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SWIPE FREEZE: HOW THE “DURBIN AMENDMENT” IS PREVENTING YOUR MOBILE PHONE FROM REPLACING YOUR WALLET

INTRODUCTION

On July 21, 2010, Congress passed the Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd–Frank or Act) to “promote the financial stability of the United States” through increased financial regulation.¹ The Act is a sprawling, catchall regulation for financial reform, the full scope of which remains unclear. Despite the complexity of the Act, one amendment provided a regulation that was, on its surface, very straightforward. The so-called Durbin Amendment (Amendment), sponsored by Senator Richard Durbin, tasked the newly formed Board of Governors of the Federal Reserve System (Board) with making the fee charged to a merchant for a debit transaction “reasonable and proportional” to the actual cost incurred by the card issuer.² Additionally, the Amendment provides that each debit card must be capable of processing payments on at least two different networks, such as Visa and MasterCard.³ Commentators reacted to the inclusion of the Durbin Amendment with equal parts adoration and abhorrence, though they universally overlooked its effect on the blossoming mobile-payment industry.

It should come as no surprise that the U.S. marketplace is increasingly capable of processing payments directly from a consumer’s mobile phone. As of February 2012, 49% of U.S. mobile subscribers owned smartphones.⁴ Moreover, technological advances have made it possible for consumers to integrate their finances directly into their phones, prompting one writer to ask, “How long before we could get by using *just* our smartphones as our wallets?”⁵ She found that, al-

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

2. 15 U.S.C. § 1693o-2(a)(2) (2012).

3. *Id.* § 1693o-2(b)(1)(A).

4. *Smartphones Account for Half of All Mobile Phones, Dominate New Phone Purchases in the US*, NIELSON (March 29, 2012) [hereinafter NIELSON, *Smartphones*], <http://www.nielsen.com/us/en/newswire/2012/smartphones-account-for-half-of-all-mobile-phones-dominate-new-phone-purchases-in-the-us.html>.

5. Christina Bonnington, *My Walletless Month: Happier, Healthier, and Ready to Ditch Cash Forever*, WIRED (Oct. 19, 2012), <http://www.wired.com/gadgetlab/2012/10/one-month-of-wallet-less/all/>.

though we are progressing toward making our wallets obsolete, a completely “walletless” life is still many years away.⁶ Still, the advent of mobile payments is not all that recent. In 2004 the U.S. market for mobile payment at the physical point of sale was already beginning to emerge, and by the end of 2004 the global market for mobile commerce and e-payments totaled \$200 billion.⁷ Outside of the United States, pilot programs have demonstrated that consumers highly value the convenience of mobile payment at the physical point of sale.⁸ Indeed, that convenience is equally valuable to merchants. One industry analyst remarked that “if [merchants] can shave 10 seconds off wait times, same-store sales could go up a lot It’s substantial.”⁹

Unfortunately, one modest amendment to Dodd–Frank threatens to derail the expansion of the mobile-payment industry. This Comment discusses how Dodd–Frank will ultimately impede the burgeoning technologies necessary to make mobile payments more accessible. Specifically, it analyzes the Amendment’s unintended impact on the mobile-payment industry and demonstrates why the provision should be amended to provide a mobile-payment exception.

Part II of this Comment discusses the events leading up to the financial crisis of 2008 and subsequent passage of Dodd–Frank, as well as the relevant provisions of the Amendment.¹⁰ Additionally, Part II examines the relatively new field of mobile payments by detailing the specific technology employed by mobile-payment platforms and the major players in the industry.¹¹ Part III analyzes the interplay between the Amendment and the mobile-payment industry and argues that the Amendment’s drafters overlooked its constraining effect on the industry.¹² This Comment makes two arguments to support that contention. First, by cutting into card-issuer revenues, the Amendment disincentivizes investment in the fledgling mobile-payment market, where merchants are unable or unwilling to provide the necessary infrastructure.¹³ Second, the interchange-fee regulation and two-network requirement have the anticompetitive effect of blocking new

6. *Id.*

7. SMART CARD ALLIANCE, MOBILE PAYMENTS AT THE PHYSICAL POINT-OF-SALE: ASSESSING U.S. MARKET DRIVERS AND INDUSTRY DIRECTION 5 (2005), available at http://www.it.itb.ac.in/~tijo/seminar/Mobile_Payments_Physical_POS.pdf.

8. *Id.* at 6.

9. Alistair Barr, *PayPal Could Heat Up Mobile Payments Race if McDonald’s Test Pays Off*, REUTERS (Aug. 17, 2012), <http://www.reuters.com/article/2012/08/17/us-paypal-mcdonalds-idUSBRE87G0ZB20120817>.

10. See *infra* notes 16–57 and accompanying text.

11. See *infra* notes 58–128 and accompanying text.

12. See *infra* notes 129–211 and accompanying text.

13. See *infra* notes 129–202 and accompanying text.

market entrants that would otherwise have priced their interchange fee lower than the industry giants.¹⁴ Finally, Part IV discusses the overall impact of the Amendment on the implementation of electronic payments and advocates for the addition of a mobile-payment exception to the Amendment.¹⁵

II. BACKGROUND

A. *The 2008 Financial Crisis and Congress's Response*

Beginning in 2008, the United States endured a financial crisis—one later characterized as the worst since the Great Depression¹⁶—during which \$17 trillion worth of personal savings was lost.¹⁷ From 2008 to 2009 alone, 8.3 million American jobs were eliminated.¹⁸ The situation prompted then-Secretary of the Treasury Henry Paulson to call together congressional leaders and proclaim that unless they acted, “the financial system of this country and the world [would] melt down in a matter of days.”¹⁹ The crisis initially triggered two pieces of reactive legislation aimed at controlling the effects of the recession.²⁰ The first, the Emergency Economic Stabilization Act of 2008,²¹ made \$700 billion available for government purchase of toxic mortgage assets.²² The second, the American Recovery and Reinvestment Act of 2009,²³ was a \$787 billion stimulus bill designed to curb the recession and associated job losses.²⁴ However, these bills did little to silence the demands for increased financial regulation going forward. A *New York Times* editorial demanded a complete overhaul of the financial indus-

14. See *infra* notes 203–211 and accompanying text.

15. See *infra* notes 212–252 and accompanying text.

16. Arthur E. Wilmarth, Jr., *The Dodd-Frank Act: A Flawed and Inadequate Response to the Too-Big-To-Fail Problem*, 89 OR. L. REV. 951, 953 (2011) (quoting Angela Maddaloni & José-Luis Peydró, *Bank Risk-Taking, Securitization, Supervision and Low Interest Rates: Evidence from the Euro Area and the U.S. Lending Standards* 7 (European Cent. Bank, Working Paper No. 1248, 2010), available at <http://ssrn.com/abstract=1679689>).

17. Eugene A. Ludwig, *Assessment of Dodd-Frank Financial Regulatory Reform: Strengths, Challenges, and Opportunities for a Stronger Regulatory System*, 29 YALE J. ON REG. 181, 182 (2012).

18. *Id.* (citing FIN. CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT: FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES 390 (2011)).

19. Charles W. Murdock, *The Dodd-Frank Wall Street Reform and Consumer Protection Act: What Caused the Financial Crisis and Will Dodd-Frank Prevent Future Crises?*, 64 SMU L. REV. 1243, 1244–45 (2011) (citing *Frontline: Inside the Meltdown* (PBS television broadcast Feb. 17, 2009), available at <http://video.pbs.org/video/1082087546>).

20. *Id.* at 1246.

21. Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, 122 Stat. 3765.

22. Murdock, *supra* note 19, at 1245.

23. American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115.

24. Murdock, *supra* note 19, at 1245.

try's regulatory structure, stating that "[a]nything less than a new rules-based regime would be inadequate to the task of restoring confidence and, eventually, reviving the economy."²⁵ A similar sentiment was echoed during the 2008 U.S. congressional hearings before the Senate Committee on Banking, Housing, and Urban Affairs.²⁶

The result was a third piece of legislation, the Dodd–Frank Act, signed into law on July 21, 2010.²⁷ Dodd–Frank was aimed squarely at preventing future crises.²⁸ President Obama pledged that the Act would

rein in the abuse and excess that nearly brought down our financial system [and] bring transparency to the kinds of complex and risky transactions that helped trigger the financial crisis [T]he American people will never again be asked to foot the bill for Wall Street's mistakes.²⁹

Dodd–Frank marked “the largest financial industry reform package since the Securities and Exchange Act of 1934.”³⁰ Although Congress passed Dodd–Frank as an 848-page document, it had ballooned to 8,843 pages by its two-year anniversary and still contained less than one-third of its required rulemaking.³¹ Dodd–Frank's breadth was seemingly endless: for example, it created a council of regulators to monitor the state of the economy, an agency to regulate consumer financial products, and new regulations directed towards derivatives trading.³² Proponents of the Act praise its all-inclusiveness and claim that it places regulators in the best position to prevent future crises.³³

25. Ludwig, *supra* note 17, at 183 (alteration in original) (quoting Editorial, *Starting the Regulatory Work*, N.Y. TIMES, Jan. 8, 2009, at A30).

26. See *id.* (citing *Turmoil in the U.S. Credit Markets: The Genesis of the Current Economic Crisis: Hearing Before the S. Comm. on Banking, Hous., & Urban Affairs*, 110th Cong. 56–65 (2008) (statement of Eugene A. Ludwig, Chief Executive Officer, Promontory Financial Group) (“The real question is how far do we go in terms of regulating the financial system [W]e have to massively change how we have been regulating and supervising. We have to take better control of the revolutions in technology and globalization.”)).

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

28. Murdock, *supra* note 19, at 1246.

29. *Id.* at 1247 (quoting President Barack Obama, Remarks by the President at Signing of Dodd-Frank Wall Street Reform and Consumer Protection Act (July 21, 2010) (transcript available at <http://www.whitehouse.gov/the-press-office/remarks-president-signing-dodd-frank-wall-street-reform-and-consumer-protection-act>)).

30. Cody Vitello, *The Wall Street Reform Act of 2010 and What It Means for Joe and Jane Consumer*, 23 LOY. CONSUMER L. REV. 99, 99 (2010).

31. *Dodd-Frank Progress Report*, DAVIS POLK & WARDWELL LLP 4 (July 18, 2012), http://www.davispolk.com/files/uploads/FIG/071812_Dodd.Frank.Progress.Report.pdf.

32. Jessica Luhrs, Note, *Encouraging Litigation: Why Dodd-Frank Goes Too Far in Eliminating the Procedural Difficulties in Sarbanes-Oxley*, 8 HASTINGS BUS. L.J. 175, 175–76 (2012).

