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A Call for Change in Interchange Fee Regulation: Examining the Durbin Amendment Disaster Through the Lens of NACS v. Federal Reserve Board

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NOTE

A CALL FOR CHANGE IN INTERCHANGE FEE REGULATION: EXAMINING THE DURBIN AMENDMENT DISASTER THROUGH THE LENS OF *NACS V. FEDERAL RESERVE BOARD*

Kaitlyn E. Evans†

I. INTRODUCTION

Retailers are responsible for billions of dollars in debit card interchange fees[1] each year, but these charges are ultimately passed along to American consumers.[2] In order to reduce costs to consumers and retailers alike, Congress intervened with the passage of the Durbin Amendment[3] to the Dodd-Frank Wall Street Reform and Consumer Protection Act.[4] Congress addressed the interchange fee issue by authorizing the Board of Governors of the Federal Reserve to issue regulations requiring interchange fees be "reasonable and proportional" to the cost incurred by the cardholder's bank in completing a debit card transaction.[5] Congress gave the Federal Reserve Board certain bank costs to consider in establishing the interchange fee regulations, and prohibited the Board from allowing banks to recover other specific costs through interchange fees.[6] The Federal Reserve Board's final

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1. *See* discussion *infra* Part II.C.1.

2. Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43397 (July 20, 2011).

3. Electronic Fund Transfer Act § 920, 15 U.S.C. § 1693o-2(a) (2012); Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 479-80 (D.C. Cir. 2014) ("Seeking to correct the market defects that were contributing to high and escalating fees, Congress passed the Durbin Amendment as part of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act. The amendment . . . modified the Electronic Funds Transfer Act . . . .").

4. Dodd-Frank Wall Street Reform & Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

5. 15 U.S.C. § 1693o-2(a).

6. 15 U.S.C. § 1693o-2(a)(4).

rule implementing the Durbin Amendment prohibits banks from recovering more than twenty-one cents (plus a small *ad valorum* fee[7]) per transaction,[8] which is less than half the value of the average interchange fee charged before governmental intervention.[9] The final rule also requires that a debit card-issuing bank not restrict the number of card transaction networks over which a transaction may be processed.[10] However, retailers and merchant groups are unsatisfied with the regulation and want to see an even greater reduction in interchange fees. Particularly, these groups argue that in establishing the final regulations, the Federal Reserve Board considered bank costs that Congress explicitly excluded from the Board's consideration.[11] Thus, the cost considerations in the Durbin Amendment have proven to be quite contentious, and the subject of litigation between merchant groups and the Federal Reserve Board—litigation that was appealed all the way to the United States Supreme Court.[12]

This Note will examine the effects of the Durbin Amendment and the Federal Reserve Board's final rules through the lens of *National Ass'n of Convenience Stores v. Board of Governors of the Federal Reserve System*.[13] Part II will provide a summary of the debit card system and the interchange fees critical to the case. Part III will give a detailed discussion of the legislative history behind the Durbin Amendment and a comprehensive summary of the Federal Reserve Board's proposed and final rules implementing the Durbin Amendment. Part IV will discuss the litigation in *National Ass'n of Convenience Stores*, including a detailed analysis of the district court's decision, the D.C. Circuit Court's reversal, and the arguments presented to the Supreme Court following an unsuccessful appeal. Part V will discuss the consequences to consumers, merchants, and banks of the Federal Reserve Board's final rule and the Durbin Amendment generally. Finally, Part VI will

7. Debit Card Interchange Fees & Routing, 12 C.F.R. § 235 app. A § 235.3(b) (2014).

8. 12 C.F.R. § 235.3(b).

9. Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43397 (July 20, 2011) (stating that before the Durbin Amendment's implementation, the average interchange fee for all debit card transactions was 44 cents per transaction).

10. 12 C.F.R. § 235.7(a).

11. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 958 F. Supp. 2d 85, 96 (D.D.C. 2013).

12. Petition for Writ of Certiorari, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., (No. 14-200), 2014 WL 4102151; Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474 (D.C. Cir. 2014), *cert. denied*, (U.S. Jan. 20, 2015) (No. 14-200).

13. *Nat'l Ass'n of Convenience Stores*, 746 F.3d 474.

propose how the ongoing problems surrounding the debit card market regulation should be addressed.

II. THE DEBIT CARD SYSTEM

A. *The Debit Card Industry*

Today, an unprecedented volume of debit card transactions occurs every day in the United States.[14] Despite almost universal use of debit cards in recent decades, debit cards were first introduced in the late 1960s and early 1970s simply as a means to withdraw cash at automated teller machines (ATMs).[15] Before debit cards, account holders could only access their bank accounts by making "in-person withdrawals from human bank tellers" or issuing paper checks.[16] Within a few years, banks introduced debit cards that could not only be used to perform banking activities at ATMs, but also allowed consumers to purchase goods and services directly from retailers and merchants without cash or checks.[17] "Unlike other payment options, debit cards allow consumers to pay for goods and services at the point of sale using cash drawn directly from their bank accounts, and to withdraw and receive cash back as part of the transaction."[18]

Due to technological and financial innovations, debit cards have significantly "eclipsed checks as the most frequently used noncash payment method."[19] In terms of use frequency, debit cards ranked third among non-cash payment methods—behind checks and credit cards—in the year 2000.[20] Since then, debit card payments have increased more than any other form of non-cash payment.[21] "[B]y 2009, debit cards ranked first, accounting for 35 percent of the total volume of noncash, retail payments."[22] "According to the 2009 Survey of Consumer Payment Choice, debit cards are used for 29.3 [percent] of all transactions and have become the most frequently used

14. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395.

15. *Id.*

16. *Nat'l Ass'n of Convenience Stores*, 958 F. Supp. 2d at 87.

17. M. Pierce Sandwith, *Debit Card Interchange Fees and the Durbin Amendment's Small Bank Exemption*, 16 N.C. BANKING INST. 223, 225 (2012).

18. *Nat'l Ass'n of Convenience Stores*, 958 F. Supp. 2d at 87.

19. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395.

20. Fumiko Hayashi, *The New Debit Card Regulations: Initial Effects on Networks and Banks*, 2012 FED. RES. BANK OF KAN. CITY ECON. REV. 79, 81-82 (4th Quarter 2012), *available at* http://www.kansascityfed.org/publicat/econrev/pdf/12q4Hayashi.pdf.

21. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395.

22. Hayashi, *supra* note 20, at 82.

method of payment, eclipsing cash, credit cards, and checks individually."[23] Every year, consumers in the United States swipe their debit cards approximately 50 billion times—more than 100 million times per day—to complete transactions worth more than 1.4 trillion dollars.[24] In 2009 alone, debit card transactions generated over 20 billion dollars in fees for banks and card networks, which subsidized many of their operating costs, including the cost of offering free checking accounts and producing debit cards.[25]

Due to the convenience that debit cards offer consumers, it is not surprising that they are accepted at millions of merchant locations throughout the United States.[26] However, the massive usage increase in recent years has changed how banks and merchants are interacting with both consumers and each other; and the increasing cost to merchants for processing debit card transactions in the form of bank fees has stirred controversy, triggering congressional intervention.[27]

B. *The Mechanics of a Debit Card Transaction*

The simplicity that debit card use affords consumers is not reflected in the behind the scenes processing of debit card transactions. Although most debit card transactions are processed using what is commonly known as the "four-party system," five parties actually participate in every debit card transaction.[28] The five key parties are the cardholder, the cardholder's bank (the "issuer"), the merchant, the merchant's bank (the "acquirer"), and a card network.[29] The issuer issues a debit card to the cardholder, approves or declines transactions initiated by the cardholder with a merchant, and debits

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23. Patrick C. McGinnis, *Misguided Regulation of Interchange Fees: The Consumer Impact of the Durbin Amendment*, 25 LOY. CONSUMER L. REV. 285, 290 (2013) (citing Kevin Foster et al., *The 2009 Survey of Consumer Payment Choice*, Fed. Reserve Bank of Boston, Public Policy Discussion Paper No. 11-1 (April 2011)).

24. Petition for Writ of Certiorari, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., (No. 14-200), 2014 WL 4102151; *see* Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395 (noting that in 2009, debit cards were used in 37.5 billion transactions, but projecting that debit card transactions would total about 50 billion by 2011).

25. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 477 (D.C. Cir. 2014); Kathleen A. McConnell, *The Durbin Amendment's Interchange Fee and Network Non-Exclusivity Provisions: Did the Federal Reserve Board Overstep its Boundaries?*, 18 N.C. BANKING INST. 627, 651 (2014).

26. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395 ("Debit cards are accepted at about 8 million merchant locations in the United States.").

27. Hayashi, *supra* note 20, at 79.

28. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 477; Hayashi, *supra* note 20, at 82.

29. Hayashi, *supra* note 20, at 82.

the cardholder's account after approval.[30] The acquirer connects "the merchant to the card network and after approval from the [issuer], credits the merchant's account for the [transaction]."[31] Networks, such as Visa and MasterCard, build and maintain the payment infrastructure that links all of the parties to a transaction, so that information is easily transmitted between the acquiring side of the transaction and the issuing side.[32]

To ensure that only an authorized cardholder has initiated a transaction, networks use personal identification number (PIN) transactions or signature transactions, each of which employs a different method of authentication[33] and requires a different infrastructure.[34] PIN authentication generally requires a cardholder to enter his PIN into a terminal, whereas signature authentication usually requires the cardholder to sign a copy of the purchase receipt.[35] The infrastructure for PIN networks is based on the infrastructure employed by ATMs, while the infrastructure of signature networks utilizes the infrastructure of credit card networks.[36]

Regardless, all debit card transactions are processed in three stages: authorization, clearance, and settlement.[37] The first stage, authorization, begins when the cardholder offers his debit card to the merchant to tender payment.[38] As soon as the debit card is swiped, "an electronic authorization request for a specific dollar amount, along with the cardholder's account information, is sent from the merchant to the acquirer to the network, which sends the request to the appropriate [issuer]."[39] Within seconds, but after verifying that the cardholder's account has sufficient funds to complete the transaction and that there is no evidence that the debit card was lost or stolen, the issuer returns a message to the merchant via the network, either approving or declining the transaction.[40] However, "[e]ven if the issuer

30. McConnell, *supra* note 25, at 630.

31. *Id.*

32. Hayashi, *supra* note 20, at 82.

33. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 477-78.

34. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 958 F. Supp. 2d 85, 88 (D.D.C. 2013).

35. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 478.

36. Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43395 (July 20, 2011).

37. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 478.

38. *Id.*

39. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43396.

40. *Id.*

approves the transaction, that transaction still must be cleared and settled before any money changes hands."[41]

The second stage, clearance, "constitutes a formal request for payment sent from the merchant on the network to the issuer."[42] Because the cardholder enters his PIN immediately after swiping his debit card, the authorization and clearing information for a PIN transaction is carried in a single message, allowing such transactions to be authorized and cleared simultaneously.[43] Conversely, signature transactions require the merchant to send a subsequent clearance message to the issuer after the authorization request, because the cardholder generally signs the receipt only after the issuer has approved the transaction.[44] Although a large majority of debit cards allow both PIN and signature transactions,[45] the difference between PIN and signature transaction processing explains why certain transactions, such as those for rentals, hotel accommodations, restaurant meal purchases, and other transactions where the exact purchase price is not known at the time of authorization, require signature transaction processing.[46] Because of this distinction, "[i]nternet, telephone, and mail-based merchants also generally do not accept PIN transactions. Of the eight million merchants in the United States that accept debit cards, the [Federal Reserve] Board estimates that *only* one-quarter have the ability to accept PIN transactions."[47]

Finally, settlement "involves the actual transfer of funds from the issuer to the acquirer."[48] During settlement, the issuer debits the cardholder's account, and the acquirer credits the merchant for the transaction.[49] Rather than settle

41. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 478.

42. *Id.*

43. *Id.*; Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395.

44. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 478; Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43396.

45. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395.

46. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 478 ("Car rental companies authorize transactions at pick-up to ensure that customers have enough money in their accounts to pay but postpone clearance to allow for the possibility that the guest might damage the vehicle or return it without a full tank of gas. Hotels authorize transactions at check-in but postpone clearance to allow for the possibility that the guest might trash the room, order room service, or abscond with the towels and robes. And sit-down restaurants authorize transactions for the full amount of the meal but postpone clearance to give diners an opportunity to add a tip."); Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43395.

47. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 958 F. Supp. 2d 85, 88 (D.D.C. 2013) (citation omitted).

48. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 478.

49. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43396.

each transaction individually, networks calculate and communicate to acquiring and issuing banks their net debit or credit position at the close of each day.[50] Then settlement is effected for many transactions at once through a settlement account at a commercial bank or through automated clearing house transfers.[51] If the acquiring bank is also the issuing bank for a particular transaction, that bank may authorize and settle the transaction in-house.[52]

C. *Debit Card Fees*

Throughout the transaction clearing process, the parties charge each other a variety of fees in order to settle the transaction.[53] During settlement, the acquirer credits the merchant's account the value of the transaction, less the "merchant discount" fee.[54] The merchant discount fee is composed of three different fees—the interchange fee, the network fee, and the processing fee—each of which is imposed by a different party to the transaction.[55] Thus, "[i]n comparison to a purchase made by check, for which the merchant receives the full face value, when a consumer pays with her debit card, the merchant receives less than the full purchase amount."[56]

1. Interchange Fees

Of the three fees associated with the merchant discount fee, the interchange fee is the largest cost component.[57] For this reason, the network and processing fees are set in response to the amount of the interchange fee, making the interchange fee the driving factor in determining the merchant

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50. *Id.*

51. *Id.*

52. *Id.*

53. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 479-80; Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43396.

54. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43396.

55. Hayashi, *supra* note 20, at 85; *see* Harrison J. McAvoy, *Regulation or Competition? The Durbin Amendment, the Sherman Act, and Intervention in the Card Payment Industry*, 37 SETON HALL LEGIS. J. 309, 313-14 (2013) ("By way of illustration, a typical electronic payment transaction might proceed as follows. First, a consumer making a $100 purchase will be charged $100 by his issuing bank, . . . in the form of a debit from his account . . . . Next, the acquirer will pay the merchant $98 after deducting the merchant discount fee. Of the $2 merchant discount fee, the acquirer might retain [a $0.70 processing fee] and pass on the remaining $1.30. The card network will receive $0.15 in the form of [network] fees (for coordinating the transaction), and the issuing bank will receive $1.15 in the form of an interchange fee.").

56. McConnell, *supra* note 25, at 632.

57. McAvoy, *supra* note 55, at 314.

discount.[58] Although the card networks set interchange fees, interchange fees are credited to the issuers.[59] Card networks "channel[] this fee revenue to [issuers] as an incentive for the [issuers] to choose that network for their cards."[60] Networks are motivated to incentivize issuers to issue their cards to consumers because the more network cards issued, the more network fees the card network can collect.[61]

> [The amount of an interchange fee is based on a variety of different] factors related to characteristics of the transaction, including the type of card being used . . . , the type of merchant for which the card is being used, the transaction volume of the merchant, and the form of processing (e.g., point-of-sale versus over the phone, or PIN versus signature). These factors are believed to both account for the risk associated with accepting payment from certain types of merchants and provide incentives to certain merchants to accept a particular card network's cards.[62]

Interchange fees vary depending on whether a transaction is processed over a PIN network or a signature network.[63] "Historically, PIN debit interchange fees have been lower than signature debit interchange fees, but the gap has narrowed over the last 15 years . . . ."[64] In 2009, interchange fees totaled $16.2 billion.[65] Networks reported that "[t]he average interchange fee for signature debit transactions was 56 cents, or 1.53 percent of the average transaction amount. The average interchange fee for PIN debit transactions was significantly lower, at 23 cents per transaction, or 0.58 percent of the average transaction amount."[66] There is disparity in interchange fees based on the authentication method "because signature transactions are leveraged on the credit card system, and therefore have interchange fees similar to those for credit cards. [In contrast], PIN fees are lower because the risk of nonpayment is virtually nonexistent."[67] Thus, prior to congressional intervention, card networks reported that the overall average interchange fee

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58. *Id.*
59. Hayashi, *supra* note 20, at 86.
60. *Id.*
61. McConnell, *supra* note 25, at 633.
62. McAvoy, *supra* note 55, at 314.
63. McConnell, *supra* note 25, at 633.
64. Hayashi, *supra* note 20, at 86.
65. Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43397 (July 20, 2011).
66. *Id.*
67. McConnell, *supra* note 25, at 634.

for "debit card transactions was 44 cents per transaction, or 1.15 percent of the average transaction amount."[68]

2. Merchant Discount

Merchants must pay acquirers a fee, known as the merchant discount, in order to process a debit card transaction.[69] The merchant discount is imposed by way of a reduction in the value of the transaction credited to the merchant.[70] As previously noted, the merchant discount is composed of interchange fees, network fees, and processing fees.[71] Acquirers and issuers pay network fees, also known as switch fees, to the network to compensate the network for its role in processing the transaction.[72] Processing fees are essentially a mark-up charged by the acquirer over and above the amount necessary to cover the fees charged to the acquirer by the other parties to the transaction.[73] Thus, the acquirer only retains a small percentage of the merchant discount and passes the remaining amount to the issuer and network to cover the fees those parties charge the acquirer.[74]

III. THE DURBIN AMENDMENT AND THE FEDERAL RESERVE BOARD'S RULES

A. *Legislative History*

President Barack Obama signed into law the infamous Dodd-Frank Wall Street Reform and Consumer Protection Act ("the Dodd-Frank Act") on July 21, 2010.[75] The 2008 United States financial crisis prompted enactment of this massive overhaul legislation,[76] which is the most significant financial regulatory legislation in the United States since the Great Depression.[77] The Dodd-Frank Act was constructed mainly "[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail', to protect the American taxpayer by

68. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43397.

69. *Id.* at 43396.

70. *Id.*

71. *Id.*

72. *Id.*

73. McAvoy, *supra* note 55, at 315.

74. Hayashi, *supra* note 20, at 86.

75. McGinnis, *supra* note 23, at 293.

76. *Id.* at 292-93.

77. McAvoy, *supra* note 55, at 334.

ending bailouts, [and] to protect consumers from abusive financial services practices . . . ."[78]

As the Dodd-Frank legislation was moving through Congress, Senator Richard ("Dick") Durbin took advantage of the "opportunity to implement regulations regarding bank fees on debit card transactions."[79] With a goal of enhancing transparency, competition, and choice in debit card markets,[80] Senator Durbin introduced an amendment to the Dodd-Frank Act on May 12, 2010, the "Durbin Amendment," which directly regulates debit card transactions.[81] The Durbin Amendment, "which arguably had no place in [a financial] reform bill meant to avoid a future [recession],"[82] passed the United States Senate on May 13, 2010, the day after its introduction.[83] Because there was no floor discussion or debate on the Durbin Amendment other than Senator Durbin's own words,[84] this last minute addition passed along with the rest of the Dodd-Frank Act almost unnoticed.[85] In subsequent litigation, the D.C. Circuit Court even noted that because "the Durbin Amendment was crafted in conference committee at the eleventh hour, its language is confusing and its structure convoluted."[86]

1. Interchange Fee Provision

The Durbin Amendment amends the Electronic Fund Transfer Act ("EFTA") by adding section 920, codified at 15 U.S.C. § 1693o-2.[87] The modification to EFTA contains two main provisions. The first provision, EFTA § 920(a)(2), provides that the amount of an interchange fee that an issuer may receive for processing a debit card transaction shall be "reasonable and proportional to the cost incurred by the issuer with respect to the

78. Dodd-Frank Wall Street Reform & Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

79. McGinnis, *supra* note 23, at 294.

80. Letter from Sen. Richard J. Durbin to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System 2 (Feb. 22, 2011) *available at* http://www.federalreserve.gov/SECRS/2011/April/20110405/R-1404/R-1404_022211_67820_571445654740_1.pdf.

