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COMMENT

Merchant Restraints: Credit-Card-Transaction Surcharging and Interchange-Fee Regulation in the Wake of Landmark Industry Changes

I. Introduction

A customer orders an espresso-based beverage at her favorite local coffee shop. Thumbing past cash, she retrieves a debit card. An idea strikes. She can accrue a few reward points by using a credit card in lieu of debit or cash. The cashier swipes the customer's credit card. Soon, a barista shouts the customer's name and the customer collects her drink. She leaves, likely not knowing that the owner of her favorite coffee shop just made significantly less on the sale simply because she elected to pay with a credit card instead of with a debit card or cash.

Each day, merchants across America cumulatively make millions of dollars less on sales than they otherwise would have simply based on the method of payment a customer uses. Unbeknownst to most consumers, credit-card transactions cost merchants an average of six times more than cash transactions because of the increased fees credit-card companies and banks charge merchants for those transactions.¹ As Federal Reserve economists have noted, "What most consumers do not know is that their decision to pay by credit card involves merchant fees, retail price increases, a nontrivial transfer of income from cash to card payers, and consequently a transfer from low-income to high-income consumers."² A majority of these fees fund reward programs, meaning merchants actually pay for credit-card customers' reward perks—not credit-card companies. Historically, merchants have been expressly or effectively restrained from surcharging³ to recover these fees or even steering customers toward using a payment

1. David Humphrey et al., *What Does It Cost to Make a Payment?*, 2 REV. NETWORK ECON. 159, 162-63 (2003); see also Adam J. Levitin, *Priceless? The Social Costs of Credit Card Merchant Restraints*, 45 HARV. J. ON LEGIS. 1, 1-2 (2008).

2. Scott Schuh et al., *Who Gains and Who Loses from Credit Card Payments? Theory and Calibrations*, FED. RES. BANK BOS. 1 (Pub. Pol'y Discussion Paper No. 10-03, Aug. 31, 2010), <http://www.bostonfed.org/economic/ppdp/2010/ppdp1003.pdf>.

3. The United States Code defines "surcharge" as "any means of increasing the regular price to a cardholder which is not imposed upon customers paying by cash, check, or similar means." 15 U.S.C. § 1602(r) (2012). See also, *Surcharge*, BLACK'S LAW DICTIONARY (10th ed. 2014) (defining surcharge as imposing "[a]n additional tax, charge, or cost"). The term "checkout fee" is becoming more widely used by retailers.

alternative that is cheaper for the merchant. This forces the merchant into a troubling dichotomy: either accept less profit on a sale or increase prices on all products to account for the interchange fees incurred from credit-card users. The former option harms the merchant, while the latter harms non-credit-card users like customers paying with cash, check, or debit card.

Visa and MasterCard charged U.S. merchants \$35.56 billion in credit-card-processing fees in 2013, almost three times as much as the \$12.75 billion in debit-card fees charged for virtually the same purchase volume: \$1.6 trillion.⁴ Some 60%-80% of credit-card companies' revenues come directly from merchants.⁵

While these fees may seem like "the cost of doing business," merchant-credit-card fees have been the subject of numerous Department of Justice⁶ and international antitrust actions,⁷ private class-action lawsuits,⁸ and scholarly criticism.⁹ These challenges allege or adjudge collusion among credit-card companies to artificially determine and inflate merchant fees, amounting to antitrust violations.¹⁰ For example, in 2013 Visa and MasterCard settled a class-action lawsuit alleging conspiracy among credit-card companies and banks to fix fees in violation of the Sherman Antitrust Act.¹¹ As one of the terms of the record \$7 billion settlement, Visa and MasterCard agreed to end the contractual no-surcharge policy they imposed

4. *Merchant Processing Fees in the U.S.*, NILSON REP. (HSN Consultants Inc., Carpinteria, Cal.), May 2014, at 12 (excluding private label cards). The weighted average fee for all Visa and MasterCard credit cards was 2.17% in 2013, while the same average for debit cards was almost a third, or 0.76%. *Id.*

5. DAVID S. EVANS & RICHARD SCHMALENSSEE, *PAYING WITH PLASTIC: THE DIGITAL REVOLUTION IN BUYING AND BORROWING* 150 (2d ed. 2005).

6. *See, e.g.*, *United States v. Visa U.S.A., Inc.*, 344 F.3d 229, 232 (2d Cir. 2003); *United States v. Am. Express Co.*, No. 10-CV-4496(NGG)(RER), 2015 WL 728563, at *7 (E.D.N.Y. Feb. 19, 2015).

7. *See, e.g.*, Commission Decision 264/04, 2009 O.J. (C 264) 9-11 (EC), <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C:2009:264:FULL&from=EN>; Case C-382/12 P, *MasterCard v. Eur. Comm'n*, 2014 EUR-Lex CELEXLEXIS 1 (Jan. 30, 2014), <http://curia.europa.eu/juris/document/document.jsf?text=&docid=157521&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=3927>.

8. *See, e.g.*, *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214 (E.D.N.Y. 2013), *appeal filed*, No. 14-241 (2d Cir. 2014).

9. *See, e.g.*, Alan S. Frankel & Allan L. Shampine, *The Economic Effects of Interchange Fees*, 73 ANTITRUST L.J. 627, 628 (2006); Adam J. Levitin, *Priceless? The Economic Costs of Credit Card Merchant Restraints*, 55 UCLA L. REV. 1321, 1343 (2008).

10. *See* sources cited *supra* notes 6-9.

11. *In re Payment Card Interchange*, 986 F. Supp. 2d at 213.

on merchants.¹² American Express and Discover appear to be ending their no-surcharge policies as well.¹³ Accordingly, merchants may now choose to recover these fees by surcharging credit-card transactions at the point of sale without violating agreements with credit-card networks or banks.

Nine states, however, still impose *statutory* no-surcharge prohibitions.¹⁴ These nine states' statutes, cloaked as consumer-protection statutes, are the result of heavy lobbying by credit-card companies in targeted states in the 1980s.¹⁵ Interestingly, Oklahoma stands as the only state with two seemingly identical no-surcharge statutes.¹⁶ Even though Visa and MasterCard have ended their contractual prohibition against surcharging, merchants in these nine states cannot surcharge without violating state laws. In addition to these current statutes, eighteen states are currently considering no-surcharge laws.¹⁷ Minnesota stands as the only state that expressly *protects* merchants' ability to surcharge, subject to proper disclosure to customers.¹⁸

To complicate this area of law further, federal district courts in California and New York recently found their states' no-surcharge statutes unconstitutional.¹⁹ In the New York case, the court disapprovingly stated the following:

Alice in Wonderland has nothing on section 518 of the New York General Business Law. Under the most plausible interpretation of that section, if a vendor is willing to sell a

12. Settlement Agreement, *In re* Payment Card Interchange Fee & Merch. Disc. Antitrust Litig., No. 05-MD-1720(JG)(JO), 2012 WL 3932046 (E.D.N.Y. July 13, 2012) [hereinafter Settlement Agreement].

13. See *infra* notes 162-163 and accompanying text.

14. See Table 1 (Appendix).

15. See *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 2d 430, 439 (S.D.N.Y. 2013) ("In 1984, . . . Congress allowed the [federal] no-surcharge provision to lapse. In response, the credit-card industry began lobbying for state-level no-surcharge laws . . ."); Levitin, *supra* note 1, at 9 n.35 ("Based on barebones legislative history for eleven of the twelve states with no-surcharge rules, most state no-surcharge rules appear to be the result of credit card industry lobbying in the 1980s.").

16. 14A OKLA. STAT. § 2-211 (2011) (regulating "Maximum Charges" in the Oklahoma Consumer Credit Code); *id.* § 2-417 (regulating "Limitations on Agreements and Practices" in the Oklahoma Consumer Credit Code)

17. Kevin Wack, *18 States Considering Bans on Credit Card Surcharges*, AM. BANKER, Apr. 1, 2013, at 4.

18. See MINN. STAT. § 325G.051(a) (2012).

19. *Italian Colors Rest. v. Harris*, No. 2:14-IC-00604-MCE-DAD, 2015 WL 1405507, at *9 (E.D. Cal. Mar. 26, 2015), *appeal filed*, No. 15-15873 (9th Cir. 2015); *Expressions*, 975 F. Supp. 2d at 447.

product for \$100 cash but charges \$102 when the purchaser pays with a credit card, the vendor risks prosecution if it tells the purchaser that the vendor is adding a 2% surcharge because the credit card companies charge the vendor a 2% “swipe fee.” But if, instead, the vendor tells the purchaser that its regular price for the product is \$102, but that it is willing to give the purchaser a \$2 discount if the purchaser pays cash, compliance with section 518 is achieved. . . . [T]his virtually incomprehensible distinction between what a vendor can and cannot tell its customers offends the First Amendment and renders section 518 unconstitutional.²⁰

Notwithstanding this rebuke, federal district courts in Florida²¹ and Texas²² dismissed similar cases with prejudice, finding their state no-surcharge laws constitutional under rational-basis review. Adding a final layer of complication to this landscape, this issue has developed into a circuit split. The Second Circuit recently vacated the opinion of the federal district court in New York and determined that New York’s no-surcharge law was indeed constitutional,²³ while the Eleventh Circuit came to the exact opposite conclusion and found Florida’s no-surcharge law unconstitutional in late 2015.²⁴

This Comment analyzes these issues and provides workable solutions for both merchants and practitioners to follow. Part I reviews the intricate structure of credit-card networks and analyzes industry policies after Visa and MasterCard’s landmark class-action settlement. Part II examines state and federal no-surcharge statutes and analyzes the incongruity in the federal courts regarding the constitutionality of these statutes. Part III discusses adjudication and regulation of related credit-card fees in foreign countries tackling this issue. Part IV provides arguments for and against industry reform. Part V concludes with suggested improvements to the current system which more adequately balance consumer and merchant protections while allowing market forces to work in favor of both. Specifically, this Comment supports freeing merchants from anticompetitive surcharge

20. *Expressions*, 975 F. Supp. 2d at 435-36.

21. Clerk’s Judgment, *Dana’s R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Mar. 5, 2014) (order entered Sept. 2, 2014).

22. Final Judgment, *Rowell v. Pettijohn*, No. 1:14-cv-00190 (W.D. Tex. Mar. 4, 2014) (order entered Feb. 4, 2015).

23. *Expressions Hair Design v. Schneiderman*, No. 13-4533, 2015 WL 5692296 (2d Cir. Sept. 29, 2015).

24. *Dana’s R.R. Supply v. Att’y Gen., Fla.*, No. 14-14426, 2015 WL 6725138 (11th Cir. Nov. 4, 2015).

restrictions and recognizes the need for federal regulation of credit-card-interchange fees similar to the federal regulation of debit-card-interchange fees. Federal regulation of debit-card-interchange fees has resulted in price decreases, job growth, and market transparency.²⁵

A. Processing a Credit-Card Transaction

A credit-card transaction is similar to a check transaction except that the ultimate financing or credit underlying the purchase differs.²⁶ Credit-card transactions generally involve five parties: the cardholder, the merchant, the issuing bank, the merchant bank, and the network.²⁷ The cardholder and the merchant are, as primary transactors, necessary parties in a credit transaction. The remaining parties are payment-service providers. The issuing bank issues the credit card to the cardholder.²⁸ When a cardholder presents a credit card to a merchant for a purchase, the merchant relays the purchase information to the “merchant bank,”²⁹ sometimes referred to as the “merchant acquiring bank”³⁰ or “merchant acquirer.”³¹ Upon receiving the sale information from the merchant, the merchant bank processes the information through the “the network.”³² The network consists of credit-card companies, primarily owned by banks.³³ Visa, MasterCard, American Express, and Discover make up the four major networks in the United

25. Robert J. Shapiro, *The Costs and Benefits of Half a Loaf: The Economic Effects of Recent Regulation of Debit Card Interchange Fees*, NAT'L RETAIL FED'N (Oct. 2013), at 2, https://nrf.com/sites/default/files/The_Costs_and_Benefits_of_Half_a_Loaf.pdf.

26. Alan S. Frankel, *Monopoly and Competition in the Supply and Exchange of Money*, 66 ANTITRUST L.J. 313, 339 (1998).

27. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214 (E.D.N.Y. 2013).

28. *Id.* J.P. Morgan Chase, Bank of America, American Express, Citibank, and Capital One are the largest credit-card issuers worldwide, respectively by credit-card portfolios. *Largest Credit Card Portfolios Worldwide 2013*, NILSON REP. (HSN Consultants, Inc., Carpinteria, Cal.), Dec. 2014, at 11.

