished by setting a fee that is "approximately half of the pre-Rule level." Appellant's Br. at 6.

In its efforts to accommodate the banks, the Board's Final Rule failed in several respects to follow the law. As discussed below, the Board's implementing regulations exceeded the statutory authority that Congress gave the Board. Further, the Board's Final Rule contravened the text and intent of the Durbin Amendment by failing to preclude network exclusivity arrangements for many debit card transactions.

ARGUMENT

I. THE BOARD EXCEEDED ITS STATUTORY AUTHORITY UNDER SECTION 920 IN ITS FINAL RULEMAKING.

The Durbin Amendment carefully and clearly delineated the Board's authority with respect to the setting of interchange transaction fee standards. Unfortunately, the Board has attempted in its Final Rule to exercise discretion that Congress has not given it and to assert authority it does not have. The Board's inclusion of certain issuer costs within its interchange transaction fee standards is clearly inconsistent with the Durbin Amendment's text, structure, legislative history and purpose.

A. Congress Did Not Grant the Board the Authority to Consider and Include an Unspecified Universe of Issuer Costs in the Interchange Fee Standards Required under Section 920(a).

In Section 920(a)(2), Congress expressly conditioned the legality of regulated interchange transaction fees upon a reasonable and proportional relationship to the cost incurred by the issuer with respect to the electronic debit transaction for which the fee was charged or received. In Section 920(a)(3)(A), Congress authorized the Board to establish standards for assessing whether the amount of any interchange transaction fee is reasonable and proportional to the cost incurred by the issuer with respect to the transaction. Congress then provided the Board with Section 920(a)(4)'s specific directives on how to effectuate the mandate in 920(a)(2) and to prescribe appropriate regulations pursuant to (a)(3)(A). Notably, in Section 920(a)(4)(B)(i), Congress directed that "the incremental cost incurred by an issuer for the role of the issuer in the authorization, clearance, or settlement of a particular electronic debit transaction" be considered under the mandate Congress laid out in 920(a)(2). Senator Durbin explained the purpose and impact of 920(a)(4) on the Senate floor, stating that:

> Paragraph (a)(4) makes clear that the 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.

156 Cong. Rec. S5925 (daily ed. July 15, 2010) (statement of Sen. Richard Durbin). The plain text of the statute and Senator Durbin's legislative history make clear that the singular cost the Board was expressly authorized under (a)(4)(B) to consider under (a)(2)'s reasonable and proportional analysis and to include in its regulations under (a)(3)(A) was the incremental ACS cost of a particular electronic debit transaction – and no other cost. By attempting to include in its Final Rule other cost considerations that are not mentioned in the statute's text, the Board attempts to claim regulatory authority that Congress did not give it.

The Board argues that Congress "created a statutory gap that is within the Board's discretion to fill" in Section 920(a)(4)(B), and the Board then concluded that it had been authorized by Congress to include in its interchange fee standards a "significant third category of costs" regarding which the "the statute is silent." Appellant's Br. at 49-50. In making this argument, the Board relies on a tortured parsing of statutory language that ignores Congress's intent and defies the Amendment's purpose.

Congress knew prior to the enactment of the Durbin Amendment that the financial services industry had long sought to justify its exorbitant interchange rates by claiming those rates were needed to cover a broad and ever-shifting panoply of bank costs.[10] Congress also knew that if it permitted the Board to establish a "reasonable and proportional standard" that was linked to an unspecified and potentially boundless universe of costs, then any interchange rate, no matter how exorbitant, could potentially be justified as reasonable and proportional. Thus, the effectiveness of the Durbin Amendment's "reasonable and proportional" mandate in reducing the high interchange rates fixed by Visa and

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[10] *See, e.g.*, U.S. Gov't Accountability Office, *supra* note 4, at 21 ("Issuers report that the revenue they receive from interchange fees is used to cover a variety of costs in their card programs. . . . Although issuers incur costs for offering cards, concerns remain about the extent to which interchange fee levels closely relate to the level of card program expenses or whether they are set high so as to increase issuer profits."); Letter from Joseph W. Saunders, Chairman & CEO of Visa, to Senators Durbin, Kohl, Snowe & Specter, June 3, 2008, at 1, *available at* http://durbin.senate.gov/public/index.cfm/files/serve?File_id=85c0f9c3-5f33-456e-ba3e-c2e9681756eb ("[I]t is important to make clear that interchange was not designed to recoup costs but as a transfer of value generating a form of revenue to card-issuing financial institutions. Visa's interchange rates are not set at levels equal to or based on overall costs. If this were the case, interchange would be significantly higher as aggregate issuer costs overwhelm the level of interchange."); *See also* Shareholder Letter from Jamie Dimon, Chairman and CEO JPMorgan Chase, at 24, Apr. 4, 2011, *available at* http://files.shareholder.com/downloads/ONE/1279744849x0x458384/6832cb35-0cdb-47fe-8ae4-1183aeceb7fa/2010_JPMC_AR_letter_.pdf (arguing that banks need debit interchange fees to pay for the "fixed costs of servicing checking accounts and debit cards" such as "the costs of ATMs and branches.").

