Interchange Works: Protect Consumers' Credit

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Topline: Routing mandates on credit cards will lead to less secure, less innovative, and higher-risk transactions for American consumers. This time, they're proposing new credit routing mandates that would give retailers—not consumers—the power to decide which credit card network is used—all to increase the bottom line of mega retailers. **Consumers, small businesses, and small community financial institutions will lose the most if this happens.**

The Fundamentals: Credit cards are a fundamentally different product than debit cards. Credit cards are an extension of unsecured credit to a consumer, meaning financial institutions make a loan to a consumer every time a credit card is used to purchase goods or services from a retailer. This credit card network allows retailers to avoid the cost of processing transactions and offers them quick, guaranteed payment. This increases the number and value of their sales. Interchange is the cost of doing business.

This Legislation Will Hurt Consumers

Consumer Choice for Credit Cards Would Disappear. Instead of preserving consumer choice in their trusted card network, Marshall-Durbin would put that decision in the hands of the retailers. With only their bottom line as motivation due to the protections provided by financial institutions through the interchange system, the retailer will choose the cheapest – not the most secure – option. 86% of consumers use credit cards because they feel their information is secure from data breach. Consumers have a wide variety of cards, processors, and issuing institutions to choose from, and their choice must be respected.

Cybersecurity Will Be at Risk. If retailers are allowed to simply choose the cheaper networks that haven't invested in the latest security technology, consumer payment data will be vulnerable to foreign networks.

Prices Will Rise for Consumers. Establishing a dual-routing system will represent a significant expense that raises costs for consumers. The Richmond Fed determined that over 20% of retailers increased their prices following enactment of the Durbin Amendment, and only 1% of retailers passed their savings onto consumers.

This Legislation Will Hurt Small Businesses

Credit routing mandates would hurt small businesses when they are still recovering from the economic impact of the pandemic. With billions driven from the credit market, lenders will be forced to reduce small business lending to recoup their losses.

Routing mandates reduce merchant satisfaction with electronic payments while in many cases also increasing their costs — paradoxically putting many small retailers in the position of paying more for less. Given the high value that small retailers place on high-quality payment processing services, the concerning corollary is that as regulators limit interchange prices, the quality of service they receive will decline. Research by Javelin Strategy & Research reveals that for most small retailers, the value of services received from electronic payments providers is more important to them than price.

This Legislation Disproportionately Harms Small Financial Institutions

Small financial institutions will face higher costs. In addition to reduced revenue, recent Federal Reserve data shows that community banks and credit unions also face higher costs as a result of these price controls. These institutions typically have a lower number of debit transactions than covered issuers. This means it is more difficult for them to absorb costs compared to larger issuers with a higher number of transactions. Due to their reduced revenue after Durbin, community banks and credit unions, the so-called "exempt" issuers, have less money to pay for more services.

Small financial institutions are harmed even with exemptions. While most credit unions and community banks are not directly subject to the proposed credit routing requirements, they will undoubtedly suffer the consequences. The Merchant Discount Fee, of which interchange is a portion, is an interconnected network of contracts between card processors, financial institutions, and retailers. Changes to any part of this ecosystem will have significant ripple effects throughout the card network because the cost of running the card program will only increase and those costs will be passed down to other system participants. This means those with the least bargaining power—community financial institutions, small businesses, and consumers.