Joshua R. Floum,
General Counsel, Visa Inc.

Written Testimony

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House Committee on the Judiciary
Task Force on Competition Policy and Antitrust Laws

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Chairman Conyers and Members of the distinguished committee, my name is Josh Floum, and I am an Executive Officer and General Counsel for Visa Inc. I want to thank the Antitrust Task Force for the opportunity to participate in this important hearing and explain why Visa's interchange-setting methodology is a highly efficient and pro-consumer way to manage its payment network and why regulated interchange fees would leave the vast majority of participants in the Visa payment system worse off than they are today.

It is important to start out by recognizing the enormous benefits that payment cards deliver to both cardholders and merchants — benefits that are available only because of interchange fees. Cardholders are able to avoid the risks of carrying cash, can make payments by telephone or over the Internet, and have the right to a "chargeback" if the goods or services they receive are not as promised. And by accepting Visa cards, retailers can receive reliable, convenient, secure and safe payment from any of hundreds of millions of cardholders throughout the world. Retailers without the resources to operate their own financing business can also attract consumers who wish to buy on credit. This can dramatically expand the markets available to such retailers. Retailers also gain access to new customers who either prefer to pay with a Visa card or who are not carrying cash, checks, or other payment methods accepted by the retailer.

The payments market is an exceptionally dynamic, ever-evolving space characterized by shifting market shares, efficiency-enhancing innovations in products and processing, and frequent entry of new players. To be a viable competitive alternative at the point-of-sale, Visa must provide value both to issuers, so that they will choose to provide Visa cards to consumers and encourage cardholders to pay with them, and to acquirers, so that they can negotiate with and sign retailers to accept Visa cards. This is the essence of a two-sided market: balancing the push and pull of demand between the system's two groups of customers, making the system appealing to both.

In seeking that balance, Visa considers the effects on *both* sides of the payments market and sets its default interchange rates so that retailers will accept Visa products for payment and contribute to the costs and incentives of developing the system, recognizing that issuers impose fees on cardholders for their use of Visa cards on the other side of the ledger. Interchange, however, is not set simply to reflect or exchange these costs. Visa sets interchange to optimize total participation in its network, provide high quality data and other processing incentives to strengthen network performance for the benefit of all participants, and ultimately maximize the number of transactions processed securely through the Visa network.

Visa's default interchange rates also foster competition and innovation. Visa has every incentive to maximize its card transaction volume, which it does by setting interchange rates that provide incentives for banks to issue Visa cards that cardholders desire to use and for retailers to accept Visa cards. Because interchange is paid by acquirers to issuers and is not Visa revenue, Visa's primary interest in interchange fees is setting them at a level that balances demand on both sides of the network. If retailers do not accept Visa, cardholders will not carry Visa cards, banks will not issue Visa cards, and Visa will suffer competitively. Visa, therefore, fosters robust competition on both sides of the market through the mechanism of interchange. This competition benefits consumers, retailers, and the economy by providing thousands of choices for payment services.

Visa's use of interchange to maximize system output takes a variety of forms. Default interchange rates can be set to encourage issuers to fund rewards programs, increase acceptance among merchants in historically under-penetrated market segments, or simply to reflect the value of payment cards in enabling remote transactions in electronic commerce. Visa also has made its products more attractive to participants in its payment system by creating incentives through reduced interchange rates to encourage marketplace behaviors that reduce fraud and improve the timeliness and accuracy of the Visa system to the benefit of all participants.

The proposed regulation of interchange — a system functioning efficiently and competitively today — would harm competition and innovation. Government regulators would do a worse job setting interchange rates to maximize output and encourage innovation than Visa does. A non-market driven reduction in Visa's interchange rates would drive issuers and cardholders to American Express, or other potentially more expensive and lesser utility networks, and thereby simply re-allocate output on the Visa system to another network. Price controls would thus have the perverse effect of driving transactions to a payment network that is generally *more expensive* for retailers. The harmful effects of interchange regulation are evident from the recent experience in Australia. There, interchange regulation has led to higher prices and reduced rewards for cardholders, all without any reduction in the prices that consumers pay when they make a purchase from a retailer, let alone a reduction sufficient to offset the higher costs and reduced rewards.

Interchange regulation would also skew competition in the banking sector. Interchange enables the over 13,000 local and community banks, credit unions, savings and loans, and thrifts to offer payment products and reduces their disadvantages in competing with larger banks. Even if the largest players in banking might find a way to adapt to the regulation of Visa's interchange rates (either by moving their card portfolios to American Express or by creating customized card programs to attract consumers), smaller financial institutions would be particularly vulnerable if interchange were artificially suppressed. Interchange regulation would thus tip the competitive scale in favor of the largest banks and have broader impacts on banking competition, likely accelerating the trend towards bank consolidation. This harm to smaller local financial institutions would have a deeply-felt impact on every community that depends upon the vital role played by community banks, thrifts, and credit unions.

Moreover, much of the criticism of interchange reflects a misunderstanding of payment markets. Arguments that interchange has high "social costs" because it encourages "overuse" of payment cards are based on the flawed belief that cash and checks come at no cost. Comparison shows that PIN-debit, signature-debit, and credit are actually cheaper than cash and checks. Criticisms concerning the cost of interchange to retailers are similarly unfounded. The dramatic increase in payment card volume has benefited retailers, and an increase in the *total* cost of payment-card acceptance reflects primarily increased system volume. Visa's average interchange on a per-transaction basis has *decreased* over the last thirty years and has remained steady over the last ten years. Retailers, in fact, have many options with regard to accepting Visa, including determining not to accept Visa at all. That over seven million U.S. retailer locations accept Visa clearly indicates that the benefits of accepting Visa exceed the cost to most retailers. More than 1,600 acquirers compete for the business of these retailers, and retailers can and do use this competition to their advantage. Groups of retailers, including the National Association of Convenience Stores, have negotiated favorable merchant discount rates for their members. And retailers that are not happy with their rates can switch acquirers — more than 500,000 retailers switch to a new acquirer every year. Retailers, just like car buyers, need not pay the "sticker price."

Finally, as I will discuss, any claim that Visa violates the antitrust laws by setting default interchange rates is equally baseless, and the courts have consistently rejected such claims in every case in which they have been presented. And while retailers' prior unsuccessful challenges have been based on Visa's membership structure and incorrect claims that Visa's rules and practices result from horizontal agreements between Visa's member financial institutions, Visa is no longer majority owned or otherwise controlled by its customer banks.

I. Background

Visa competes in the vibrantly competitive payments market, which has included general-purpose payment cards since Diners Club introduced the first card in 1950. This market also includes cash, checks, ACH, PIN-debit cards, signature-debit cards, prepaid/gift cards, and store-branded cards, among other payment forms. From the Diners Club system, which had fewer than twenty thousand cardholders and charged retailers 7% for accepting the card in 1950, the payments marketplace has grown to the point at which, by 2007, 81% of American households owned at least one credit card, and the average merchant discount charged on a Visa transaction by the banks engaged in retailer acquiring — across credit, signature-debit, and PIN-debit — is roughly 2%.

Competition in the payments market takes place not only among different firms, but also among different payment types. General-purpose payment cards must compete aggressively with two forms of payment that have existed for centuries: cash and checks. In 2005 cash and checks accounted for more than 44% of consumer payments at the point-of-sale (33% for cash, 11% for check), versus 19% for credit cards, 4% for gift/prepaid cards, 19% for PIN-debit, and 14% for signature-debit.[1] The fastest growth in payments (over the last five years, and

[1] *See* Nasreen Quibria, Federal Reserve Bank of Boston, *Understanding Emerging Payments - Moving Towards a Cashless Society?*, at 10 (May 8, 2007) (citing a Dove/ABA study), *available at* http://www.bos.frb.org/economic/eprg/presentations/quibria050807.pdf.

anticipated for the next five years) is coming from automated clearinghouse (ACH) payments and debit cards, with credit card transactions growing at a slower rate.