33. See *id.* at 176.

However, the Act has also been met by quite a bit of dissension. Representative John Boehner called Dodd–Frank “just another big-government power grab,” and Representative Michele Bachmann introduced a bill to repeal it altogether.³⁴ Another critic has described it as “a train wreck,” “legislative gibberish,” and “a betrayal of New Deal progressive ideals that served this country well.”³⁵ While regulators continue to implement Dodd–Frank’s provisions, the consequences of the Act are not yet fully understood.

B. *The Durbin Amendment*

One particularly controversial section of Dodd–Frank is a last-minute addition known as the Durbin Amendment. The irony of the controversy surrounding the Amendment is that its provisions are simple in comparison to nearly every other section of Dodd–Frank. The Amendment’s stated purpose was to “help small businesses, merchants, and consumers by providing relief from high interchange fees for debit card transactions.”³⁶ Interchange fees—which averaged forty-four cents in 2010³⁷—are the costs paid by a merchant to a card issuer (e.g., Visa or MasterCard) for each debit transaction processed by the merchant.³⁸ The fee “compensates an issuer for its involvement in an electronic debit transaction.”³⁹ Senator Durbin believed that the interchange system was “entirely unregulated,” with “no competition and no recourse for merchants exploited by the rate structures and fees.”⁴⁰ Thus, the Amendment charged the Board of Governors of the Federal Reserve System with the task of setting the interchange fee for electronic debit transactions at a level that was “reasonable and proportional to the cost incurred by the issuer.”⁴¹

34. Murdock, *supra* note 19, at 1247.

35. Cornelius K. Hurley, Book Review, *AM. BANKR. INST. J.*, June 2011, at 40 (reviewing DAVID A. SKEEL, JR., *THE NEW FINANCIAL DEAL: UNDERSTANDING THE DODD-FRANK ACT AND ITS (UNINTENDED) CONSEQUENCES* (2011)).

36. M. Pierce Sandwith, Note, *Debit Card Interchange Fees and the Durbin Amendment’s Small Bank Exemption*, 16 *N.C. BANKING INST.* 223, 232–33 (2012) (quoting 156 *CONG. REC.* S3695 (daily ed. May 13, 2010) (statement of Sen. Richard Durbin)).

37. *Id.* at 224.

38. 12 C.F.R. § 235.2(j) (2012).

39. *Id.*

40. Sandwith, *supra* note 36, at 223 (quoting Letter from Senator Richard J. Durbin, U.S. Senate, to Camden Fine, President and CEO, Indep. Cmty. Bankers of Am., and Dan Mica, President and CEO, Credit Union Nat’l Ass’n (June 11, 2010), *available at* <http://durbin.senate.gov/public/index.cfm/pressreleases?ID=d9c42bd5-b945-4bee-b025-55aab2fd586a>).

41. 15 U.S.C. § 1693o-2(a)(2) (2012).

Accordingly, the Board requested comment on two alternative standards for determining the new cost of interchange fees.⁴² The first alternative, an “issuer-specific standard,” mandated that the interchange fee could not exceed each individual issuer’s allowable costs and imposed a ceiling of twelve cents.⁴³ The second alternative, a stand-alone cap, recommended a uniform fee of twelve cents regardless of the issuer’s costs.⁴⁴ The Board’s final rule adopted a variation of the latter proposal that set the cap at twenty-one cents per transaction.⁴⁵ The Amendment also required that all payment cards be capable of processing on at least two networks.⁴⁶ This provision allows the merchant to select the least expensive network and process the transaction with that provider.⁴⁷

The manner in which the Amendment was enacted was highly controversial. The subject of debit interchange was a commonly researched and debated topic, even before the Amendment was introduced. Debit interchange was the focus of numerous studies, House and Senate committee hearings, and a large amount of academic literature.⁴⁸ Still, “not a single syllable can be located” in any of those materials that addresses the Amendment’s specific interchange ceiling.⁴⁹ In fact, during his floor speech, Senator Durbin “relied on the

42. Debit Card Interchange Fees and Routing, 75 Fed. Reg. 81,722, 81,726 (proposed Dec. 28, 2010).

43. *Id.* The issuer’s allowable costs are costs “attributable to the issuer’s role in authorization, clearance, and settlement of the transaction.” *Id.* The issuer would add up all allowable costs from its debit transactions over a calendar year and divide that by the number of debit transactions in that year to calculate its interchange fee. *Id.*

44. *Id.*

45. 12 C.F.R. § 235.3(b)(1) (2012). Thousands of retailers challenged the Board’s twenty-one cent interchange fee, asserting that it was set too high. Complaint for Declaratory Relief, *NACS v. Bd. of Governors of Fed. Reserve Sys.*, No. 11-02075 (RJL), 2013 WL 3943489 (D.D.C. July 31, 2013) (No. 11-2075). On July 31, 2013, the United States District Court for the District of Columbia invalidated the interchange fee, holding that the Board set the fee too high by impermissibly accounting for costs that Dodd-Frank precluded the Board from considering. *NACS*, 2013 WL 3943489, at *17. However, as of this Comment’s publication, the Board is appealing that decision. Michael R. Crittenden, *Judge Agrees to Delay Ruling on Debit-Card Fees*, WALL ST. J. (Sept. 20, 2013), <http://online.wsj.com/news/articles/SB10001424127887323808204579087160027260166>. The appellate court stayed the district court’s decision and allowed the fee to remain at its current level, pending resolution of the appeal. *Id.* The court’s schedule requires briefs to be filed in December of 2013, so a final determination will not likely come until 2014, or perhaps longer. *Id.*

46. 15 U.S.C. § 1693o-2(b)(1)(A).

47. Todd Zywicki, *Durbin’s Innovation Killer*, AMERICAN (June 11, 2010), <http://www.american.com/archive/2011/june/durbin2019s-innovation-killer/>.

48. Richard A. Epstein, *The Constitutional Paradox of the Durbin Amendment: How Monopolies are Offered Constitutional Protections Denied to Competitive Firms*, 63 FLA. L. REV. 1307, 1325 (2011).

49. *Id.*

private statements of the head of a major corporation . . . [who attested] that interchange fees were too high because they were the fourth largest item on the corporation's books."⁵⁰ The Senate voted for the Amendment's inclusion only three days after it was introduced.⁵¹

The Amendment's small-bank exemption is indicative of the bizarre circumstances leading to its approval. Senator Durbin's original proposal lacked sufficient votes, prompting him to add a small-bank exemption for those with assets of less than \$1 billion.⁵² In order to build support for the Amendment, Senator Durbin hand-wrote edits in the margins of the bill that made exceptions for smaller financial institutions.⁵³ When the bill again came up short, he revised the exemption ceiling to \$10 billion, and it finally passed.⁵⁴ These circumstances have sparked broad skepticism regarding whether the Amendment's enactment was the product of political posturing.⁵⁵ Given the Amendment's last-minute inclusion, and its absence from the original House version, the House did not have an opportunity to review the Amendment.⁵⁶ Shortly after the vote, 131 bipartisan members of Congress wrote a letter voicing their "grave concerns" about the inclusion of the Amendment.⁵⁷

C. Mobile Payments

A 2010 Federal Reserve study of the most popular noncash methods of payment found that debit cards were the most prevalent, accounting for nearly 35% of all noncash payments.⁵⁸ Further, interchange fees from debit transactions in 2009 netted \$16.2 billion in revenue for banks.⁵⁹ Increased debit card use has coincided with an

50. *Id.*

51. *Durbin Amendment*, ELECTRONIC PAYMENTS COALITION, <http://www.electronicpayment-coalition.org/key-issues/durbin-amendment/> (last visited Oct. 2, 2013).

52. Epstein, *supra* note 48, at 1326.

53. *Durbin Amendment*, *supra* note 51.

54. Epstein, *supra* note 48, at 1326.

55. See, e.g., Todd Zywicki, *Economic Uncertainty, the Courts, and the Rule of Law*, 35 HARV. J.L. & PUB. POL'Y 195, 203–05 (2012); Thomas McGarity, *Administrative Law as a Blood Sport: Policy Erosion in a Highly Partisan Age*, 61 DUKE L.J. 1671, 1693 (2012).

56. *Durbin Amendment*, *supra* note 51.

57. *Id.* (citing Letter from Rep. Debbie Wasserman Schultz et al., U.S. House of Representatives, to Conferees (June 16, 2010), available at <http://wassermanschultz.house.gov/legislation/Interchange%20Letter%20to%20Conferees%20with%20Signatures.pdf>).

58. FED. RESERVE SYS., THE 2010 FEDERAL RESERVE PAYMENTS STUDY: NONCASH PAYMENT TRENDS IN THE UNITED STATES: 2006-2009 16 (2011), available at http://www.frbservices.org/files/communications/pdf/press/2010_payments_study.pdf.

59. Debit Interchange Fees and Routing, 76 Fed. Reg. 43,394, 43,397 (July 20, 2011) (codified at 12 C.F.R. pt. 235 (2012)).

explosion of smartphone use in this country.⁶⁰ In fact, smartphones are replacing an increasing number of everyday items, including alarm clocks, watches, cameras, and laptop computers.⁶¹ Perhaps most telling is that smartphone users spend on average more than two hours per day using their devices.⁶² These technological trends are consistent with those in the mobile-banking industry. A March 2011 survey found that nearly one in five Americans with both a bank account and a mobile phone had used his or her phone to conduct banking with a financial institution within the previous ninety days.⁶³ Clearly, the infrastructure is in place for mobile payments to succeed.

1. *Technological Overview of Mobile Payments*

Experts estimate that since 2010 about five billion people worldwide have logged mobile phone subscriptions.⁶⁴ In the United States, it is estimated that 91% of the population has cell phones.⁶⁵ The improved storage and computing capacity opens the door for phones to become repositories for coupons, loyalty information, and the contents of our wallets.⁶⁶ Cell phones' entry into the e-commerce market presents an obvious opportunity for consumers who desire convenience and expediency.⁶⁷ These technological innovations have resulted in the proliferation of mobile payments, or payments "where a mobile device is used to initiate, authorize, and confirm an exchange of financial value in return for goods and services."⁶⁸

There are two primary forms of mobile payments. The first, remote payment, allows consumers to use a phone equipped with either short messaging service (SMS) or wireless application protocol (WAP) tech-

60. See NIELSON, *Smartphones*, *supra* note 4 (stating that nearly half of all American cell phone users own a smartphone).

61. Press Release, O2, Making Calls Has Become Fifth Most Frequent Use for a Smartphone for Newly-Networked Generation of Users (June 29, 2012), <http://news.o2.co.uk/?press-release=Making-calls-has-become-fifth-most-frequent-use-for-a-Smartphone-for-newly-networked-generation-of-users>.