29. *In re Payment Card Interchange*, 986 F. Supp. 2d at 214.

30. *See, e.g.*, Kathleen A. McConnell, *The Durbin Amendment's Interchange Fee and Network Non-Exclusivity Provisions: Did the Federal Reserve Board Overstep Its Boundaries?*, 18 N.C. BANKING INST. 627, 630 (2014).

31. *See, e.g.*, Debit Card Interchange Fees and Routing, 76 Fed. Reg. 43394-01 (July 20, 2011).

32. *In re Payment Card Interchange*, 986 F. Supp. 2d at 214.

33. Visa and MasterCard “are organized as open joint ventures, owned by the numerous banking institutions that are members of the networks.” *United States v. Visa U.S.A., Inc.*, 344 F.3d 229, 235 (2d Cir. 2003). Member banks of the MasterCard and Visa “networks may function either as ‘issuers’ or ‘acquirers’ or both.” *Id.*

States.³⁴ The network relays the information it receives to the customer's issuing bank.³⁵ As the bank that has the information about the customer's account and availability of funds, the issuing bank approves or declines the transaction based on the available credit balance and other factors.³⁶ The merchant bank receives the approval or denial information and relays it to back the merchant at the point of sale.³⁷ The merchant bank credits the merchant's account for the sale price minus a fee, and the issuing bank credits the merchant bank minus a fee.³⁸ Sometime later, the issuing bank collects a payment from the cardholder on a deferred, revolving-credit basis.³⁹

1. TANSTAAFL.⁴⁰ The Relevant Fees in a Credit-Card Transaction

As the saying goes, nothing is free. The issuing bank generally charges the cardholder interest,⁴¹ annual fees, and other finance charges.⁴² The intermediaries—the merchant bank, network, and issuing bank—receive fees from the merchant behind the scenes. When the issuing bank charges the cardholder the amount of the transaction, it transmits the amount of the

34. Douglas Akers et al., *Overview of Recent Developments in the Credit Card Industry*, 17 FDIC BANKING REV. 23, 25 (2005).

35. *In re Payment Card Interchange*, 986 F. Supp. 2d at 214.

36. RONALD J. MANN, CHARGING AHEAD: THE GROWTH AND REGULATION OF PAYMENT CARD MARKETS AROUND THE WORLD 25 (2005).

37. *In re Payment Card Interchange*, 986 F. Supp. 2d at 214.

38. Frankel, *supra* note 26, at 339.

39. 2 BARKLEY CLARK & BARBARA CLARK, THE LAW OF BANK DEPOSITS, COLLECTIONS AND CREDIT CARDS ¶ 15.02 (rev. ed. 2007).

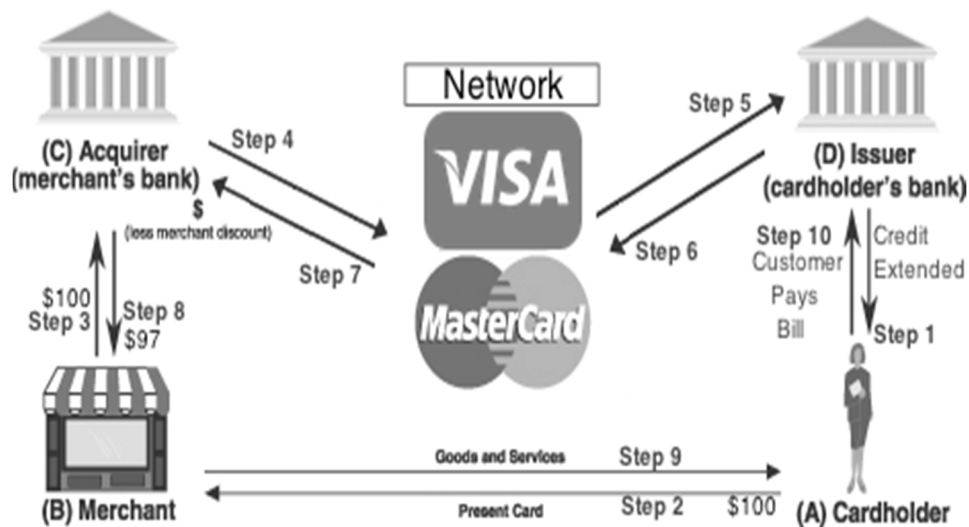
40. "There ain't no such thing as a free lunch." John Hanna, Book Review, 45 COLUM. L. REV. 803, 805 (1945) (reviewing ROBERT H. SKILTON, GOVERNMENT AND THE MORTGAGE DEBTOR (1929 TO 1939) (1944)) (applying "this profound economic truth" to government loan rates, stating, "Government has nothing to give anybody. What it gives to one man it must take from his neighbor."). The phrase was initialized "Tanstaaf" in the economics context in PIERRE DOS UTT, TANSTAAFL: A PLAN FOR A NEW ECONOMIC WORLD ORDER (1949), and popularized in MILTON FRIEDMAN, THERE AIN'T NO SUCH THING AS A FREE LUNCH (1975).

41. Approximately 70% of a typical card issuer's revenue comes from interest paid by cardholders for financed purchases. Evans & Schmalensee, *supra* note 5, at 223.

42. 2 PAYMENT SYSTEMS § 17:2, Westlaw (database updated Dec. 2012). Between 1998 and 2013, average credit-card-interest rates fluctuated between 12.76% and 15.85%. BD. OF GOVERNORS FOR THE FED. RES. SYS., REPORT TO THE CONGRESS ON THE PROFITABILITY OF CREDIT CARD OPERATIONS OF DEPOSITORY INSTITUTIONS (2014), <http://www.federalreserve.gov/publications/other-reports/files/ccprofit2014.pdf>.

purchase through the network to the merchant's bank, minus an "interchange fee"⁴³ charged to the merchant's bank. The merchant's bank

FIGURE 1: FLOW CHART OF CREDIT OR DEBIT TRANSACTION



then transmits the amount of the purchase price to the merchant, but not before withholding the interchange fee paid to the issuing bank and other fees for its services, collectively called a merchant-discount fee.⁴⁴ In sum, "[T]he total amount the merchant receives for the transaction is the purchase price minus the sum of the interchange fee and the merchant

43. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214 (E.D.N.Y. 2013). This is because the acquiring bank must "interchange" the transaction with the issuer so that the issuer can bill the cardholder in accordance with the terms of their contract. See *Nat'l Bancard Corp. v. VISA U.S.A., Inc.*, 779 F.2d 592, 594 (11th Cir. 1986).

44. See *In re Payment Card Interchange*, 986 F. Supp. 2d at 214; see also *MasterCard Interchange Rates and Fees*, MASTERCARD, <https://www.mastercard.us/en-us/merchants/get-support/merchant-interchange-rates.html> (last visited Sept. 14, 2015) [hereinafter *MasterCard Fees*] ("Interchange fees are one component of the Merchant Discount Rate (MDR) established by acquirers, which is paid by merchants to acquirers in consideration for card acceptance services.").

discount fee.⁴⁵ In material provided to merchants, Visa and MasterCard both state the merchant does not pay these fees—acquirers do.⁴⁶ It is clear, however, that acquirers do not effectively pay interchange fees because they pass these fees directly to merchants, incorporated into the merchant-discount fee.⁴⁷

With some merchant-discount fees nearing 3.5%,⁴⁸ on a \$100 credit-card transaction, the merchant will receive \$96.50 with the issuing bank retaining a percentage of the sale and the acquiring bank retaining a percentage. These fees are significant when compared to cash, where a merchant incurs “negligible”⁴⁹ indirect costs, or debit-card transactions carrying an average interchange fee of 0.79%.⁵⁰ Under no-surcharge

45. *In re Payment Card Interchange*, 986 F. Supp. 2d at 214. It is worth noting, “Visa and MasterCard invented ‘interchange fees’ in the 1970s in order to make participation in their networks more profitable for card-issuing banks, thus giving the card-issuing banks incentives to promote credit card use by their customers.” JANE KAUFMAN WINN & BENJAMIN WRIGHT, LAW OF ELECTRONIC COMMERCE § 7.07, 2014 WL 2531717 (database updated June 2014).

46. See, e.g., *Interchange: Facilitating Benefits to Cardholders, Merchants and Society*, MASTERCARD, http://www.mastercard.com/us/merchant/pdf/Interchange_backgrounder.pdf (last visited Oct. 27, 2015) (“An interchange fee is a small fee paid by a merchant’s acquiring bank to a cardholder’s issuing bank as part of an electronic payment card transaction.”); *Visa USA Interchange Reimbursement Fees*, VISA USA 1 (Apr. 18, 2015), <https://usa.visa.com/dam/VCOM/download/merchants/Visa-USA-Interchange-Reimbursement-Fees-2015-April-18.pdf> [hereinafter *Visa USA Fees*] (“Merchants do not pay interchange reimbursement fees; merchants pay ‘merchant discount’ to their financial institution.”).

47. EVANS & SCHMALENSEE, *supra* note 5, at 155. MasterCard admits this. See *MasterCard Fees*, *supra* note 44 (“[I]nterchange fees are one component of the Merchant Discount Rate (MDR) established by acquirers, which is paid by merchants to acquirers in consideration for card acceptance services.”).

48. See discussion *infra* Part I.A.2.

49. Bhaskar Chakravorti & Benjamin D. Mazzotta, *The Cost of Cash in the United States*, INST. FOR BUS. GLOBAL CONTEXT 27, 29 (Sept. 2013), <http://fletcher.tufts.edu/CostofCash/~media/Fletcher/Microsites/Cost%20of%20Cash/CostofCashStudyFinal.pdf>. These costs include “securing the cash, deposit preparation, armored car service, [and] bank visits.” *Id.* at 58. These costs also include accounting and cashier labor costs, but these costs “are generally not thought to be marginal to the consumer’s payment choice decision.” *Id.* at 59. Costs are incurred regardless of the payment method because “often the cashiers are there no matter whether they are actively running the till or not.” *Id.* at 57.

50. *Regulation II: Debit Card Interchange Fees and Routing*, BD. OF GOVERNORS OF THE FED. RES. SYS., <http://www.federalreserve.gov/paymentsystems/regii-average-interchange-fee.htm> (last updated May 12, 2015); see also *Visa USA Fees*, *supra* note 46, at 2; *MasterCard 2015-2016 Interchange Programs and Rates*, MASTERCARD 4 (Apr. 17, 2015), http://www.mastercard.com/us/merchant/pdf/Merchant_Rates_April_2014.pdf [hereinafter *MasterCard 2015-2016 Rates*].

policies with credit-card companies, merchants could not pass these costs to credit-card users. A merchant had to either absorb these fees from profit or raise prices across the board, effectively forcing non-credit-card customers to subsidize the fees introduced by credit-card users.

Merchant-discount fees (the portion not including the interchange fee) may simply be regarded as “the cost of doing business,” akin to fees for accepting debit cards or checks. Credit-card-interchange fees, however, have been the subject of numerous Department of Justice⁵¹ and international antitrust actions,⁵² private class-action lawsuits,⁵³ and extensive scholarly criticism.⁵⁴ While it is conceptually important to understand the distinction between interchange fees and merchant-discount fees, the terms are effectively interchangeable insofar as the merchant ultimately pays the interchange fee as a portion of its merchant-discount fee.

The abovementioned review describes “open” networks like Visa or MasterCard.⁵⁵ American Express and Discover are “closed-loop” networks meaning they operate as the issuer, the acquirer, and the network.⁵⁶ Under this organization, “[T]here is only a merchant-discount fee; there is no interchange rate because the same party serves as both issuer and acquirer.”⁵⁷ The analysis discussed herein applies to both open and closed networks, as closed networks’ interchange fees and merchant restraints have also been the subject of antitrust suits.⁵⁸

51. See, e.g., *United States v. Visa U.S.A., Inc.*, 344 F.3d 229, 232 (2d Cir. 2003); *United States v. Am. Express Co.*, No. 10-CV-4496(NG)(RER), 2015 WL 728563, at *7 (E.D.N.Y. Feb. 19, 2015).

52. See sources cited *supra* note 7.

53. See, e.g., *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214 (E.D.N.Y. 2013).

54. See, e.g., Frankel & Shampine, *supra* note 9, at 627; Levitin, *supra* note 9, at 1343.

55. “MasterCard and Visa are structured as open, joint venture associations with members (primarily banks) that issue payment cards, acquire merchants who accept payment cards, or both.” *United States v. Visa U.S.A., Inc.*, 163 F. Supp. 2d 322, 332 (S.D.N.Y. 2001), *aff’d*, 344 F.3d 229 (2d Cir. 2003) (internal citation omitted).