Even within the electronic payments segment, consumers can choose to pay with, and retailers can choose to accept, an enormous variety of charge and credit cards, along with PIN-debit, signature-debit, and prepaid cards. A number of established players in addition to Visa, including MasterCard, Discover, American Express, and First Data/STAR, offer a variety of products in multiple payment segments. These established players also compete with a variety of more recent entrants. Firms including PayPal, Google, and Bill Me Later are offering new payment services for electronic commerce and Internet retail. Tempo has entered the market with a number of other products, including decoupled debit, PIN-debit, and stored-value cards. Revolution Money, another recent entrant, is marketing its RevolutionCard, a PIN-secured credit card, as well as an Internet-based solution for transferring money between account holders. Not only are these new entrants motivating continued innovation across the entire payments industry, they also are growing rapidly in transaction volume, retailer acceptance locations, and consumer accounts.

II. Interchange

A. The Role of Interchange in a Two-Sided Market

Any discussion of payment card interchange must take into account the two-sided market in which payment cards compete. Sellers in a two-sided market serve two distinct groups of customers, and the number of participants on one side of the market affects the demand on the other side. Payment systems are a classic example of a two-sided market because they bring together two distinct groups of customers: cardholders and retailers. The demand for payment cards by cardholders and retailers is interdependent — the greater the number of consumers who use payment cards, the more valuable the network is to retailers, and the greater the number of retailers that accept payment cards, the more cardholders value those cards. Payment networks use interchange to balance demand between the two sides of the market, promoting growth of the total system.

The two types of payment network systems — “open” and “closed” systems — both use a form of interchange to balance the two sides of the market. A closed system, sometimes called a three-party system, prices directly to retailers and cardholders, and operates without the use of independent issuers or acquirers. Today, American Express and Discover generally follow this model, as do newer payment systems like PayPal. Payment networks operating a closed system balance acceptance and cardholder usage by directly setting the retailer’s cost for card acceptance, which is called the merchant discount rate.

Visa’s payment system is more complex than the closed three-party system. In a four-party payment system (also called an “open-loop” system), issuing financial institutions provide payment cards to consumers, and acquiring institutions provide payment card transaction services to retailers. In addition to Visa, MasterCard, STAR, NYCE, PULSE, and other debit networks operate similar four-party systems.[2] Operators of open-loop systems do not issue cards, establish cardholder fees, or set the interest rates that cardholders pay, nor do they typically contract with retailers or set merchant discount rates. Instead, the network facilitates the transaction between the issuer and the acquirer, each of which is, in turn, responsible for establishing these rates and fees in contract with their respective cardholders and retailers. When a cardholder uses his or her credit card with a retailer, the retailer transfers the billing

[2] In more recent years, both American Express and Discover also have begun to emulate the four-party model by opening their network to other acquirers and issuers. In doing so, American Express and Discover apply acceptance charges and offer an “issuer rate” or yield on volume that serves the same function as interchange from the perspective of an issuing bank, in an effort to attract issuers.

information to its acquirer, which transfers the billing request to the cardholder's issuer. The acquirer then credits the transaction amount charged to the retailer's account, less the merchant discount rate that it charges to the retailer. Accordingly, the retailer receives prompt payment. The issuer subsequently pays the acquirer the amount of the transaction less the interchange fee, which (absent a bilateral agreement) is set in default form by the open-loop system, and posts the transaction to the cardholder's account. The cardholder thereafter pays the issuer the transaction amount.

In order for an open system to operate efficiently, it must have an interchange mechanism that establishes a default rate of exchange between the issuer of the card and the acquirer that contracts with the retailer. While issuers and acquirers are free to negotiate bilateral interchange agreements, default interchange rates promote efficiency by ensuring that both the issuer and the acquirer know the exact financial terms that will apply to any given transaction between any two participants in the system absent a bilateral agreement. While closed payment systems balance demand between cardholders and retailers directly by setting discounts to the retailers and card fees, interest rates, and rewards to consumers, open payment networks do not control issuers or acquirers. Issuers and acquirers in an open system set their own prices and provide their own benefits to cardholders and retailers. Thus, to balance the demand between cardholders and retailers, networks in open systems must establish an interchange rate.

B. Visa Uses Interchange to Foster Competition and Innovation

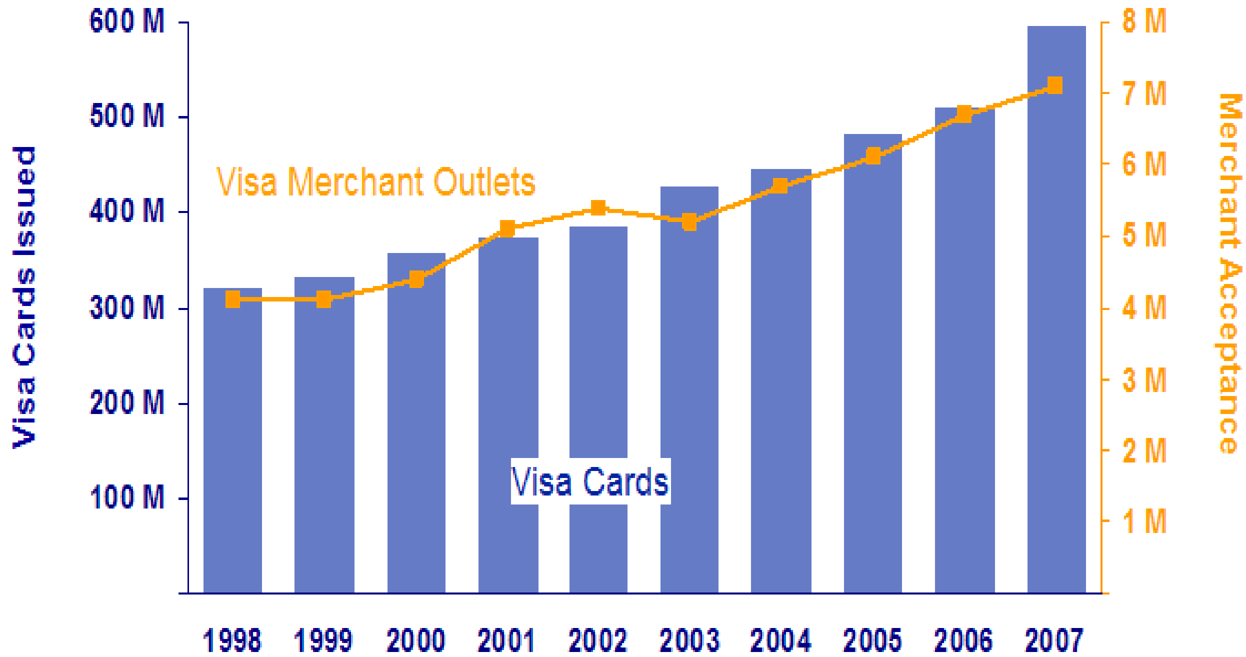
Visa sets default interchange to maximize network card volume by balancing demand between retailers and cardholders. Visa also sets interchange fees to ensure that participants in the Visa network have the proper incentives to innovate and invest in new technologies. Without the proper incentives, which result from the stimulus of interchange, payment networks would be less competitive and, therefore, less innovative.