81. 156 Cong. Rec. S3588–90 (daily ed. May 12, 2010) (statement of Sen. Richard Durbin); McAvoy, *supra* note 55, at 334.

82. McAvoy, *supra* note 55, at 335, n.178.

83. McAvoy, *supra* note 55, at 334; *see* 156 Cong. Rec. S3703–05 (daily ed. May 13, 2010).

84. McAvoy, *supra* note 55, at 334; *see* 156 Cong. Rec. S3703–05 (daily ed. May 13, 2010).

85. McAvoy, *supra* note 55, at 335.

86. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 483 (D.C. Cir. 2014).

87. Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43394 (July 20, 2011).

transaction."[88] The statute requires the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") to prescribe regulations establishing standards to assess whether interchange fees are reasonable and proportional to debit card transaction costs incurred by issuers.[89] In determining the appropriate standards, Congress directed the Federal Reserve Board to "distinguish between the incremental cost incurred by an issuer for [its role] in the authorization, clearance, and settlement of a particular electronic debit transaction, which cost shall be considered . . . , and other costs incurred by an issuer which are not specific to a particular electronic debit transaction, which costs shall not be considered."[90] In this regard, "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."[91] According to Senator Durbin,

> [t]he legislative intent behind EFTA 920(a) was to place reasonable constraints on the debit interchange price-setting that card networks like Visa and MasterCard currently perform on behalf of all their issuing banks[,] . . . [because n]etwork setting of interchange fees has negative implications for the efficiency of issuer's card operations and also prevents fee rates from being tempered by competitive market forces.[92]

2. Network Non-Exclusivity Provision

The second main provision, EFTA § 920(b), the "network non-exclusivity" provision, directs the Federal Reserve Board to issue regulations prohibiting issuers and payment card networks from restricting the number of payment card networks on which an electronic debit transaction may be processed to one exclusive network (or two or more networks that are affiliated).[93] According to Senator Durbin,"[t]he intent behind [the network non-exclusivity] provision was to inhibit the continued consolidation of the

88. Electronic Fund Transfer Act § 920, 15 U.S.C. § 1693o-2(a)(2) (2012).

89. 15 U.S.C. § 1693o-2(a)(3)(A).

90. 15 U.S.C. §1693o-2(a)(4)(B)(i)–(ii).

91. Letter from Sen. Richard J. Durbin to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System 6 (Feb. 22, 2011) *available at* http://www.federalreserve.gov/SECRS/2011/April/20110405/R-1404/R-1404_022211_67820_571445654740_1.pdf.

92. *Id.* at 5.

93. 15 U.S.C. § 1693o-2(b)(1)(A).

dominant debit networks' market power and to ensure competition and choice in the debit network market."[94]

B. The Federal Reserve Board's Rules

After the enactment of the Dodd-Frank Act in 2010, the Federal Reserve Board began collecting data from industry participants to determine the costs associated with a typical debit card transaction in order to promulgate rules as directed by the Durbin Amendment.[95]

> The Board met with debit card issuers, payment card networks, merchant acquirers, consumer groups, and industry trade associations on a number of occasions to discuss a host of issues including debit transaction processing flows, transaction fee structures and levels, fraud-prevention activities, fraud losses, routing restrictions, card-issuing arrangements, and incentive programs.[96]

1. The Federal Reserve Board's Proposed Rules

On December 16, 2010, in a live telecast meeting, the Federal Reserve Board "approved proposing a rule to implement the Durbin Amendment . . . ."[97] Shortly thereafter, "[o]n December 28, 2010, the [Federal Reserve Board] issued a [notice of proposed rulemaking ("NPRM"),] implementing the Durbin Amendment and requesting public comments."[98]

a. Interchange fee standards

In an effort to "include[] only those costs that are specifically mentioned for consideration in the statute," the Federal Reserve Board proposed that the interchange fee standard be "limited to those [costs] associated with authorization, clearing, and settlement of a transaction."[99] Although the

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94. Letter from Sen. Richard J. Durbin to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System 11 (Feb. 22, 2011) *available at* http://www.federalreserve.gov/SECRS/2011/April/20110405/R-1404/R-1404_022211_67820_571445654740_1.pdf.

95. Debit Card Interchange & Routing, 75 Fed. Reg. 81722, 81724 (Dec. 28, 2010).

96. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 958 F. Supp. 2d 85, 92 (D.D.C. 2013).

97. Christine Edwards, Jerry Loeser & Jacob Calvani, *Implementing the Durbin Amendment: What was the Fed Thinking?*, WINSTON & STRAWN, LLP (Apr. 2011), *available at* http://cdn2.winston.com/images/content/7/8/v2/782.pdf.

98. *Nat'l Ass'n of Convenience Stores*, 958 F. Supp. 2d at 93; *see* Debit Card Interchange & Routing, 75 Fed. Reg. at 81722.

99. Debit Card Interchange & Routing, 75 Fed. Reg. at 81734-35.

statute specifically requires consideration of the "incremental" cost of authorization, clearance, and settlement of a particular transaction, the Board never settled on an applicable definition of "incremental."[100] Regardless, the Board proposed that "the interchange fee standard allow for the inclusion of the per-transaction value of costs that vary with the number of transactions (i.e., average variable cost) within the reporting period."[101] In the NPRM,

> [t]he Board noted that, by focusing on the issuer's variable, per-transaction [authorization, clearance, and settlement] costs, it was carrying out Congress's mandate to establish standards to assess whether an interchange fee is reasonable and proportional to the cost incurred by the issuer with respect to the transaction.[102]

Consequently, the Board suggested that network processing fees, fixed costs,[103] overhead costs, cardholder rewards programs, fraud prevention and fraud losses be excluded from recovery by issuers under the interchange fee standard because these costs are not attributable to the transaction.[104] The Board requested comments on whether it should consider and allow recovery through interchange fees of transaction costs beyond those related to authorization, clearance, and settlement, and if so, what other transaction costs should be considered allowable costs.[105]

With these allowable costs in mind, the Federal Reserve Board originally proposed two alternatives to regulate interchange fee standards.[106] Although the Board only planned to adopt one alternative, it requested comments on both proposed alternative standards.[107]

The first alternative proposed "an issuer-specific approach combined with a safe harbor and a cap."[108] Under this alternative, an issuer could have charged and received interchange fees at or below the safe harbor amount, or based on a determination of its individual allowable costs, up to a specified

100. *Id.* at 81735.

101. *Id.*

102. *Nat'l Ass'n of Convenience Stores*, 958 F. Supp. 2d at 93.

103. Fixed costs, which are incurred regardless of transaction volume, make it possible for banks to process debit card transactions. Notably, fixed costs include the cost of equipment, hardware, and software. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 489 (D.C. Cir. 2014).

104. Debit Card Interchange & Routing, 75 Fed. Reg. at 81735, 81760.

105. *Id.* at 81735.

106. *Id.* at 81736.

107. *Id.*

108. *Id.*

cap.[109] The safe harbor limit was set at seven cents per transaction, meaning that any interchange fee charged at seven cents or below would automatically be in compliance with the regulatory standard, regardless of the issuer's allowable per-transaction cost.[110] The proposed cap on interchange fees was set at twelve cents per debit card transaction; thus, had the first alternative proposal been adopted, an issuer could not have received an interchange fee above the twelve-cent cap regardless of its allowable cost calculation.[111] Therefore, an issuer could charge an interchange fee greater than seven cents, but not more than twelve cents, if it chose to determine its individual allowable costs.[112]

> [T]his approach reduces administrative burden [sic] on those issuers that choose to rely on the safe harbor, rather than determine their allowable costs, and allows issuers with costs above the safe harbor to receive an interchange fee directly linked to their costs, up to the level of the cap. At the same time, for an issuer with costs below the safe harbor value, this approach provides a reward for efficient production while also encouraging cost reductions to maximize the spread between the issuer's costs and the safe harbor value.[113]

The second alternative interchange fee standard proposed a stand-alone cap.[114] Under this alternative, an issuer could charge and receive interchange fees up to the specified cap, regardless of the issuer's actual allowable costs.[115] The Federal Reserve Board proposed that as long as an interchange transaction fee was no greater than twelve cents per transaction, it would be considered per se reasonable and proportional to the issuer's cost.[116]

Instead of the Federal Reserve Board proposing standards and factors for assessing whether a fee is reasonable and proportional to a transaction's cost, the Board's

> staff explained that it chose . . . to recommend a simple rate cap in order to reduce the administrative burden that may come from having to demonstrate various and multiple categories of costs

109. *Id.*
110. *Id.*
111. *Id.*
112. *Id.* at 81738.
113. *Id.*
114. *Id.* at 81736.
115. *Id.* at 81738.
116. *Id.*

> associated with rates assessed. [A] memorandum from the staff to the Board explains that the administrative burden the staff sought to avoid is in implementation and enforcement, a burden seemingly not on issuers, but on the Board and its staff.[117]

Although most people expected the Federal Reserve Board to propose standards enabling issuers to recover costs associated with their debit card programs and a reasonable rate of return, the Board's twelve-cent-per-transaction cap would have only allowed "[eighty] percent of issuers to recoup all of their per transaction costs, but not costs such as card production and distribution, research and development, marketing, responding to customer inquiries and overhead."[118] In other words, while the twelve-cent cap would have allowed most issuers to recover costs associated with individual transactions, it would not have allowed any of those issuers to recover enough revenue to remain in business, and "[twenty] percent of issuers [would] not even [have been] able to recoup all of their per transaction costs."[119]

b. Network exclusivity provisions

The Federal Reserve Board also proposed two alternative approaches to implement the Durbin Amendment's prohibition against network exclusivity agreements. The first alternative prohibited issuers and payment card networks from restricting the number of networks over which an electronic debit card transaction may be carried to fewer than two unaffiliated networks.[120] The second alternative prohibited issuers and networks from restricting the number of networks over which electronic debit transactions may be carried to less than two unaffiliated networks for each method of authorization.[121] Thus, under the first alterative, it would be sufficient for an issuer to issue a debit card that could be processed over one signature-based network and one PIN-based network, provided the networks are not affiliated.[122] However, under the second alternative, an issuer that used both signature and PIN-based authorization would have to enable its debit cards to be processed over two unaffiliated signature-based networks and two unaffiliated PIN-based networks.[123]

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117. Edwards, *supra* note 97, at 1.

