

# HOW PROPOSED INTERCHANGE FEE CAPS WILL AFFECT CONSUMER COST

In November 2023, the Federal Reserve Board proposed to further reduce debit interchange rates, which could lead to higher costs for consumers.<sup>i</sup> In a recently-published white paper, Nick Bourke, the creator and former Executive Director of Pew Charitable Trusts' Consumer Finance and Housing program, shows that the Federal Reserve Board's proposed rule could increase consumers' costs for checking accounts by \$1.3 to \$2 billion dollars.<sup>ii</sup>

## WHAT IS DEBIT CARD INTERCHANGE?

Whenever a consumer uses his or her debit card to make a transaction, the merchant pays the bank that issued the debit card an "interchange fee". These can vary, but the average interchange fee is \$0.23 per covered debit card transaction.<sup>iii</sup>

## WHAT IS THE NEW PROPOSAL?

The Federal Reserve's new proposal seeks to reduce the current debit interchange cap by more than 20%, decreasing average interchange by 5.4 cents per covered transaction. This may seem like a small amount. And it may seem like lower "fees" would benefit consumers. But we can look to history and the last time that a debit interchange fee cap was implemented to predict that the Federal Reserve Board's proposal would in reality lead to higher costs for consumers, particularly low-income consumers.

## WHAT DID THE DURBIN AMENDMENT DO?

Passed as part of the 2010 Dodd-Frank Act, the Durbin Amendment (among other things) limited interchange fees to 21 cents plus 0.05% of the transaction's value for large banks.<sup>iv</sup> Smaller banks, with assets below \$10 billion, are exempt from the Durbin Amendment's cap on interchange rates. According to Sen. Durbin, the amendment aimed to reduce transaction costs for merchants so they would pass-through cost savings for consumers.<sup>v</sup>

However, as summarized by a recent Government Accountability Office report, it is unclear that consumers benefited from any such cost savings. Further, a wide range of researchers have demonstrated that the interchange caps mandated by the Durbin Amendment hamper banks' ability to offer free checking accounts and accounts without

minimum balance requirements. These researchers, including economists at the Federal Reserve, have shown that the Durbin Amendment increased consumer costs and reduced choice in the market.<sup>vi</sup>

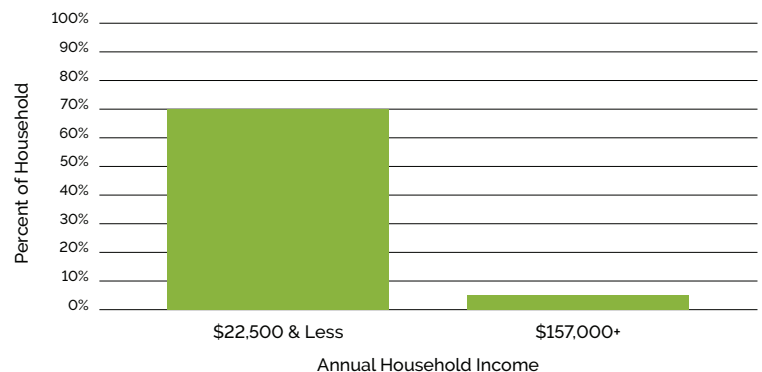
### How the Durbin Amendment increased consumer costs.<sup>vii,viii</sup>

- Average monthly maintenance fees on checking accounts increased by nearly 100%.
- Availability of free checking accounts with no maintenance fees dropped by 33%.
- Average account minimums needed to avoid a monthly fee increased by 20% or more, an average monthly increase of \$200.
- Banks were forced to institute minimum balance requirements on a greater share of accounts.

These costs have disproportionately affected lower-income Americans, who have less financial flexibility. According to a recent study analyzing the effects of the Durbin Amendment's interchange cap, more than 70% of the lowest income households were charged a fee for their checking account because their average monthly account balances fell below the post-Durbin minimum amount requirement. Conversely, only 5% of the highest earners were charged the same fees.<sup>ix</sup>