Visa's interest in setting default interchange rates is to maximize the volume of transactions on Visa's system because that is the way Visa maximizes its own revenue. Visa earns revenue from fees charged to the banks that issue Visa cards and acquire Visa transactions that are based upon these banks' transaction and sales volumes. Visa does not earn revenue from interchange paid on U.S. transactions, which is paid by acquiring banks to issuing banks (except on ATM transactions, where interchange is paid by issuers to the acquirers who operate ATMs). Thus, Visa has no stake in setting a "high" interchange rate or a "low" interchange rate; its interest is solely in setting the optimum interchange rate to maximize the level of Visa transactions and sales volume.

Visa's financial institution customers play no role in setting Visa's U.S. interchange rates. The minority of Visa directors affiliated with Visa financial institution customers (although they owe fiduciary duties to Visa when acting as Visa directors) have played no role in reviewing Visa's interchange strategy or setting or recommending rate levels since Visa U.S.A. added independent directors to its board in 2006. Rather, interchange today is solely in the hands of Visa's management.

In order to maximize transaction volume, Visa sets interchange rates to balance issuance and card usage with retailer acceptance. On the issuance and card usage side of the system, given the highly competitive business of issuing credit cards in the U.S., increases in interchange benefit cardholders by resulting in reduced cardholder costs and increased cardholder benefits. This leads to greater transaction volume and revenue for Visa. Issuers also use these benefits to encourage consumers to use electronic payments instead of cash and checks. Increased cardholder demand to use a Visa card also makes it more attractive for banks to issue Visa cards instead of cards from MasterCard, American Express, and Discover. By the same token, Visa's failure to respond appropriately to interchange rates set by its competitors can lead to a reduction in transaction volume on the Visa network, as cardholders shift their purchases to cards that offer superior rewards or other valuable card benefits funded by interchange, and as issuers switch their portfolios to competing networks in order to be able to offer cardholders the competitive terms and card benefits they demand.

Visa, however, must use interchange to balance *both* sides of the two-sided market. Visa must set default interchange rates that not only avoid the loss of existing retailer acceptance, but also to win acceptance at retailers that have not previously accepted Visa cards. To the extent increases in interchange inform the acquirer's pricing to the retailer, higher interchange makes it less attractive for retailers to accept Visa cards. If retailers stop accepting or exhibit less preference for Visa cards, Visa not only loses transactions at those retailers (which results in a loss of Visa revenue from processing transactions), but this loss of acceptance also makes Visa cards less attractive to consumers (resulting in a loss of transaction volume and Visa revenue as consumers switch purchases to competing cards) and less attractive to issuers (resulting in a loss of transaction volume as issuers switch their portfolios to competing networks). As the chart below shows, Visa has been successful in setting default interchange to balance merchant acceptance and cardholder participation. Visa has added acceptance at 1.5 million merchant locations in the last two years, and both acceptance and cards issued are growing at roughly 7%/year.



Retailers make a choice about both the costs and benefits of accepting Visa cards, and while the merchant discount is a cost of accepting Visa cards, those costs are balanced against the benefits that Visa acceptance provides. By accepting Visa cards, retailers can receive reliable, convenient, secure and safe payment from any of hundreds of millions of cardholders throughout the world. Retailers without the resources to operate their own financing business can attract consumers who wish to buy on credit. Accepting Visa cards can dramatically expand the sales channels — such as mail order and/or Internet shopping — available to retailers. Retailers also gain access to customers who either prefer to pay with a Visa card or who are not carrying cash, checks, or other payment methods accepted by the retailer. Where Visa offers an attractive value proposition given these and other benefits, it is able to win acceptance at new retailers (and avoid losing acceptance with existing retailers), gaining not only increased revenue from new transactions at those retailers but also new transactions at other retailers as it increases the value of issuing and holding Visa cards.

In an effort to further maximize system output by setting interchange rates that reflect the costs and benefits of a Visa transaction, Visa sets default interchange rates at different levels depending upon the type of transaction, merchant category, and type of payment card. Visa uses interchange to create incentives to implement technologies that make the Visa network more valuable to all participants. As an example, by using interchange rates to create incentives for retailers to implement technologies that reduce fraud rates, Visa makes its network more attractive to issuers (who generally bear the cost of fraud), to retailers (who bear the cost of fraud in some circumstances), and to cardholders (for whom dealing with fraud is troubling and time-consuming, even if their direct financial exposure is limited). For example, Visa transactions at some retailers can qualify for lower interchange rates if the retailer implements Payment Card Industry Data Security Standard (PCI DSS) compliance, which requires the retailer to encrypt sensitive cardholder data and prohibits storage of sensitive data (such as magnetic stripe data or CVV2 security codes).

Visa has also successfully created incentives for electronic authorization of transactions in lieu of manually looking up card numbers in a book listing stolen or otherwise unauthorized cards by offering favorable interchange rates for electronically authorized transactions. Although implementing electronic authorization imposed costs on retailers in the form of new card terminals and telecommunications charges, the percentage of Visa transactions processed electronically rapidly increased after the introduction of favorable interchange rates for electronic transactions in 1980. Within ten years the percentage of Visa transactions processed electronically grew from 5% of sales volume to 80%. Today over 99% of Visa retail transactions are processed electronically. Retailers and cardholders alike have benefited from the increased security and reduced fraud that these innovations brought to the system.

Visa also provides incentives to retailers to improve fraud performance and customer satisfaction by setting higher interchange rates for transactions at retailers that have high chargeback rates (which reflect either high fraud rates or a large number of customers dissatisfied with the retailer's product or service performance). Visa has successfully lowered fraud rates by 20% in the past 10 years. At the other end of the spectrum, Visa has established preferred interchange rates for "high-quality" transactions that are submitted to cardholders quickly, include enhanced data, or have undergone supplemental validation by the retailer. The faster clearing times, extra data, and additional validation benefit cardholders and retailers alike by reducing fraud and increasing security.

In addition, because interchange is a significant component of the costs that acquirers face when they charge a merchant discount to retailers, Visa has set lower interchange rates in some merchant categories to enable acquirers to enroll additional retailers in historically under-penetrated segments (such as quick-service restaurants, department stores, and supermarkets) to accept Visa cards, while it sets higher interchange rates in merchant categories where the cards deliver more value to retailers (such as travel and entertainment).

By the same token, to encourage issuers to invest in and promote rewards programs (such as frequent-flier miles or cash back), interchange rates on rewards credit cards generally are higher than interchange rates on cards that do not offer rewards. These rewards programs deliver benefits to retailers as well as consumers by encouraging higher spend on cards and acting as a discount on card purchases. (In other words, when a cardholder receives a 1% cash rebate, it is indistinguishable in effect for the cardholder from a 1% reduction in the retailer's price to the cardholder.) Visa also sets higher interchange rates on rewards cards to compete with American

Express (whose products target higher-income customers that value rewards) for banks' issuance decisions.

Most fundamentally, Visa uses interchange to enable it to deliver new types of products that offer new benefits. Visa created the debit card, but without interchange banks would have had no incentive to issue debit cards and promote their use to the extent that there are now more Visa debit transactions in the U.S. than Visa credit transactions. Visa prepaid cards are attractive to governments as a lower cost way of delivering benefits like social security and child support payments, while also helping benefit recipients avoid the cost and burden of cashing checks and the risks of carrying cash. But without interchange, banks would have no incentive to compete for the government's business to issue these cards, or would do so only by charging the government far higher fees. Mobile payments from cell phones have the potential to be the "next big thing" — allowing consumers to make payments without carrying a wallet or a card. But without interchange revenue, banks will have no interest in enabling it. Without interchange, the electronic payments revolution could never have occurred. And if interchange is regulated, consumers will miss out on the benefits that Visa's substantial investment in innovation is poised to deliver.