56. Levitin, *supra* note 9, at 1328.

57. *Id.* at 1332; see also *Debit Card Interchange Fees and Routing*, 76 Fed. Reg. 43,396 (July 20, 2011) (“In some circumstances, an acquirer that is also the issuer with respect to a particular transaction may authorize and settle that transaction internally.”).

58. See, e.g., *United States v. Am. Express Co.*, No. 10-CV-4496(NGG)(RER), 2015 WL 728563 (E.D.N.Y. Feb. 19, 2015); Case C-382/12 P, *MasterCard Inc. v. Eur. Comm’n*, 2014 EUR-LexCELEXLEXIS 1 (Jan. 30, 2014), <http://curia.europa.eu/juris/document/document.jsf?text=&docid=157521&pageIndex=0&doclang=EN&mode=lst&dir=&occ=firs t&part=1&cid=3927>.

2. How Networks Calculate Interchange Fees

Interchange fees and merchant discounts vary depending on the type of business accepting the credit card. Merchants conducting different types of business fall into a particular “Merchant Category Code” (MCC) designated by the IRS for card-transaction reporting pursuant to IRS Revenue Procedure 2004-43.⁵⁹ For example, the MCC for a convenience store is 5499, a chiropractor 8041, and a college or university 8220.⁶⁰ Major card brands use MCCs to influence the interchange fees that a business pays.⁶¹

The most significant factor for determining interchange fees within the present scope is the reward program that attaches to a particular card. The more rewards a customer is offered on a credit card, the more expensive the card is for merchants to accept.⁶² “Those rewards cost money, and thus these cards, referred to in the industry . . . as ‘premium cards,’ are associated with higher interchange fees.”⁶³

For example, instead of the 0.79% debit-card-interchange fee a merchant would pay or the nominal, indirect fee for accepting cash or check, the Standard Rate paid by a merchant when accepting a Visa Signature Preferred card is 2.95%, plus a flat fee of \$0.10.⁶⁴ The same transaction for a customer with a Visa Traditional Rewards card would cost the merchant 2.70% plus \$0.10.⁶⁵ Visa will charge merchants with a restaurant MCC 2.40% plus \$0.10 on a ticket paid using a Visa Signature Preferred card, or 1.95% plus \$0.10 where a Visa Traditional Rewards card is used.⁶⁶ As Figure 2 shows, a majority of this fee goes to pay for customer rewards.

59. Joseph P. Dewald, *Internal Revenue Bulletin 2004-31*, IRS (Aug. 2, 2004), http://www.irs.gov/irb/2004-31_IRB/ar17.html. Payments using cards for *services* (as opposed to payments for *merchandise*) must be reported.

60. *Id.*

61. Ben Dwyer, *Merchant Category Code: Reporting & Rates*, CARDFELLOW, <http://www.cardfellow.com/blog/merchant-category-code-mcc/> (last visited Oct. 27, 2015) (where MasterCard TCCs may be obtained); see also *Merchant Category Codes for IRS Form 1099-MISC Reporting*, VISA USA 5 (2004), https://web.archive.org/web/20150905093513/http://usa.visa.com/download/corporate/resources/mcc_booklet.pdf. MasterCard uses the same MCCs but uses an additional Transaction Category Code (TCC) to identify general business categories.

62. Levitin, *supra* note 9, at 1343.

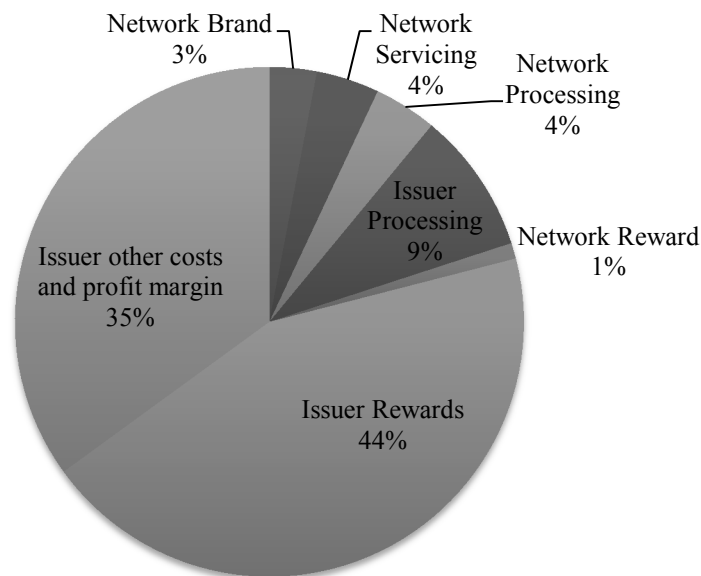
63. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214 (E.D.N.Y. 2013).

64. *Visa USA Fees*, *supra* note 46, at 4.

65. *Id.*

66. *Id.*

FIGURE 2: ESTIMATED COMPONENTS OF CREDIT-CARD-INTERCHANGE FEES⁶⁷



Similarly, the Standard Rate for a MasterCard World Elite card is 3.25% plus \$0.10, a MasterCard Enhanced Value card carries a 2.95% plus \$0.10 fee, and a restaurant MCC would be charged 2.20% plus \$0.10 if a customer opted for a MasterCard World High Value credit card instead of cash or debit card.⁶⁸ These are “default interchange rates” that an issuer charges an acquiring bank, and a merchant eventually pays.⁶⁹ In a closed-loop system like American Express, a restaurant will pay up to 3.50% plus \$0.05⁷⁰ and other possible fees.⁷¹ American Express has justified its higher

67. See AMY DAWSON & CARL HUGENER, DIAMOND MGMT. & TECH. CONSULTANTS, INC., A NEW BUSINESS MODEL FOR CARD PAYMENTS 9 (2014), <http://c0462491.cdn.cloudfiles.rackspacecloud.com/Diamond.pdf>; Fumiko Hayashi, *Do U.S. Consumers Really Benefit from Payment Card Rewards?*, FED. RES. BANK OF KAN. CITY 42 (1st Quarter 2009), <http://www.kc.frb.org/PUBLICAT/ECONREV/PDF/09q1Hayashi.pdf>.

68. *MasterCard 2015-2016 Rates*, *supra* note 50, at 2.

69. *MasterCard Fees*, *supra* note 44.

70. *Competitive Pricing Plans Your Business Can Afford*, AM. EXPRESS, https://qwww209.americanexpress.com/merchant/services/en_US/accept-credit-cards#profession=Full%20Service%20Restaurant (last visited Feb. 12, 2015).

merchant-discount fee by stating that customers spend more when using American Express, though this claim is contested.⁷²

These fees reflect “card-present” transactions, or “face-to-face transaction[s] in which a consumer physically presents a [credit] card to pay for goods or services from a ‘brick and mortar’ merchant.”⁷³ Conversely, “card-not-present” transactions differ in that the merchant never sees the card or cardholder but obtains the card number and other necessary information by phone or online.⁷⁴ Card-not-present transactions generally carry higher fees than card-present transactions,⁷⁵ in part because of the increased security involved in remote acceptance.

The brilliance behind this scheme is in credit-card companies’ ability to stimulate increased credit card use through customer reward programs while externalizing the cost of these incentives. Credit-card companies aggressively promote the use of reward cards through constant television ads, Internet marketing, and direct mail.⁷⁶ These advertisements offer generous rewards and bonuses for simply using one payment method over another. As one Chase executive remarked, “[R]ewards are obviously a key determinant in customers’ use of the credit cards, so the behavior of the customers that have rewards is that they tend to spend more and use the

71. For other fees a merchant may incur from American Express, see *American Express Merchant Reference Guide-U.S.*, AM. EXPRESS 54-58 (Apr. 2014), https://icm.aexp-static.com/Internet/NGMS/US_en/Images/Merchant%20Reference%20Guide_US_%20RefGuide.pdf [hereinafter *American Express Reference Guide*].

72. See Isabelle Lindenmayer, *Warnings of a Downside for Amex in Bank Cards*, AM. BANKER, Mar. 22, 2005, http://www.americanbanker.com/specialreports/170_8/-244549-1.html (subscription required).

73. *Paycom Billing Servs., Inc. v. MasterCard Int’l, Inc.*, 467 F.3d 283, 286 (2d Cir. 2006); see also *The 2013 Federal Reserve Payments Study*, FED. RES. 26 (July 2014), http://www.frbservices.org/files/communications/pdf/general/2013_fed_res_paymt_study_detailed_rpt.pdf (“Payments initiated when the card is read by a terminal are called card-present payments.”).

74. *Paycom Billing Servs.*, 467 F.3d at 287.

75. See, e.g., *Visa USA Fees*, *supra* note 46, at 2-3.

76. See ELIZABETH RENUART & KATHLEEN E. KEEST, NAT’L CONSUMER LAW CTR., *THE COST OF CREDIT: REGULATION, PREEMPTION, AND INDUSTRY ABUSES* § 11.8.6-8 (4th ed. 2009) (analyzing aggressive marketing and “marketing abuses” performed by credit-card lenders).

card more frequently.”⁷⁷ Issuing banks generate revenue directly from cardholders in the form of interest, fees, and other finance charges, and the increased use as a result of heavy marketing and rewards entails a greater likelihood that cardholders will pay more in interest and fees.⁷⁸ Any rewards given to cardholders come at relatively little or no expense to credit-card companies because merchants’ interchange fees pay for these programs.

In an open system like Visa and MasterCard, the networks establish and enforce rules regarding the use of their cards.⁷⁹ Additionally, each network sets its default interchange fees.⁸⁰ These rules and fees ultimately govern the contract between the acquirer and the issuer.⁸¹ One significant problem is that “[i]nstead of negotiating a separate agreement with each issuer, each acquirer simply joins the relevant network and agrees to comply with the network rules for all transactions on that network.”⁸² Thus, the small-business owner has no bargaining power to negotiate policies or fees, which ultimately “insulate[s] the interchange rate from market discipline. [Merchants] can only negotiate on the merchant discount fee.”⁸³ Of course, no acquirer negotiates a merchant-discount fee *lower* than the interchange fee plus a small profit. Thus, the default-interchange rate “becomes a fixed rate that applies to every credit card transaction (with the narrow exception of transactions by very large merchants who have sufficient volume that they can negotiate their own private interchange fees).”⁸⁴

77. Levitin, *supra* note 9, at 1346 (quoting H. Michael Jalili, *New Approaches Advised to Cure ‘Rewards Fatigue,’* AM. BANKER 8 (May 21, 2007), http://www.americanbanker.com/issues/172_100/-312658-1.html (subscription required)).

78. RENUART & KEEST, *supra* note 76, § 11.8.6-8. “The substantially worsening condition of the credit card consumer’s condition has been accompanied by credit card earnings that have been consistently higher than returns on all commercial bank activities.” *Id.* § 2.3.2.3.2.

79. Mann, *supra* note 36, at 21.

80. *Id.* at 26.

81. *Id.* at 21.

82. *Id.*

83. Levitin, *supra* note 9, at 1333.

84. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214-15 (E.D.N.Y. 2013).

Because small businesses constitute 99.7% of businesses in the United States⁸⁵ and contribute to 46% of the GDP,⁸⁶ their lack of bargaining power is significant. The largest merchants like Wal-Mart may have the ability to negotiate lower interchange rates from Visa and MasterCard⁸⁷ but will nonetheless incur an interchange fee higher than that of other payment methods because of the embedded cost of reward programs on credit-card-interchange rates. Moreover, networks may recover any discounted rate successfully negotiated by larger merchants by increasing default-interchange rates on smaller merchants that yield no bargaining power, further exacerbating the problem. In any event, merchants large and small agree that traditional interchange rules involve unlawful practices, as demonstrated by a \$3.5 billion law suit by Wal-Mart and other large retailers against Visa in 2005⁸⁸ and a \$7 billion class-action antitrust lawsuit settlement in 2013⁸⁹ involving a record twelve million merchant-class members.⁹⁰

Consider emergency auto repair as an example. At the Standard Rate of 2.95% plus \$0.10,⁹¹ upon completing a \$2,500 repair, your local repair shop pays \$73.85 for accepting a Visa Signature Preferred card over other payment methods. This fee could have paid for virtually the entire workday for a shop cashier at \$10.00 per hour.⁹²

85. *Small Business Facts & Data*, SMALL BUS. & ENTREPRENEURSHIP COUNCIL, <http://www.sbecouncil.org/about-us/facts-and-data/> (last visited Feb. 15, 2015) (“Firms with fewer than 500 workers accounted for 99.7 percent of those businesses, and businesses with less than 20 workers made up 89.8 percent. Add in the number of nonemployer firms . . . and the share of U.S. businesses with less than 500 workers increases to 99.9 percent, and firms with less than 20 workers increases to 98 percent.”) (emphasis omitted).