62. *Id.*

63. BD. OF GOVERNORS OF THE FED. RESERVE SYS., CONSUMERS AND MOBILE FINANCIAL SERVICES 3 (2012), available at <http://www.federalreserve.gov/econresdata/mobile-device-report-201203.pdf> (citing JAVELIN STRATEGY & RESEARCH, SMARTPHONE BANKING SECURITY: MOBILE BANKING UTILIZATION STALLS ON CONSUMER FEARS (2011)).

64. Meena Aharam Rajan, *The Future of Wallets: A Look at the Privacy Implications of Mobile Payments*, 20 COMM.LAW CONSPECTUS 445, 446 (2012).

65. *Id.* at 446–47.

66. Chris Jay Hoofnagle et al., *Mobile Payments: Consumer Benefits & New Privacy Concerns* 3 (Apr. 24, 2012) (unpublished manuscript), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2045580.

67. Rajan, *supra* note 64, at 447.

68. *Id.*

nology to send a payment to a merchant or individual.⁶⁹ SMS payments require a consumer to link a bank account or credit or debit card to an account that the consumer establishes with a mobile-payment service provider (MPSP).⁷⁰ When the consumer wants to make a payment, she sends a text message to the MPSP stating how much money should be transferred and to what destination.⁷¹ Similarly, WAP payments, while not considered true mobile payments, allow consumers to access a merchant's website using their mobile devices in order to make a purchase.⁷² This type of payment has also been successfully housed in a virtual, preloaded gift card that appears on a consumer's phone.⁷³

The other primary form of mobile payment, proximity payment, employs near field communication (NFC) technology and allows consumers to make purchases simply by waving their phone in front of an NFC-equipped terminal.⁷⁴ These transactions are completed in precisely the same way as with a credit or debit card.⁷⁵ The NFC chip in a consumer's phone accesses his or her financial account and sends the data to the merchant's acquiring bank.⁷⁶ The acquiring bank then sends the transaction data to the customer's bank, which authenticates and authorizes the transaction.⁷⁷ This technology is often praised as a way to consolidate "all of consumers' financial needs in an easy-to-use device that consumers already carry."⁷⁸

For all of their promise, mobile payments cannot become more conventional unless harmony is achieved between multiple industry players. Industry insiders believe that financial institutions must be the catalysts that drive the growth of mobile payments.⁷⁹ This belief is

69. *Id.*

70. *Id.* at 448.

71. *Id.*

72. Rajan, *supra* note 64, at 449.

73. *Id.* Starbucks is the most prominent merchant to use this method and has processed over twenty million mobile payments. See Paula Berger, *Starbucks Hits 20M M-Payments*, NFC WORLD (Nov. 8, 2011, 4:28 PM), <http://www.nfcworld.com/2011/11/08/311155/starbucks-hits-20m-mobile-payments/>.

74. Rajan, *supra* note 64, at 447.

75. *Id.* at 449.

76. *Id.* at 450. Alternatively, some companies are obviating the need to own a phone that is pre-equipped with an NFC chip. See Suzanna Martindale & Gail Hillebrand, *Pay at Your Own Risk? How to Make Every Way to Pay Safe for Mobile Payments*, 27 BANKING & FIN. L. REV. 265, 270 (2012). Bling Nation, for example utilizes stickers that contain an NFC chip that can be affixed to a consumer's phone. *Id.* at 270–71.

77. Rajan, *supra* note 64, at 450.

78. *Id.* at 449–50.

79. *Id.* at 463 (citing Ryan Kim, *Mobile Payments: Financial Players are in the Driver's Seat*, GIGAOM (Jan. 3, 2012), <http://gigaom.com/2012/01/03/mobile-payments-financial-players-are-in-the-drivers-seat/>).

primarily based on consumer privacy concerns. A 2011 KPMG survey found that 56% of consumers trusted their financial institution with their payment data, while only 6% trusted their mobile and internet service providers.⁸⁰ Wireless providers will also play a pivotal role in the development of mobile payments. For example, in 2010, AT&T, Verizon Wireless, and T-Mobile formed the company Isis with the goal of creating a uniform nationwide mobile-payment system.⁸¹ The three companies promised more than \$100 million to Isis, which also partnered with Visa, MasterCard, and American Express.⁸² Of course, such a system depends on participation by handset manufacturers such as Samsung, Blackberry, and LG, all of which have begun including NFC chips in their phones.⁸³ Merchants as a group must also embrace the trend by equipping themselves with NFC-enabled point-of-sale terminals, an investment that many are still unwilling to make.⁸⁴ Finally, third-party developers are a necessary component to the mobile-payment ecosystem. Google Wallet, for example, is an application that allows consumers to pay using NFC by storing their credit and debit cards on their mobile phone.⁸⁵ If even one of these parties declines to participate, the mobile-payment system fails.

Google Wallet's struggles vividly illustrate the importance of coordination between each of the aforementioned players. Initially, it was only available on one phone and supported only two kinds of cards, one of which was a Google prepaid card, effectively eliminating a substantial portion of the marketplace.⁸⁶ Merchants also needed to install NFC readers in order for Google Wallet to function, and consumers needed to trust Google's platform to safely store their financial information.⁸⁷ Predictably, the interested parties in this country have had a difficult time agreeing on standards and working together to effectu-

80. *Id.* at 464 (citing Press Release, KPMG Int'l, KPMG's 5th Annual Global Consumer & Convergence Survey Confirms Trend of Accelerated Pace of Consumer Adoption of New Digital Business Models (Dec. 5, 2011), <http://www.kpmg.com/global/en/issuesandinsights/articles-publications/press-releases/lists/expired/consumer-convergence-5-survey.aspx>).

81. Zywicki, *supra* note 47.

82. Rajan, *supra* note 64, at 463.

83. *Id.* at 463-64.

84. *Id.* at 464. Each NFC reader costs approximately \$200, while it is estimated that only 10% of mobile users will be actively using NFC payments by 2015. *Id.* Those figures, coupled with an uncertainty over how merchants will be able to send and receive information to consumers' phones, result in a reluctance to invest in the necessary infrastructure. *Id.*

85. *Id.* at 465.

86. Rajan, *supra* note 64, at 465. Sprint's Samsung Nexus S 4G was the only phone that allowed Google Wallet, and the Citi MasterCard credit card was the only non-Google card that was supported. *Id.*

87. *See id.*; *see also* GOOGLE WALLET, <http://www.google.com/wallet> (last visited Aug. 19, 2013).

ate this synchronization, despite the fact that NFC technology is now commonplace overseas.⁸⁸ For a population that has existed for centuries largely with a checkbook and a wallet, this flurry of innovation requires a substantial leap of faith.

2. *Mobile-Payment Companies*

The Durbin Amendment's effects are perhaps best understood in the context of several of today's most popular mobile-payment options. Mobile payments first gained notoriety around 1997, when Nokia allowed customers to use SMS text messaging to purchase drinks from Finnish vending machines.⁸⁹ More recently, SMS payments played a prominent role in the response to the 2010 earthquake in Haiti.⁹⁰ The four major wireless carriers allowed customers to text donations to Haiti through the American Red Cross.⁹¹ Since then, mobile-payment platforms have moved toward applications that allow users to make purchases directly.

The simplest of the name brand platforms is PayPal, which allows users to download an application to their phones and send money to a merchant or individual.⁹² Recently, PayPal unveiled a system at about 3,000 locations that allows customers to enter a mobile-phone number and PIN into a retailer's payment terminal to complete a transaction.⁹³ However, funds for PayPal transactions are still run through the user's PayPal account,⁹⁴ making this process less direct than its mobile-wallet counterparts.

Mobile wallets allow users to link their credit and debit cards to their mobile devices in virtual wallets and pay at the register of participating merchants. One of the first true mobile wallets was a startup company called Square.⁹⁵ Square has consistently been on the cutting edge of mobile-payment innovation; it recently integrated a GPS-

88. Brian X. Chen, *A Digital Wallet Now Available on Some Smartphones*, N.Y. TIMES (Jan. 18, 2012, 7:29 AM), http://bits.blogs.nytimes.com/2012/01/18/visa-digital-wallet/?_r=0. The "interested parties" enumerated are "credit-card companies, banks, technology manufacturers, and software makers and carriers." *Id.*

89. Martindale & Hillebrand, *supra* note 77, at 270.

90. *See id.*

91. *Id.* Wireless customers' text donations were charged to their phone bills. *Id.*

92. *How to Purchase in Stores*, PAYPAL, <https://www.paypal.com/webapps/mpp/use-paypal-in-stores> (last visited Oct. 6, 2013).

93. Andrew R. Johnson & Robin Sidel, *PayPal Discovers the Mall*, WALL ST. J., August 23, 2012, at C1.

94. PAYPAL, *supra* note 92.

95. *Square Wallet*, SQUARE, <http://www.squareup.com/wallet> (last visited Oct. 6, 2013); *see also* Issie Lapowsky, *The Man Who Made the Cash Register Obsolete*, INC. MAGAZINE (last updated April 18, 2013), <http://www.inc.com/audacious-companies/issie-lapowsky/square.html/1>.

based system that allows a merchant's register to detect a user's presence in the store and pull up her name and payment information.⁹⁶ Other prominent mobile wallets include Google Wallet, Isis, and LevelUp, which all operate in substantially the same way.⁹⁷ Even MasterCard and Visa have unveiled plans to enter the mobile-wallet marketplace, effectively removing third-party applications from the equation.⁹⁸ MasterCard went so far as to call the product its "big play" for the next generation of payments technology.⁹⁹ Unsurprisingly, these innovations provide a number of advantages to consumers.

3. *The Benefits of Mobile Payments*

The potential benefits of mobile payments have led some in the technology industry to conclude that a transition to mobile banking is inevitable,¹⁰⁰ recognizing that "this freedom has been in the palm of [consumers'] hands for years."¹⁰¹ That conclusion is easy to understand considering that NFC-based technology has been rated by experts from various Swiss mobile-payment consultancies as either "good" or "excellent" in variables such as scalability, reliability, speed, ease of use, flexibility, security, cost, and value proposition improvement.¹⁰² While privacy and security typically dominate the mobile-payment conversation, this Comment focuses on the benefits of consumer convenience, merchant savings, and the ability of merchants and consumers to isolate pertinent advertisements and deals.

The most fundamental benefit of mobile-payment technology is its convenience. One Starbucks executive aptly summed up what many consumers believe about mobile payments: they are "really futuristic"

96. See *Square Wallet*, *supra* note 95.

97. See GOOGLE WALLET, *supra* note 87; see also *How to Pay with Isis*, Isis, <http://www.paywithisis.com/how.html> (last visited Oct. 6, 2013); LEVELUP, <https://www.thelevelup.com/how-it-works> (last visited Oct. 6, 2013).

98. Laura Noonan, *MasterCard Aims at Mobile Payment Market with Launch of "Digital Wallet"*, REUTERS (Feb. 25, 2013), <http://www.reuters.com/article/2013/02/25/us-mastercard-payment-idUSBRE91O0MU20130225>.