MasterCard necessarily depended on carefully limiting the nature of the costs that the Board could include in the interchange fee standards.

Congress in Section 920(a)(4)(B)(i) wrote language that expressly authorized the Board to consider only incremental ACS cost under Section 920(a)(2)'s reasonable and proportional analysis. As made clear in Senator Durbin's July 15, 2010 floor statement, Congress did not intend for other unspecified costs to be considered under (a)(2). The fact that Congress did not intend the Board to allow consideration of other unspecified costs in its interchange fee standards is reflected by the reporting requirement Congress created in Section 920(a)(3)(B). This reporting requirement directed the Board to report solely on information it collected "concerning the costs incurred…in connection with the authorization, clearance or settlement of electronic debit transactions" and not other costs. If Congress had intended to authorize the Board to also consider under (a)(2)'s analysis an additional, unbounded and unspecified universe of costs that are specific to a particular electronic debit transaction but that are not incremental ACS costs, as the Board claims, Congress would have written language in the statute expressly directing the Board to consider that universe of costs and would have directed the Board in (a)(3)(B) to report on its findings concerning those costs.[11]

The flaws in the Board's argument are further highlighted by the unauthorized "third category" costs that the Final Rule specifically incorporated into its higher interchange fee cap: fixed ACS costs, transaction monitoring costs, fraud losses, and network processing fees. In his amicus brief before the District Court, Senator Durbin not only explained how Congress had not authorized the Board to consider these costs but also articulated how each of these specific costs was actually precluded by the plain language and intent of the statute.[12] The court below agreed.[13]

Thus, the Board, by adopting a counterintuitive statutory construction and including in its final interchange fee standards costs that Congress neither authorized nor intended the Board to include, has exceeded the authority given to it under the Durbin Amendment. This stands in stark contrast to the interchange fee

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[11] Additionally, had Congress intended to give the Board authorization in 920(a)(4) to consider unspecified costs, Congress could have done in (a)(4) what Congress did in (a)(5), a provision that directs the Board to prescribe regulations allowing for fraud prevention adjustments to interchange fee amounts. In 920(a)(5)(B)(ii)(VII), Congress provided for the Board to consider "such other factors as the Board considers appropriate" in prescribing regulations relating to fraud prevention adjustments. But Congress did not so provide in (a)(4).

[12] *See* Amicus Brief of Senator Durbin, *supra* note 2, at 16-22.

[13] JA 77-81.

standards that the Board proposed in its NPRM[14] which Senator Durbin commended in his Comment Letter as being consistent with the statute's text and intent. JA 432. In order for its Final Rule to comply with the text and intent of the statute, the Board would be well served to return to the analysis and standards that it presented in the NPRM.

B. The Board Incorrectly Claims that its Interpretation of Section 920(a) Is "In Complete Fealty to the Text and the Purpose of the Statute."

The Board is mistaken in its claim that it "exercised its rulemaking authority in complete fealty to the text and purpose of the statute" by setting a fee that is "approximately half of the pre-Rule level" of 44 cents on average per transaction. Appellant's Br. at 18, 6. This claim reflects an apparent lack of understanding by the Board about the impact of its Final Rule and the purpose of the Durbin Amendment.