86. Kathryn Kobe, *Small Business GDP: Update 2002-2010*, SBA OFF. ADVOC. 4, 14 (Jan. 2012), http://www.sba.gov/sites/default/files/rs390tot_1.pdf.

87. Gwendolyn Bounds, *Merchants Balk at Higher Fees for Credit Cards*, WALL ST. J., Apr. 12, 2005, at B1.

88. *Wal-Mart Stores, Inc. v. Visa U.S.A., Inc.*, 396 F.3d 96, 101 (2d Cir. 2005).

89. *In re Payment Card Interchange*, 986 F. Supp. 2d at 213.

90. Discussed *infra* Part II.B.

91. *Visa USA Fees*, *supra* note 46, at 4.

92. Credit-card companies have used this example in lobbying for the consumer protection efficacy of merchant restraints. Visa executives discussed a hypothetical wrecker operator “on a rural road in the middle of the night imposing a surcharge” only where the cardholder does not have access to alternative payment systems. Mann, *supra* note 36, at 125-26. Professor Mann notes, however, that “[t]he risks of price gouging should not be allowed to drive a systemic issue such as pricing payment system options in competitive markets.” *Id.* at 126.

There is an important impact on the largest merchants as well. On Black Friday in 2012 for example, “From 6 p.m. to 10 p.m., Wal-Mart processed more than 10 million register transactions in its stores.”⁹³ Conservatively assuming an average ticket price of two hundred dollars⁹⁴ and a negotiated merchant-discount rate of 2.0% with a \$0.10 flat fee, if only half the customers paid with a credit card, Wal-Mart would have paid \$20.5 million in merchant-discount fees in those four hours alone.

In addition to paying a merchant-discount fee proportionate to the purchase price, merchants must also include any associated taxes⁹⁵ or tips⁹⁶ into the sale price and pay a fee to accept those amounts. Merchants primarily furnishing services may report these fees for tax purposes, but merchants primarily selling merchandise cannot.⁹⁷ Thus, merchants selling goods must pay an interchange fee on the sales tax they are required to collect but ultimately forward to the government.

State and federal governments are not immune from interchange fees. In 2007, the federal government paid \$433 million in credit-card fees, the majority of which were interchange fees.⁹⁸ While Wal-Mart may have been able to negotiate lower fees,⁹⁹ networks were unwilling to negotiate with the government to lower interchange rates.¹⁰⁰

93. *Black Friday Shoppers Have Spoken: Walmart Delivers Biggest Shopping Day of the Season*, WALMART (Nov. 29, 2013), <http://news.walmart.com/news-archive/2013/11/29/black-friday-shoppers-have-spoken-walmart-delivers-biggest-shopping-day-of-the-season>.

94. The top-selling items included televisions, tablets, and bicycles. *Id.*

95. *Card Acceptance Guidelines for VISA Merchants*, VISA USA 9 (2014), <https://usa.visa.com/dam/VCOM/download/merchants/VBS-06-APR-14-card-acceptance-guide-for-merchants.pdf> [hereinafter *Visa Acceptance Guidelines*] (“INCLUDE TAX IN THE TOTAL TRANSACTION AMOUNT. Any tax that you are required to collect must be included in the total transaction amount. Never collect taxes separately in cash.”).

96. Levitin, *supra* note 9, at 1333 (“Interchange rates typically include both a flat fee of 5 cents to 25 cents and a fee of 1 to 3 percent of the total transaction amount (including taxes and tips).”).

97. T.D. 9136, 2004-31 I.R.B. 112, 115 (“The second revenue procedure provides an optional procedure . . . in determining whether payment card transactions are reportable under section 6041 or section 6041A . . . according to whether they predominantly furnish services (for which payments are reportable) or predominantly provide goods (for which payments are not reportable).”).

98. 156 CONG. REC. 4977 (2010) (comments of Sen. Durbin).

99. *See* Bounds, *supra* note 87.

100. 156 CONG. REC. at 4977 (comments of Sen. Durbin). This denial to negotiate with the federal government may have provided part of the impetus for federal recognition of the need to reform the interchange fee system. *See id.*

In total, personal-consumption expenditures on credit cards amounted to \$2.49 trillion in the United States in 2013, and economists expect this number to increase by a remarkable 65% to \$4.11 trillion by 2018.¹⁰¹ In 2013, 93.32 billion credit, debit, and electronic bank-transfer transactions were processed in the United States,¹⁰² each presumably incurring some kind of processing fee. These figures and projections demonstrate that interchange fees are so significant in the United States economy that they can no longer be ignored.

II. Contractual Merchant Restraints

A. The Different Types of Contractual Restraints

Credit-card companies have contractual rules that restrain how merchants can accept credit cards and how they may (or may not) charge to recoup the fees they incur.¹⁰³ Historically, there have been five significant restraints imposed on merchants based on their contracts with credit-card companies: (1) no-surcharge rules; (2) no-discount rules; (3) “honor-all-cards” rules; (4) anti-steering and nondisclosure rules; and (5) no-minimum and no-maximum purchase rules.

1. No-Surcharge Rules

The term “surcharge” means “any means of increasing the regular price to a cardholder which is not imposed upon customers paying by cash, check, or similar means.”¹⁰⁴ No-surcharge rules prohibit merchants from surcharging the merchant-discount fee at the point of sale.¹⁰⁵ For example, if a company decides to purchase a \$100,000 piece of machinery and pays with a MasterCard World Elite Business card, the seller could not surcharge its \$3,250.10 fee.¹⁰⁶ The seller would either have to (1) absorb this fee from its profit on the sale or (2) raise the price of all machinery, effectively

101. *Consumer Payment Systems in the U.S. 2013 vs. 2018*, NILSON REP. (HSN Consultants, Inc., Carpinteria, Cal.), Dec. 2014, at 1.

102. *Id.* at 11.

103. David Herr & Steve Baicker-McKee, *Law and Motion: Class Actions—Settlement Approval*, 29 No. 3 FED. LITIGATOR 8, Westlaw (Mar. 2014).

104. 15 U.S.C. § 1602(r) (2012).

105. *See, e.g.*, Levitin, *supra* note 1, at 11 n.39 (quoting MASTERCARD INT’L, MERCHANT RULES MANUAL, BYLAW 9.12.2 (2006) (“A merchant must not directly or indirectly require any MasterCard cardholder to pay a surcharge or any part of any merchant discount or any contemporaneous finance charge in connection with a MasterCard card transaction.”)).

106. $\$100,000 \times 3.25\%$ (MasterCard World Elite Standard Rate) + \$0.10 (per-transaction fee) = \$3,250.10.

requiring buyers using other payment methods to subsidize the fee. American Express¹⁰⁷ and Discover¹⁰⁸ have “piggyback”¹⁰⁹ rules, requiring a merchant who surcharges any cards to surcharge all cards.

2. No-Discount Rules

A discount is a reduction from the regular price.¹¹⁰ In the past, contractual no-discount rules prohibited merchants from offering discounted prices based on the payment method used. Congress amended the Truth in Lending Act (TILA) in 1974 to require networks to allow merchant discounting, subject to proper disclosure and an arbitrary 5% cap.¹¹¹ Congress removed this cap in 1981,¹¹² and in 2010, the Durbin Amendment to the Dodd-Frank Act removed networks’ restrictions on discounting credit cards at the network level such that credit-card companies can no longer prohibit merchants from discounting their cards.¹¹³ Permitting discounts only at the network level means that merchants can discount certain payment methods (*e.g.*, discounting cash payments but not credit cards) but cannot discount based on a particular issuer or card type (*e.g.*, discounting all Visa credit cards but not discounting MasterCard). For example, a merchant incurring a \$3 credit-card-processing fee could discount a television from \$100 to \$97 for Customer *A* who pays with cash instead of a credit card. However, under no-surcharge rules, a merchant cannot impose a surcharge on Customer *B*’s

107. *American Express Reference Guide*, *supra* note 71, at 14 (“Merchants must not . . . impose any restrictions, conditions, disadvantages or fees when the Card is accepted that are not imposed equally on all Other Payment Products . . .”).

108. *Merchant Operating Regulations*, DISCOVER 6 (Oct. 15, 2010), <http://www.indyhost.net/images/surcharge/Discover-Operating-Regulations-4-2011.pdf> (“[Y]ou may not . . . provide[] unequal and unfavorable treatment [to] any Person who elects to pay using a Card . . . and you may not in any way discriminate among various Issuers of Cards”) (emphasis omitted).

109. Levitin, *supra* note 1, at 11 n.39 (using the term “piggy-back”).

110. 15 U.S.C. § 1602(q) (2012). The term “regular price” means “the tag or posted price charged for the property or service if a single price is tagged or posted, or the price charged for the property or service when payment is made by use of an open-end credit plan or a credit card if either (1) no price is tagged or posted, or (2) two prices are tagged or posted, one of which is charged when payment is made by use of an open-end credit plan or a credit card and the other when payment is made by use of cash, check, or similar means.” *Id.* § 1602(y).

111. Fair Credit Billing Act of 1974, Pub. L. No. 93-495, § 306, 88 Stat. 1500, 1515.

112. Cash Discount Act, Pub. L. No. 97-25, § 101, 95 Stat. 144, 144 (1981).

113. 15 U.S.C. § 1693o-2(b)(3)(A)-(B) (2012).

credit-card purchase of the same \$100 television and make the full price \$103.

3. Honor-All-Cards Rules

“Honor-all-cards” rules require a merchant who accepts any card from a particular credit-card network to accept *all* cards bearing that name, regardless of the issuing bank or interchange fee.¹¹⁴ For example, under contracts with Visa, “merchants must accept all categories of Visa debit, credit, and prepaid cards.”¹¹⁵ A merchant who accepts a low interchange-fee card from Customer *B* must accept a high interchange-fee card from Customer *C*. In the past, honor-all-cards provisions required merchants that accepted a brand’s debit cards to also accept its credit cards.¹¹⁶ However, because of a settlement with Wal-Mart, Sears, and other retailers in 2003, merchants now do not have to accept a Visa or MasterCard credit card simply because they accept a Visa or MasterCard debit card.¹¹⁷

4. Anti-Steering and Nondisclosure Rules

Some contracts prohibit merchants from using price signals at the point of sale to steer customers to other payment systems with less expensive fees.¹¹⁸ Steering would be considered an expression of preference for or against a certain network, brand, product, or payment type. After antitrust settlements and lawsuits brought by the Department of Justice,¹¹⁹ Visa,¹²⁰ and MasterCard¹²¹ now allow some steering. American Express is currently

114. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 214 (E.D.N.Y. 2013) *appeal filed*, no. 14-241 (2d Cir. 2014).

115. *Visa Acceptance Guidelines*, *supra* note 95, at 9; *see also MasterCard Rules*, MASTERCARD Bylaw 5.8.1, at 83 (Dec. 11, 2014), http://www.mastercard.com/us/merchant/pdf/BM-Entire_Manual_public.pdf [hereinafter *MasterCard Rules*].

116. Adam J. Levitin, *Payment Wars: The Merchant-Bank Struggle for Control of Payment Systems*, 12 STAN. J.L. BUS. & FIN. 425, 433 n.26 (2007).

117. *See In re Visa Check/Mastermoney Antitrust Litig.*, 297 F. Supp. 2d 503, 508 (E.D.N.Y. 2003).

118. *In re Payment Card Interchange*, 986 F. Supp. 2d at 215.

119. *See Chad Bray, Visa, MasterCard Win Approval of Settlement in ‘Anti-Steering’ Case*, WALL ST. J., July 20, 2011; *see also United States v. Am. Express Co.*, No. CV-10-4496(NGG)(RER), 2015 WL 728563, at *7 (E.D.N.Y. 2015). While defendants Visa and MasterCard settled their claims in that case, American Express did not and is still litigating its claims. As a result, Visa explicitly permits steering while American Express expressly prohibits steering.

120. *Visa Acceptance Guidelines*, *supra* note 95, at 9.