99. *Id.*

100. See, e.g., Chen, *supra* note 88. Moreover, Bill Gajda, Visa's global head of mobile products, said that "all the elements [are coming] into place that's going to make [mobile payments] take off." *Id.* The industry is spreading quickly in Canada, Singapore, and Hong Kong, "which should help pique interest among banks and vendors in the American Market." *Id.*

101. Kelly Clay, *Could Your Smartphone Replace Your Wallet?*, FORBES (May 25, 2012), <http://www.forbes.com/sites/kellyclay/2012/05/25/could-your-smartphone-replace-your-wallet/>.

102. Hussein Issa, *Assessment and User Adoption of NFC in Comparison to Other Mobile Payments Systems* 8 (August 16, 2011) (unpublished manuscript), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1910471.

and “just plain cool.”¹⁰³ As previously mentioned, nine out of every ten Americans currently use a mobile phone,¹⁰⁴ and surely a greater number carry some form of wallet. Safely combining these into a single device is a logical progression. Additionally, mobile wallets can serve as a repository for purchases records, thus eliminating the problem of lost receipts and rejected returns.¹⁰⁵

However, money talks. Regardless of a new payment technology’s convenience, its success will ultimately depend on merchants’ willingness to facilitate mobile payments—a determination that starts and ends with the bottom line. Starbucks was one of the first to adopt a mobile-payment scheme, and its success is a prime example of how mobile payments may save merchants money. In January of 2011, Starbucks began offering a mobile-phone application that essentially operates as a prepaid gift card.¹⁰⁶ Through a consumer’s phone or computer, she can load funds from an existing credit or debit card onto the Starbucks card.¹⁰⁷ Then, when it comes time to pay, customers need only wave a barcode displayed on their mobile phone in front of the store’s scanner, which will automatically deduct the funds directly from the consumer’s virtual Starbucks card.¹⁰⁸ The card also has a loyalty function that offers special deals and allows consumers to earn a free drink for every twelve purchases made.¹⁰⁹ The program has resulted in an “unprecedented relationship between [Starbucks] and [the] customer.”¹¹⁰

More importantly, the mobile-payment option has increased Starbucks’s revenue by enticing customers into stores more frequently¹¹¹ and reducing transaction costs.¹¹² In May of 2012, Starbucks reported that over 25% of its customers paid with either a

103. Clay, *supra* note 101.

104. Rajan, *supra* note 64, at 446–47.

105. Hoofnagle et al., *supra* note 66, at 3.

106. Olga Kharif, *Starbucks Schools Other Retailers on Mobile Payments*, BLOOMBERG BUSINESSWEEK (August 23, 2012), <http://www.businessweek.com/articles/2012-08-23/starbucks-schools-other-retailers-on-mobile-payments>.

107. *Id.*

108. *Id.*

109. *My Starbucks Rewards*, STARBUCKS COFFEE CO., www.starbucks.com/card/rewards (last visited Aug. 22, 2013). This reward is only available to “gold” level customers—those who have made thirty purchases in a twelve-month period. *Id.*

110. Kharif, *supra* note 106 (statement of Adam Brotman, Starbucks’s chief digital officer).

111. *Id.* One Penn State University student began visiting Starbucks twice as frequently as a result of the iPhone application because “[t]hey send me daily specials, and that makes me want to run to Starbucks.” *Id.*

112. See Clay, *supra* note 101; see also Hoofnagle et al., *supra* note 66, at 3 (stating that “interchange fees represent the second highest expense (after payroll) at Target stores”).

virtual or physical Starbucks card.¹¹³ By reducing other noncash transactions by 25%, Starbucks has significantly reduced its purchase process costs by eliminating the credit or debit card company from the transaction without sacrificing convenience for the customer.¹¹⁴ Ideally, these merchant savings will lead to lower prices for the consumer.¹¹⁵ Similarly, reduced transactional costs can be achieved even without removing traditional debit and credit card issuers from the process. As of November 2012, consumers are able to use Square at Starbucks.¹¹⁶ Square reduces Starbucks's payment processing costs by linking consumers' preexisting credit or debit cards to Square's application, as opposed to loading funds onto a Starbucks card.¹¹⁷ Of course, Starbucks is not the only merchant to employ mobile-payment methods,¹¹⁸ but it is a case study in the industry's evolution and benefits for the involved parties.

Finally, mobile payments help grow consumer loyalty to particular merchants who employ the technology, thus increasing sales.¹¹⁹ Whereas payments by traditional debit or credit cards provide no incentive for consumers to become repeat customers of particular merchants, mobile-payment systems allow merchants to send specialized offers and incentives directly to consumers' phones.¹²⁰ Reward programs are mutually beneficial: they provide additional value to consumers for buying products they would have purchased anyway, and they increase merchant sales through incentive programs that in-

113. Clay, *supra* note 101.

114. *See id.*

115. Hoofnagle et al., *supra* note 66, at 4.

116. Press Release, Starbucks Coffee Co., Starbucks Offers Square Wallet Beginning Today, (November 7, 2012), <http://news.starbucks.com/news/starbucks-offers-square-wallet-beginning-today>.

117. *See id.*; *see also* Kharif, *supra* note 106 ("By letting its customers make purchases with their smartphones, Starbucks manages to pay fewer fees—which sometimes top 2 percent—on credit-card transactions.").

118. *See* Clay, *supra* note 101. PayPal recently announced partnerships with fifteen major retailers that will allow consumers to pay directly from their PayPal account through either their mobile phone or a point-of-sale system. *Id.* Those merchants include Abercrombie & Fitch, Advance Auto Parts, Aéropostale, American Eagle Outfitters, Barnes & Noble, Foot Locker, Guitar Center, Jamba Juice, and Office Depot. *Id.*

119. SMART CARD ALLIANCE, *supra* note 7, at 38.

120. *See, e.g.,* David Hatch, *Starbucks Brews Loyalty with Mobile Payment*, U.S. NEWS & WORLD REP. (May 15, 2012), <http://money.usnews.com/money/business-economy/articles/2012/05/15/starbucks-brews-loyalty-with-mobile-payment> (noting Starbucks's use of the mobile-payment technology by allowing customers to "download an app that's synced with their Starbucks loyalty card, which rewards frequent purchasers with free beverages"); *Rewards with Square Wallet*, SQUARE, <http://www.squareup.com/help/en-us/article/3922-rewards-with-square-wallet> (last visited Oct. 26, 2013) (providing special rewards for the first time a consumer visits a merchant, storing loyalty cards on your phone so that reward points are never lost, and automatically keeping track of the reward points you receive from each merchant).

spire consumers to shop more than they otherwise would.¹²¹ Similarly, merchants and advertisers will be able to tailor specific offers or sales to consumers based on their typical purchases.¹²² This benefit extends to the card issuer as well by allowing issuers to combine individualized customer purchase information with retailer data in order to deliver more personalized offers.¹²³

Despite all of the potential advantages of mobile payments, many consumers still harbor deep-seated privacy concerns with the technology.¹²⁴ Current privacy legislation, such as the Right to Financial Privacy Act of 1978¹²⁵ and the Gramm–Leach–Bliley Act,¹²⁶ is still being interpreted with respect to mobile payments.¹²⁷ It is clear that before mobile payments can become truly commonplace, these privacy concerns will need to be addressed;¹²⁸ however it is equally clear that the framework is in place for the industry to evolve.

III. ANALYSIS

The Durbin Amendment’s numerous unintended effects on banks are severely burdening and perhaps stifling the growth of the mobile-payment industry in two primary ways. First, the redistribution of costs in the banking industry is limiting innovation by merchants, card issuers, and financial institutions. Second, the twenty-one cent interchange fee’s anticompetitive consequences are closing the only viable avenue for new participants to enter the market. As a result, the Amendment is creating unnatural and inefficient forces in the debit card marketplace and inhibiting the natural progression of electronic payments in this country. Although intended as a financial sector regulation, the Amendment has inadvertently imposed ill-suited and inflexible government controls on the advancement of technology.

121. See SMART CARD ALLIANCE, *supra* note 7, at 38.

122. *Id.*

123. Chen, *supra* note 88.

124. Rajan, *supra* note 64, at 463 (“[Ninety percent] of consumers are concerned about data privacy and security in mobile transactions, and see financial institutions in the best position to address these concerns.”).

125. Right to Financial Privacy Act of 1978, Pub. L. No. 95-630, 92 Stat. 3697 (codified at 12 U.S.C. §§ 3401–3422 (2012)).

126. Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338 (1999) (codified in scattered sections of 12, 15 U.S.C.).

127. See Rajan, *supra* note 64, at 468.

128. Ultimately, the broad privacy concerns surrounding mobile payments are beyond the scope of this Comment and will not be discussed.

A. *The Durbin Amendment Disincentivizes
Mobile-Payment Innovation*

1. *The Durbin Amendment's Direct Impact on the Current
Financial Landscape*

In order to comprehend the severity of the Durbin Amendment's ramifications on innovation within the banking industry, one need only look at the numbers. The Amendment's regulations, which apply only to banks with greater than \$10 billion in assets,¹²⁹ affect only about sixty banks and three large credit unions.¹³⁰ The largest banks, including Bank of America and JPMorgan Chase (Chase), have nearly \$2 trillion in assets, while other banks, such as TCF Bank, just barely surpass the Amendment's \$10 billion threshold.¹³¹ Despite these enormous disparities, the Amendment's fee regulation applies equally to all banks within this category.¹³² Perhaps more significant than the size discrepancy is the fact that TCF Bank has no credit card business, instead dealing solely in debit cards.¹³³ Thus, the Amendment's fee restrictions have a far greater effect on TCF Bank's revenue than on that of most of the other banks that fall within the Amendment's purview.¹³⁴ Conversely, banks with assets of less than \$10 billion escape the reach of the Amendment and do not need to mitigate lost revenue.¹³⁵ In fact, there are about 7,000 banks and 7,500 credit unions that fall below the asset threshold.¹³⁶

129. 15 U.S.C. § 1693o-2(a)(6)(A) (2012).

130. Richard A. Epstein, *The Dangerous Experiment of the Durbin Amendment: Congress' Interchange Fee Limit is a Reckless Exercise in Price Regulation*, REGULATION, Spring 2011, at 24, 24.

131. FED. RESERVE BD., FEDERAL RESERVE STATISTICAL RELEASE: LARGE COMMERCIAL BANKS, <http://www.federalreserve.gov/releases/lbr/current/default.htm> (last updated June 30, 2013); see also Epstein, *supra* note 130, at 25 ("TCF Bank . . . has about \$18 billion in assets, less than 1 percent the size of the three biggest banks.").