III. Interchange Price Controls and Government Regulation of Visa's Rules Will Harm Competition and Innovation

Retailers are seeking comprehensive government regulation that would prevent Visa from using its independent, marketplace-driven judgment to determine core business functions, namely the rate and terms of exchange between its customers. Specifically, retailers want Congress to reject the free market and to impose price controls and regulatory micro-management on Visa's payments business.

Legislation recently introduced in the House of Representatives would create a panel of three "Electronic Payment System Judges" with the power to set not only the price that retailers pay for Visa (and MasterCard) transactions, but also all of the rules and terms that govern retailers' participation in the Visa network.[3] Under the proposed legislation, the rates and terms would be the same for all retailers regardless of merchant category or volume of transactions.[4] In other words, the pending legislation would introduce price controls and regulate terms of service on Visa and MasterCard, but not on other payment networks. This proposed legislation is as misguided as it is extreme and unprecedented.

Given that Visa uses interchange to foster competition and innovation, it naturally follows that interchange price controls such as those contemplated by the House bill will harm competition and reduce the pace of innovation. Indeed, the experience in Australia, which has experimented with interchange price controls, demonstrates that consumers are *worse off*, and that price controls have failed to accomplish the goals that their proponents claimed.

A. Price Controls Are Bad Policy

Americans know from experience that price controls do not work. Price controls inherently misallocate resources, create inefficiencies, and retard innovation, without providing consumer benefits. A shining example of the folly of price controls is the price caps imposed on gasoline in 1973 and again in 1979. These efforts resulted in massive inefficiencies, including

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[3] *See* Credit Card Fair Fee Act of 2008, H.R. 5546, 110th Cong. (2008).

[4] *Id*. at § 2(d)(2) ("For any given covered electronic payment system, such rates and terms shall be the same for all merchants, regardless of merchant category or volume of transactions (either in number or dollar value) generated.").

huge lines of consumers waiting to purchase gasoline, and consumer harm that swamped any possible benefits.[5]

It has been the consistent policy of the United States in both Democratic and Republican Administrations to oppose unjustified regulation, and particularly to oppose price controls in competitive markets.[6] As the Antitrust Modernization Commission ("AMC") created by Congress[7] recognized in its recent report, "[i]n the vast majority of cases, competition is more likely to benefit consumers than economic regulation."[8] The AMC specifically warned that "[i]n general, Congress should be skeptical of claims that economic regulation can achieve an important societal interest that competition cannot achieve," for "in many instances, regulation reflects successful rent-seeking by private economic interests and generally reduces consumer welfare by restricting output."[9] That describes precisely the efforts of the proponents of interchange price controls.

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[5] William Simon, the administrator of the Nixon price control program, concluded in retrospect that, "the kindest thing I can say about it is that it was a disaster. The normal market distribution system is so complex, yet so smooth, that no government mechanism could simulate it." William E. Simon, *A Time for Truth* (1978), quoted in Michael R. Baye, Director, Bureau of Economics, Federal Trade Commission, Remarks for Breakfast with the Federal Trade Commission Bureau Directors: Is There a Doctor in the House? The Value of Economic Expertise in Antitrust, Consumer Protection, and Public Policy (Mar. 28, 2008), *available at* http://www.ftc.gov/speeches/baye/080328aba.pdf.

[6] *See, e.g.*, Exec. Order 12,866, 58 Fed. Reg. 51,735 (Sept. 30, 1993), *available at* http://www.whitehouse.gov/omb/inforeg/riaguide.html (stating a presumption against regulatory actions such as price controls); *see also* Exec. Order 13,422, 72 Fed. Reg. 2763 (Jan. 18, 2007) (amending Executive Order 12,866 to clarify the description of market failures that justify regulation but retaining the language quoted above).

[7] The members of the Commission were appointed by the President and the respective majority and minority leadership with the goal of ensuring "fair and equitable representation of various points of view in the Commission." Antitrust Modernization Commission Act of 2002, Pub. L. No. 107-273, §11054(h), 116 Stat. 1856, 1857 (2002).

[8] Antitrust Modernization Commission, *Report and Recommendations* 337-38 (2007).

[9] *Id.* at 337-38.

B. Price Controls Would Harm Competition By Interfering With Visa’s Ability to Maximize Output

Price controls are particularly unworkable for a system as complex as open-loop card networks and the interchange rates that enable them to function. Artificially capping interchange rates — and particularly requiring that the same interchange rates apply to all transactions — would disturb the balance Visa establishes when it sets interchange at levels that maximize issuance, acceptance, and cardholder usage of Visa cards. While a reduction in interchange might in theory lead to increased retailer acceptance in the short term, Visa cards are already accepted at more than seven million locations, and it is implausible that the added transactions from retailers that might begin to accept Visa would outweigh the loss of transactions stemming from the reduction in Visa issuance and card usage that are the inevitable result of any mandated artificial reduction in interchange. At any interchange level, if there were a drop in the level of Visa card issuance, retailer demand for Visa products would likely fall as well. Indeed, if reducing interchange would cause Visa to gain more transactions than it would lose, Visa would have every incentive to reduce its interchange rates today.

The proposed regulation of Visa’s interchange rates would have the perverse effect of driving issuers and consumers to American Express, which without similar constraints would be able to continue to offer cards that provide elevated cardholder benefits funded through merchant discount revenues. These transactions would move to American Express’s network, even though retailers pay significantly more on average when their customers pay with Amex than with Visa. Evidence from interchange regulation in Australia (where the Reserve Bank of Australia capped Visa’s[7] and MasterCard’s interchange rates but left Amex’s and Diners Club’s rates unregulated) bears this out: American Express gained share even though the merchant discount on American

Express transactions is about 2.5 times higher than the merchant discount on Visa transactions in Australia.[10]

If Congress regulates Visa like a public utility, we all will end up with significantly less competition, slower growth, and reduced innovation. The payments industry is simply too dynamic and complex to regulate as a public utility. It is the lifeblood of the modern economy. As the Commerce Department has recognized, "Electronic payments expand the consumer market, increase banking access to the unbanked, improve macroeconomic efficiency, and encourage entrepreneurial activity."[11]

Provisions of the proposed legislation requiring Visa to set the same interchange rate for all transactions at all retailers would have particularly pernicious effects. Because Visa would lose the ability to offer reduced interchange to gain acceptance in new merchant categories, the legislation would raise costs to some retailers rather than reduce them. The legislation also would impede Visa's ability to create strong incentives via reduced interchange for retailers to implement technologies that reduce fraud or otherwise improve the quality of transactions processed on VisaNet, reducing network quality to the detriment of all participants: issuers, acquirers, consumers, and retailers.

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[10] *See* Reserve Bank of Australia Payments System Board, *Reform of Australia's Payments System: Preliminary Conclusions of the 2007/08 Review* 20 ("RBA 2007/08 Review"), *available at* http://www.rba.gov.au/PaymentsSystem/Reforms/RevCardPaySys/Pdf/preliminary_conclusions_2007_2008_review.pdf.

[11] Department of Commerce, International Trade Administration, *Credit Card Market: Economic Benefits and Industry Trends* (March 2008), at 2, *available at* http://www.ita.doc.gov/td/finance/publications/creditcards.pdf.