121. *MasterCard Rules*, *supra* note 115, at 215.

litigating antitrust steering claims brought by the Department of Justice¹²² and still prohibits merchant steering.¹²³

5. *No-Minimum and No-Maximum Purchase Rules*

No-minimum/no-maximum rules prevent merchants from declining to accept credit cards on particularly low- or high- dollar-amount transactions.¹²⁴ Small-ticket and small-margin transactions result in less profit for merchants when a customer uses a credit card or debit card because of the flat transaction fee.¹²⁵ Suppose a customer purchases a \$0.25 item at a convenience store and pays with a Visa Signature Preferred card. The default rate for small-ticket items purchased with a Visa Signature Preferred card is 2.10% plus \$0.10.¹²⁶ Assuming the purchase occurs in a city with 9.0% state and local sales taxes,¹²⁷ the transaction leaves the merchant with around \$0.15 after accounting for only the flat interchange fee and sales tax.¹²⁸ Considering the cost of the item, other transaction fees, and overhead, the merchant will almost certainly lose money accepting credit cards on small-ticket transactions. Networks' contractual no-minimum rules forced merchants to lose money by accepting credit cards on small-ticket items. As with no-discount rules, the Dodd-Frank Act limits contractual restrictions on no-minimum purchase rules, freeing merchants to set a minimum credit-card purchase of up to \$10.¹²⁹

122. See Melissa Lipman, *Judge Urges DOJ, AmEx to Pursue Antitrust Settlement*, LAW360 (Oct. 9, 2014), <http://www.law360.com/articles/568752/judge-urges-doj-amex-to-pursue-antitrust-settlement>; see also *Am. Express Co.*, No. CV-10-4496(NGG)(RER), 2015 WL 728563.

123. See, e.g., *American Express Reference Guide*, *supra* note 71, at 14 (“Merchants must not . . . indicate or imply that they prefer, directly or indirectly, any Other Payment Products over our Card, . . . [nor] try to persuade or prompt Cardmembers to use any Other Payment Products or any other method of payment (e.g., payment by check) . . .”).

124. Levitin, *supra* note 116, at 436.

125. *Id.*

126. *Visa USA Fees*, *supra* note 46, at 4.

127. The average state and local sales tax was 9.6% in 2012. William P. Barrett, *Average U.S. Sales Tax Rate Drops—A Little*, FORBES (Feb. 2, 2012), <http://www.forbes.com/sites/williambarrett/2012/02/02/average-u-s-sales-tax-rate-drops-a-little/>.

128. $\$0.25 + 9\% \text{ tax} = \0.27 .
 $(\$0.27 - \$0.10 \text{ flat interchange fee}) - \$0.02 \text{ tax} = \$0.15$.

129. 15 U.S.C. § 1693o-2(b)(3)(A) (2012).

As the name suggests, no-maximum rules¹³⁰ prevent merchants from setting a maximum amount for a credit-card transaction. Suppose a pecunious customer has saved \$30,000 in cash to purchase a new car but would rather use his credit card in order to accrue the substantial reward points he stands to gain. The average dealer profit over invoice might only be \$1000-\$1500¹³¹ on this purchase, assuming incentives and manufacturer-to-dealer cash have not reduced the purchase price below invoice already.¹³² With an interchange fee of just 3%, \$900 of the estimated \$1000-\$1500 profit goes exclusively to credit-card-acceptance fees. One can see why many merchants would favor setting a maximum limit on credit-card purchases.

The Dodd-Frank Act provides no relief for merchants regarding no-maximum rules, though it permits federal agencies and institutes of higher learning to set maximum allowable credit-card amounts.¹³³

B. Visa and MasterCard Terminate Their No-Surcharge Policy: In re Payment Card Interchange Fee & Merchant Discount Antitrust Litigation

A lawsuit filed in 2005¹³⁴ eventually morphed into a putative class action containing approximately twelve million large and small merchant-members who alleged that Visa and MasterCard, as well as issuing and acquiring banks, conspired to fix interchange fees in violation of section 1 of the Sherman Act.¹³⁵ After nearly eight years of litigation on several consolidated cases, Visa, MasterCard, and the class plaintiffs agreed to settle the case in 2012.¹³⁶ Judge John Gleeson of the Eastern District of

130. See, e.g., *Minimum Transaction Amount on a Visa Credit Card*, VISA USA (2013), <http://usa.visa.com/download/merchants/minimum-transactions-credit-card.pdf> (“Only federal agencies or institutions of higher education can impose a maximum transaction amount.”).

131. Allie Johnson, *Buying a Car with a Credit Card Often an Uphill Fight*, CREDITCARDS (Sept. 4, 2014), <http://www.creditcards.com/credit-card-news/buying-car-with-credit-card-1280.php>.

132. *10 Steps to Buying a New Car*, KELLEY BLUE BOOK, <http://www.kbb.com/car-advice/car-buying/step-5-know-when-the-price-is-right/?r=857748394366353800> (last visited Feb. 12, 2015). Kelley Blue Book notes that the average dealer mark-up over invoice is less than 10% on new cars, which, compared with other industries, is “quite low.” *Id.*

133. See 15 U.S.C. § 1693o-2(b)(3)(A)(ii) (2012).

134. *Complaint, Photos Etc. Corp. v. Visa U.S.A. Inc.*, No. 3:05-CV-01007 (D. Conn. Jun. 22, 2005).

135. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 213 (E.D.N.Y. 2013), *appeal filed*, No. 14-241 (2d Cir. 2014).

136. Settlement Agreement, *supra* note 12, ¶¶ 42, 55.

New York approved the settlement in December 2013.¹³⁷ The terms of the settlement included the following:

- \$7.25 billion claim settlement¹³⁸ (believed to be the largest antitrust settlement in history).¹³⁹
- Rule modifications to permit merchants to surcharge on Visa or MasterCard credit cards at both the brand level (e.g., all Visa or MasterCards) and product levels (e.g., only Visa Signature cards or MasterCard World Elite cards).¹⁴⁰ Surcharges must be disclosed before they are incurred and on a receipt.¹⁴¹
- Obligations on the part of Visa and MasterCard to negotiate interchange fees in good faith.¹⁴²
- Merchants operating multiple businesses may now accept Visa and/or MasterCard at fewer than all of their businesses.¹⁴³
- Permanent implementation of the reforms in the Durbin Amendment¹⁴⁴ and the Department of Justice's consent decree with Visa and MasterCard,¹⁴⁵ even if those reforms are repealed or otherwise undone.¹⁴⁶

137. *In re Payment Card Interchange*, 986 F. Supp. 2d at 241.

138. Settlement Agreement, *supra* note 12, ¶¶ 9-10, 11-13.

139. David McAfee, *\$7.25B Visa, MasterCard Swipe Fee Deal Gets Approval*, LAW360 (Dec. 13, 2013), <http://www.law360.com/articles/495780/7-25b-visa-mastercard-swipe-fee-deal-gets-approval>; Christie Smythe, *Visa, MasterCard Judge Asked to Approve Settlement, Fees*, BLOOMBERG (Apr. 12, 2013), <http://www.bloomberg.com/news/2013-04-12/visa-mastercard-judge-asked-to-approve-settlement-fees.html>.

140. Settlement Agreement, *supra* note 12, ¶¶ 42, 55.

141. *In re Payment Card Interchange*, 986 F. Supp. 2d at 234.

142. Settlement Agreement, *supra* note 12, ¶¶ 43, 56.

143. *Id.* ¶¶ 41, 54.

144. The Durbin Amendment, *inter alia*, removes merchant restrictions on discounting at the network level and permits setting minimum credit-card purchases of up to \$10.00. *See* 15 U.S.C. § 1693o-2(b)(3)(A)-(B) (2012).

145. A 2010 DOJ investigation ended in consent decrees in which Visa and MasterCard agreed to permit product-level discounting of credit and debit cards. *In re Payment Card Interchange*, 986 F. Supp. 2d at 215.

146. Settlement Agreement, *supra* note 12, ¶¶ 40, 44, 53, 57.

Many unsatisfied class merchants, including half of the top one hundred retailer-class members¹⁴⁷ like Wal-Mart, Home Depot, and Amazon.com, have appealed the decision to the Second Circuit.¹⁴⁸ Appellants' most relevant arguments for present purposes involve default interchange rules, honor-all-cards rules, and no-surcharge rules.

Appellants first argue that the combination of networks' honor-all-cards rules and default interchange rules violate antitrust laws and that the settlement offers no relief in these areas "whatsoever."¹⁴⁹ One of the terms of the settlement is a mandatory release of all future injunctive and damages claims against Visa or MasterCard on topics related to the suit.¹⁵⁰ Objecting merchants claim that the networks have therefore "purchased . . . immunity" in the \$7 billion settlement, barring all future claims involving the controversial honor-all-cards and default interchange rules.¹⁵¹ "Far from enjoining the restrictive rules at issue, . . . this Settlement expressly ratifies both rules for all time."¹⁵² Judge Gleeson noted that plaintiffs would have a difficult time proving that default interchange rules violate antitrust laws and that "default interchange rules played an essential role in the construction of the networks at issue here, and those networks provide substantial benefit to both merchants and consumers."¹⁵³

Regarding honor-all-cards rules, Judge Gleeson determined that these rules are not anticompetitive, but are actually *procompetitive*, given the complex credit-card system comprised of thousands of issuing banks, thousands of acquiring banks, and millions of merchants.¹⁵⁴ The need for a seamless card acceptance in the form of honor-all-cards rules, he determined, is integral to the success of the networks.¹⁵⁵ Honor-all-cards practices previously required merchants accepting a Visa or MasterCard

147. *Another Interchange Opt-Out Lawsuit*, NILSON REP. (HSN Consultants, Inc., Carpinteria, Cal.), July 2013, at 5.

148. See *In re Payment Card Interchange*, No. 14-241 (2d Cir. filed Jan. 22, 2014).

149. Brief for National Retail Federation at 3, *In re Payment Card Interchange*, No. 14-00663 (2d Cir. June 16, 2014).

150. Settlement Agreement, *supra* note 12, ¶¶ 40, 44, 53, 57.

151. The Merchant Trade Groups' Reply Brief at 4, *In re Payment Card Interchange*, No. 14-00663 (2d Cir. Feb 14, 2014).

152. *Id.*

153. *In re Payment Card Interchange Fee & Merc. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 227 (E.D.N.Y. 2013) *appeal filed*, No. 14-241 (2d Cir. 2014); see also *supra* notes 117-118 and accompanying text.

154. *In re Payment Card Interchange*, 986 F. Supp. 2d at 228.

155. *Id.*

debit card to also accept all of that brand's credit cards, but these practices were ended as terms of another class action antitrust settlement in 2003.¹⁵⁶

Another potential problem with the settlement is that by its terms, “[i]f another more expensive network brand that the merchant accepts continues to restrict surcharging, the merchant may not surcharge Visa and MasterCard without also surcharging transactions on that competitor network.”¹⁵⁷ The plain language of this “level-playing field”¹⁵⁸ provision leads to a dilemma: American Express¹⁵⁹ and Discover¹⁶⁰ have piggyback rules that force a merchant who surcharges any card to surcharge all cards equally. The interplay between the different networks’ rules means that a merchant who surcharges a Visa or MasterCard transaction but does not surcharge an American Express or Discover transaction operates in violation of American Express or Discover piggyback provisions. But a merchant imposing surcharges uniformly across credit-card networks operates in violation of no-surcharge provisions of American Express, Discover, and the terms of the settlement. Merchants are left to either not surcharge any credit-card transaction, effectively rendering these rule changes in the settlement useless, or surcharge Visa and MasterCard transactions and terminate contracts with American Express and Discover. Thus, lifting contractual no-surcharge prohibitions provides no effective relief for 90% of merchants (based on card volume) who accept American Express and Discover.¹⁶¹

Fortunately for merchants, American Express and Discover appear to have agreed to end their no-surcharge provisions—American Express pursuant to the terms of a pending settlement in a different class-action lawsuit¹⁶² and Discover pursuant to the terms of an agreement to drop the

156. See *In re Visa Check/Mastermoney Antitrust Litig.*, 297 F. Supp. 2d 503, 508 (E.D.N.Y. 2003).

157. *In re Payment Card Interchange*, 986 F. Supp. 2d at 234.

158. *Id.*

159. *American Express Reference Guide*, *supra* note 71, at 14 (“Merchants must not . . . impose any restrictions, conditions, disadvantages or fees when the Card is accepted that are not imposed equally on all Other Payment Products . . .”).

160. See *supra* note 108 and accompanying text.

161. Brief for National Retail Federation at 4, *In re Payment Card Interchange*, No. 14-00663 (2d Cir. June 16, 2014).

162. Press Release, Am. Express, American Express Agrees to Settle Class Action Litigations (Dec. 19, 2013), <http://about.americanexpress.com/news/pr/2013/amex-agrees-to-settle-class-action.aspx>.

company as a party in the *Payment Card Interchange* case.¹⁶³ Thus, the piggyback objection appears moot, except in the event that one network caps its surcharge allowance, effectively capping surcharges on all cards. For example, if Discover were to permit only a surcharge up to 2%, the level-playing field provision would permit a merchant the ability to surcharge only up to 2% on Visa, MasterCard, or American Express as well.