132. See 15 U.S.C. § 1693o-2(a)(2). TCF Bank challenged the constitutionality of the Amendment for this reason. According to TCF's counsel in that suit, "TCF cannot raise fees in the face of direct competition from small banks that can continue to offer free debit cards," and as a result, "TCF must fight the Durbin Amendment because it receives no new revenue source from the passage of the legislation, for its preexisting right to charge customers is worth nothing under the current tilted playing field." Epstein, *supra* note 130, at 29; accord *TCF Nat'l Bank v. Bernanke*, 643 F.3d 1158, 1163–64 (8th Cir. 2011) (finding the Amendment constitutional).

133. Epstein, *supra* note 130, at 25.

134. *Id.*

135. 15 U.S.C. § 1693o-2(a)(6)(A); see also Odysseas Papadimitriou, *The Durbin Amendment Will Make You Give Up Your Debit Card*, BUS. INSIDER (Dec. 14, 2010), <http://www.businessinsider.com/the-durbin-amendment-will-make-you-give-up-your-debit-card-2010-12>.

136. Epstein, *supra* note 130, at 24. For example, Texas Capital Bank has a mere \$298 million more in assets than Israel Discount Bank of New York, but Texas Capital Bank is regulated by the Amendment while Israel Discount Bank may set its interchange rates as high as it likes. See FED. RESERVE BD., *supra* note 131.

The most obvious, palpable effect of the Amendment is the billions of dollars banks have lost from the reduced interchange fee.¹³⁷ It is estimated that in order to offset anticipated losses caused by the regulations, banks would have to charge account holders \$100 annually.¹³⁸ Instead, in what seems like a consumer-friendly gesture by comparison, Bank of America announced in September of 2011 that it would charge customers \$5 per month to maintain their debit card accounts.¹³⁹ This fee applied to all customers who made at least one purchase per month using their debit cards, regardless of whether they chose “debit” or “credit” as the method of transaction.¹⁴⁰ Bank of America openly acknowledged that the fee’s purpose was to compensate for losses incurred under the Amendment.¹⁴¹ Chase also discussed implementing a \$5 ATM withdrawal fee for non-Chase customers and a \$3 monthly debit fee in select markets.¹⁴² Not surprisingly, the public outcry against these fees was swift and intense.¹⁴³ The consumer base was so incensed that a Financial Securities Index poll found that 64% of consumers would change banks if a fee were imposed.¹⁴⁴ In addition to new account fees, many banks also considered eliminating debit card rewards programs and reducing the scale, flexibility, or availability of their debit card offerings.¹⁴⁵

The impact of the banks’ scramble to recover revenue lost as a result of the Amendment has disturbed even the most fundamental elements of the transaction framework. For instance, early checking systems required the merchant to bear the risk of bounced checks because the bank had little or no information about an account balance

137. Banks lost \$8 billion in the first year after the passage of the Amendment alone. Timothy H. Lee, *When Even Barney Frank Sings the Praises of Free Markets, We Must Listen*, FORBES (May 28, 2013), <http://www.forbes.com/sites/realspin/2013/05/28/when-even-barney-frank-sings-the-praises-of-free-markets-we-must-listen/>.

138. Epstein, *supra* note 130, at 26.

139. Eryk J. Wachnik, Consumer News, “*The Durbin Tax*” and *How the Banks Tried to Insure Their Bottom Line*, 24 LOY. CONSUMER L. REV. 318, 325 (2011).

140. *Id.*

141. *Id.* at 320.

142. *Id.* at 321.

143. *See id.* at 322 (“[S]ocial networking sites, such as Twitter, exploded with posts about the unfairness of Bank of America’s fee and the willingness of many consumers to take their business to another bank.”).

144. *Id.* (citing Claes Bell, *Americans Say They’d Bolt Bank Over Fees*, BANKRATE.COM (Mar. 21, 2011), <http://www.bankrate.com/finance/consumer-index/march-2011-financial-security-poll.aspx>). Twenty-eight percent of respondents stated that they would not change banks and the remaining eight percent did not know what they would do or did not have a checking account. *Id.*

145. Mary J. Dent, *A Rose by Any Other Name: How Labels Get in the Way of U.S. Innovation Policy*, 8 BERKLEY BUS. L.J. (SYMP. EDITION) 128, 159–60 (2011); *see also* Papadimitriou, *supra* note 135.

when a check was drawn.¹⁴⁶ Today, technology enables banks to continuously monitor credit and debit transactions, thereby allowing banks to assume the risk of bounced payments from the merchants.¹⁴⁷ Consequently, banks are more willing to authorize a payment on an overdrawn account into which they know a monthly paycheck will soon be deposited.¹⁴⁸ The charge for assuming that risk is then folded into the interchange fee.¹⁴⁹ The Amendment has upset this system and “introduc[ed] a serious regulatory inefficiency” into the debit market.¹⁵⁰ This will result in the shuffling of costs within the marketplace.

2. *The Redistribution of Costs in the Banking Industry Will Depress the Value of Payment Networks and Discourage Investment*

Payment cards are, by any measure, more innovative than other payment methods.¹⁵¹ Debit and credit cards provide an “instantaneous, convenient, global, secure payment system accessible 24 hours a day, anywhere in the world.”¹⁵² Moreover, innovation has led to longer bank hours, more bank branches, and new online and mobile banking products.¹⁵³ Compared to checks, which have remained fundamentally the same since their advent in the Middle Ages, it is easy to see how the marriage of payment cards and technology has succeeded.¹⁵⁴ Unfortunately, the Durbin Amendment’s price controls discourage innovation by making it more difficult to recoup investment in industry infrastructure.¹⁵⁵ Without innovation in the debit card industry, the prospect of developing a successful mobile-payment network is remote.

The structure of the payment-card marketplace makes it uniquely vulnerable to slowed growth as a result of these government-imposed losses. In an ordinary market, a buyer and seller operate independently of each other and without concern for the other’s success or

146. Epstein, *supra* note 130, at 27.

147. *Id.*

148. *See id.*

149. *Id.*

150. *Id.*

151. Zywicki, *supra* note 47.

152. *Id.*

153. Todd Zywicki, *The Dick Durbin Bank Fees*, WALL ST. J., Sept. 30, 2011, at A15.

154. *See* Zywicki, *supra* note 47. One significant change to checks has occurred in the past decade now that banks have begun converting paper checks into electronic images. *Id.* Still, checks have become so obsolete that Great Britain has announced a plan to terminate the acceptance of checks by 2018 in favor of electronic transactions. *Id.*

155. *Id.*

failure.¹⁵⁶ The payment-card market, however, operates differently. It is a two-sided market—a market without the same autonomy, where “the ability to satisfy one side of the market depends on the continued participation of the other.”¹⁵⁷ In the payment-card market, the debit interchange system creates equilibrium because both banks and merchants benefit from the increased use of debit cards.¹⁵⁸ That is, issuing banks receive payments from merchants in the form of interchange fees to support the banks’ efforts to draw in consumers.¹⁵⁹ The merchants must develop their own processing systems, while issuing banks must price their services most effectively to attract customers.¹⁶⁰

Consider this common scenario: an issuing bank offers debit cards for free but charges consumers for defaulting; in exchange for attracting customers to the payment system used by the merchant, the merchant pays the issuing bank an interchange fee.¹⁶¹ The Amendment, however, obstructs the payment from merchants to card issuers by imposing an artificially low ceiling on the value of that transaction.¹⁶² The Amendment considers only the marginal cost of transactions, as opposed to the overall cost of building, maintaining, and improving the network—a failure that has forced banks to cut costs in other areas.¹⁶³ One such cut involves issuing banks offering a smaller bundle of services to merchants.¹⁶⁴ For instance, merchants may be asked to assume the losses from overdrawn accounts, or banks may simply stop contributing funds to the introduction of new technologies, such as mobile-payment platforms.¹⁶⁵ The resulting inefficient

156. Epstein, *supra* note 130, at 26 (citing William F. Baxter, *Bank Interchange of Transactional Paper: Legal and Economic Perspectives*, 26 J.L. & ECON. 541 (1983)) (“[T]he seller of apples wants high prices from customers who seek low prices.”).

157. *Id.* Epstein uses the example of a singles bar to illustrate a two-sided market. *Id.* According to Epstein, it is easier to get men than women to attend a singles bar. *Id.* Therefore, charging men and women the same price for drinks would result in an excess of men, which would cause the bar to fail. *Id.* Assuming that the uniform price of a drink is \$10, men will be willing to pay \$15 to attract women, while women will only have to pay \$8. *Id.* Some of the men’s surplus is used to bring the market into equilibrium, making both sides better off. *Id.* In this or any two-sided market, Epstein explains, there is a transfer of payment between the two groups facilitated by a “network”—in this case the bar. *Id.*

158. *See id.*

159. *Id.*

160. *Id.* at 27.

161. *See* Epstein, *supra* note 130, at 27. In this example, the interchange network operated by Visa or MasterCard is serving the same function as the singles bar owner. *See supra* note 157.

162. Lee, *supra* note 137; *see also* 12 C.F.R. § 235.3 (2012).

163. Lee, *supra* note 137.

164. Epstein, *supra* note 130, at 27.

165. *Id.*

funding structure will likely lead to system-wide cutbacks, thus preventing the introduction of new technologies.¹⁶⁶

Banks could also avoid the Amendment's reach by only investing in new technologies that operate outside of the Amendment's purview. The definition of "debit card" under the Amendment includes any product that directly debits a consumer's account.¹⁶⁷ This definition encompasses mobile-payment systems that similarly deduct funds directly from a consumer's account; thus, banks will be less likely to contribute to that payment model knowing that their profit potential is statutorily capped. New technology and infrastructure are needed to get started, but the Amendment does not allow for banks and merchants to fund these efforts.¹⁶⁸ Notably, the Amendment does not regulate prepaid mobile accounts,¹⁶⁹ such as those offered by Starbucks or PayPal.¹⁷⁰ The likely result will be "regulatory arbitrage" as financial institutions will be forced to design products "not solely to maximize their economic and technological viability but to gerrymander them out of the Durbin [A]mendment's net."¹⁷¹

Lastly, the Amendment will depress the marketplace as a whole. The payment-card industry is based on a network that links together consumers, merchants, and financial institutions.¹⁷² Similar to any other profit-based network, the payment-card network's value increases as the number of users on all sides increases and the costs of operating the network decrease.¹⁷³ Therefore, if the Amendment forces banks to impose new and greater fees on consumers, causing consumers to exit the banking industry, the overall value of the network will decrease.¹⁷⁴ The upshot would be that by significantly deterring investment in the new infrastructure, card issuers would instead focus on minimizing the cost of operations.¹⁷⁵ Put simply, "[i]f card issuers cannot recover the cost of new innovation, then they sim-

166. *See id.*

167. 15 U.S.C. § 1693o-2(c)(2) (2012). The Amendment defines "debit card" as "any card, or other payment code or device, issued or approved for use through a payment card network to debit an asset account (regardless of the purpose for which the account is established), whether authorization is based on signature, PIN, or other means." *Id.*; *see also* Zywicki, *supra* note 47.