C. Interchange Regulation Would Lead to Higher Prices for Consumers

The harm to consumers from interchange regulation is evident in Australia, where credit card fees have increased substantially since interchange regulation was imposed and if any retailer cost savings were realized, they have not been passed on to consumers in the form of lower prices. In a recent study of Australia's rate regulation, economists estimated that cardholders had seen their annual fees and finance charges increase by AU$148 million.[12] Another analyst estimates that consumers have faced increases in card-related fees of about 40%.[13] Lest there were any doubts, in a report released earlier this month, Australia's interchange regulator, the Reserve Bank of Australia ("RBA") itself concluded that "[l]ower interchange fees in the MasterCard and Visa credit card systems have resulted in a reduction in the value of reward points and higher annual fees, increasing the effective price of credit card transactions facing many consumers."[14] Consumers must now spend over 30 percent more to receive the same rewards they did prior to the imposition of interchange caps.[15] Not only do cardholders face higher fees on the regulated networks, but American Express and Diners Club

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[12] Howard H. Chang et al., *An Assessment of the Reserve Bank of Australia's Interchange Fee Regulation*, The Federal Reserve Bank of New York Conference: Antitrust Activity in Card-Based Payment Systems: Causes and Consequences (Sept. 15-16, 2005). Some economists estimate the increase in fees to Visa and MasterCard cardholders as high as AU$ 480 million. *See* Robert Stillman et al., *Regulatory Intervention in the Payment Card Industry by the Reserve Bank of Australia: An Analysis of the Evidence* 13 (Apr. 28, 2008), *available at* http://www.crai.com/ecp/assets/Regulatory_Intervention.pdf.

[13] *See* Mercator Advisory Group, *Australian Interchange Regulation: Credit Card Issuer Effects* 17 (Dec. 2007) (including annual fees, over-limit fees, and cash advance fees).

[14] *See RBA 2007/08 Review*, *supra* note 10, at 17; *see also* Stillman, *supra* note 12, at 15-16 (noting that cardholder rewards have been reduced by approximately 23% since 2003).

[15] *See* Reserve Bank of Australia Payments System Board, *Annual Report 2007* 27, *available at* http://www.rba.gov.au/PublicationsAndResearch/PSBAnnualReports/2007/Pdf/2007_psb_annual_report.pdf.

have taken the opportunity to raise their annual fees on rewards-based charge cards at similar rates as increases on rewards-based Visa and MasterCard cards.[16]

What did consumers get in return for these higher prices for the use of payment cards? As the RBA conceded earlier this month, in the five years since interchange was regulated "no concrete evidence has been presented to the Board regarding the pass-through of [retailers' interchange] savings."[17] Indeed, the vast majority of retailers that reported a reduction in the merchant discount applicable to their transactions did not reduce prices to consumers.[18] In short, the Australian experiment with interchange regulation has brought consumers higher prices with no demonstrable benefits.

Indeed, there is every reason to believe that regulation of Visa's rules and interchange rates would subject consumers to three different types of harm: (1) artificially suppressed interchange would lead to a reduction in cardholder rewards (such as cash back), which operate as a discount on card transactions; (2) evidence suggests retailers would not reduce their prices to offset reduced merchant discount; and (3) elimination of Visa's no-surcharge rule could result in retailers surcharging Visa transactions at the point-of-sale.[19] In all three ways, consumers stand to lose at the hands of retailers.

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16 *See* Stillman, *supra* note 12, at 12.

17 *RBA 2007/08 Review*, *supra* note 10, at 23.

18 David S. Evans, *Turbulent Times: Recent Developments in the Payment Card Business in the United States, European Community, and Japan*, Modern Bankers Bankcard Seminar, Beijing, China (June 29, 2006) ("No change in relevant prices at point of sale to consumer"); Howard Chang et al., *The Effect of Regulatory Intervention in Two-Sided Markets: An Assessment of Interchange-Fee Capping in Australia*, AEI-Brookings Joint Center for Regulatory Studies 18 (Dec. 2005).

19 *See e.g.*, Bi-Lo Complaint at ¶12(G); Kroger Complaint at ¶23(G); Meijer Complaint at ¶12(G); Publix Complaint at ¶ 12(G); QVC Complaint at ¶12(G); Raley's Complaint at ¶12(G); Rite Aid Complaint at ¶12(G); Supervalu Complaint at ¶12(G); Wakefern Complaint at

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D. Interchange Regulation Would Have a Disproportionate Impact on Smaller Banks, Thrifts, and Credit Unions and the Communities They Serve

Interchange (and Visa's establishment of a default interchange rate that applies absent individual negotiation between issuers and acquirers) enables the over 13,000 local and community banks, credit unions, savings and loans, and thrifts to offer payment products and reduces their disadvantages in competing with larger banks. Even if the largest financial institutions might find a way to adapt to the regulation of Visa's interchange rates (either by moving their card portfolios to American Express or by creating customized card programs to attract consumers), smaller banks would be particularly vulnerable if interchange were artificially suppressed or Visa could not establish default interchange fees. Community banks and credit unions lack both the resources and the leverage to negotiate rates with thousands of acquirers. They also are far less attractive as issuers to American Express and lack the scale to create customized card offerings that would allow them to compete with larger financial institutions.

Smaller financial institutions often act as acquirers for small businesses in their communities, and absent a default interchange rate established by Visa would be unable to continue in this role because it would be impracticable for them to negotiate agreements with thousands of other Visa issuers. Interchange regulation would harm local merchants that prefer to do business with local community bank acquirers instead of the large national acquirers.

Because community banks and credit unions have less diversified revenue sources than larger banks, they are more dependent upon interchange revenues, and regulation of interchange

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¶12(G) ("The 'No Surcharge Rule" forbids retail merchants from charging cardholders a surcharge on their cards to reflect cost differences among various payment methods."); First Amended Consolidated Complaint ¶ 154.

would have a disproportionate impact on their revenues and profitability, as well as the benefits that credit unions provide to their members. Interchange regulation would thus tip the competitive scale in favor of the largest institutions and have broader impacts on banking competition, likely accelerating the trend towards bank consolidation.

Harm to community banks raises concerns far beyond competition in the banking sector. Small banks, thrifts, and credit unions play an essential role in local communities, focusing on the needs of local families, police and firefighter associations, and farmers, and remaining deeply involved in local community affairs. Regulation of interchange rates would thus have deeply-felt impacts not only in the payments industry and among community banks, but also in every community that depends upon the vital role played by community banks.

E. There Is No Evidence That Interchange Regulation Increases Overall Efficiency

Interchange rate regulation leads to reduced output of the regulated card system, higher card usage costs for consumers, and no reduction in the prices that retailers charge to consumers. All of these effects represent harm to competition and a reduction in market efficiency. Absent any basis to allege a reduction in output — the classical measure of harm to competition or an anticompetitive effect — critics of interchange are left to argue either that interchange harms consumers because it encourages over-usage of payment cards, or that it forces consumers who pay with cash to subsidize those who pay with credit cards. Both of these arguments demonstrate a fundamental misunderstanding of payment networks.

Discussions of the "high" cost of payment cards and claims that consumers "over-consume" payment cards are based on the erroneous assumption that other payment forms, such as cash and check, come at no cost. In fact, cash and check also have costs, and comparison shows that PIN-debit, signature-debit, and credit are actually cheaper than cash and checks.

When only retailer per-transaction processing costs are included, payment cards seem more expensive relative to cash or checks, and cash seems the cheapest payment instrument.[20] But proper assessment of the overall costs of a payment mechanism measures costs across all participants in the system, and should account for the benefits as well as additional private and social costs of the payment instrument. These include consumer costs (processing time and queue time, both in terms of opportunity cost; explicit price, such as ATM fees and the price of a paper check; and implicit price, such as time spent going to the ATM), central bank costs (production, as in the cost of maintaining high-quality currency; and processing), and commercial bank costs (ATM maintenance; production, for example of payment cards; processing, including float; and reward costs, such as payment of airline miles and cash back).