In their last objection, appellants argue that statutes in nine states (including the four most populous states)¹⁶⁴ prohibit merchant surcharging,¹⁶⁵ so contractual relaxing of no-surcharge provisions provides no relief for merchants in these states or national merchants conducting business in these states.

Judge Gleeson notes that the level-playing field and state-law objections “place[] in sharp relief the limited extent to which the problems merchants complain about in this industry can be addressed in a single lawsuit.”¹⁶⁶ Merchants cannot expect a settlement involving Visa and MasterCard to confer new obligations upon non-party networks like American Express and Discover. Additionally, Judge Gleeson stated that he cannot preempt state law with this settlement,¹⁶⁷ but optimistically noted that a federal court in New York recently found that state’s no-surcharge statute unconstitutional, perhaps signaling a trend among states diminishing these laws.¹⁶⁸ Judge Gleeson seems to have been incorrect in this prediction, however, as the Second Circuit recently vacated the New York opinion,¹⁶⁹ and courts in Florida¹⁷⁰ and Texas¹⁷¹ have recently upheld the validity of their states’ no-surcharge statutes.

163. *Discover to Drop “No Surcharge” Ban*, GREEN SHEET, http://www.greensheet.com/gs_archive.php?issue_number=060301&story=9 (last visited Feb. 15, 2015); see also *Merchant Surcharge Notification Form*, DISCOVER, <https://www.discoversurcharge.com> (last visited Feb. 15, 2015).

164. See table *infra* note 198.

165. See discussion *infra* Part III.B.

166. *In re Payment Card Interchange Fee & Merc. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 233 (E.D.N.Y. 2013), *appeal filed*, No. 14-291 (2d Cir. 2014).

167. *Id.* at 219.

168. *Id.* at 232-33.

169. *Expressions Hair Design v. Schneiderman*, No. 13-4533, 2015 WL 5692296, at *1 (2d Cir. Sept. 29, 2015).

170. *Clerk’s Judgment, Dana’s R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Mar. 5, 2014) (order entered Sept. 2, 2014).

171. *Final Judgment, Rowell v. Pettijohn*, No. 1:14-cv-00190 (W.D. Tex. Mar. 4, 2014) (order entered Feb. 4, 2015).

Regarding the Second Circuit's review of the settlement approval, it is worth noting that in 2003, the same circuit affirmed a settlement approved by Judge Gleeson in a similar Visa and MasterCard class-antitrust case.¹⁷² Similar objections existed in that appeal, but the Second Circuit affirmed the settlement approval as "substantively fair" under an abuse-of-discretion standard.¹⁷³ Even if this settlement is not preserved in its entirety through the appeals process, the trend is clearly in favor of credit-card networks ending their contractual no-surcharge provisions.

III. Statutory Merchant Restraints

A. Federal Law

The Federal prohibition against surcharging and discounting began with the Truth in Lending Act (TILA) in 1968.¹⁷⁴ Congress amended TILA in 1974 to permit cash discounts of no more than 5% as long as merchants properly disclose the discount.¹⁷⁵ The surcharge prohibition had a sunset provision, which Congress renewed twice. One renewal came by way of the Financial Institutions Regulatory and Interest Rate Control Act of 1978 (FIRIRCA)¹⁷⁶ and another in 1981 through the Cash Discount Act.¹⁷⁷ In 1984, however, Congress allowed the sun to set on the surcharge prohibition.¹⁷⁸

In 1981, the Senate committee argued that the policy behind the federal surcharge ban was consumer protection:¹⁷⁹ "consumers cannot be lured into an establishment on the basis of the 'low, rock-bottom price' only to find at the cash register that the price will be higher if a credit card is used."¹⁸⁰ The consumer-protection basis for these laws has drawn both skepticism and complete rejection for two significant reasons.

172. *In re Visa Check/Mastermoney Antitrust Litig.*, 297 F. Supp. 2d 503, 507 (E.D.N.Y. 2003).

173. *See Wal-Mart Stores, Inc. v. Visa U.S.A., Inc.*, 396 F.3d 96, 117, 124 n.12 (2d Cir. 2005).

174. Pub. L. No. 90-321, tit. 1, 82 Stat. 146 (1968) (codified as amended at 15 U.S.C. §§ 1601-1667(f) (2012)).

175. Fair Credit Billing Act of 1974, Pub. L. No. 93-495, § 306, 88 Stat. 1500, 1515.

176. Pub. L. No. 95-630, § 1501, 92 Stat. 3641, 3713 (two-year extension).

177. Pub. L. No. 97-25, § 201, 95 Stat. 144, 144 (1981) (three-year extension).

178. S. REP. NO. 97-23, at 3 (1981); Cash Discount Act § 201, 95 Stat. at 144 (sunset on February 27, 1984).

179. *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 2d 430, 449 (S.D.N.Y. 2013).

180. S. REP. NO. 97-23, at 4 (1981).

First, many consider the distinction between a discount and a surcharge dubious¹⁸¹ or nonexistent.¹⁸² One may ask why, if mathematically identical, would credit-card companies oppose a surcharge when the freedom to discount based on payment type is protected by federal law? The answer lies with a psychological phenomenon known as “loss aversion,” which indicates (perhaps intuitively) that “changes that make things worse (losses) loom larger than improvements or gains’ of an equivalent amount.”¹⁸³ Similarly, the “framing effect” demonstrates that framing a price differential as a discount receives far less negative customer reaction than framing a price differential as a surcharge.¹⁸⁴ “Because of the framing effect, surcharges are far more effective than discounts at signaling to consumers the relative costs of a payment system.”¹⁸⁵ Put another way, a surcharge above the retail price is more likely to frustrate customers away from credit card use than a discounted price is to entice them towards paying with cash. With discounts and surcharges being economically equal, however, critics question¹⁸⁶ the logic behind the traditional prohibition against surcharges while the ability to discount remains protected by statute.¹⁸⁷

Second, consumer advocates and numerous federal agencies, including the Federal Trade Commission, “[u]nanimous[ly] dissent[ed] . . . against extending the ban on surcharges.”¹⁸⁸ They argued “state and federal no-surcharge laws . . . were enacted in the name of consumer protection at the behest of the credit-card industry over the objection of consumer advocates.”¹⁸⁹ Various merchants have alleged that Visa and MasterCard even created and funded a “fake” consumer protection group called

181. *Id.* at 15 (comment of Sen. Dalton) (“In any event, the actual difference between a discount and surcharge is unclear, and we believe it would be anomalous to allow one and not the other.”).

182. *Expressions*, 975 F. Supp. 2d at 436 (“In terms of their immediate economic consequences, surcharges and discounts are merely different labels for the same thing—a price difference between cash and credit.”).

183. *Expressions Hair Design v. Schneiderman*, No. 13-4533, 2015 WL 5692296, at *1 (2d Cir. Sept. 29, 2015) (quoting Daniel Kahneman et al., *Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias*, 5 J. ECON. PERSP. 193, 199 (1991)).

184. Adam J. Levitin, *The Antitrust Super Bowl: America’s Payment Systems, No-Surcharge Rules, and the Hidden Costs of Credit*, 3 BERKELEY BUS. L.J. 265, 280 (2005).

185. *Id.* at 282 (emphasis omitted).

186. See *supra* notes 180-182 and accompanying text.

187. See, e.g., 15 U.S.C. § 1693o-2(b)(3)(A)-(B) (2012); Cash Discount Act, Pub. L. No. 97-25, § 102, 95 Stat. 144, 144 (1981).

188. S. REP. NO. 97-23, at 10 (1981) (comments of Sen. Proxmire).

189. *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 430, 449 (S.D.N.Y. 2013).

“Consumers Against Penalty Surcharges” to support state and federal no-surcharge prohibitions in response to “real” consumer advocacy group opposition.¹⁹⁰ Some federal legislators considering the Cash Discount Act called no-surcharge laws “special interest legislation” for legislators’ “friends in the credit card industry” and “costing the American people billions of dollars.”¹⁹¹

Federal legislators allowed the surcharge ban to sunset in 1984, and merchants can now discount or surcharge without violating federal law.¹⁹² The current law, however, only expressly *protects* merchants’ ability to discount. Accordingly, networks and states cannot restrict merchants’ ability to discount but may still freely restrict merchant surcharging.

B. State Law

As a result of heavy lobbying by credit-card companies in the 1980s,¹⁹³ nine states currently prohibit credit-card surcharging by statute: California, Colorado, Connecticut, Florida, Kansas, Massachusetts, New York, Oklahoma, and Texas,¹⁹⁴ as listed in Table 1 (Appendix). Like federal no-surcharge statutes, the purported policy behind these state statutes is consumer protection.¹⁹⁵ The fact that federal law *permits* surcharging has been held not to preempt state no-surcharge laws.¹⁹⁶

The no-surcharge-rule changes that occurred as a result of the Visa, MasterCard, American Express, and Discover agreements clearly do not provide surcharge relief for merchants in these states. As Judge Gleeson noted in *In re Payment Card Interchange*, “[T]he state laws prohibiting

190. Corrected Brief for Plaintiffs-Appellees, *Expressions Hair Design v. Schneiderman*, No. 13-4533 at 12 (2d Cir. 2014); Memorandum of Law in Support of Plaintiffs’ Motion for Summary Judgment, *Italian Colors Rest. v. Harris*, No. 2:14-cv-00604, at 6 (E.D. Cal. Mar. 5, 2014).

191. S. REP. NO. 97-23, at 9-10 (1981) (comments of Sen. Proxmire).

192. 15 U.S.C. § 1666f (2012).

193. *Expressions*, 975 F. Supp. 2d at 439.

194. See CAL. CIV. CODE § 1748.1(a) (West Supp. 2015) (found unconstitutional in *Italian Colors Rest. v. Harris*, No. 2:14-cv-00604 (E.D. Cal. Mar. 5, 2014)); COLO. REV. STAT. ANN. § 5-2-212(1) (2014); CONN. GEN. STAT. § 42-133ff(a) (2013); FLA. STAT. § 501.0117(1) (2014); KAN. STAT. ANN. § 16a-2-403 (2007); MASS. GEN. LAWS ANN. ch. 140D, § 28A(a)(2) (West 2012); N.Y. GEN. BUS. LAW § 518 (McKinney 1984); 14A OKLA. STAT. § 2-211 (2011); 14A OKLA. STAT. § 2-417 (2011); TEX. FIN. CODE ANN. § 339.001(a) (West Supp. 2014).

195. *Expressions*, 975 F. Supp. 2d at 449.

196. *People v. Fulvio*, 135 Misc. 2d 93 (N.Y. Crim. Ct. 1987).

surcharging . . . are real, and they in fact undermine to an extent the immediate utility of the rules reforms in the proposed settlement.”¹⁹⁷

Perhaps more importantly, heavy lobbying successfully orchestrated these no-surcharge statutes in states with the highest populations.¹⁹⁸ States with no-surcharge statutes make up only 20% of the states in the United States, but they collectively contain 40% of the U.S. population according to the 2010 United States Census.¹⁹⁹ Indeed, the top four states in terms of population—California, Texas, New York, and Florida, respectively—all passed no-surcharge statutes. Since most national merchants are generally located in the most populous cities in these states, these national merchants see a significant number of transactions subject to state no-surcharge prohibitions. For example, First Data Corporation (FDC), merchant-appellant in the Visa and MasterCard settlement, points out that the states

197. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 219 (E.D.N.Y. 2013).

198. The following table illustrates the state population of states with no-surcharge statutes as a percentage of U.S. Population in 2010.

State	Population Rank	Percentage of U.S. Population	2010 Population
California	1	12.07	37,253,956
Texas	2	8.14	25,145,561
New York	3	6.28	19,378,102
Florida	4	6.09	18,801,310
Massachusetts	14	2.12	6,547,629
Colorado	22	1.63	5,029,196
Oklahoma	28	1.22	3,751,351
Connecticut	29	1.16	3,574,097
Kansas	33	0.92	2,853,118
Maine	41	0.43	1,328,361
Total		40%	123,662,681

Data taken from *United States Census 2010*, U.S. CENSUS BUREAU, <http://www.census.gov/2010census/> (last visited Aug. 30, 2015).

199. *Id.*

that prohibit “the passing of fees onto consumers for use of credit cards . . . account[] for over 77% of FDC’s credit-card transactions.”²⁰⁰

Only one state expressly protects credit-card surcharging by statute. Since 1987, Minnesota has allowed surcharging, subject only to the condition that the merchant fully disclose any surcharge to consumers.²⁰¹ This statute was largely ineffective in the face of contractual no-surcharge rules, but now that Visa and MasterCard have eliminated those rules, this statute offers renewed significance.