168. *See* Zywicki, *supra* note 47.

169. 15 U.S.C. § 1693o-2(a)(7); *see also* Papadimitriou, *supra* note 135 ("[P]repaid cards are unregulated by the Durbin Amendment . . .").

170. *See supra* notes 106–118 and accompanying text.

171. Zywicki, *supra* note 47.

172. *Id.*

173. *Id.*

174. *Id.*

175. *Id.*

ply will not innovate.”¹⁷⁶ If that occurs, mobile-payment technology is sure to be one of the first casualties.

3. *The Durbin Amendment’s Interchange-Fee Limit and Small-Bank Exception Are Driving Consumers Away from the Large Banks that Are More Likely to Fuel Innovation*

While the overall value of the marketplace will certainly drive investment decisions, the most persuasive factor will be the number of consumers participating in the market. As it stands, the Durbin Amendment is likely to drive consumers either (1) away from the regulated large financial institutions to smaller, exempt banks, or (2) out of the banking system altogether and into the comforting arms of cash and prepaid cards. Both of these consumer migrations will drastically reduce the value of the debit card industry and disincentivize the largest banks from growing mobile-payment options within it. Finally, these two appreciable shifts in the payment marketplace will likely negate any savings that Senator Durbin claims to have intended for merchants.

The first way the Amendment will shift consumers is through the small-bank exception, which applies to banks with less than \$10 billion in assets.¹⁷⁷ While larger banks must consider recouping Durbin-created losses through cost-saving measures such as slashing rewards programs, small banks will remain unregulated and thus able to offer more appealing rewards programs on their debit cards.¹⁷⁸ Large banks have even eliminated free checking accounts in an attempt to recover lost revenue.¹⁷⁹ The percentage of bank accounts eligible for free checking at Durbin-affected large banks peaked at 76% in 2008—up drastically from under 10% in 2001—but has since plummeted to

176. *Id.*

177. 15 U.S.C. § 1693o-2(a)(6)(A) (2012).

178. Papadimitriou, *supra* note 135. For example, “Co-op Services Credit Union of Livonia, MI, announced a policy involving a \$105 new account bonus to any first time customer who opened an account with direct deposit.” Laura Brown et al., *The Durbin Derby – Are There Any Winners?* 16 n.73 (Jan. 9, 2012) (unpublished manuscript), available at http://www.americanbar.org/content/dam/aba/events/business_law/2012/01/consumer/2012_consumer_committee_meeting_agenda.authcheckdam.pdf (presented at the ABA Committee on Consumer Financial Services 2012 Winter Meeting, Jan. 7–10, 2012). Also, “Randolph-Brooks Federal Credit Union of Texas offered to give members \$0.10 back for every debit card purchase they made over a three month period.” *Id.* Finally, and perhaps most telling, FirstBank Colorado of Lakewood, Colorado “launched a campaign to provide any potential customers with comparison information on his current bank’s fees, in order to show that potential customer how much he could save with FirstBank’s free checking account.” *Id.*

179. See Lee, *supra* note 137.

45% in 2012 following the passage of the Amendment.¹⁸⁰ Taken together, it is clear that small banks stand to gain an increased share of the debit card marketplace by luring consumers who are unwilling or unable to sustain the increased cost of banking at large banks.¹⁸¹ This shift is likely to be especially drastic among low-income consumers. While wealthier consumers may choose to remain with large banks and avoid new banking fees by using their credit cards, low-income consumers are less likely to be approved for credit and thus more likely to switch banks.¹⁸²

Many analysts maintain that the small-bank exception will not yield these positive effects on exempt institutions, and that a shift in consumers from large to small banks will not occur.¹⁸³ Even Federal Reserve Board Chairman Ben Bernanke believed that the exception would not operate as intended because small banks would be forced to lower their transaction costs in order to compete with the statutorily restricted large banks.¹⁸⁴ However, a recent survey by the Federal Reserve allayed those concerns, finding instead that the small-bank exception is “working as intended” because small banks and credit unions were able to charge “more than double the average fee of large lenders for debit transactions” in 2012.¹⁸⁵

Consumer migration to small, less expensive banks may appear to epitomize the free market, but it will have untoward consequences on the future of mobile payments. Large banks drive innovation: they possess the resources and motivation to invest in new systems such as

180. Todd Zywicki, *Consumers are the Winners in the Visa/MasterCard Antitrust Settlement*, FORBES (Aug. 21, 2012), <http://www.forbes.com/sites/realspin/2012/08/21/consumers-are-the-winners-in-the-visamastercard-antitrust-settlement/>.

181. See Papadimitriou, *supra* note 135.

182. Zywicki, *supra* note 153.

183. See, e.g., Stephen J. Shapiro, *The Small Bank Exemption to Dodd-Frank's Swipe Fee Regulations: "Honor-All-Cards" Contractual Provisions May Not Protect Small Banks*, BLOOMBERG L. REP. – BANKING & FIN., Apr. 4, 2011, at 4 (“[T]he industry has argued[] the market will force smaller banks to lower their swipe fees to compete with the capped rates the larger banks will be required to charge.”).

184. *Congress Updated on Dodd-Frank, Debit Card Interchange Fee Rule*, FED. BANKING L. REP. (CCH), Report Letter No. 2407, at 6, 6–7 (Feb. 24, 2011) (Bernanke stated the possibility that, “because merchants will reject more expensive cards from smaller institutions, or because networks will not be willing to differentiate the interchange fee for issuers of different sizes . . . [the] exemption will not be effective in the marketplace” (alteration in original)).

185. Michael Crittenden, *Study Rebuts Banks on Swipe Fees*, WALL ST. J., May 24, 2013, at C2. Banking industry and retailer representatives have questioned that study because of the small sample size and anecdotal evidence to the contrary. *Id.* A spokesman for the Credit Union National Association stated that he welcomed the results of the study, but cautioned that the Association “continue[s] to have grave concerns about debit-interchange income for credit unions over the long term.” *Id.*

mobile payments.¹⁸⁶ In contrast, small institutions generally do not spearhead innovation within the banking system.¹⁸⁷ Thus, while it may appear that consumers remain unaffected by the Amendment because they will simply obtain no-fee debit accounts from other banks, that shortsighted analysis ignores the need for large banks to champion the growth of mobile payments. If returns are the primary reason for anyone to consider an investment, the Amendment has all but sealed the fate of mobile-payment innovation by guaranteeing that no return is possible.¹⁸⁸

Additionally, the higher cost of debit transactions may drive a large number of consumers out of the mainstream banking system altogether. When faced with increased fees, many consumers will choose to rely more heavily on unregulated payment methods such as prepaid cards and cash.¹⁸⁹ In fact, it is estimated that new fees on previously free checking accounts will drive more than one million customers out of the mainstream banking system.¹⁹⁰ Even consumers who do not wholly abandon their debit accounts will be disincentivized to use their newly regulated debit cards.¹⁹¹

This anticipated shift to small, unregulated banks would negate the cost benefit that merchants (and therefore consumers) were meant to enjoy and that served as the primary impetus for the Amendment.¹⁹² Heartland Payment Systems, one of the nation's largest payment processors, estimated that the average merchant would save around \$1,000 per year because of the Amendment.¹⁹³ However, that estimate gave no consideration to the possibility that merchants may, in turn, be forced to assume costs that were previously paid by banks. In fact, a recent study found that one year after the Amendment took effect, consumers were paying, on average, 1.5% more at popular retailers than they were prior to its enactment.¹⁹⁴ Sixty-seven percent of the retailers visited for that study had either kept prices the same or

186. See Zywicki, *supra* note 47.

187. *Id.*

188. See generally *id.* (“[T]he Durbin [A]mendment’s price controls on debit cards by definition will reduce the incentive to make any investments that cannot be recouped . . .”).

189. *Id.*

190. *Id.*

191. See Zywicki, *supra* note 47.

192. See *id.*

193. Wachnik, *supra* note 137, at 325.

194. Elec. Payments Coal., *Where’s the Debit Discount? The Durbin Effect: Retailers Gain Without Consumer Benefit*, WHERE’S MY DEBIT DISCOUNT? 3 (Sept. 28, 2012), http://wheresmydebitdiscount.com/wp-content/themes/epc/media/Durbin%20White%20Paper_092812_small.pdf.

increased prices since the enactment of the Amendment.¹⁹⁵ Despite those price increases and the Amendment's favoritism, merchants have not realized increased profits—strong evidence that the interchange-fee ceiling was ill-conceived. Merchants represented the only group that the Amendment could potentially have encouraged to invest in mobile-payment infrastructure. Now that merchants must shuffle costs and reassess business strategies in the same way as large banks, innovation will necessarily be put on hold.

The Amendment's underlying policy goals also undermine the mobile-payment industry's growth. Given that the Amendment was passed in the wake of the 2008 financial crisis and applies only to banks with greater than \$10 billion in assets, the government's hierarchy of interests seems obvious: "The prevailing political winds favored the interests of small banks over merchants and the interests of merchants over big banks."¹⁹⁶ After all, debit cards obviously played no part in what was "at heart a *credit* crisis."¹⁹⁷ Still, Senator Durbin exploited "the frenzied anti-bank environment of the post-crisis era" to pass an interchange-fee regulation designed to create a windfall for retailers.¹⁹⁸ While politicians appear to favor certain players and redistribute wealth in the market, new mobile-payment companies will likely find themselves unable to gain footing. Without oversight of politicians' true motives, it remains relatively easy for them to grant "political favors"—a term some use to describe the Amendment.¹⁹⁹

Lastly, the most authoritative support for these contentions, and what should serve as the coup de grâce for the Amendment, came from one of the coauthors of Dodd–Frank. Congressman Barney Frank, a man described as "hyper-regulatory," recently conceded that "a free market approach in this area will be better for the economy and all concerned parties than the current system [under the Amendment]."²⁰⁰ The banking industry continues to endure the unintended consequences of the Amendment's unnatural legislative pressures on what was a free market, which has forced the industry's players to

195. *Id.* That study found that prices were \$2.22 (or 6.6%) more for the same items at Home Depot in Atlanta, Georgia. *Id.* at 10. Walmart saw increases of \$0.80 (or 5.4%) for the same items in Portland, Maine. *Id.* 7-Eleven prices increased \$1.00 (or 2.6%) for the same items in Washington, D.C. *Id.* Finally, Walgreens showed a price increase of \$0.30 (or 2.9%) for the same items in Boston, Massachusetts. *Id.*

196. Zywicki, *supra* note 55, at 204.

197. *Id.*

198. *Id.*

199. *See id.* at 206.