118. *Id.* at 2.

119. *Id.*

120. Debit Card Interchange & Routing, 75 Fed. Reg. at 81726.

121. *Id.* at 81726-27.

122. *Id.*

123. *Id.*

c. Comments received

In response to the proposed regulations issued and their potential consequences, the Federal Reserve Board received comments from approximately 11,570 commentators, including trade groups, merchants, payment card networks, payment processors, individual consumers, and other interested parties.[124] Of these groups, "merchants and groups representing such merchants hoped the [Board] would lower the maximum interchange fee cap even lower, [while] payment card networks and issuers protested the lower cap of twelve cents because of lost revenue and diminished debit card services."[125]

Merchants and merchant trade groups overwhelmingly supported the proposal to limit allowable costs to only the variable costs of authorization, clearance, and settlement.[126] However, issuers and card networks advocated for the expansion of allowable costs "to include such costs as the payment guarantee costs, fraud losses, network processing fees, customer service costs, the costs of rewards, fixed costs, and a return on investment."[127] Issuers and card networks noted that the EFTA § 902(a)(4)(B) does not require that allowable costs be *limited* to the incremental costs of authorization, clearance, and settlement of a particular transaction, only that such cost be *considered*.[128] Even Senator Durbin authored a comment letter analyzing the proposed regulations and supporting certain provisions of the proposed rules.[129] With respect to allowable costs, Senator Durbin stated:

> The Board properly proposes to limit allowable costs to the costs of authorization, clearance, and settlement. . . . [T]hese are the costs Congress deemed appropriate for a debit card network to set on behalf of its issuers. Thus, the Board's proposed calculation of incremental costs as average variable cost[s] . . . is consistent with the legislative intent, and the inclusion of other cost[s] in this

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124. Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43402 (July 20, 2011).

125. Sandwith, *supra* note 17, at 233.

126. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43424.

127. *Id.* at 43402.

128. *Id.* at 43425.

129. *See generally* Letter from Sen. Richard J. Durbin to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System (Feb. 22, 2011) *available at* http://www.federalreserve.gov/SECRS/2011/April/20110405/R-1404/R-1404_022211_67820_571445654740_1.pdf.

> analysis would be inconsistent with the language and intent of EFTA Section 920.[130]

Thus, the Durbin Amendment's namesake sponsor supported the Board's proposed allowable costs and opposed the inclusion of additional costs beyond those related to authorization, clearance, and settlement of a specific transaction in the interchange fee standard.

With respect to the two interchange fee standard alternatives, merchants and their trade groups supported the first, issuer-specific alternative "arguing that issuer-specific fees would be a proxy for fees in a competitive issuer market place and that many covered issuers had per-transaction authorization, clearance, and settlement costs significantly below the proposed 12-cent cap."[131] Further, the merchant groups urged the Federal Reserve Board to lower the cap.[132] Issuers and networks, on the other hand, "urged the Board to adopt a more flexible approach to the standards by prescribing guidelines rather than a cap."[133] Given the two alternatives, issuers generally favored the second, stand-alone cap alternative, but advocated that the safe harbor level be raised "to a level that permits a 'substantial majority' of issuers to avail themselves of it."[134] Like the merchant groups, Senator Durbin supported the first alternative interchange fee standard, declaring it to be "more consistent with the legislative intent of constraining network-established interchange fees to levels that reflect the incremental authorization, clearance and settlement costs incurred by a regulated issuer for a particular transaction."[135] Although Senator Durbin was unsure whether the specific safe harbor and cap amounts proposed were proper, he argued that the first alternative could be deemed "reasonable and proportional" as contemplated by the amendment, because it offered standards to consider the average variable costs of authorization, clearance, and settlement constrained by a maximum fee.[136]

In response to the two alternative approaches to implement the network non-exclusivity provision of the Durbin Amendment, issuers and networks

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130. *Id.* at 7.

131. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43402.

132. *Id.* Some merchant groups suggested that the Federal Reserve Board drop the cap to as low as four cents. *Id.*

133. *Id.*

134. *Id.*

135. Letter from Sen. Richard J. Durbin to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System 7 (Feb. 22, 2011) *available at* http://www.federalreserve.gov/SECRS/2011/April/20110405/R-1404/R-1404_022211_67820_571445654740_1.pdf.

136. *Id.*

preferred the first alternative, requiring two unaffiliated networks for processing without regard to the method of authentication.[137] Merchants preferred the second alternative because they believed that this alternative would provide the most routing choices and the most market discipline on interchange and network fees.[138] In his comment letter, Senator Durbin described the congressional intent behind the network non-exclusivity provision stating, "[T]his provision was to inhibit the continued consolidation of the dominant debit networks' market power and to ensure competition and choice in the debit network market."[139] Senator Durbin never endorsed either network non-exclusivity provision proposed by the Board, but rather stressed the importance of prohibiting network exclusivity arrangements in the final rule in order to enhance competition in the debit card industry.[140]

2. The Federal Reserve Board's Final Rules

In response to the thousands of comments received, the Federal Reserve Board drafted a final rule, which was published on July 20, 2011, and went into effect on October 1 of that year.[141]

a. The final interchange fee regulation

In adopting a final rule establishing a standard for assessing whether interchange transaction fees are reasonable and proportional to issuer costs, the Federal Reserve Board ultimately settled on a modified version of the second alternative, a stand-alone cap, but raised the cap from twelve cents per transaction to twenty-one cents per transaction, plus an *ad valorem* component of .05 percent of the transaction's value, which corresponds to the average per-transaction fraud losses of the median issuer.[142] Although the final interchange fee cap of twenty-one cents per transaction is almost double the proposed cap, it is still more than half the amount of the average

137. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43403.

138. *Id.*

139. Letter from Sen. Richard J. Durbin to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System 11 (Feb. 22, 2011) *available at* http://www.federalreserve.gov/SECRS/2011/April/20110405/R-1404/R-1404_022211_67820_571445654740_1.pdf.

140. *Id.* at 13.

141. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 958 F. Supp. 2d 85, 94 (D.D.C. 2013); Debit Card Interchange Fees & Routing, 12 C.F.R. § 235 (2014).

142. 12 C.F.R. § 235.3; Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43422; McConnell, *supra* note 25, at 642.

interchange fee pre-Durbin.[143] The Board justified the increase in allowable interchange fees

> after concluding that the language and purpose of the Durbin Amendment allow the Board to consider additional costs not explicitly excluded from consideration by the statute. According to the Board, [15 U.S.C.] § 1693o-2(a)(4)(B) on the one hand *requires* the Board to consider incremental [authorization, clearance, and settlement] costs incurred by issuers, and on the other hand *prohibits* consideration of any issuer costs that are not specific to a particular transaction; but it is *silent* with respect to costs that fall into neither category (*e.g.*, costs specific to a particular transaction but are not incremental [authorization, clearance, and settlement] costs). The Board concluded that it had discretion to consider costs on which the statute is silent.[144]

Additionally, based on survey data and comments in response to the proposed rules, the Board found that issuers incur transaction costs other than the variable authorization, clearance, and settlement costs originally proposed as the only allowable costs in the interchange fee, which are necessary for each electronic debit transaction.[145] As a result, the Federal Reserve Board's final interchange transaction fee standard considers authorization, clearance, and settlement costs, as well as "(1) fixed costs related to processing a particular transaction, such as network connectivity and software, hardware, equipment, and labor; (2) transaction monitoring costs; (3) an allowance for fraud losses (the *ad valorem* component); and (4) network processing fees."[146]

b. The final non-network exclusivity regulation

With respect to network exclusivity, the Federal Reserve Board adopted the first alternative proposed, requiring that two unaffiliated networks be available for each debit card, not for each authorization method.[147] Consequently, issuers are in compliance with the regulation if they have one payment card network available for signature based transactions and a

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143. *See* Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43397 (stating that the pre-Durbin average interchange fee was forty-four cents per transaction); Debit Card Interchange Fees & Routing, 75 Fed. Reg. at 81738 (stating the proposed interchange fee cap is twelve cents per transaction).

144. *Nat'l Ass'n of Convenience Stores*, 958 F. Supp. 2d at 94-95 (citations omitted).

145. *Id.* at 95.

146. *Id.*

147. Debit Card Interchange Fees & Routing, 76 Fed. Reg. at 43447.

second, unaffiliated payment card network available for PIN based transactions.[148] In finalizing this rule, the Federal Reserve Board concluded that "[t]he plain language of the statute does not require that there be two unaffiliated payment card networks available to the merchant for each method of authentication . . . [because] the statute does not expressly require issuers to offer multiple unaffiliated signature and multiple unaffiliated PIN debit card network choices on each card."[149]

Unsurprisingly, the final interchange transaction fee standards and network exclusivity provision have "been criticized for seemingly bending to the card issuers' and banks' lobbying efforts and favoring those parties more than Congress intended."[150] In a press release issued shortly after the publication of the Federal Reserve Board's final rule, Senator Durbin expressed his disapproval of certain aspects of the Board's final rules.[151] However, Senator Durbin is not the only one displeased with the Board's final rule—merchants and retailers, issuers, and networks are all unsatisfied with the outcome of the Durbin Amendment's implementation.[152]

IV. CHALLENGE TO THE FINAL RULE—*NACS V. BOARD OF GOVERNORS*

Upset by the "nearly doubled . . . interchange fee cap (as compared to the proposed rule) and . . . the less restrictive anti-exclusivity option, several merchant groups, including NACS, the organization formerly known as the National Association of Convenience Stores, filed suit in district court"[153] on

148. *Id.* at 43446.