1. Inconsistent Federal District Court Adjudication of State No-Surcharge Statutes

In 2012, five retailers sued the New York Attorney General and district attorneys of three counties challenging the constitutionality of New York General Business Law section 518,²⁰² which prohibited any seller in sales transactions from imposing a surcharge, or “swipe fee,” on a cardholder using a credit card instead of another payment method.²⁰³ In an opinion highly critical of state no-surcharge laws, Judge Rakoff held that the statute was both an unconstitutional restriction on commercial speech and was void for vagueness.²⁰⁴

Commercial speech generally triggers intermediate scrutiny, and courts consider:

- (1) whether the regulated speech concern[s] lawful activity and [is] not . . . misleading, (2) whether the asserted governmental interest justifying the regulation is substantial, (3) whether the regulation directly advances the governmental interest asserted, and (4) whether the regulation is not more extensive than is necessary to serve the governmental interest.²⁰⁵

The Southern District of New York determined that New York’s statute violated merchants’ First Amendment protection of commercial speech

200. Objectors-Appellants First Data Corporation et al. Page Proof Opening Brief at 40, *In re Payment Card Interchange*, No. 14-00663 (2d Cir. June 16, 2014), 2014 WL 2794831.

201. See MINN. STAT. § 325G.051 (2012).

202. N.Y. GEN. BUS. LAW § 518 (McKinney 2015) (“No seller in any sales transaction may impose a surcharge on a holder who elects to use a credit card in lieu of payment by cash, check, or similar means. Any seller who violates the provisions of this section shall be guilty of a misdemeanor punishable by a fine not to exceed five hundred dollars or a term of imprisonment up to one year, or both.”).

203. *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 2d 430 (S.D.N.Y. 2013).

204. *Id.* at 448; see also *supra* note 20 and accompanying text.

205. *Expressions*, 975 F. Supp. 2d at 445 (internal citations and quotations omitted).

because the difference between a “surcharge” and a “discount” exists “based on words and labels, rather than economic realities. So read, the statute clearly regulates speech, not conduct, and does so by banning disfavored expression.”²⁰⁶ For the court, liability therefore turned merely on the content of the merchant’s speech used to describe effectively identical conduct. Responding to New York’s argument that *setting* price is speech but *communicating* price is conduct, Judge Rakoff stated, “Pricing is a routine subject of economic regulation, but the manner in which price information is conveyed to buyers is quintessentially expressive, and therefore protected by the First Amendment.”²⁰⁷

Additionally, the court determined that the statute was far broader than necessary and did not directly advance any interest in protecting consumers from deception.²⁰⁸ To the contrary “the statute actually perpetuates consumer confusion by preventing sellers from using the most effective means at their disposal to educate consumers about the true costs of credit card usage.”²⁰⁹ The defendants also could not justify the numerous exceptions to the law, like exempting the State of New York itself and exempting certain favored utilities from the law.²¹⁰ Finally, the no-surcharge law was far broader than necessary to serve any antifraud purpose, as New York could have simply limited the ban to only deceptive or misleading surcharges or passed a law similar to Minnesota’s, which permits surcharging only upon proper disclosure.²¹¹

While challenges involving commercial speech generally trigger intermediate scrutiny, courts apply the strictest scrutiny to vague laws when those vagaries implicate constitutional protections.²¹² A law can be void for vagueness under the Due Process Clause if it either (1) “fails to provide people of ordinary intelligence a reasonable opportunity to understand what conduct it prohibits,” or (2) “authorizes or even encourages arbitrary and discriminatory enforcement.”²¹³ The *Expressions* court cited *People v. Fulvio*,²¹⁴ in which a New York criminal court held that it was “intolerable” that a gasoline station operator who is careful enough to state that a lower

206. *Id.* at 444.

207. *Id.* at 445.

208. *Id.* at 446.

209. *Id.*

210. *Id.*

211. *Id.* at 447.

212. *Id.* at 448.

213. *Id.* (quoting *Hill v. Colorado*, 530 U.S. 703, 705 (2000)).

214. 517 N.Y.S.2d 1008, 1015 (N.Y. Crim. Ct. 1987).

price is a “discount for cash” “may enter his automobile at the end of his business day and drive home a free man,” but if a gas station operator or his employee simply describes a higher price as a “credit price,” “he faces the prospect of criminal conviction and possible imprisonment.”²¹⁵ Plaintiffs in *Expression* raised a simple yet significant question regarding state no-surcharge statutes: what can merchants lawfully tell their customers?²¹⁶ “If a customer asks us whether we charge more for paying with a credit card . . . should we ignore or dodge the question? Are we required to answer falsely?”²¹⁷ Recognizing the constitutional significance of these problems, and the fact that there is no effective difference between a surcharge and a discount, the *Expressions* court held that New York’s no-surcharge statute was void for vagueness.²¹⁸

The court also decided that merchants plausibly alleged that New York’s no-surcharge law violates the rule of reason.²¹⁹ This is because state no-surcharge bans like New York’s are “indistinguishable from the bans that Visa and MasterCard recently dropped from their retailer contracts as part of an antitrust settlement” and because of the dubiousness of consumer protection aims of no-surcharge rules.²²⁰

Expressions has nationwide significance because New York’s section 518 employs almost the exact same language as many other states’ no-surcharge statutes.²²¹ Indeed, after *Expressions*, merchants filed lawsuits in at least three other states (California, Texas, and Florida)²²² challenging the constitutionality of their no-surcharge statutes.²²³ Under virtually the exact analysis in *Expressions*, the Eastern District of California deemed

215. *Expressions*, 975 F. Supp. 2d at 448 (quoting *Fulvio*, 517 N.Y.S.2d at 1015).

216. Corrected Brief for Plaintiffs-Appellees at 53, *Expressions Hair Design v. Schneiderman*, No. 13-4533 (2d Cir. June 24, 2014).

217. *Id.*

218. *Expressions*, 975 F. Supp. 2d at 448.

219. *Id.* at 449.

220. *Id.*

221. *See Appendix I.*

222. *See Italian Colors Rest. v. Harris*, No. 2:14-cv-00604 (E.D. Cal. Mar. 5, 2014); *Dana’s R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Mar. 5, 2014); *Rowell v. Pettijohn*, No. 1:14-cv-00190 (W.D. Tex. Mar. 4, 2014).

223. Kelly Knaub, *Fla., Calif. Retailers Fight No-Surcharge Credit Card Laws*, LAW360 (Mar. 6, 2014), <http://www.law360.com/articles/515881/fla-calif-retailers-fight-no-surcharge-credit-card-laws>; Elizabeth Warmerdam, ‘Surcharge’ Bans Challenged in Three Major States, COURTHOUSE NEWS SERV. (Mar. 7, 2014), <http://www.courthousenews.com/2014/03/07/65915.htm>.

California's no-surcharge statute unconstitutional in *Italian Colors*.²²⁴ Contrary to these decisions, courts in Florida²²⁵ and Texas²²⁶ recently dismissed challenges to their no-surcharge statutes with prejudice.²²⁷ All of these cases were appealed to their respective circuit courts.²²⁸

Florida's no-surcharge law is very similar to New York's in that it imposes criminal liability on a merchant operating in violation of the statute.²²⁹ In a relatively brief²³⁰ district court order accepting the arguments rejected in New York, Judge Hinkle applied the rational-basis test and found Florida's no-surcharge statute constitutional because "the statute [was] within the Florida Legislature's broad discretion in regulating economic affairs."²³¹ Preventing "at least a small measure of bait and switch" that occurs when a merchant applies a surcharge at the point of sale was a "legitimate legislative goal."²³²

Judge Hinkle also rejected plaintiffs' void-for-vagueness arguments in *Dana's Railroad Supply*, supplying an unsettlingly brief analysis: "Nor have I overlooked the plaintiffs' assertion that the statute is impermissibly vague. It is not. The core of the statute is clear, and it clearly applies to the plaintiffs' pricing of their products."²³³

224. *Italian Colors Rest. v. Harris*, No. 2:14-CV-00604-MCE, 2015 WL 1405507 (E.D. Cal. Mar. 26, 2015).

225. *Dana's R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Mar. 5, 2014).

226. *Rowell v. Pettijohn*, No. 1:14-cv-00190 (W.D. Tex. Mar. 4, 2014).

227. Clerk's Judgment, *Dana's R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Mar. 5, 2014) (order entered September 2, 2014).

228. *Italian Colors Rest. v. Harris*, *appeal docketed*, No. 15-15873 (9th Cir. Apr. 30, 2015); *Rowell v. Pettijohn*, *appeal docketed*, No. 15-50168 (5th Cir. Feb. 26, 2015); *Dana's R.R. Supply v. Att'y Gen.*, *appeal docketed*, No. 14-14426 (11th Cir. Sept. 30, 2014); *Expressions Hair Design v. Schneiderman*, *appeal docketed*, No. 13-04537 (2d Cir. Dec. 03, 2013).

229. Compare FLA. STAT. ANN. § 501.0117(2) (2014) ("A person who violates the provisions of subsection (1) is guilty of a misdemeanor of the second degree.") with N.Y. GEN. BUS. LAW § 518 (McKinney 2015) ("Any seller who violates the provisions of this section shall be guilty of a misdemeanor punishable by a fine not to exceed five hundred dollars or a term of imprisonment up to one year, or both.").

230. Compare the six-page analysis of Florida's no-surcharge law in *Dana's Railroad Supply* with *Expressions Hair Design's* twenty-page analysis of New York's no-surcharge law or the seventeen-page analysis of California's law in *Italian Colors*.

231. Order Granting Summary Judgment at 2, *Dana's R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Aug. 2, 2014).

232. *Id.* at 3-4.

233. Order Granting Summary Judgment at 6, *Dana's R.R. Supply v. Bondi*, No. 4:14-cv-00134 (N.D. Fla. Aug. 2, 2014).

Similarly, the Western District of Texas “decline[d] to adopt or follow the *Expressions* court’s analysis and reasoning,” rejecting First Amendment application and applying the rational-basis test to determine that Texas’ no-surchARGE statute falls within state police power.²³⁴

2. *The Circuit Split Between the Second and Eleventh Circuits*

In late 2015, the Second Circuit vacated the district court’s decision in *Expressions* and determined that New York’s no-surchARGE statute did *not* violate the First Amendment’s free-speech guarantee and was not void for vagueness under the Due Process Clause.²³⁵ Rejecting plaintiffs’ First Amendment arguments, the court determined that the statute regulates conduct, not speech, and therefore free-speech guarantees were not implicated.²³⁶ The court cited precedent that affirmed the validity of price-control statutes which “necessarily prevent sellers from communicating certain (illegal) prices.”²³⁷ Thus, “If prohibiting certain prices does not implicate the First Amendment, it follows that prohibiting certain relationships between prices also does not implicate the First Amendment.”²³⁸ Concluding that section 518 simply regulates conduct (by banning the setting of a difference between a seller’s sticker price and the ultimate price that the seller charges credit-card customers), the court determined that the First Amendment free-speech guarantee was simply not implicated.²³⁹

Regarding plaintiffs’ void-for-vagueness arguments under the Due Process Clause, the court applied the strict rule that “a law is facially unconstitutional only if it is ‘impermissibly vague in all of its

234. Order Granting Motion to Dismiss at 6, *Rowell v. Pettijohn*, No. 1:14-cv-00190-LY (W.D. Tex. Feb. 4, 2015).

235. *Expressions Hair Design v. Schneiderman*, No. 13-4533, 2015 WL 5692296, at *1 (2d Cir. Sept. 29, 2015).

236. *Id.* at *8-10.

237. *Id.* at *8, 10; *see, e.g., Munn v. Illinois*, 94 U.S. 113, 125 (1876) (“[It] has been customary . . . in this country from its first colonization, to regulate ferries, common carriers, hackmen, bakers, millers, wharfingers, innkeepers, & c., and in so doing to fix a maximum of charge to be made for services rendered, accommodations furnished, and articles sold.”); *Nat’l Ass’n of Tobacco Outlets, Inc. v. City of Providence, R.I.*, 731 F.3d 71, 77 (1st Cir. 2013) (“[P]rice regulations and other forms of direct economic regulation do not implicate First Amendment concerns.”). *But cf. Rumsfeld v. Forum for Acad. & Institutional Rights, Inc.*, 547 U.S. 47, 66 (2006) (stating that laws that exclusively regulate conduct may nonetheless implicate the First Amendment in cases where the conduct at issue is “inherently expressive”).

238. *Expressions*, 2015 WL 5692296, at *9.