200. Lee, *supra* note 137. Indeed, "[w]hen Barney Frank sings the praises of the free market as a superior alternative, it speaks volumes." *Id.*

reassign costs and risks.²⁰¹ Unsurprisingly, banks and merchants are less willing to innovate in the arena of mobile payments while their own finances and the marketplace remain atrophied due to Dodd–Frank.²⁰²

B. The Durbin Amendment is Naturally Anticompetitive and Prevents New Participants from Entering the Mobile-Payment Marketplace

One of the Durbin Amendment’s most egregious offenses is its exclusion of new entrants from the payment-card market. The Amendment’s provisions operate as a barrier to entry in two ways: (1) the interchange-fee limit of twenty-one cents²⁰³ leaves little room for new mobile-payment companies to price themselves below the market; and (2) the requirement that card transactions be offered on at least two networks²⁰⁴ prevents new technologies from competing for a share of the market that is primarily occupied by Visa and MasterCard.²⁰⁵

First, the Amendment has arbitrarily reduced interchange fees for incumbent providers of payment systems.²⁰⁶ This cap discourages a new mobile-payment-industry participant from entering the market as a “low-cost provider.”²⁰⁷ Where a startup is forced to compete at the same price point as a well-established market participant, such as Bank of America, it is unlikely that the startup will achieve economic viability. This consequence is exacerbated by the small-bank exception to the Amendment, which is expected to afford small banks an increased share of the marketplace.²⁰⁸

Moreover, if the interchange-fee regulation merely discourages market entrants, the dual network requirement essentially forecloses entry. The Amendment now requires that every payment card be accessible by at least two card networks.²⁰⁹ As the startup Isis articulated in its plea to the Federal Reserve,²¹⁰ it is nearly impossible for a

201. See Wachnik, *supra* note 137, at 325; see also Zywicki, *supra* note 47.

202. Zywicki, *supra* note 47.

203. 12 C.F.R. § 235.3(b)(1) (2012); cf. 15 U.S.C. § 1693o-2(a)(2) (2012).

204. 15 U.S.C. § 1693o-2(b)(1)(A).

205. See Laura Brown et al., *supra* note 178 (manuscript at 4) (“The Visa and MasterCard systems are responsible for processing 83% of all debit card transactions, with other small network operators controlling the remainder.”).

206. Zywicki, *supra* note 47.

207. *Id.*

208. Papadimitirou, *supra* note 135.

209. 15 U.S.C. § 1693o-2(b)(1)(A).

210. For a more detailed analysis of the rise and fall of Isis, see *infra* notes 212–223 and accompanying text.

startup to secure investments when its service is necessarily pitted against the industry's biggest players from the start.²¹¹

Taken together, these two provisions serve as difficult hurdles to prospective market entrants at best, and insurmountable obstacles at worst. As a result of the Amendment's restrictions, new entities will be unable to compete as alternatives to traditional banking because they cannot price themselves below the market. Mobile-payment entrepreneurs will be equally unable to garner support as an alternative to traditional payment networks because the Amendment dictates that they must immediately compete with the likes of Visa and MasterCard. Seemingly, the only remaining option for new mobile-payment companies looking to break into the market is to align with preexisting market players.

For these reasons, this Comment advocates for a mobile-payment exception to the Amendment. Congress should not allow Senator Durbin's eleventh hour, unsubstantiated regulation of the complex financial industry to prevent the natural and beneficial evolution toward mobile payments.

IV. IMPACT AND RECOMMENDATIONS

A. *The Growth and Stagnation of Isis*

Before turning to this Comment's purposed solution to the stifling effects of the Durbin Amendment, it is helpful to briefly recount the story of Isis, a real-world example of the aforementioned concepts in action. In its current form, Isis is the prototypical mobile wallet; it holds consumers' payment cards in virtual form on a user's phone and uses NFC technology to make payments at the point of sale.²¹² However, Isis is dramatically different from the technology imagined in its original business plan. It began as a joint venture formed by three major wireless companies: AT&T, T-Mobile, and Verizon.²¹³ Their stated goal was to "build[] a mobile payment network that utilizes mobile phones to make point-of-sale purchases."²¹⁴ This was an ambi-

211. See Letter from Michael J. Abbott, CEO, Isis, to Bd. of Governors of the Fed. Reserve Sys. (Feb. 22, 2011) [hereinafter Abbott Letter], available at http://www.federalreserve.gov/SECRS/2011/March/20110302/R-1404/R-1404_022211_67244_584250173294_1.pdf.

212. *How to Pay with Isis*, supra note 97.

213. Colin C. Richard, *Dodd-Frank, International Remittances, and Mobile Banking: The Federal Reserve's Role in Enabling International Economic Development*, 105 NW. U. L. REV. COLLOQUY 248, 254 (2011).

214. *Id.* (alteration in original) (quoting Press Release, AT&T Mobility LLC, AT&T, T-Mobile and Verizon Wireless Announce Joint Venture to Build National Mobile Commerce Network (Nov. 16, 2010), available at <http://www.att.com/gen/pressroom?pid=1867-&cdvn=news&newsarticleid=31369&mapcode=>).

tious objective, albeit a subtle one that warrants emphasis: Isis did not want to operate its platform on the preexisting networks run primarily by Visa and MasterCard. Rather, Isis aimed to *compete* with Visa and MasterCard as a payment network, a goal that seemed to indicate “the beginning of the transition from a card-based payment economy to a mobile-based payment economy.”²¹⁵ Isis’s network was to be the uniform standard for mobile payments²¹⁶ and would have provided unbanked customers with electronic bill pay and banking services.²¹⁷

Unfortunately, not only was Isis’s ambition never realized, it did not even have the opportunity to make a sincere attempt. Isis planned to charge merchants a lower interchange price than the prevailing market rate.²¹⁸ The lower rate was intended to entice merchants to make the substantial up-front investment needed to equip their stores with the mobile-payment infrastructure—in Isis’s case, an NFC reader.²¹⁹ That plan became untenable in the wake of the Amendment’s interchange regulation, which essentially halved the fee that Isis sought to undercut.²²⁰ Consequently, Isis filed a comment letter to that effect with the Federal Reserve in February of 2011.²²¹ The letter also explained how the requirement that transactions be capable of processing on two networks stifled innovation: “Why would anyone invest in a new payment system if they are forced . . . to add a scale-competitor? This would seem akin to requiring small businesses to locate only next to an established national ‘category killer’ retailer in the same product line.”²²² The letter also asserted more broadly that “it is still unclear if any new debit network will emerge if there is no viable return on investment due to fee caps,” and it strongly urged the Board to “consider the unintended consequences [of the Amendment] and their potential impact on innovation, jobs and the competitiveness of the U.S. payments market.”²²³

The Isis case study demonstrates how the government’s overregulation of the financial industry has had devastating effects on card issu-

215. *Id.* at 254 & n.45.

216. Rajan, *supra* note 64, at 463.

217. Zywicki, *supra* note 47. It should also be noted that the pool of unbanked consumers is expected to grow in the wake of the Amendment. *Id.*

218. *Id.*

219. *Id.*

220. See 12 C.F.R. § 235.3(b) (2012) (capping interchange fees for electronic debit transactions at 21 cents); see also Debit Interchange Fees and Routing, 76 Fed. Reg. 43,394, 43,397 (July 20, 2011) (“The average interchange fee for all debit card transactions [in 2009] was 44 cents per transaction . . .”).

221. See Abbott Letter, *supra* note 211.

222. *Id.* at 1–2.

223. *Id.* at 2.

ers, merchants, banks, and as a result, the mobile-payment industry. The Amendment has become the quintessential example of public policy gone wrong.²²⁴ The obvious solution for overregulation is deregulation, which would mean a wholesale repeal of the Amendment.²²⁵ However, it is clear that the Amendment's effect on mobile payments would not be a sufficient impetus for repealing such a far-reaching regulation. Nonetheless, the mobile-payment industry has the potential to make a substantial enough impact on the economy to warrant redress. One industry analyst estimates that the total value of mobile payments globally will reach \$670 billion by 2015.²²⁶ Apart from total repeal, two viable solutions warrant discussion: (1) provide incentives for merchants to install mobile-payment infrastructure, and (2) create an exception to the Amendment's regulations for mobile-payment transactions.

B. Incentives for the Adoption of Mobile-Payment Technology

One potential solution is to incentivize the use of mobile payments in order to offset some of the costs created by the Durbin Amendment. The need for incentives to jumpstart the mobile-payment industry was apparent even before consideration of the Amendment's damaging effects. For instance, the debate over chip-enabled cards, largely the same technology as mobile payments, centers on a similar "chicken-and-egg issue."²²⁷ "Many merchants say they don't want to invest in the new technology if banks won't issue the cards. The banks, meanwhile, say they don't want to invest in the cards because newer technology, such as mobile-device payments, will leapfrog the need for chip-enabled plastic."²²⁸

In response to that conflict, some of the industry's key players have implemented incentives for merchants to invest in the necessary infrastructure. Visa has instituted a program encouraging merchants to

224. See Lee, *supra* note 137.

225. The repeal of the Amendment has support. U.S. Representatives Jason Chaffetz and Bill Owens introduced a bill to repeal the Amendment in 2011. Robb Mandelbaum, *In Battling Merchants, Banks Still Hope to Overturn Durbin Rules*, N.Y. TIMES (Oct. 17, 2011, 1:00 P.M.), <http://boss.blogs.nytimes.com/2011/10/17/in-battle-with-merchants-banks-still-hope-to-overturn-durbin-amendment/>.

226. Olga Kharif, *Visa Unveils Incentives to Speed Shift to Mobile-Payment Systems*, BLOOMBERG (Aug. 9, 2011), <http://www.bloomberg.com/news/2011-08-09/visa-unveils-plan-to-speed-adoption-of-mobile-payment-systems.html>.

227. Robin Sidel & Ann Zimmerman, *Visa Pushing New Card Technology*, WALL ST. J. (Aug. 10, 2011), <http://online.wsj.com/article/SB10001424053111904480904576498484264333872.html> ("In addition to accepting traditional swipe cards and the chip-enabled cards, the cash-register terminals also will be equipped to process payments made with cell phones.").

228. *Id.*

adopt mobile-payment-ready technology at their establishments.²²⁹ As with any effective incentive, Visa's plan contains both a carrot and a stick. The carrot is Visa's elimination of its requirement that merchants certify their compliance with anti-fraud security standards if at least 75% of Visa transactions come from the terminal.²³⁰ By eliminating the certification requirement, merchants save more than \$2 billion per year.²³¹ Conversely, the stick is that merchants who do not install the technology will be liable for costs of fraud arising from the chip-enabled card—costs that are currently borne by banks.²³² McDonald's and Nordstrom have come forward in support of Visa's plan.²³³ Similarly, PayPal plans to subsidize its point-of-sale service, meaning that merchants would pay less for PayPal transactions than they do for more established credit and debit processors.²³⁴ These incentive-based strategies are aimed at facilitating the growth of mobile-payment technology by making the necessary infrastructure more accessible to merchants.