Accounting for these costs in addition to retailer processing costs reveals that cash is not the least expensive way of paying when all costs to the economy are considered. Signature-debit transactions are cheapest, followed by PIN-debit and credit.[21] Paper instruments, especially cash and non-verified checks, are more costly than Visa's electronic payment offerings. As the Department of Commerce noted in a report last month, "[e]lectronic payment networks have the potential to provide cost savings of at least 1 percent of GDP annually over paper-based systems through increased velocity, reduced friction, and lower costs."[22]

Proponents of interchange regulation sometimes claim that customers who pay with cash are forced to subsidize consumers that pay with credit cards. As an initial matter, this argument portrays a group of cash spenders and a separate group of card users. In fact, most consumers

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[20] *See* Daniel D. Garcia-Swartz *et al.*, *The Move Toward a Cashless Society: Calculating the Costs and Benefits*, 5 Rev. of Network Econ. 199 (2006).

[21] *Id*.

[22] Department of Commerce, International Trade Administration, *supra* note 11, at 2.

have ready access to multiple credit cards of different brands, debit cards, personal checks, and cash and coins. This, therefore, is not a case of one set of consumers subsidizing another; it is a case of individuals exercising an option to choose one payment method over another. From a consumer perspective, welfare is being enhanced by the availability of these options. Retailers benefit as well when the consumer has the option to utilize a number of different methods of payment. And common sense and experience tells us that, for example, if acceptance of credit cards speeds up the checkout line at the grocery store, as it does, all shoppers benefit — those paying with cash as well as those paying with cards.

In addition, nearly every U.S. consumer has access to a payment card,[23] and to the extent that there are under-served portions of the population, Visa is making efforts to expand access to electronic payment products and increase the financial literacy of these individuals. And even the "unbanked" are, to a greater and greater extent, using payment cards that operate on Visa's and MasterCard's debit networks to receive payroll distributions and government benefits.[24] Use of prepaid debit cards allows the unbanked to avoid high check-cashing fees and provides protection from loss or theft of checks or cash because Visa cardholders have zero liability for unauthorized card usage. It also saves time and money by, for example, allowing people without a checking account to make household payments (such as utility payments) online, rather than

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[23] According to TNS's Consumer Card Strategies Research Program, 90.4% of the households in their survey (English-speaking only) had a credit or debit card. This is consistent with data in an ABA/Dove consulting study, which showed that of consumers that pay with cash, only 11% reported doing so because they lacked access to another payment method.

[24] *See* Marianne Crowe, Federal Reserve Bank of Boston, *Emerging Payments — The Changing Landscape*, at 16 (Apr. 15, 2008), *available at* http://www.bos.frb.org/economic/eprg/presentations/2008/crowe04151708.pdf. The federal government and more than 30 states, including the two largest states (California and Texas), are using or are in the process of implementing Visa prepaid cards to disburse child support, unemployment, and other social benefits.

making cash payments in person.[25] These cards also save the government money — more than $125 million by switching to prepaid cards from checks (which cost 89 cents each to issue and mail).[26]

In all events, if there is any "subsidization," the subsidy flows in the opposite direction from what the retailers contend because electronic payments have lower total costs to society than cash and checks. Indeed, while signature-debit transactions usually have lowest total societal costs, followed by PIN-debit and credit,[27] because Visa sets different interchange rates for different types of retailers and different categories for payments, credit cards sometimes have even lower societal net costs than debit cards (and cash and checks). For example, the chart below, reproduced from a presentation by a vice president of the Minneapolis Federal Reserve Bank, shows that credit card transactions have the lowest societal cost net of benefits for a typical grocery store transaction, closely followed by signature-debit transactions.[28] Cash and check remain the most expensive forms of payment for grocery transactions when total societal costs are considered.

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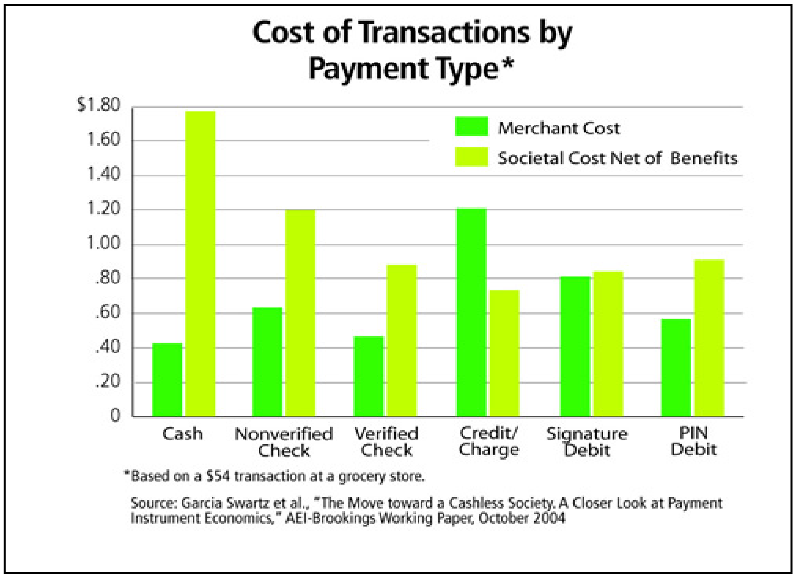
[25] According to the Federal Reserve Bank of Boston, almost 4% of payments by unbanked prepaid cardholders were online payments for household expenses — the most common use for the cards after purchases at grocery stores, restaurants, and gas stations. *Id*. at16.

[26] *See Banks Compete To Issue Debit Cards for Treasury*, ATM & Debit News (Oct. 11, 2007); *see also* U.S. Department of the Treasury, *U.S. Treasury to Launch Prepaid Cards for Unbanked Social Security, SSI Benefit Recipients* (Jan. 4, 2008) (Treasury to launch "a new initiative to give millions of unbanked Americans the option of using a prepaid debit card for receiving Social Security and other federal benefit payments," which could save taxpayers up to $44 million/year), *available at* http://www.fms.treas.gov/news/press/financial_agent.html.

[27] *See* Garcia-Swartz *et al.*, *supra* note 20.

[28] *See* James M. Lyon, First Vice President, Federal Reserve Bank of Minneapolis, *The Interchange Fee Debate: Issues and Economics* (June 2006), *available at* http://www.minneapolisfed.org/pubs/region/06-06/interchange.cfm.



Finally, there is no good evidence that interchange regulation is effective at steering consumers to forms of payment that reduce even the costs that retailers pay, let alone total societal costs. While the costs of interchange regulation are clear — higher costs for consumers with no offsetting reduction in retail prices — after the imposition of interchange regulation in Australia the more expensive payment systems of American Express and Diners Club have taken share from Visa and MasterCard.