As the Board earlier acknowledged in its NPRM, debit interchange transaction fees have for years been established by networks as a combination of an *ad valorem* (*i.e.*, percentage of the value of transaction) fee component plus a flat fee component. JA 100. This fee structure meant that before the Final Rule

[14] *See* JA 110-111, in which the Board said: "After considering several options for the costs that may be taken into account in setting interchange transaction fees ('allowable costs'), the Board proposes such costs be limited to those associated with authorization, clearing, and settlement of a transaction. This formulation includes only those costs that are specifically mentioned for consideration in the statute."

took effect, small ticket (*i.e.*, small dollar) debit transactions were typically assessed interchange fees that amounted to significantly less than 44 cents. However, by setting a high fee cap that far exceeded the customary fees levied on small ticket transactions, the Board gave its regulatory blessing to the setting of interchange rates by Visa and MasterCard that are over three times larger than rates previously charged on small dollar transactions. After the issuance of the Final Rule, first MasterCard and then Visa raised their small ticket interchange rates for regulated issuers to the Final Rule's maximum allowable level, increasing fees significantly for small ticket transactions.[15]

The statutory purpose of the Durbin Amendment's fee regulation has been clearly expressed by Senator Durbin:

> Our language will help every single Main Street business that accepts debit cards keep more of their money, which is a savings they can pass on to their consumers. Every grocery store, every convenience store, flower shop, and every restaurant will be able to reduce the fees they paid to the big banks for debit card transactions….It is not just businesses that will benefit from the amendment. Charities will benefit. Think about that. Charities that accept donations by debit cards will see a savings. Universities will save money on card fees,

[15] *See* Digital Transactions News, *Applying the Durbin Maximum, Visa and MasterCard Could Squash Small Tickets*, Sept. 27, 2011, http://www.digitaltransactions.net/news/story /3217 ("The new schedules will raise merchants' acceptance costs considerably when a customer presents a card from a big bank to pay for a small purchase. For example, under the April rates, a merchant on a $2 sale for a cup of coffee currently pays 7.1 cents when either a Visa or MasterCard debit card is presented. Now that cost will more than triple to 23 cents, assuming the Fed approves the proposed 1-cent fraud fee. On an $8 sale, the cost will increase 59%.").

> and so will public agencies, such as your local motor vehicle commission in your home state, public transit agencies, and even the U.S. Postal Service.

156 Cong. Rec. S4839 (daily ed. June 10, 2010) (statement of Sen. Richard Durbin). Senator Durbin's statement on the Senate floor makes plain Congress's intent that under the Durbin Amendment each merchant, charity, university and government agency that accepts debit cards should see fees lowered on each transaction involving debit cards issued by large regulated issuers. But because of the misguided nature of the Board's Final Rule, that has not happened. Contrary to the Board's claim that its interpretation gives effect to the "purpose" of the statute, we have ended up with an absurd situation where the Board's Final Rule has approved the charging of significantly higher interchange rates for small ticket transactions, and has even blessed the charging of a 22 cent interchange fee on the debit card purchase of a 10 cent pencil.

Further, the Board has crafted a Final Rule that twists and tortures the plain meaning and clear intent of the Durbin Amendment in an apparent effort to split the baby between big banks and merchants and set a fee that is "approximately half" of the 44 cents per transaction pre-Rule average. Appellant's Br. at 6. But Congress neither instructed nor empowered the Board to impose its own policy judgments and engage in a balancing act between the low fee wishes of merchants and the high fee desires of the banks. Congress had made its own policy determination that the Durbin Amendment was needed as "a response to price fixing by Visa and MasterCard." 156 Cong. Rec. S3589 (daily ed. May 12, 2010) (statement of Sen. Richard Durbin). Congress knew that Visa and MasterCard are the dominant fee-setting entities for debit card transactions, which are the most frequently used form of noncash payment in the United States, and that a significant body of literature had shown that inefficiency is subsidized and competition is avoided when a network duopoly centrally sets fees on behalf of thousands of issuing banks. Congress had also heard from consumer groups who noted that consumers ultimately bear the cost of subsidizing the interchange system and asserted that consumers would benefit from the Durbin Amendment's reforms.[16] Congress's goals were to enhance competition, transparency and choice in the debit system and squeeze out inefficiencies by reducing network-fixed interchange fee rates to cover only a limited measure of incremental ACS cost,

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[16] *See, e.g.*, 156 Cong. Rec. S3698 (daily ed. May 13, 2010) (letter from Americans for Financial Reform) (Americans for Financial Reform, a coalition including over "250 consumer, civil rights, investor, retiree, community, labor, religious and business groups as well as Nobel Prize-winning economists[,] . . . supports the Durbin Reasonable Fees and Rules for Payment Card Transactions Amendment #3989 because it is good for merchants and good for consumers."); *Oversight of Federal Payment of Interchange Fees: How to Save Taxpayer Dollars, Before the Subcomm. on Financial Services and General Government of the S. Comm. on Appropriations*, 111th Cong. at 2, 5 (June 16, 2010) (testimony of Edmund Mierzwinski, Consumer Program Director, U.S. Public Interest Research Group) ("All consumers, even those who pay with cash and checks, pay more at the store and more at the pump because these interchange fees are passed on in the overall cost of goods sold…[The Durbin Amendment] will have a positive effect.").