149. *Id.* at 43447.

150. McConnell, *supra* note 25, at 643.

151. Press Release, Senator Richard J. Durbin, Durbin Statement on the Final Federal Reserve Rule on Interchange Fees (June 29, 2011), *available at* http://www.durbin.senate.gov/newsroom/press-releases/durbin-statement-on-the-final-federal-reserve-rules-on-interchange-fees ("I am disappointed . . . to see that the Federal Reserve has yielded to the big banks in certain parts of its final rulemaking. The inflated cap . . . that the Fed announced . . . will unnecessarily take money out of the pockets of consumers and small businesses and give it to big banks that neither need it nor deserve it.").

152. Donna Borak & Rob Blackwell, *Everybody Hates Interchange: Bankers, Retailers Object to Fed Final Rule*, Am. Banker (June 29, 2011, 6:57 PM), http://www.americanbanker.com/issues/176_125/interchange-fed-final-rule-1039602-1.html; David C. John, *Consumers Lose, No One Happy, With Final Fed Swipe Fee Regulations*, Daily Signal (July 5, 2011), http://dailysignal.com/2011/07/05/consumers-lose-no-one-happy-with-final-fed-swipe-fee-regulations/.

153. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 481 (D.C. Cir. 2014).

November 22, 2011, shortly after the Board's final rules went into effect.[154] The plaintiff merchant groups, consisting of four major trade associations and two individual retail operators, sued the Federal Reserve Board "seeking a declaratory judgment that the Final Rule's interchange fee and network non-exclusivity provisions are arbitrary, capricious, an abuse of discretion, and otherwise not in accordance with the law."[155] The plaintiffs argued that in issuing the Final Rule, the Federal Reserve Board unreasonably interpreted the Durbin Amendment by ignoring congressional intent.[156] Specifically, the plaintiffs asserted that in establishing "reasonable and proportional" interchange transaction fee standards, the Federal Reserve Board acted unreasonably and beyond the limits of its statutory authority because "the Durbin Amendment limits the [Federal Reserve] Board's consideration of allowable costs to the 'incremental cost' of authorization, clearance and settlement of a particular electronic debit transaction" and the Board included other costs in the fee interchange fee standard.[157] As to the network exclusivity provisions, the plaintiffs argued that the Federal Reserve Board "disregarded the plain meaning of the Durbin Amendment and misconstrued the statute by adopting a network non-exclusivity rule requiring all debit *cards* be interoperable with at least two unaffiliated payment networks, rather than requiring that all debit *transactions* be able to run over at least two unaffiliated networks."[158]

On March 2, 2012, the plaintiffs moved for summary judgment, "arguing that the Final Rule's interchange transaction fee and network non-exclusivity regulations should be declared invalid under the Administrative Procedure Act, because the Board impermissibly implemented the Durbin Amendment's statutory command and thus exceeded its authority."[159] The Federal Reserve Board filed a cross-motion for summary judgment on April

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154. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 958 F. Supp. 2d 85, 95-96 (D.D.C. 2013).

155. *Id.*

156. *Id.* at 96.

157. *Id.*

158. *Id.*

159. *Id.* (citing 5 U.S.C. § 706(2) ("To the extent necessary to decision and when presented, the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action. The reviewing court shall (1) compel agency action unlawfully withheld or unreasonably delayed; and (2) hold unlawful and set aside agency action, findings, and conclusions found to be (A) arbitrary, capricious, and abuse of discretion, or otherwise not in accordance with law; . . . (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right . . . .")).

13, 2012, asserting that the plaintiffs' claims against the Board lacked merit.[160] In addition to hearing the parties' arguments, the court received amicus curiae briefs from three other outside parties: "(1) a consortium of major nationwide bank and credit union trade associations in the United States; (2) Senator Richard J. Durbin, a member of Congress and the primary author of the Durbin Amendment; and (2) a group of convenience stores, quick-service restaurants and specialty coffee shops that operate small business franchises and licensed stores."[161] Senator Durbin along with the group of convenience stores, quick-service restaurants, and other small business franchises filed their briefs in support of the plaintiffs' motion, while the group of various financial institutions supported neither party.

A. *Outcome at the District Level: The Federal Reserve Overstepped its Statutory Authority*

After thorough analysis, Judge Richard J. Leon of the United States District Court for the District of Columbia granted summary judgment to the plaintiff merchants.[162] The court held that the Federal Reserve Board's Final Rule regarding the interchange transaction fees and the network non-exclusivity provisions exceeded the Board's statutory authority as granted by the Durbin Amendment.[163]

1. Standard of Review

While evaluating the Federal Reserve Board's final regulations under the Administrative Procedure Act, Judge Leon properly recognized that "the Court must set aside agency action that exceeds the agency's statutory jurisdiction, authority, or limitations."[164] In order to determine whether the Federal Reserve Board overstepped its statutory boundaries when it implemented the final rules, the court applied the two-step framework

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160. *Id.* (citations omitted).

161. *Id.* at 96, nn.20-22; *see generally* Amici Curiae Brief of the Clearing House Ass'n L.L.C. et al. (No. 22). Amici are The Clearing House Association L.L.C., American Bankers Association, Consumer Bankers Association, Credit Union National Association, The Financial Services Roundtable, Independent Community Bankers of America, Mid-Size Bank Coalition of America, National Association of Federal Credit Unions, and National Bankers Association. *Id. See generally* Amicus Curiae Brief of Senator Richard J. Durbin (No. 27); Amici Curiae Brief of 7-Eleven, Inc., et al. (No. 30). Amici are 7-Eleven, Inc., Auntie Anne's Inc., Burger King Corporation, CKE Restaurants, Inc., International Dairy Queen, Inc., Jack in the Box, Inc., Starbucks Corporation, and The Wendy's Company. *Id.*

162. *Nat'l Ass'n of Convenience Stores*, 958 F. Supp. 2d at 115.

163. *Id.* at 115-16.

164. *Id.* at 97 (quoting 5 U.S.C. § 706(2)(C)).

analysis developed in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*[165]

Under the *Chevron* analysis, a reviewing court must first determine whether Congress has directly addressed the specific question at issue.[166] In doing so and in deciding "whether the intent of Congress is clear . . . , the court must exhaust the traditional tools of statutory construction, including textual analysis, structural analysis, and (when appropriate) legislative history."[167] If the congressional intent is clear after exhausting these tools of statutory interpretation, the court, and the relevant administrative agency, must "give effect to the unambiguously expressed intent of Congress."[168] However, if after utilizing the methods of statutory interpretation, the court decides that the statute at issue is silent, ambiguous, or unclear on the contested issue, the court must move on to the second step in the *Chevron* analysis.[169] Under this second step, the court is required to defer to any agency interpretation of the statute, as long as the agency interpretation "is based on a permissible construction of the statute."[170] An agency's construction of a statute is presumed to be permissible "unless it is arbitrary or capricious in substance, or manifestly contrary to the statute."[171]

2. The Interchange Fee Regulation is Impermissible

In applying the *Chevron* standard to the interchange fee standards, the court properly recognized that if the Durbin Amendment and Congress's intent for enacting the statute were clear and unambiguous as to the issuer costs to be considered in the interchange fee standard, the Federal Reserve Board had no authority to enact interchange fee regulations which considered costs beyond those expressed by Congress in the Amendment.[172] However, if the court found that the Durbin Amendment was ambiguous or silent on whether some other issuer costs could be considered in establishing the interchange fee standards, the Federal Reserve Board was entitled to clarify those ambiguities and consider and include issuer costs not mentioned

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165. *Id.*

166. *Id.*

167. *Id.* (quoting *Chevron*, 467 U.S. at 843 n.9) (internal quotation marks omitted).

168. *Id.* (quoting *Chevron*, 467 U.S. at 842-43) (internal quotation marks omitted).

169. *Id.*

170. *Id.* (citing *Chevron*, 467 U.S. at 843).

171. *Id.* (quoting *Mayo Found. for Med. Educ. & Research v. United States*, 131 S. Ct. 704, 711 (2011)) (internal quotation marks omitted).

172. *See id.* at 99-110.

in the statute when establishing the interchange fee standards, provided the final rule was based on a permissible construction of the statute.[173]

Conveniently,[174] as the court put it, the Federal Reserve Board argued that it was entitled to deference under the *Chevron* analysis because the Durbin Amendment was silent and ambiguous "with respect to issuer costs not explicitly addressed in the statute,"[175] and their final interchange fee standard was a reasonable construction of the statute.[176] However, Judge Leon agreed with the plaintiffs, who argued that the Federal Reserve Board's "interchange transaction fee standard [was] plainly foreclosed by the text, structure, and purpose of the Durbin Amendment and [was] arbitrary, capricious, and contrary to law."[177] In examining the statutory language, plain text of the statute, legislators' statements, and legislative history, the court found that the congressional intent of the Durbin Amendment was clear, and that Congress intended that only those issuer costs specifically enumerated in the statute were to be included in the establishment of the interchange transaction fee standards.[178] The court easily came to the conclusion that the Durbin Amendment's statutory language and legislative history evidenced Congress's intent to bifurcate the entire universe of costs associated with interchange fees—those incremental authorization, clearance, and settlement costs includable in the interchange transaction fee standards and *all* other costs which Congress intended to be excluded from consideration.[179] Thus, according to the court, the Federal Reserve Board's inclusion of other issuer costs in the final interchange fee standard could not survive scrutiny under the first step of the *Chevron* analysis.[180]

3. The Network Non-Exclusivity Regulation is Invalid

After employing the *Chevron* analysis a second time, the court again agreed with the plaintiffs and found that the Federal Reserve Board's final rule regarding network non-exclusivity was invalid under the Administrative Procedure Act.[181] The plaintiffs contended that the Federal Reserve Board's determination that the Durbin Amendment required "issuers and networks