Unfortunately, while these privatized incentives encourage merchants to invest in the corresponding point-of-sale technology, they do nothing to offset the enormous Durbin-created losses incurred by banks. Incentives also do little to reduce the barriers to entry that, for example, prevented Isis from participating in the market. Thus, although private programs may have the long-term effect of bringing mobile payments into more businesses, this is likely insufficient redress.

C. A Mobile-Payment Exception

Alternatively, legislators could create an exception to the interchange-fee ceiling for mobile payments, which can be modeled after the interchange-fee-cap exemption for banks with less than \$10 billion in assets.²³⁵ This additional exception should be drafted with banks and merchants' input and should allow them to privately agree on the proper fee for all transactions processed over a user's mobile device. Allowing natural market forces to dictate the costs and fees associated with mobile payments will encourage merchants and banks

229. See generally *id.*

230. Sidel & Zimmerman, *supra* note 227.

231. See Kharif, *supra* note 226.

232. Sidel & Zimmerman, *supra* note 227.

233. Kharif, *supra* note 226.

234. Alistair Barr, *PayPal Exec Woos Big Retailers with Pricing, Data*, REUTERS (Feb. 10, 2012), <http://www.reuters.com/article/2012/02/10/paypal-kingsborough-idUSL2E8D8AE720120210>.

235. See 15 U.S.C. § 1693o-2(a)(6)(A) (2012).

to invest in the technology, as well as reopen the door for startups to enter the market at a discounted rate. It is therefore the conclusion of this Comment that an exception for transactions made with mobile-payment technology would be best suited to mend the damage caused by the Durbin Amendment.

To address feasibility concerns, it must initially be noted that alterations to Dodd–Frank have been discussed in Congress as recently as December 2012.²³⁶ Republican lawmakers, resigned to the fact that Dodd–Frank will not be repealed in its entirety, are turning to “technical corrections” of the Act.²³⁷ Indeed, some corrective measures have already been approved in the House.²³⁸ “But what constitutes a technical correction is in the eye of the beholder,” and while proponents of Dodd–Frank intend to use the corrections to enhance the regulations, opponents see it as an opportunity to undermine the entire Act.²³⁹

As a correction to Dodd–Frank, an exception for mobile payments would be beneficial to both banks and merchants. First, it would allow issuers to charge a rate comparable to the forty-four cent interchange fee that existed prior to Dodd–Frank for all debit transactions conducted with a user’s mobile device.²⁴⁰ If issuers could receive twice as much revenue from mobile transactions as they did from traditional card payments, they would be more likely to encourage consumers to adopt the technology. This could manifest itself as a greater number of mobile options or more enticing rewards programs for mobile accounts. Notably, the fee would not need to be very high; a carefully drafted exception would allow banks to set fees commensurate with costs. Moreover, issuers would be more willing to provide merchants with the necessary point-of-sale equipment if they knew they could receive a higher interchange fee. At the very least, issuers would be likely to subsidize costs of new infrastructure for merchants.

236. See Cheyenne Hopkins, *Technical Fixes Prompt Suspicion from Dodd-Frank Backers*, BLOOMBERG (Dec. 9, 2012), <http://www.bloomberg.com/news/2012-12-10/technical-fixes-prompt-suspicion-from-dodd-frank-backers.html>.

237. Derek Klobucher, *Dodd-Frank Stands Technically Corrected and Small Banks Lose*, FORBES (Dec. 17, 2012), <http://www.forbes.com/sites/sap/2012/12/17/dodd-frank-stands-technically-corrected-and-small-banks-lose/>.

238. See Hopkins, *supra* note 236 (“The chamber approved a bill in March to exempt manufacturers and commercial swap-users from collateral requirements and ease regulations on inter-company trades. Other measures have won committee approval and are awaiting floor votes.”).

239. Klobucher, *supra* note 237.

240. Sandwith, *supra* note 36, at 224.

Most importantly, the exception would create an impetus for sellers of inexpensive items to invest in mobile-payment technology. Before the Amendment took effect, card issuers gave merchants discounts on small transactions.²⁴¹ When the interchange cap took effect, the banking industry eliminated those discounts.²⁴² Chris McWilton, president of U.S. markets for MasterCard, explained that old interchange fees subsidized the small-ticket discounts, but the model could no longer be sustained under the Amendment.²⁴³ In response, small-item merchants such as Dairy Queen and Redbox are raising prices or considering incentives for customers who pay with cash.²⁴⁴ Therefore, if mobile payments are beyond the Amendment's reach, card issuers may once again have discretion to gradate the interchange rate according to the size of purchases. Just as issuers once offered discounts to encourage a greater use of debit cards,²⁴⁵ this proposed exception would similarly encourage greater use of mobile payments.

The cumulative effect of this exception would carry over to larger retailers as well. As more consumers are persuaded to utilize mobile payments, retailers of all sizes will be likely to follow suit in an effort to attract that demographic. At the outset, a higher fee for mobile payments would almost certainly trouble merchants. This was the same concern expressed when OpenTable first gained notoriety, and its proliferation is analogous to this Comment's mobile-payment proposal. OpenTable allows users to make dining reservations online and collects a fee from the corresponding restaurant.²⁴⁶ Additionally, OpenTable requires a large up-front investment in technology infrastructure.²⁴⁷ Although restaurants concede that the price is "insanely high," they recognize that the service is "amazing," "incredible," and "money well spent" because of the increase in business OpenTable creates.²⁴⁸ In 2012, more than 26,000 restaurants subscribed to

241. Robin Sidel, *Debit-Fee Cap Has Nasty Side Effect*, WALL ST. J. (Dec. 8, 2010), http://online.wsj.com/article/SB10001424052970204319004577084613307585768.html?mod=WSJ_hp_LEFTTopStories#printMode.

242. *Id.*

243. *Id.*

244. *Id.*

245. *See id.*

246. Mark Caro, *Reservations Please: Open Table's Online Service Convenient for Diners but Pricey for Restaurants*, CHI. TRIB., Nov. 15, 2012, § 5, at 1. OpenTable charges one dollar per seat for all reservations made through OpenTable's own website and twenty-five cents per seat for all reservations made from a restaurant's website that directs diners to OpenTable. *Id.*

247. *See id.* The subscription price for an OpenTable computer is \$199 per month and there is an initial installation and equipment fee of \$200. *Id.* The OpenTable bill for the Publican restaurant in Chicago is more than \$3,400 per month. *Id.*

248. *Id.*

OpenTable, up from 17,000 the year before.²⁴⁹ One prominent Chicago restaurant group estimated that 50%–60% of its restaurants' reservations are made through OpenTable.²⁵⁰

Just as OpenTable is seen as a necessary evil for restaurants, larger retailers may someday have the same view of mobile-payment technology. As issuers and financial institutions work to shepherd consumers toward mobile payments, consumers may choose to conduct their business at retailers that accept mobile payments. This will be especially true with "big box" retailers, which sell products that are identical to the products sold by competitors.²⁵¹ If, for example, a bank offers a lucrative rewards program for mobile payments in order to encourage participation, those utilizing the service will shop at retailers accepting mobile payments before turning to those that do not.

Finally, an exception for mobile payments would eliminate the barrier to entry that prevented Isis from implementing its original business model.²⁵² Isis intended to offer a mobile-payment platform to merchants for a smaller fee than mainstream issuers such as Visa and MasterCard.²⁵³ If the ceiling for interchange fees were eliminated, issuers would increase the price for mobile payments, allowing startups capable of pricing themselves below the market to enter.

V. CONCLUSION

The Dodd–Frank Act was passed as the federal government's attempt to reform the financial industry in the wake of the 2008 financial crisis.²⁵⁴ It was a lofty piece of legislation with an admirable intention: to prevent another similar crisis.²⁵⁵ The Act also included a narrow amendment, known as the Durbin Amendment, which sought only to reduce the fees that debit card issuers were charging

249. *Id.* In 2011, 44% of all reservation-taking North American restaurants used OpenTable, and "12[%] of diners seated with reservations at *any* North American restaurant made those arrangements through OpenTable." *Id.*

250. *Id.* Ian Goldberg, vice president of Boka Restaurant Group, opined that "a lot of people are going online and checking it out, and if they don't see your restaurant, they might not go." *Id.*

251. This argument presupposes that price and convenience of obtaining the products are the same across retailers. Obviously, if one retailer offers a sale on a particular product, consumers may be willing to forgo whatever benefits they derive from the use of mobile payments in exchange for the lower price.

252. *See Zywicki, supra* note 47.

253. *Id.*

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

255. Murdock, *supra* note 19, at 1246.

merchants per transaction.²⁵⁶ This Amendment was both applauded²⁵⁷ and abhorred by observers, who nervously predicted the effects it would have on the banking industry.²⁵⁸ One of the Amendment's unintended and unforeseen consequences, though, is the potential destruction of the budding mobile-payment industry.

The use and prominence of mobile payments continues to rise as the technology becomes more available and convenient.²⁵⁹ Mobile payments can take many forms; however, the true success of these payments requires harmony between each institution contributing to a transaction, rather than the exact method of mobile payment.²⁶⁰ To be sure, the industry's success is desirable because mobile payments provide greater convenience, speed, and value to consumers and merchants alike.²⁶¹

Unfortunately, the Amendment's restriction on interchange fees is wreaking havoc on mobile payment's potential success. The Amendment devalues the entire payment industry and redistributes its wealth in a way that stifles innovation.²⁶² Further, the Amendment has anticompetitive consequences in that it erects barriers that prevent startups from competing with established mobile-payment institutions.²⁶³

These consequences, however, need not be permanent. This Comment recommends that an exception be added to Dodd-Frank that allows payments made by mobile devices to avoid the twenty-one cent interchange cap. Allowing natural market forces to govern the industry will reverse the damage done by the Durbin Amendment and promote the growth of necessary technology.

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256. 15 U.S.C. § 1693o-2(a)(2) (2012).

257. See, e.g., Lisa Farrell, Comment, *A Step in the Right Direction: Regulation of Debit Card Interchange Fees in the Durbin Amendment*, 15 LEWIS & CLARK L. REV. 1077 (2011).

258. See, e.g., Zywicki, *supra* note 55.

259. See Rajan, *supra* note 64, at 447.

260. See *supra* notes 79–85 and accompanying text.

261. See *supra* notes 100–123 and accompanying text.

262. See *supra* notes 129–202 and accompanying text.

263. See *supra* notes 203–211 and accompanying text.

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