thereby compelling large issuers to compete against each other to manage their other costs more efficiently. Further, as Congress was aware, past experience in this country[17] and present examples in other countries[18] demonstrate that banks can easily offer debit card services without the subsidy of unreasonably high interchange fees – and Congress was not persuaded by the financial services industry's arguments to the contrary. In short, Congress made its own policy determinations in crafting the Durbin Amendment, and Congress tasked the Board to follow the law Congress passed.

The NPRM was far truer to the statutory purpose of the Durbin Amendment than the Final Rule, which is why Senator Durbin commended the Board in his Comment Letter on the NPRM. JA 432. However, Senator Durbin was prescient when he pointed out in his Comment Letter that "the card companies and the $13 trillion dollar banking industry have engaged in near-hysterical criticism of the

[17] *See* Andrew Martin, *How Visa, Using Card Fees, Dominates a Market*, N.Y. Times, Jan. 4, 2010. ("Fees were not an issue when debit cards first gained traction in the 1980s…. Merchants were not charged a fee for accepting PIN debit cards, and sometimes they even got a small payment because it saved banks the cost of processing a paper check. That changed after Visa entered the debit market.").

[18] *See e.g.*, Dennis W. Carlton, *Externalities in Payment Card Networks: Theories and Evidence, Commentary*, Nov. 9-10, 2009 at 125, 129, *available at* http://www.kc.frb.org/publicat/pscp/2009/PDF/A1.completeproceedings.pdf (finding that "in seven of the eight countries with the highest debit card usage per capita there is no interchange fee."); Testimony of Edmund Mierzwinski, *supra* note 16, at 7 **(**"numerous countries operate payment systems without the use of interchange fees. In those countries the ultimate costs of these systems is modest and the systems operate quite efficiently.").

interchange reform that Congress enacted" and warned that "[a]s we move toward the issuance of final rules, there is no doubt the Board will face a sustained advocacy barrage from financial industry lobbyists." *Id.* This was indeed the case, and Senator Durbin was disappointed that the Board's final rulemaking did not heed Senator Durbin's counsel that "[i]t is imperative that interchange reform be based on the facts and the law, not on the lobbying might and scare tactics of the financial industry." JA 433.

II. THE BOARD'S FINAL RULE FAILS TO PROPERLY IMPLEMENT THE NETWORK EXCLUSIVITY PROVISIONS OF SECTION 920(b).

A. The Final Rule Does Not Preclude Network- or Issuer-Imposed Arrangements that Require Exclusivity for Certain Electronic Debit Transactions.

Section 920(b)(1)(A) of the Durbin Amendment provides that the Board "shall prescribe regulations providing that an issuer or payment card network shall not…by contract, requirement, condition, penalty or otherwise, restrict the number of payment card networks on which an electronic debit transaction may be processed" to less than two unaffiliated payment card networks. This provision was intended to put an end to network or-issuer-imposed exclusivity agreements that had rapidly taken hold in the debit card industry.[19] As Senator Durbin said in his Comment Letter, "(t)his trend toward exclusivity agreements, particularly when

[19] *See* Appellant's Br. at 37, noting that nearly half of all debit cards in circulation had become subject to such exclusivity agreements.

utilized by dominant four-party networks such as Visa, is troubling in three ways: it limits merchant and consumer choice; it diminishes competition by threatening to drive competing debit networks out of business; and it creates significant barriers to entry for new debit networks." JA 440.

The Board's Final Rule adopted a proposal requiring at least two unaffiliated payment card networks be enabled on each card, but deemed a card to be in compliance with the Rule if it has been enabled with one PIN debit network and another unaffiliated signature debit network. JA 193. This falls short of complying with the language and intent of the Durbin Amendment. The Board has acknowledged that there are a significant number of transaction types in which PIN debit is not available as an authentication method, leaving signature debit as the only currently available option in the marketplace. For example, the Board noted in its Final Rule that "[i]n the current environment…certain transactions, such as hotel stays or car rentals, where the exact amount of the transaction is not known at the time of authorization, cannot readily be accommodated on PIN-based, single-message systems. In addition, PIN debit transactions generally are not currently accepted for Internet, telephone, and mail transactions." JA 141. For such types of transactions, it is not a question of the merchants' or consumers' preference whether or not to process transactions on a PIN debit network; rather, the nature of the transaction is simply incompatible with the current PIN authorization technology and thus PIN is not a feasible[20] means of authorization on which the transaction "may be processed" under Section 920(b)(1)(A). Currently, signature debit networks have arranged for the exclusive use of their signature networks on debit cards,[21] and the Board's Final Rule permits these signature network exclusivity arrangements to continue unabated. The Final Rule thus fails to ensure that an electronic debit transaction "may be processed" over at least two unaffiliated networks, because for those transactions where PIN is not a feasible option, the Final Rule fails to guarantee that networks do not have contracts or requirements providing for exclusive use of one signature debit network.