173. *See id.*
174. *Id.* at 100.
175. *Id.* at 99.
176. *Id.*
177. *Id.* (citation omitted).
178. *Id.*
179. *Id.* at 100.
180. *Id.* at 99.
181. *Id.* at 109.

to make available two unaffiliated networks for *each debit card*, not for *each method of authentication* (signature and PIN)" ignored the Durbin Amendment's language and purpose.[182] The plaintiffs argued that the Durbin Amendment required issuers to offer merchants a choice between multiple unaffiliated networks for each transaction, not only for each card.[183]

In employing the first step of the *Chevron* analysis, the court easily found that the language of the network non-exclusivity provision of the Durbin Amendment and the relevant legislative history indicated that "the statute instruct[ed] the Board to ensure that issuers and networks stop restricting merchants' ability to route *each transaction* over different networks."[184] Judge Leon agreed with the plaintiffs that in enacting the Durbin Amendment, "Congress's focus was on the number of networks over which each *transaction*—as opposed to each debit card—can be processed."[185] Further, the court explained, Congress aimed to end network exclusivity agreements in order to promote merchants' choice, "not restrict that choice or even preserve the status quo."[186] Therefore, because Congress's intent was clear and unambiguous, the court held that the Federal Reserve Board was not authorized to enact regulations beyond those expressed by the statute and that in doing so, the Board erred by enacting its network non-exclusivity final rule, since it was inconsistent with the Durbin Amendment and failed under the first step of *Chevron*.[187]

B. The D.C. Circuit's Ruling: The Federal Reserve's Regulations are Consistent with the Durbin Amendment

Shortly after the district court's ruling, the Federal Reserve Board appealed Judge Leon's decision to the United States Court of Appeals for the District of Columbia Circuit.[188] Just as it had done in the lower court, the Federal Reserve Board argued that both the final interchange fee rule and the final network non-exclusivity rule are reasonable constructions of ambiguous statutory language and are thus permissible under the Administrative Procedure Act.[189] The merchant groups maintained that the district court's

182. *Id.* at 110 (citations omitted).

183. *Id.*

184. *Id.*

185. *Id.*

186. *Id.* at 112.

187. *Id.*

188. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 482 (D.C. Cir. 2014).

189. *Id.*

ruling should be upheld because the court properly applied the *Chevron* analysis with respect to the Federal Reserve Board's final rules regarding interchange fees and network non-exclusivity provisions.[190]

Because the District Court reviewed the Federal Reserve Board's rulemaking under the Administrative Procedure Act, the circuit court recognized that it had the authority to review the "administrative [agency] action directly, according no particular deference to the judgment of the District Court."[191] Therefore, the court applied the two-step *Chevron* framework,[192] rather than giving deference to the district court's opinion.[193] In so doing, Judge David Tatel, writing for the unanimous three-judge panel,[194] reversed the district court's decision and held that the Federal Reserve Board's final interchange fee standard and network non-exclusivity rule were appropriate.[195]

1. The Interchange Fee Standard is Proper

In administering the *Chevron* analysis, the court agreed with the Federal Reserve Board that the Durbin Amendment contained several instances of ambiguous language.[196]

> Recall[ing] that [EFTA] section 920(a)(4)(B)(i) *requires* the Board to include 'incremental costs incurred by an issuer for [its role] in the authorization, clearance, or settlement of a particular electronic debit transaction,' and that section 920(a)(4)(B)(ii) *prohibits* the Board from including 'other costs incurred by an issuer which are not specific to a particular electronic debit transaction,'[197]

the court deferred to the Board's judgment with respect to a third category of costs.[198] This "third category of costs [are] those that are not 'incremental' [authorization, clearance, or settlement] costs but are specific to a particular

190. *See id.* at 483, 493.

191. *Id.* (quoting *In re* Polar Bear Endangered Species Act Listing & § 4(d) Rule Litig., 720 F.3d 354, 358 (D.C. Cir. 2013) (internal quotation marks omitted)).

192. *See supra* Part IV.A.1.

193. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 482-83.

194. The D.C. Circuit Court panel consisted of Circuit Judge David S. Tatel and Senior Circuit Judges Harry T. Edwards and Steven F. Williams. *Id.* at 477.

195. *Id.* at 496.

196. *Id.* at 488.

197. *Id.* at 483.

198. *See id.* at 488.

transaction."[199] Regarding this third category of costs, the Board argued that "it may but need not allow issuers to recover costs falling within this third category, subject of course to other statutory constraints."[200] After thorough analysis, the court held that

> [g]iven the Durbin Amendment's ambiguity as to the existence of a third category of costs, we must defer to the [Federal Reserve] Board's reasonable determination that the statute splits costs into three categories: (1) incremental [authorization, clearance, and settlement] costs, which the Board must allow issuers to recover; (2) costs specific to a particular transaction, other than incremental [authorization, clearance, or settlement] costs, which the Board may, but need not, allow issuers to recover; and (3) costs not specific to a particular transaction, which the Board may not allow issuers to recover.[201]

Because the court held that the "Board reasonably interpreted the Durbin Amendment as allowing issuers to recover some costs in addition to incremental [authorization, settlement, and clearance] costs," the court considered "whether the Board reasonably concluded that issuers can recover the four specific types of costs the merchants challenge[d]: 'fixed' [authorization, clearance, and settlement] costs, network processing fees, fraud losses, and transactions-monitoring costs."[202] In making this determination, the court likened the Board's inclusion of these costs to agency ratemaking, noting that "whether issuers or merchants should bear certain costs is 'far from an exact science and involves policy determinations in which the [Board] is acknowledged to have expertise.'"[203] The court recognized that in the agency ratemaking area, judicial review is "particularly deferential, as the Board is the expert body Congress has designated to weigh the many factors at issue when assessing whether a rate is just and reasonable."[204]

The merchant-appellees argued that fixed costs, which the court identified as those costs that issuers incur regardless of the transaction volume, as opposed to variable costs which increase with the transaction volume, are, "[b]y definition, . . . not 'specific' to any 'particular' transaction and fall

199. *Id.* at 483.

200. *Id.*

201. *Id.* at 488.

202. *Id.* at 489.

203. *Id.* (quoting Time Warner Entm't Co. v. FCC, 56 F.3d 151, 163 (D.C. Cir. 1995)).

204. *Id.* (quoting Time Warner Entm't Co. v. FCC, 56 F.3d 151, 163 (D.C. Cir. 1995)).

squarely within the statute's excludable costs provision."[205] However, the court sided with the Board, stating that the Board's decision to interpret the statute as not preventing the recovery of fixed costs was reasonable because "the Board interpreted [EFTA] section 920(a)(4)(B) as allowing issuers to recover costs they must incur in order to effectuate particular electronic debit card transactions but precluding them from recovering other costs too remote from the processing of actual transactions."[206] In other words, "the Board reasonably distinguished between costs issuers could recover and those they could not recover on the basis of whether those costs are 'incurred in the course of effecting' transactions."[207] Focusing on this deferential treatment, the court reviewed each of the four costs at issue in turn.[208]

Although the merchant-appellees argued that "allowing issuers to recover network processing fees through the interchange fee would [be inconsistent with] section 920(a)(8)(B), which requires the Board to ensure that 'a network fee is not used to directly or indirectly compensate an issuer with respect to an electronic debit transaction,'" the court easily found that "[n]etwork processing fees, which issuers pay on a per-transaction basis, [and] are . . . specific to particular transactions," were properly considered in establishing the interchange fee standard.[209] Contrary to the merchant-appellees' argument, the court noted that "section 920(a)(8)(B) is designed to prevent issuers and networks from circumventing the Board's interchange fee rules, not to prevent issuers from recovering reasonable network processing fees through the interchange fee."[210]

The court held that the Federal Reserve Board had discretion to include the cost of fraud losses to issuers in the interchange fee standard even though a separate, "fraud-prevention adjustment [provision], which allows issuers to recover fraud-prevention costs if those issuers comply with the Board's fraud-prevention standards," is in the statute.[211] The Board determined, and the court agreed, that fraud loss costs could be included in the interchange fee standard rather than in the fraud prevention adjustment "because fraud losses result from the *failure* of fraud-prevention, they do not themselves qualify as fraud-prevention costs."[212]

205. *Id.*

206. *Id.* at 490.

207. *Id.*

208. *Id.* at 489-93.

209. *Id.* at 490-91.

210. *Id.* at 491.

211. *Id.*

212. *Id.*

Finally, regarding transactions-monitoring costs, "the paradigmatic example of fraud-prevention costs," the Board

> distinguished between '[t]ransactions monitoring systems [that] assist in the authorization process by providing information to the issuer before the issuer decides to approve or decline the transaction,' which the Board placed outside the fraud-prevention adjustment, and 'fraud-prevention activities, . . . that prevent fraud with respect to transactions at times other than when the issuer is effecting the transaction'—for instance the cost of sending 'cardholder alerts . . . inquir[ing] about suspicious activity'—which the Board determined should be 'considered in connection with the fraud-prevention adjustment.'[213]

Because the court "agree[d] with the Board that transactions-monitoring costs can reasonably qualify both as costs 'specific to a particular . . . transaction' (section 920(a)(4)(B)) and as fraud-prevention costs (section 920(a)(5))."[214] the Court concluded that the Board might have authority to allow issuers to recover transaction-monitoring costs via interchange fees regardless of whether those issuers fall in compliance with the fraud-prevention standards.[215] However, the court remanded this aspect of the ruling back to the Federal Reserve Board for explanation because the Board failed to explain why it exercised its discretion in this manner.[216]

After administering the two-step *Chevron* analysis to determine whether the Federal Reserve Board's rulemaking complied with the Administrative Procedure Act, the court held that due to ambiguities in the Durbin Amendment's statutory language, deference was properly given to the Board

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213. *Id.* at 492 (quoting Debit Card Interchange Fees & Routing, 76 Fed. Reg. 43394, 43430-31 (July 20, 2011)).