### **Low Income Consumers Disproportionately Bear the Cost of Interchange Fee Caps**

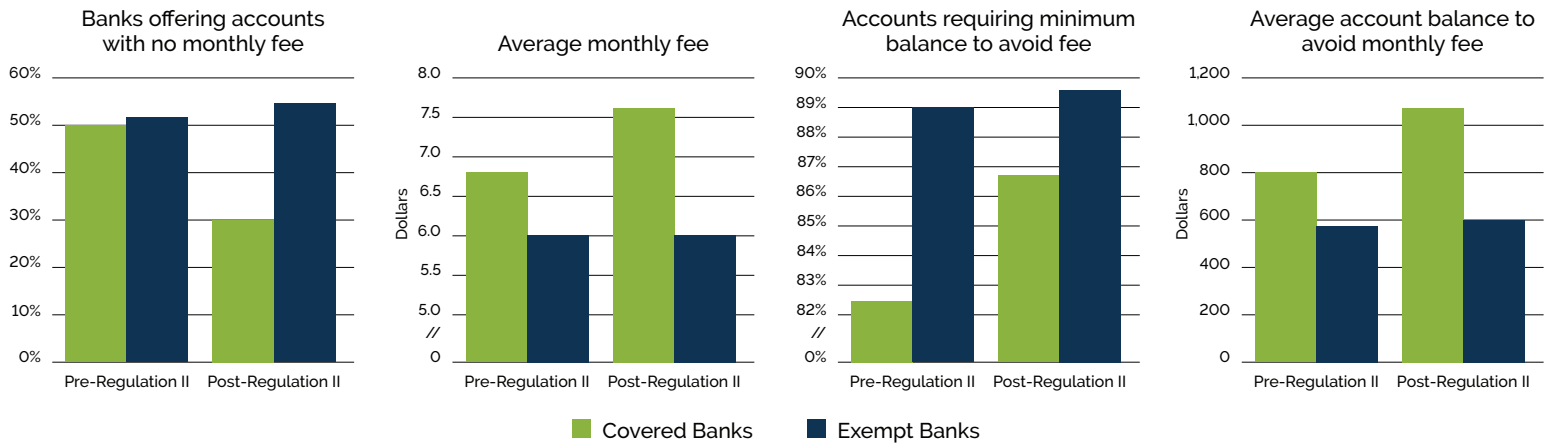
Percentage of consumers who were charged a maintenance fee after the Durbin Amendment (Mukharlyamov & Sarin, 2022)



# BASED ON THE ORIGINAL DURBIN AMENDMENT'S IMPACT, UNDER THE NEW PROPOSAL...

- Interchange fee income would be reduced by an average of **5.4 cents** per covered transaction.
- Consumers would pay an extra **\$1.3 billion to \$2 billion** annually in higher bank account fees.
- “Free” checking accounts will become less common for consumers looking to avoid bank account maintenance fees.
- The average minimum deposit to avoid monthly fees on checking accounts will increase, disproportionately impacting lower-income consumers.
- Consumers at smaller, exempt banks could face higher costs as their banks follow competitors and raise prices in some markets.

## Selected Changes to Noninterest Checking Accounts, Pre- and Post- Regulation II, January 2009-June 2014



## CONCLUSION

Judging by the effects of the 2010 Durbin Amendment, the estimated effects of any future reductions in the debit card interchange cap will cause consumers to grapple with measurably higher costs and more restrictive terms on their bank accounts; in addition, even though the average cost of debit card processing falls for merchants, any corresponding reduction in the cost of consumer goods and services is debatable and ultimately not measurable.

i. See <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231025a.htm>

ii. Bourke, Nick (2024), "How Proposed Interchange Fee Caps Will Affect Consumer Costs" Available at SSRN: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4705853](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4705853)

iii. Federal Reserve Board (2022) at Table 3 for covered transactions. <https://www.federalreserve.gov/paymentsystems/regii-average-interchange-fee.htm>

iv. 15 U.S.C 1693o-2 and 12 C.F.R 235. The Durbin Amendment included a number of other requirements for debit cards, like requiring that each debit card be operable on two different payment card networks.

v. Senator Richard Durbin, letter to Chairman Chris Dodd and Chairman Barney Frank (May 25, 2010). <https://www.durbin.senate.gov/newsroom/press-releases/durbin-sends-letter-to-wall-street-reform-conferees-on-interchange-amendment>

vi. United States Government Accountability Office (February 2022). "Regulators Have Taken Actions to Increase Access, but Measurement of Actions' Effectiveness Could Be Improved." <https://www.gao.gov/assets/gao-22-104468.pdf>

vii. Mukharlyamov, Vladimir and Sarin, Natasha (2022). "Price Regulation in Two-Sided Markets: Empirical Evidence from Debit Cards" (November 24, 2022). <http://dx.doi.org/10.2139/ssrn.3328579>.

viii. Manuszak, Mark D. and Krzysztof Wozniak (2017). "The Impact of Price Controls in Two-sided Markets: Evidence from US Debit Card Interchange Fee Regulation." Finance and Economics Discussion Series 2017- 074 Washington: Board of Governors of the Federal Reserve System, <https://doi.org/10.17016/FEDS.2017074>.

ix. Ibid.