The need for the Board's Final Rule to guarantee the availability of multiple unaffiliated networks on which every electronic debit transaction may be processed is compelled by the plain text of Section 920(b)(1)(A) as well as by Senator Durbin's statements of legislative intent. For example, Senator Durbin stated on the Senate floor that:

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[20] *See* JA 125 ("Because PIN debit transactions are single-message transactions that combine the authorization and clearing instructions, the Board understands that it is <u>currently not feasible</u> to use PIN debit in circumstances where the final transaction amount differs from the authorized transaction amount.") (emphasis added).

[21] *See, e.g.*, JA 124 ("Certain signature debit network rules also prohibit issuers of debit cards carrying the signature network brand from offering other signature debit networks or certain competing PIN debit networks on the same card.").

> This 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 run over at least two unaffiliated networks, and the Board's regulations should ensure that networks or issuers do not try to evade the intent of this amendment by having cards that may run on only two unaffiliated networks where one of those networks is limited and cannot be used for many types of transactions.

156 Cong. Rec. S5926 (daily ed. July 15, 2010) (statement of Sen. Richard Durbin) (emphasis added). The Board claims that its Final Rule satisfies the law because it requires "substantial diversification of the networks available to process electronic debit transactions," yet "substantial diversification" falls short of the statute's command by leaving a significant universe of debit transaction types subject to exclusivity arrangements and without recourse. Appellant's Br. at 37.

While the Board claims that it would be burdensome to require that every debit card be enabled with two signature debit networks, neither the text nor legislative intent of the Durbin Amendment mandated that particular outcome as the only way to achieve the statute's goal. The statute was drafted to prohibit a negative scenario (*i.e.*, network- or issuer-imposed exclusivity arrangements), and was not drafted to affirmatively require what the non-exclusive world must look like. *See* JA 440. As the court below indicated, one option available to the Board that would be compliant with the statute's requirements would be for the Board to ensure "multiple routing options for every transaction by barring the dominant networks' anti-competitive rules to allow PIN-only networks to process signature transactions, and vice versa." JA 90. The Board was aware of the feasibility and availability of this option, as it was notified about it during the comment period on the NPRM[22], but the Board chose not to follow this option and instead selected an approach that violates the statute's requirements. The Board could come into compliance with the language and intent of the Durbin Amendment by preventing networks from prohibiting cross-routing of signature and PIN transactions and by ensuring that each card has multiple unaffiliated network options on which every type of debit transaction may be feasibly processed.[23]

B. The Board Failed to Accurately Convey Senator Durbin's Views of Section 920(b).

The Board seeks to diminish the "interpretive weight" of the Senator Durbin's July 15, 2010 floor remarks about Section 920(b). Appellant's Br. at 32. However, given the absence of other legislative history on the Durbin Amendment, Senator Durbin's floor statement stands as an "authoritative indication( )" of

[22] *See* JA 90.

[23] It should be noted that PIN debit networks have been capable of performing dual message transactions for years. *See* Press Release, *SHAZAM Announces Dual Message PIN Transactions and EMV Card Support* (Aug. 22, 2011), *available at* http://epaymentnews.blogspot.com/2011/08/shazam-announces-dual-message-pin.html#axzz2kfQ0Pz8h ("The SHAZAM Network today announced the creation of a dual-message PIN product, a first for the EFT industry . . . The product will use a dual-message transaction with separate authorization and settlement messages for PIN-based transactions, a capability previously only available on signature-based transactions.").

Congress' intent behind 920(b). *Kimberlin v. U.S. Dept. of Justice*, 318 F.3d 228, 232 (D.C. Cir. 2003), quoting *N. Haven Bd. of Educ. v. Bell*, 456 U.S. 512, 527 (1982). Further, the court below did not rely solely on Senator Durbin's floor statement, but rather held that the Board's Final Rule was inconsistent with the "letter" and "plain meaning" of Section 920(b) and stated that "Congress's use of clear, defined language in the network non-exclusivity and routing provisions leaves *no* ambiguity or statutory gap for the agency to fill." JA 86, 87, 90 (emphasis in original).

