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National Association of Federally-Insured Credit Unions

June 21, 2022

The Honorable Sherrod Brown
Chairman
Committee on Banking, Housing, and
Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Patrick Toomey
Ranking Member
Committee on Banking, Housing, and
Urban Affairs
United States Senate
Washington, DC 20510

Re: Tomorrow's Hearing, "The Semiannual Monetary Policy Report to Congress."

Dear Chairman Brown and Ranking Member Toomey:

I write to you today on behalf of the National Association of Federally-Insured Credit Unions (NAFCU) to share our thoughts on how government interference with debit interchange as part of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank Act) has harmed community financial institutions and consumers as you prepare to hear from Federal Reserve Board Chairman Jerome Powell. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 130 million consumers with personal and small business financial service products. We appreciate the opportunity to share our thoughts on this incredibly important issue.

The electronic payments system is a two-sided market, with consumers on one side and merchants on the other. Both sides benefit from the arrangement, with card networks setting interchange rates based on the cost of doing business and the benefit to consumers and merchants. In the wake of the pandemic, many merchants are requesting cashless payments for employee safety and to streamline their operations. This is evidence that the electronic payments system offers real value to merchants and consumers alike. Ultimately, merchants receive far more value from accepting electronic payments than they pay in interchange fees. Any new caps or restrictions on interchange fees would only hurt community institutions such as credit unions as well as the American consumer.

When a consumer uses a credit or debit card to pay for a transaction, the merchant pays an interchange fee, or "swipe" fee, to the card-issuing bank for the benefits they receive from that transaction (such as immediate payment). Interchange fees cover a variety of expenses, including the cost of customer service, system improvements, online transactions, data security, and card production. Furthermore, interchange fees can vary significantly depending on whether or not a card was present for the transaction, whether the data is complete, the category of merchant, whether the card is credit or debit, the brand of the card, and whether the owner of the card is an individual, business, or other entity. They are not monolithic by any means.

Section 1075 of the Dodd-Frank Act, commonly referred to as the Durbin Amendment, imposed a cap on debit interchange fees for covered banks and credit unions, defined as those with assets of more than

$10 billion, and established new routing network requirements for debit cards. It also charged the Federal Reserve Board (Fed) with carrying out these new requirements, which it has done so with Regulation II. The Fed recently proposed to reopen Regulation II, a move NAFCU has urged them to reconsider. We also urge the Fed to resist requests from retailers for further changes to Regulation II that would increase the regulatory burden associated with the Durbin Amendment to the Dodd-Frank Act.

Credit unions have seen a precipitous erosion of per-transaction debit interchange income despite the fact that institutions below $10 billion in assets were "exempted" by Durbin Amendment supporters. Advocates argued the $10 billion threshold would protect the smallest institutions from the negative impacts of this amendment. They were wrong. This is now demonstrably false as shown by multiple *governmental* studies and surveys on the issue. For example, an annual survey for the Fed found that since 2016, more than 50 percent of credit unions with assets below the $10 billion threshold have seen their per-transaction interchange rates decrease.

While the intent of the Durbin Amendment was to prevent card-issuers and networks from unfairly charging merchants higher rates and thus passing higher costs along to consumers, the evidence overwhelmingly suggests that it has not helped everyday Americans. According to Fed data, this amendment has taken away $6-8 billion per year from the revenue that banks and credit unions use to serve their customers and members. The erosion of interchange fees is particularly hard on credit unions that are statutorily limited in what products they may offer and investments they can make. While a bank may be able to turn to capital markets or choose other investments, credit unions have very few options to replace this lost income. As not-for-profit, community based financial institutions, this ultimately hurts what they can do for their members. There is no evidence that merchants have passed along their savings to consumers in the form of price cuts, and the regulatory burden and loss of revenue for banks and credit unions has led to industry consolidation and the difficult choice to charge for services that were once free, such as checking accounts.

A February 2022 GAO report found that the Durbin Amendment was among the top five laws and regulations most cited as having significantly affected the cost and availability of basic banking services. Further, the merchants' promise of savings for consumers never happened—the merchants pocketed the savings. According to the Federal Reserve Bank of Richmond, after the Durbin Amendment was implemented, an overwhelming majority of merchants did not pass along savings realized from debit regulation to consumers and over 20 percent increased prices.

Since the Durbin Amendment was enacted, we have seen consumer prices increase, consolidation among community banks and credit unions, and several small debit networks have gone out of business. Big-box retailers and ever-expanding e-commerce giants have been the beneficiaries of a massive financial windfall. The top retailers in the U.S. diverted an estimated $250 billion in sales away from millions of small businesses and are now calling for government intervention in the competitive payments marketplace to increase their advantage. These are many of the same merchants, such as

Wawa, Target and Home Depot, that have suffered massive consumer payment card data breaches over the last decade and relied upon financial institutions to absorb these externalities (e.g., by issuing replacement cards) and restore consumers who were harmed—all while trying to fight the interchange system that helps financial institutions aid consumers when their payment cards have been compromised at these retailers.

As you hear from Chairman Powell, we urge you to remember that it has never been the role of the central bank to attempt to replace, through regulation, the price discovery mechanisms of a complex two-sided marketplace. We hope you will urge him to recognize that demands to reopen Regulation II are premature and motivated by the short-term and parochial economic interests of merchants, and to exercise appropriate restraint by declining to entertain those demands.

Thank you for your attention and the opportunity to share our thoughts on this important issue. Should you have any questions or require additional information, please do not hesitate to contact me or Chad Adams, NAFCU's Senior Director of Legislative Affairs, at (703) 842-2265 or cadams@nafcu.org.

Sincerely,

Brad Thaler

Brad Thaler
Vice President of Legislative Affairs

cc: Members of the Senate Banking Committee