F. Retailer Complaints About Interchange Are Unjustified

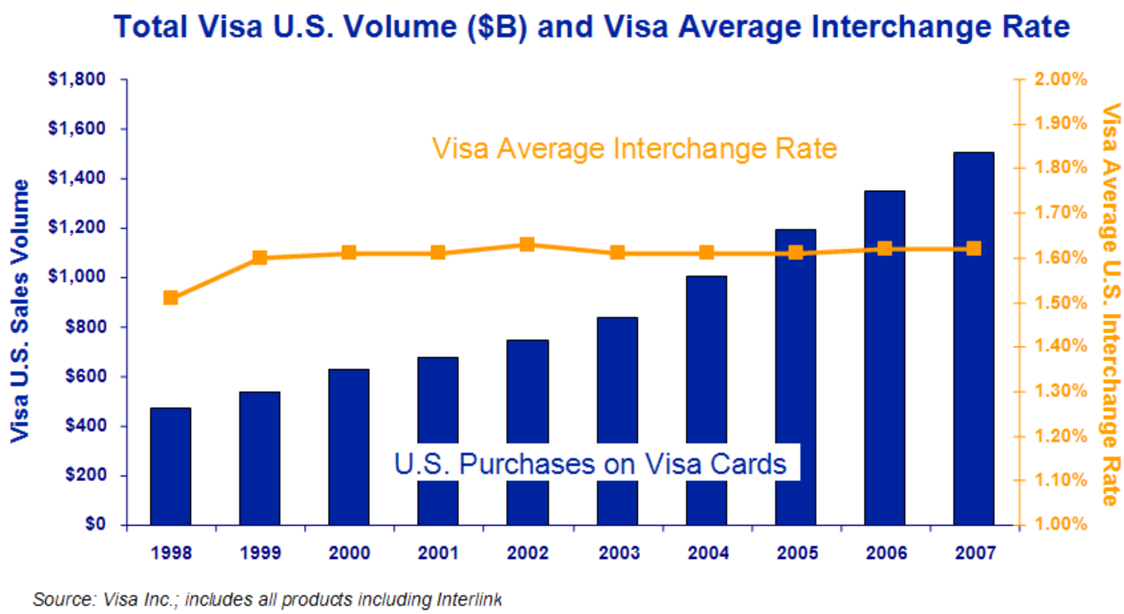
While many retailers recognize the enormous benefit they receive from payment cards — including enabling online transactions and allowing customers to buy on credit without the retailer creating a financing program — it is perhaps human nature to want more for less. Regardless, a close evaluation of retailers' critiques of interchange shows that they are unjustified.

First, it is essential to distinguish interchange fees from merchant discount fees. Acquirers negotiate their merchant discount rates and any other fees they agree to with their retailer customers without Visa's involvement. In doing so, acquirers compete for business with other Visa acquirers, other payment card systems, and other forms of payment. As a result of this competition, the largest retailers tend to accept payment cards under "interchange plus" contracts that provide for a markup on the interchange fee charged to the acquirer. Smaller and medium-sized retailers, on the other hand, usually accept cards at "blended" merchant discount rates offered by their acquirers that are the same regardless of the network that processes the transaction. All retailers, however, can and do switch among acquirers in order to ensure they are paying the most competitive rates.

According to a recent study, 82% of retailers pay a blended merchant discount rate.[29] These retailers are less directly impacted by Visa's changes in interchange rates and may see no change in their cost of accepting Visa cards even if interchange rates are regulated. This can be seen starkly in the aftermath of Visa's settlement of the *Wal-Mart* litigation, in which Visa agreed to reduce its interchange rates on Visa debit transactions by 48 basis points for most retailers between August 1 and December 31, 2003. Retailers that did not have interchange-plus contracts (where the retailer pays a merchant discount linked directly to the interchange paid by its acquirer), but rather had committed to a fixed merchant discount with their acquirer, received none of the benefit of this rate reduction.

Even ignoring the substantial benefits retailers gain from accepting payment cards, retailers have focused on the fact that their total cost of accepting payment cards has increased in recent years. This increase, however, primarily reflects an increase in payment card transaction volume, rather than any increase in Visa's interchange rates, which on average have scarcely changed in recent years, as can be seen in the chart below.

[29] Aite Group, *The State of the Merchant Acquiring Industry*, at 11 (Nov. 2007).



Cardholders have shifted their payments to cards from other payment forms because of the increased speed and convenience of paying with plastic, as well as the rewards and improved recordkeeping that electronic payments provide. A purchase made with a card instead of cash or a check also means the retailer avoids the costs associated with payment by cash and checks. Visa has also seen a shift in product mix, as cardholders have shifted their usage toward cards that offer rewards, rather than Visa's basic card offerings. Reflecting the robust competition in the payment card segment, Visa has responded to American Express's premium card offerings by increasing the interchange rates on its highest-end cards to allow its issuers to offer their cardholders a product that is attractive and to discourage issuers from switching their premium card portfolios to American Express. While Visa's average interchange rate has been flat, Visa has responded to competition and consumer demands with rewards offerings.

Further, retailer complaints that technological changes that have reduced costs of processing transactions have not been reflected in reduced interchange rates to retailers are the result of a misunderstanding of role of interchange. Interchange is not a price for transaction processing, but the means by which the card networks seek to maximize system output by balancing demand between retailers and cardholders. Visa's scale efficiencies and the cost reductions enabled by technology are reflected in the prices that Visa charges *its* customers — issuers and acquirers — for processing Visa transactions.

Moreover any retailer criticism of Visa's transparency falls well short of the mark. Visa has answered calls for transparency, and has been — and continues to be — as transparent as possible while protecting the security of its system to the benefit of cardholders *and* retailers. Ten years ago, Visa began making a summary of the rules that affect retailers publicly available on its website.[30] Visa's default interchange fees have been publicly available on the Visa website since October 2006.[31] In September 2006, Visa made its operating regulations available to retailers that are willing to keep them confidential. As of today Visa has gone one step further and eliminated the non-disclosure agreement, making the actual text of its rules, with the exception of rules relating to data security and rules that contain competitive information, available on its website with no strings attached.

Finally, retailers claiming that they have no choice but to accept payment cards are wrong. While more than seven million U.S. retailer locations accept Visa cards because they find that the value of acceptance exceeds its cost, retailers such as Costco, Neiman Marcus, and ARCO do not accept Visa credit or signature-debit cards (though Costco and Nieman Marcus accept Visa for Internet purchases). In addition to these high-profile retailers, many smaller and medium-sized retailers across the country have chosen not to accept some or all forms of

[30] *See* http://usa.visa.com/download/merchants/rules_for_visa_merchants.pdf?it=c|/merchants/|Rules%20for%20Visa%20Merchants.

[31] *See* http://usa.visa.com/download/merchants/visa-usa-interchange-rates.pdf.

electronic payment. For these retailers, apparently, the perceived costs of accepting payment cards outweigh the benefits.

Contrary to retailers' claims, retailers can influence their cost of accepting Visa cards. All retailers can also choose among more than 1,600 different acquirers who offer a range of pricing models. Indeed, according to a recent study, between 500 thousand and 600 thousand retailers change their acquirer every year.[32] A number of larger retailers have used the threat of dropping Visa acceptance to negotiate custom interchange rates with Visa that apply to their transactions, resulting in a reduced cost of acceptance because they have interchange-plus contracts with their acquirers.

Retailers have also banded together to negotiate preferred rates from their acquirers. For example, the National Association of Convenience Stores ("NACS") has created the NACS Card Processing Program with acquirer First Financial Bank (a subsidiary of First Data). All NACS members are eligible to participate in the program, which allows retailers to pay about 6 cents per transaction above Visa's interchange rates.[33] NACS estimates that the average convenience store could reduce its card-acceptance costs by more than $5,500 per year by participating in the program.[34] Organizations ranging from the National Restaurant Association[35] to the Vermont

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[32] Marc Abbey, *The Addressable Market in U.S. Acquiring*, First Annapolis Navigator, Sept. 2007, *available at* http://www.firstannapolis.com/get_navigator.cfm?navigator_id=72.

[33] *See* NACS Card Processing Program, *available at* http://www.nacsonline.com/nacs/resource/creditcards/nacscpp_details.htm.

[34] *Id*.

[35] *See* National Restaurant Association Take Charge Program, *available at* http://www.restaurant.org/business/takecharge.cfm.

Grocers' Association[36] have negotiated similar discounted group merchant discount rates with acquirers.