214. *Id.*

215. *Id.*

216. *Id.* The Federal Reserve Board failed to meet the standard described in *Motor Vehicle Mfrs. Ass'n of the U.S. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29 (1983), which requires "an agency must cogently explain why it has exercised its discretion in a given manner." *Motor Vehicle Mfrs. Ass'n*, 463 U.S. at 48. The *Nat'l Ass'n of Convenience Stores* court noted that the Board likely had "a reasonable justification for determining that transactions-monitoring costs properly fall outside the fraud-prevention adjustment," however, the Board has not yet articulated such a justification. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 493. According to the Supreme Court, "[i]f the record before the agency does not support the agency action, if the agency has not considered all relevant factors, or if the reviewing court simply cannot evaluate the challenged agency action on the basis of the record before it, the proper course, except in rare circumstances, is to remand to the agency for additional investigation or explanation." *Id.* (quoting Fla. Power & Light Co. v. Lorion, 470 U.S. 729, 744 (1985)).

to resolve the ambiguities based on a reasonable construction of the statute.[217] Thus, the court examined whether the Board's inclusion of the costs at issue in the interchange fee final rule was reasonable. The court determined that, based on the construction of the statute, the Board had reasonably interpreted the ambiguous statute by including the third category of costs in its final rule.[218] Therefore, the circuit court overruled the district court, holding that the twenty-one cent cap on interchange fees is permissible under the Durbin Amendment.

2. The Network Non-Exclusivity Regulation is Valid

With respect to the Federal Reserve Board's network non-exclusivity rule, which requires issuers and networks to offer at least two unaffiliated networks for each debit card rather than each method of authentication, the court deferred to the Federal Reserve Board's statutory interpretation.[219] The court quickly recognized that "Congress directed the Board to issue rules that would accomplish a particular objective, leaving it to the Board to decide how best to do so, and the Board's rule seems to comply perfectly with Congress's command."[220]

The Board and the merchant groups agree that Congress's intent in enacting the network non-exclusivity provision of the Durbin Amendment was to increase competition among networks in order to drive down network processing fees.[221] While the merchants argued that requiring two unaffiliated networks for each debit transaction would increase competition among networks, thereby fulfilling Congress's wishes, the Board presented "evidence demonstrating that its rule has, as predicted, substantially increased network competition."[222] Therefore, the court reasoned that "[g]iven that the Board's rule advances the Durbin Amendment's purpose, we decline to second-guess its reasoned decision to reject an alternative option that might have further advanced that purpose."[223]

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217. *Nat'l Ass'n of Convenience Stores*, 746 F.3d at 488.

218. *Id.*

219. *Id.* at 492, 496.

220. *Id.* at 494.

221. *See id.* at 494-95.

222. *Id.* at 495. "According to the Board, as a result of the rule over 100 million debit cards were activated on new networks, and '[Visa], which had previously accounted for approximately 50-60% of the [PIN debit] market, lost roughly half that share.'" *Id.* (quoting Appellant's Br. 37 & n.6).

223. *Id.*

C. Appeal to the Supreme Court

Undeterred by the circuit court's decision, the NACS and the other merchant groups filed a Petition for Writ of Certiorari with the United States Supreme Court on August 18, 2014.[224] The merchants urged the Supreme Court to take up this case due to the importance of the final rule and the gravity of the circuit court's "legal error in upholding an agency rule that has multi-billion-dollar consequences for millions of parties every year."[225] The merchants warned that if allowed to stand, the final "rule will unlawfully permit banks to inflate by billions of dollars each year the interchange fees they charge American merchants, and in turn, American consumers."[226]

Along with their usual arguments supporting the contention that the Federal Reserve Board overstepped its statutory boundaries when it finalized the larger interchange fee cap, and the more restrictive non-exclusivity rule, the merchants' petition for writ argued that the D.C. Circuit committed a significant legal error in deferring to the Board's authority.[227] According to the merchants, the Circuit Court's reasoning that the Durbin Amendment allows the Board to engage in the equivalent of ratemaking is flawed for several reasons.[228] Particularly, the merchant-petitioners contend that by considering the Board's action a "ratemaking"—something the Board itself rejected—the court granted the Board far greater discretion than it was due.[229] The merchant-petitioners also found fault with the circuit court's application of *Chevron*, arguing that the court was wrong to defer to the Board's judgment since the Durbin Amendment is unambiguously clear and the Board's final rule was "quite simply, incoherent," and did not reflect Congress's obvious intent.[230]

In response, the Federal Reserve Board urged the Supreme Court to pass on hearing the case because it argued that the court of appeals correctly rejected the merchant-petitioners' arguments.[231] Noting that nothing in the

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224. Petition for Writ of Certiorari, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474 (D.C. Cir. 2014) (No. 14-200), 2014 WL 4102151 (U.S.) (Aug. 18, 2014).

225. *Id.* at 17.

226. *Id.* at 18.

227. *Id.* at 17.

228. *Id.* at 24-32.

229. *Id.* at 24.

230. *Id.* at 26-27.

231. Brief for the Respondent in Opposition, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474 (D.C. Cir. 2014) (No. 14-200), 2014 WL 6478964 (U.S.) (Nov. 19, 2014).

statute forbids the recovery of the costs at issue in the interchange fee, the Board argued that the inclusion of these costs in the final interchange fee standard was not in violation of the *Chevron* rule.[232] In direct response to the petitioners' argument, the Board argued that, because the regulations are consistent with *Chevron* without having to appeal to a higher deferential standard, the fact that the court of appeals alluded to ratemaking is irrelevant and does not require Supreme Court intervention.[233]

In addition to the briefs filed by the parties, several interested outside parties filed amicus curiae briefs encouraging the Supreme Court to act in compliance with their interests.[234] Senator Durbin, the primary sponsor behind the Durbin Amendment, filed a brief in support of the petitioners discussing the congressional intent behind the Amendment and the effects Congress intended it to have on the debit card industry.[235] Durbin's brief argued that his namesake amendment was carefully authored to respond to the failures of the interchange fee system.[236] Relevant to this litigation, Durbin noted that Congress specifically limited the Board's cost considerations to the incremental cost of authorization, clearance, and settlement because Congress identified those as the core costs of conducting a debit transaction and hoped that by only allowing interchange fee recovery of these limited costs, card issuers would be incentivized to manage their operations more effectively, thus reducing consumer costs.[237] Durbin argued that Congress's mandate to the Board was clear through the statutory language and legislative intent, and that the Board's final rule was invalid because it ignored all congressional directives.[238]

232. *Id.* at 13-14.

233. *Id.* at 21.

234. *See generally* Brief for Ahold, U.S.A., Inc. as Amicus Curiae Supporting Petitioners, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., No. 14-200 (2014), 2014 WL 4730626; Brief for 7-Eleven, Inc., Arby's Restaurant Group, Inc., Brookshire Grocery Co., CKE Restaurants Holdings, Inc., Starbucks Corp., and Wendy's Co. as Amici Curiae Supporting Petitioners, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., No. 14-200 (2014), 2014 WL 4730628; Brief for Retail Litigation Center, Inc. as Amicus Curiae Supporting Petitioners, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., No. 14-200 (2014), 2014 WL 4730629; Brief for Wal-Mart Stores, Inc., as Amicus Curiae Supporting Petitioners, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., No. 14-200 (2014), 2014 WL 4730630.

235. Brief for U.S. Sen. Richard J. Durbin as Amicus Curiae Supporting Petitioners at 4-14, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., No. 14-200 (2014), 2014 WL 4704636.

236. *Id.* at 4-7.

237. *Id.* at 10-11.

238. *Id.* at 11.

Senator Durbin was not the only one lining up behind the merchant-petitioners begging the Supreme Court to take up this case. Retail giants such as Wal-Mart, 7-Eleven, and Starbucks also submitted amicus briefs in support of the petitioners, arguing that the high interchange fee standards cost them millions of dollars each year.[239] These retailers argued that they have no choice but to pay the unreasonably high interchange fees because they have to accept one of the most common forms of payment—debit cards—in order to stay in business.[240]

Interestingly enough, no banking groups or financial institutions filed amicus curiae briefs with the Supreme Court, even though those groups were quick to file briefs when the case was before the circuit court.[241] The banking groups filed their brief in support of neither party, arguing that the district court was wrong in holding that costs that are specific to particular debit card transactions, but that are not incremental authorization, clearance, and settlement costs, could not be considered by the Board in its rulemaking.[242] However, the financial groups did not file their brief in support of the Federal Reserve Board because they argued that while the Board's final rule was an improvement on their proposed rule, the regulations still did not allow for banks to recover all their costs or a reasonable rate of return, both of which, they argued, the Durbin Amendment allows.[243]

Despite the pleas of petitioners, retailers, and merchant groups, the Supreme Court passed on the opportunity to hear this case.[244] The Supreme

239. Brief for Wal-Mart Stores, Inc. as Amicus Curiae Supporting Petitioners at 1, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., No. 14-200 (2014), 2014 WL 4730630; Brief for 7-Eleven, Inc., Arby's Restaurant Group, Inc., Brookshire Grocery Co., CKE Restaurants Holdings, Inc., Starbucks Corp., and Wendy's Co. as Amici Curiae Supporting Petitioners, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Federal Reserve Sys., No. 14-200 (2014), 2014 WL 4730628.

240. Brief for 7-Eleven, Inc., Arby's Restaurant Group, Inc., Brookshire Grocery Co., CKE Restaurants Holdings, Inc., Starbucks Corp., & Wendy's Co. as Amici Curiae Supporting Petitioners, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Federal Reserve Sys., No. 14-200 (2014), 2014 WL 4730628.

241. *See* Brief for Clearing House Ass'n, L.L.C., Am. Bankers Ass'n, Consumer Bankers Ass'n, Credit Union Nat'l Ass'n, The Fin. Serve. Roundtable, Indep. Comty. Bankers of Am., Mid-Size Bank Coal. of Am., Nat'l Ass'n of Fed. Credit Unions, & Nat'l Bankers Ass'n as Amici Curiae Supporting Neither Party and Reversal, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474 (D.C. Cir. 2014) (No. 14-200), 2013 WL 5720157.