The Board also selectively quotes other passages from Senator Durbin's floor statements and Comment Letter in a misleading effort to characterize Senator Durbin's July 15 floor remarks as inconclusive. But the full passages cited by the Board actually reinforce Section 920(b)'s language and meaning. The passage cited on pp. 33-34 of the Board's brief makes clear that Section 920(b) blocks networks from engaging in certain anti-competitive practices, including (b)(1)'s prohibitions against exclusivity arrangements for electronic debit transactions, and that the statute does not permit networks to cross back into a world where such exclusivity agreements persist. Further, while the Board represents that Senator Durbin's Comment Letter "took no position"[24] with respect to the alternatives proposed by the NPRM, the actual language of Senator Durbin's letter makes plain

[24] Appellant's Br. at 34.

the Senator's position and the statute's goal of ending network- or issuer-imposed exclusivity agreements, particularly in the signature debit space:

> The amendment did not write specific authorization methods (e.g., PIN and signature) into statute and then mandate how those authorization methods must be treated in a non-exclusive world. The concern was that doing so would lock acceptance of those authorization methods into federal law, which would run contrary to the overall amendment's goal of incentivizing the development and use of more efficient and more fraud-proof authorization methods than those currently in use in this country. For example, a key goal of the overall amendment is to incentivize the use of better authorization and authentication technologies than the current signature debit system. Thus, it would not be optimal for EFTA 920(b)(1) to specifically require an overhaul of the debit industry to ensure that every card can be transacted over two signature debit networks if the amendment succeeds in incentivizing new authorization methods that quickly supplant signature debit altogether. On the other hand, it would be even less optimal for the goals of ensuring competition and choice if signature debit managed to survive as a common authorization method and if exclusivity arrangements were allowed to continue to predominate in the signature debit space.
>
> Statutory language is limited in its ability to keep pace with potentially fast-moving technological developments in the debit card system. It is for that reason that EFTA 920(b)(1) confers rulemaking discretion upon the Board on how best to guide us through a non-exclusive world. <u>What the statute makes clear is that network- or issuer-imposed network exclusivity agreements (as well as network- or issuer-imposed routing restrictions that achieve the same effect) are to be prohibited under the regulations that the Board prescribes when those regulations take effect</u>. This is essential to the goals of preserving and enhancing competition and choice in the debit system.

JA 441-2 (emphasis added).

Finally, the Board claims that "the legislative history of section 920 *suggests*" that Congress did not demand "sweeping changes" when it comes to exclusivity agreements. Appellant's Br. at 35 (emphasis added). But what the text and legislative history of Section 920(b) actually *say* is that the Board's regulations must provide that every type of transaction involving a debit card – including the significant universe of transactions where the exact amount of the transaction is not known at the time of authorization, as well as Internet, telephone and mail transactions – shall not be subject to network- or issuer-imposed exclusivity agreements that restrict the number of unaffiliated networks on which the transaction may be processed to less than two. The Board knew it had technologically feasible options (such as providing for PIN and signature cross-routing) to carry out this directive and the Board also knew that Congress had given it "latitude to allow for a reasonable implementation period" to make sure that the industry could operationalize such a directive smoothly and effectively. JA 441. The Board should have complied with what the law and legislative history said.

In sum, the Board's Final Rule provisions on network exclusivity should be revised to comply with the plain language and legislative intent of 920(b)(1)(A)'s guarantee for the availability of at least two unaffiliated networks on which an electronic debit transaction may be processed.

CONCLUSION

For the foregoing reasons, the judgment of the District Court should be affirmed.

Respectfully submitted,

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1. This brief complies with the type-volume limitation of the Federal Rule of Appellate Procedure 32(a)(7)(B) because:

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/s/ David A. Balto
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Dated: November 20, 2013

CERTIFICATE OF SERVICE

I hereby certify that on November 20, 2013, I electronically filed the foregoing Brief for Amicus Curiae Senator Richard J. Durbin in Support of Plaintiffs-Appellees with the Clerk of the Court for the United States Court of Appeals for the District of Columbia Circuit using the appellate CM/ECF system. Counsel for all parties to the case are registered CM/ECF users and will be served by the appellate CM/ECF system:

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