Moreover, Visa's rules are explicit that a "[r]etailer may request or encourage a Cardholder to use a means of payment other than a Visa Card." Retailers regularly and successfully "prompt for PIN" when a customer presents a debit card to steer transactions from Visa's signature-debit network to a PIN-debit network. Retailers are completely free to provide discounts to consumers who pay with cash, check, PIN-debit cards, and private label (*i.e.*, store brand) credit cards that are not general purpose cards. Retailers may also offer discounts to customers that use so-called "affinity cards" (general purpose cards that are co-branded with the retailer's name), which may offer a reduced cost of acceptance to the retailer, or they may offer free merchandise, services or other benefits as an incentive to customers not to use a Visa card.

IV. Visa Does Not Violate the Antitrust Laws By Setting Default Interchange Rates

The same retailers pushing to enact price controls are also pursuing an antitrust case challenging interchange and certain Visa Operating Regulations in the Eastern District of New York. The retailers' arguments are not new. Over the course of more than two decades, every direct challenge to the legality of Visa's interchange rates has been firmly rejected by the courts. These decisions have upheld interchange as a legal, procompetitive, and efficient means of maintaining Visa's open payment network.

The leading case addressing interchange is *NaBanco*, which rejected a claim by a third-party processor of Visa transactions that Visa violated Section 1 of the Sherman Act by setting

[36] *See* RBS Lynk - Vermont Grocers' Association's Preferred Payment Processor, *available at* http://rbslynkpartner.com/Pages/VermontGrocersAssociation.aspx.

default interchange rates.[37] The trial court held that Visa's default interchange fees were not per se illegal price-fixing and did not unreasonably restrain trade.[38] *NaBanco* clearly recognized and established the procompetitive and efficiency-enhancing aspects of interchange. The Eleventh Circuit affirmed the trial court's findings that interchange is procompetitive "because it was necessary to achieve stability and thus ensure the one element vital to the survival of the V[isa] system — universality of acceptance."[39] Default interchange "acts as an internal control mechanism that yields procompetitive effects that its members could not create acting alone, and helps create a product that its members could not produce singly."[40] In its absence, "individual price negotiations are impractical," which would "produce instability and higher fees," possibly resulting in "the demise of the produce offered."[41]

NaBanco does not stand alone in its rejection of challenges to interchange. Just two months ago, the Ninth Circuit affirmed a district court's rejection of retailers' claims that interchange is anticompetitive.[42] *Kendall* was a putative class action filed by retailers against Visa, MasterCard, and several banks belonging to their payment card networks that alleged that the setting of interchange and merchant discount fees amount to horizontal price fixing.[43] The court held that the plaintiffs' allegations failed to describe a price fixing conspiracy or that the

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[37] *Nat'l Bancard Corp. v. Visa U.S.A., Inc.*, 596 F. Supp. 1231 (S.D. Fla. 1984), *aff'd*, 779 F.2d 592, 595 (11th Cir. 1986).

[38] *Nat'l Bancard Corp.*, 596 F. Supp. at 1260.

[39] *Id.*

[40] *Id.*

[41] *Id.*

[42] *Kendall v. Visa U.S.A., Inc.*, No. C 04-04276 JSW, 2005 U.S. Dist. LEXIS 21449 (N.D. Cal. July 25, 2005), *aff'd*, 518 F.3d 1042 (9th Cir. 2008).

[43] *Kendall*, 2005 U.S. Dist. LEXIS 21449 at *3-4.

banks had knowingly, intentionally, and actively participated in a scheme to fix interchange fees.[44] In affirming the trial court's decision earlier this year, the Ninth Circuit directly addressed the retailers' claims that interchange unlawfully set a "floor" for the acquiring banks' independent determination of their merchant discount fees.[45] The court concluded that it was not unlawful for the networks to set interchange fees that "indirectly establish the merchant discount fee, much as the cost of eggs sets a floor for the price of an omelet on a menu. Just like the restaurateur, the banks charge the merchant a higher price than their cost of business to make a profit."[46] Rather, the acquiring banks' conduct was suggestive of "a rational business decision, not a conspiracy."[47] The holdings in *NaBanco* and *Kendall* are further supported by two Northern District of California decisions rejecting challenges to interchange fees as per se illegal.[48]

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[44] *Id.* at *8.

[45] *Kendall*, 518 F.3d at 1042.

[46] *Id*. at 1049.

[47] *Id*.

[48] In *Reyn's Pasta Bella, LLC v. Visa U.S.A., Inc.*, the district court rejected claims by retailers that Visa and MasterCard member banks had agreed to abide by uniform interchange fees throughout the payment systems, as opposed to individually negotiating varying fee rates among themselves. 259 F. Supp. 2d 992 (N.D. Cal. 2003). The court held that the rule of reason should apply because "the uniform interchange fee does *not* appear to be one of the few types of restraints exhibiting a 'predictable and pernicious anticompetitive effect' without potential for procompetitive benefit." *Id.* at 1000 (quoting *State Oil Co. v. Kahn*, 522 U.S. 3, 10 (1997)) (emphasis added). On the contrary, the retailers admitted that the existence of payment card networks had procompetitive benefits for them. *Id.* And, the Northern District for California similarly held that a Section 1 challenge to the interchange fees charged by the STAR ATM network on ATM transactions should be evaluated under the rule of reason. *In re ATM Fee Antitrust Litigation*, 2008 WL 793876 at *1, *9 (N.D. Cal., Mar. 24, 2008). The district court recognized the essential role played by interchange, echoing the Eleventh Circuit's decision twenty-four years earlier in *NaBanco* that individual negotiations would be too numerous to be feasible because, "[a]s in *NaBanco*, there are too many potential entities involved in the transaction that all efficiencies would be lost," and "the fee promotes cooperation between the venture's members and *cannot* be set individually." *Id*. (emphasis in original).

The courts' consistent rejection of attacks on the legality of interchange establishes the essential procompetitive and efficiency-enhancing role that default interchange fees play in open payment networks. Both the holding and analysis in *NaBanco* were correct and remain correct today. Default interchange is necessary to the functioning of the Visa system and no court has held otherwise in the twenty-four years that have elapsed since the *NaBanco* holding. Visa enables financial institutions to issue cards under a common brand and sign retailers to a common network. This has dramatically reduced the costs of participation in the payments industry and has made possible a payment system of unsurpassed utility and breadth.

Further, while retailers' prior unsuccessful challenges have been based on Visa's membership structure and claims that Visa's rules and practices result from horizontal agreements between Visa's member financial institutions, Visa is no longer majority owned or otherwise controlled by its customer financial institutions. After Visa's initial public offering in March 2008, Visa's financial institution members became common stockholders that control only a minority of Visa's stock. Indeed, the minority equity stake held by such financial institutions is in the form of a class of shares that are entitled to very limited voting rights. Visa's board of directors and management answer to Visa's public shareholders, not Visa's financial institution customers. As such, Visa's actions can no longer be alleged to be those of a joint venture or otherwise concerted conduct within the scope of Section 1 of the Sherman Act.

V. Conclusion.

Imposing government price controls on an efficient and highly competitive payments market is unjustified. Visa's interchange rates enable it to balance the two sides of its payments system and to create incentives for the implementation of technologies and practices that make Visa's payment network more useful and more valuable by reducing fraud, speeding transactions, and otherwise improving cardholder and retailer satisfaction.

Because consumers' use of payment cards is of great value to retailers, they do not want the Visa network to be impaired or to be eliminated; they want to continue to realize the exceptional benefits of this highly functional payments network, but at a lower cost. The proposed price controls will impede this balancing, leading to higher costs, reduced output, higher fraud rates, and a payments network that is less attractive to issuers, to cardholders, and ultimately to the very retailers that are seeking price controls.