242. *Id.* at 9.

243. *Id.* at 2.

244. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474 (D.C. Cir. 2014), *cert. denied*, 2015 WL 231974 (U.S. Jan. 20, 2015) (No. 14-200).

Court's decision to deny certiorari in this case allows the D.C. Circuit Court's opinion to stand. Thus, the Federal Reserve Board's final rules—which cap interchange fees at twenty-one cents and require two unaffiliated networks to be available for each debit card—are the law of the land.[245]

V. CONSEQUENCES OF THE DURBIN AMENDMENT AND THE BOARD'S FINAL RULE

Because the Supreme Court decided not to intervene in this case, it is clear from the already-present consequences of the Federal Reserve Board's final rule that if Congress does not take action, the rule will take its toll on the economy. Although Congress tacked the Durbin Amendment onto the Dodd-Frank Act assuming that it would ultimately reduce consumer costs by offering relief from high interchange fees,[246] "two years after implementation—Congress's assumptions have proven to be wrong, with most consumers having received little to no benefit at all."[247]

Durbin Amendment advocates logically believed that regulation of interchange fees would cause a reduction in merchant costs—a reduction that would eventually be passed to consumers.[248] However, several other countries have attempted to regulate interchange fees by imposing cap limitations, but in none of these countries have consumers experienced corresponding savings, and the United States has proven to follow a similar trajectory.[249] For example, in the United States, gas retailers, who attribute one third of their sale transactions to debit card users, have "received over $1 billion in annual savings due to reduced interchange fees."[250] If the blissful theory that merchants will pass on their interchange fee savings to consumers were accurate, consumers should have seen a savings of about three cents per gallon, although no such price reduction has been realized.[251]

Further, American consumers are paying for reduced interchange fees in the form of higher prices for other banking services. As banks look to recoup their lost interchange fee revenue in creative ways, "Jamie Dimon, the president and CEO of JPMorgan Chase, compared how banks will respond

245. *See id.* at 488, 496.

246. 156 Cong. Rec. S3695 (daily ed. May 13, 2010).

247. McConnell, *supra* note 25, at 655.

248. David C. John, *The Durbin Debit Card Interchange Fee Hurts Consumers*, HERITAGE FOUND. (Mar. 17, 2011), http://www.heritage.org/research/reports/2011/03/debit-card-changes-how-the-durbin-interchange-fee-hurts-consumers.

249. McConnell, *supra* note 25, at 654.

250. McGinnis, *supra* note 23, at 296.

251. *Id.* at 296-97.

to the Durbin Amendment to how a restaurant would deal with a similar situation [by explaining,] 'if you're a restaurant and you cannot charge for the soda, you're going to charge [more] for the burger. Over time, it will all be repriced [sic] into the business.'"[252] Unsurprisingly, the banks agreed with Dimon according to a study that shows a sharp decline in the number of banks offering free checking accounts from 2009 to 2012.[253] In 2012, only thirty-nine percent of banks offered free checking accounts, a sharp decline from the seventy-six percent of banks that offered free checking before the birth of the Durbin Amendment.[254] In analyzing the years surrounding the passage of the Durbin Amendment, the study found an overall increase in almost every banking service fee considered, including monthly maintenance fees, ATM withdrawal fees, and overdraft fees in 2012—just one year after the Federal Reserve Board's final rule was published.[255] In fact, "[i]t is estimated that consumers will lose '$22 to $25 billion more per year from higher bank fees and reduced services than they are expected to gain from lower merchant prices and better merchant services'" as a result of the interchange fee regulation.[256]

Like consumers, small businesses and merchants, the other intended beneficiaries of the Durbin Amendment,[257] have not received any relief since the statute's implementation. Before Congress passed the Durbin Amendment, issuers offered discounted fees to merchants who sold low-priced goods; but in an effort to recover lost revenue due to the interchange fee cap, issuers have largely eliminated this practice and charge all merchants the maximum interchange fee allowed, regardless of transaction value.[258] As a result, many businesses that deal in low-priced goods are required to pay even higher interchange fees than they did before issuance of the cap.[259] For

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252. *Id.* at 299 (citing Anthony Randazzo, *Durbin Amendment Swipe Fee Watch III: Bank of America Debit Card Fees*, REASON FOUND. BLOG (Oct. 23, 2011, 8:52 AM), *available at* http://reason.org/blog/show/durbin-swipe-fee-watch-iii-bofa).

253. Claes Bell, *Checking Fees Rise to Record Highs in 2012*, BANKRATE.COM (Sept. 24, 2012), http://www.bankrate.com/finance/checking/checking-fees-record-highs-in-2012.aspx#slide=1.

254. *Id.*

255. *Id.*

256. McConnell, *supra* note 25, at 655 (quoting David S. Evans et al., *The Impact of the U.S. Debit Card Interchange Fee Regulation on Consumer Welfare: An Event Study Analysis* 48 (Coase-Sandor Inst. for Law & Econ., Working Paper No. 658)).

257. 156 Cong. Rec. S3695 (daily ed. May 13, 2010) (statement of Sen. Richard Durbin) ("This amendment will help small businesses, merchants, and consumers by providing relief from high interchange fees for debit card transactions.").

258. McConnell, *supra* note 25, at 656.

259. *Id.*

example, Redbox, a company that issues movie and game rentals to customers from vending machine kiosks, upped the price of a one-day rental from $1.00 to $1.20, ascribing the price increase to increased debit card fees.[260]

VI. CONCLUSION

As the circuit court recognized, "neither agencies nor courts have the authority to disregard the demands of even poorly drafted legislation."[261] This truth is the issue at the heart of this case. Arguably, because of Judge Leon's strict interpretation of the Durbin Amendment, his decision invalidating the Federal Reserve Board's final rules was correct,[262] but had the judiciary sent the Federal Reserve Board back to the drawing board with specific instructions to not consider the controversial third category of costs, the dismal consequences of the current regulation would only be amplified.[263] However, because the court deferred to the Board's judgment under *Chevron*, and upheld the final rules regarding interchange fees and network exclusivity, everyone was left unhappy;[264] and consumers, retailers, and financial institutions have continued to suffer.[265] Even Ben Bernanke, chairman of the Federal Reserve Board at the time the final regulations were issued, recognized the possible side effects of such drastic regulations and had concerns about their implementation, but "made the excuse that 'this is the

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260. McGinnis, *supra* note 23, at 298; McConnell, *supra* note 25, at 656.

261. Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474, 483 (D.C. Cir. 2014).

262. *See* Kevin Wack, *Damage to Banks from Debit Card Ruling Goes Beyond Lower Fee Cap*, AM. BANKER (Aug. 13, 2013, 12:29 PM), http://www.americanbanker.com/issues/178_156/damage-to-banks-from-debit-card-ruling-goes-beyond-lower-fee-cap-1061295-1.html.

263. *See generally* Diane Katz, *Bernanke on Dodd-Frank Fallout: Debit Card Fees Threaten Small Banks*, DAILY SIGNAL (May 17, 2011), http://dailysignal.com/2011/05/17/bernanke-on-dodd-frank-fallout-debit-card-fees-threaten-small-banks/ (stating that the proposed twelve-cent cap on interchange fees would result in a loss of $12 billion to banks); McConnell, *supra* note 25 at 651 (stating that the final rule imposing a twenty-one cent cap on interchange fees resulted in a loss of $7.3 billion to banks). The proposed twelve-cent cap, which accounted for only those costs that are specifically mentioned for consideration in the statute, would have resulted in a much larger loss to banks than the loss imposed by the final rule, thus magnifying the consequences of the final rule. *See* Debit Card Interchange & Routing, 75 Fed. Reg. 81722, 81734-35 (Dec. 28, 2010) (stating that the proposed rule only includes those costs specifically mentioned for consideration in the statute).

264. Borak & Blackwell, *supra* note 152; John, *supra* note 152.

265. *See* discussion *supra* Part V.

best available solution to implement the will of Congress.'"[266] Another Federal Reserve Board member was quoted saying "[w]e didn't craft the Durbin Amendment . . . . We are only doing what Congress directed."[267] It is almost as if even the Federal Reserve Board recognized that the Durbin Amendment required the type of restrictive regulation advocated for by the merchants and retailers, but in a last-ditch effort to save the economy from the unavoidable and dire results of such regulation, the Board found a loophole in the statute and ran with it.

Thus, although it has been said that "[s]plitting the difference does not improve bad policy"[268]—it seems that the Board attempted to do just that, leaving everyone to reap the unfortunate consequences of the regulation. However, fingers cannot be pointed at the Federal Reserve Board, because Congress passed this ill-conceived legislation without any hearings and "mere minutes of total debate in Congress."[269] Perhaps in refusing to hear the case, the Supreme Court recognized that it could not alleviate the economic strain caused by the Durbin Amendment, no matter which way it ruled. Regardless, Congress unleashed the devastating Durbin Amendment, and the floor of Congress, hopefully for more than just a few minutes this time, is where its consequences should be addressed and the legislation reconsidered.

266. John, *supra* note 152.

267. *Id.* (quoting Sarah Bloom Raskin).

268. *Id.*

269. Brief for Clearing House Ass'n, L.L.C., Am. Bankers Ass'n, Consumer Bankers Ass'n, Credit Union Nat'l Ass'n, The Fin. Serv. Roundtable, Indep. Cmty. Bankers of Am., Mid-Size Bank Coal. of Am., Nat'l Ass'n of Fed. Credit Unions, & Nat'l Bankers Ass'n as Amici Curiae Supporting Neither Party and Reversal, Nat'l Ass'n of Convenience Stores v. Bd. of Governors of the Fed. Reserve Sys., 746 F.3d 474 (D.C. Cir. 2014) (No. 13-5270).