239. *Id.*

applications.”²⁴⁰ Given this rule, “‘If a statute has a core meaning that can reasonably be understood, then it may validly be applied to conduct within the core meaning, and the possibility of such a valid application necessarily means that the statute is not vague on its face.’”²⁴¹ Because New York enacted its no-surcharge ban to mirror the federal ban after the federal statute lapsed, and the lapsed federal no-surcharge statute had a clear core meaning, the court determined that New York’s no-surcharge statute had “a core meaning that can be reasonably understood”: sellers cannot post a single price for goods or services and then increase the price at the register by surcharging.²⁴²

The court indicated one way in which New York merchants might implement a surcharge while still complying with the statute. On its face, the statute only applies to single-sticker-price sellers. The court expressly abstained from deciding whether the statute violated the First Amendment guarantees of dual-sticker-price sellers.²⁴³ The court noted that at least under a Due Process void-for-vagueness analysis, the statute would “clearly” not prevent plaintiffs from imposing a dual-price regime if New York courts interpreted the state statute as identical to the lapsed federal statute.²⁴⁴ This is because the lapsed federal statute expressly defined the “regular price” to include both prices in a dual-pricing regime.²⁴⁵ No surcharge is imposed at the register, and therefore no violation of the statute has occurred. New York’s statute does not expressly define “regular price” as the federal statute did so the court declined to reach the issue on the merits, but the court noted that if New York courts interpreted the statute the same way or if the legislature clarified the definition as Congress did, merchants could implement dual-pricing regimes.²⁴⁶ Ultimately, the court vacated the lower opinion and determined that New York’s no-surcharge

240. *Id.* at *17 (emphasis added) (quoting *Vill. of Hoffman Estates v. Flipside, Hoffman Estates, Inc.*, 455 U.S. 489, 497 (1982)).

241. *Expressions*, 2015 WL 5692296, at *17 (quoting *Brache v. Westchester County*, 658 F.2d 47, 51 (2d Cir. 1981)).

242. *Id.*

243. *Id.*

244. *Id.* at *19.

245. *See* 15 U.S.C. § 1602(y) (2012) (“The term ‘regular price’ means the tag or posted price charged for the property or service if a single price is tagged or posted, or the price charged for the property or service when payment is made by use of an open-end credit plan or a credit card if either (1) no price is tagged or posted, or (2) two prices are tagged or posted, one of which is charged when payment is made by use of an open-end credit plan or a credit card and the other when payment is made by use of cash, check, or similar means.”)

246. *Expressions*, 2015 WL 5692296, at *17.

statute did not violate the First Amendment's free-speech guarantee and was not void for vagueness under the Due Process Clause.

Two months after the Second Circuit's opinion in *Expressions*, the Eleventh Circuit created a circuit split when it struck down Florida's no-surcharge law as "an unconstitutional abridgment of free speech."²⁴⁷ Rejecting Judge Hinkle's rational-basis analysis, the court undertook an analysis similar to that of the district court in *Expressions* to determine that the no-surcharge law regulated speech—not conduct—and therefore the rational-basis test did not apply.²⁴⁸ This was because, to the Eleventh Circuit, the statute did not prohibit dual-pricing, or charging different prices depending on the method of payment; it only prohibited merchants from *describing* the price difference as a "surcharge" instead of a "discount."²⁴⁹ "Calling § 501.0117 a 'no-surcharge law,' then, is something of a misnomer. The statute targets expression alone. More accurately, it should be a 'surcharges-are-fine-just-don't-call-them-that law.'"²⁵⁰

Like the district court in *Expressions*, the Eleventh Circuit posed an entertaining hypothetical to demonstrate the dubious difference between a "discount" and a "surcharge":

After all, what is a surcharge but a negative discount? If the same copy of Plato's *Republic* can be had for \$30 in cash or \$32 by credit card, absent any communication from the seller, does the customer incur a \$2 surcharge or does he receive a \$2 discount? Questions of metaphysics aside, there is no real-world difference between the two formulations. Accordingly, Florida's no-surcharge law is a restriction on speech, not a regulation of conduct.²⁵¹

The court then analyzed and rejected four purported state interests:

1. The purported interest advanced by the Attorney General—a generalized interest in "consumer protection."
2. The law may serve as an antifraud measure against bait-and-switch tactics, whereby a merchant advertises a lower price only to later charge a higher price.

247. *Dana's R.R. Supply v. Att'y Gen., Fla.*, No. 14-14426, 2015 WL 6725138, at *1 (11th Cir. Nov. 4, 2015).

248. *Id.* at *6.

249. *Id.* at *2.

250. *Id.* at *5.

251. *Id.* at *6.

3. The law may be viewed as a prophylactic measure that protects consumers against “unpleasant surprises” that do not rise to the level of fraud.
4. The law may be seen as leveling the playing field among merchants, some of whom may otherwise select a policy of assessing credit-card surcharges while others opt for cash discounts.²⁵²

To the Eleventh Circuit, the purported “consumer protection” interest was “formulated too abstractly to provide a meaningful benchmark for weighing the no-surcharge law against the State’s purported interest.”²⁵³ The remaining justifications were inadequate to support the burden of demonstrating that the statute advances any potentially substantial state interest or is narrowly tailored.²⁵⁴ These interests “would be better served by direct and focused regulation of actual pricing behavior.”²⁵⁵ The court ultimately determined that the no-surcharge statute was unconstitutional regardless of whether intermediate or strict scrutiny applied because no justification given or contemplated was sufficient to abridge merchant’s free speech.²⁵⁶

The dissent in the case makes clear, “The majority places our circuit in direct conflict with our sister circuit on this issue.”²⁵⁷ Other appeals are currently pending before the Fifth and Ninth Circuits on the constitutionality of no-surcharge laws in Texas and California.²⁵⁸ At its core, resolution of this split turns on whether these statutes implicate the First Amendment by unconstitutionally infringing on commercial-free speech or whether they merely regulate conduct. If the First Amendment

252. *Id.* at *9.

253. *Id.*

254. *Id.* at *10.

255. *Id.* (“Florida could simply prohibit dual-pricing altogether. Or it could cap the difference in price that can be charged to customers paying with cash and those using credit cards, just as it has done for the use of credit cards at state agencies and for the use of a ‘money transmitter service.’ Or it could ban specific false and deceptive trade practices, such as bait-and-switch tactics, as it does generally for acts of unfair competition under the State’s Deceptive and Unfair Trade Practices Act. Or it could require merchants to disclose to their customers the workings of their pricing policy.”) (citations omitted).

256. *Id.* at *2.

257. *Id.* at *13 (Carnes, C.J., dissenting).

258. *Rowell v. Pettijohn*, *appeal docketed*, No. 15-50168 (5th Cir. Feb. 26, 2015) (appealing district court’s finding that Texas’ no-surcharge law is constitutional); *Italian Colors Rest. v. Harris*, *appeal docketed*, No. 15-15873 (9th Cir. Apr. 30, 2015) (appealing district court’s finding that California’s no-surcharge law is unconstitutional).

applies, courts should clarify which level of scrutiny applies. Time will tell whether the Supreme Court will grant certiorari to decide these issues. The breadth, gravity, timeliness make the constitutionality of no-surcharge laws ripe for review, though the Court will likely wait until the issue percolates and the Fifth and Ninth Circuits decide their appeals. Given (1) the clear circuit split, (2) the number of merchants affected, (3) the number of citizens affected, (4) the billions of dollars in commerce that are implicated, (5) the number of states considering new no-surcharge laws, and (6) the recent contractual changes in the industry that now permit surcharging, Supreme Court review is imperative to finally resolve this area of the law.

3. Recently Proposed Legislation in Several States

In the wake of networks' no-surcharge policy changes, at least eighteen states have considered state no-surcharge bans.²⁵⁹ No-surcharge lobbying similar to that which occurred in the 1980s seems to be in full effect after Visa and MasterCard agreed to end their contractual no-surcharge prohibitions. Arkansas, Hawaii, Illinois, Indiana, Kentucky, Maryland, Michigan, Missouri, Nevada, New Jersey, New Mexico, Pennsylvania, Rhode Island, South Carolina, Tennessee, Utah, Vermont, and West Virginia all considered some kind of no-surcharge law from 2012 to 2013.²⁶⁰ Currently, Utah has been the only state to actually pass a recent no-surcharge statute.²⁶¹ Legislators decided, however, not to extend the law past its one-year sunset provision, so merchants may currently surcharge in Utah.²⁶² Legislators also expressly eliminated the no-surcharge prohibition in proposed legislation.²⁶³

C. Recent Industry Reform in Foreign Markets

The largest western countries have outpaced the United States with regard to merchant restraints and the regulation of the credit-card industry. The United States can observe the impact of industry reforms in foreign markets to determine not only whether reform is necessary, but also the

259. Wack, *supra* note 17.

260. See *Credit or Debit Card Interest, Surcharges, and Fees 2013 Legislation*, NAT'L CONF. OF ST. LEGISLATURES, <http://www.ncsl.org/research/financial-services-and-commerce/credit-or-debit-card-surcharges-2013-legis.aspx> (last visited Aug. 31, 2015).

261. See UTAH CODE ANN. § 13-38a-302 (West 1953) (repealed).

262. UTAH CODE ANN. § 63I-1-213 (2014).

263. H.B. 330, 2014 Gen. Sess. (Utah 2014), <http://le.utah.gov/~2014/bills/hbillint/hb0330.pdf> ("This bill[] repeals sections that prohibit a seller from imposing a surcharge on a transaction for \$10,000 or less that is paid for by using a credit card . . .").

efficacy and interplay between various reform measures. These observations foreshadow the potential impact on domestic reform.

1. Australia

Australia has seen the most dramatic developments in these areas²⁶⁴ and provides the “most complete experiment to date with regulating interchange fees.”²⁶⁵ After a 1998 law enabled the Reserve Bank of Australia (RBA) to regulate payment systems “in the public interest,” the RBA announced new rules designed to improve efficiency, transparency, and competition.²⁶⁶ One of the first reforms was the abolition of no-surcharge rules that networks imposed on merchants.²⁶⁷ These reforms also included RBA regulation of interchange fees, resulting in an estimated reduction of interchange fees in Australia by \$400 million (Australian) per year, or nearly 50%.²⁶⁸ In 2013, the RBA imposed further reforms improving surcharge-price signaling to customers and eliminating potential surcharge gouging by allowing networks to limit surcharges to “the reasonable cost of acceptance.”²⁶⁹ The reasonable cost of acceptance includes, but is not limited to, the merchant-discount fee paid to the merchant bank.²⁷⁰

A 2010 RBA study found that almost 30% of merchants now surcharge at least one of the credit cards they accept, up from around 8% just three years prior.²⁷¹ The study also found that almost half of consumers that hold a credit card now seek to avoid incurring a surcharge by using a different payment method.²⁷² This addresses concerns that even if permitted to

264. Pierre V.F. Bos, *International Scrutiny of Payment Card Systems*, 73 ANTITRUST L.J. 739, 739 (2006).

265. Todd J. Zywicki, *The Economics of Payment Card Interchange Fees and Limits of Regulation*, INT’L CTR. FOR L. & ECON., at iii (2010), http://www.laweconcenter.org/images/articles/zywicki_interchange.pdf.

266. Bos, *supra* note 264, at 739-40.

267. *Id.* at 740.

268. *Id.* at 741.

269. *Reforms to Payment Card Surcharging*, FED. RES. BANK AUSTL. (Mar. 18, 2013), <http://www.rba.gov.au/payments-system/surcharging/index.html>.

270. *Id.*

271. John Bagnall et al., *Strategic Review of Innovation in the Payments System: Results of the Reserve Bank of Australia’s 2010 Consumer Payments Use Study*, FED. RES. BANK AUSTL. 16 (June 2011), <http://www.rba.gov.au/publications/consultations/201106-strategic-review-innovation/results/pdf/201106-strategic-review-innovation-results.pdf>. Supermarkets and department stores did not tend to surcharge in 2010. *Id.* at 18.

272. *Id.* at 25.

surcharge, merchants would not choose to do so,²⁷³ and it also demonstrates that consumers will indeed elect alternative payment methods based on surcharges.

2. European Union

Merchants in the United Kingdom have had the freedom to surcharge credit-card transactions since a 1991 statutory instrument made contractual no-surcharge and no-discount rules illegal.²⁷⁴ In late 2014, the European Parliament entered into an agreement with the European Council to impose sweeping new regulations on the credit-card industry.²⁷⁵ The European Commission determined that consumers ultimately suffer by paying higher prices for transactions because of the “hidden” interchange fees that merchants are forced to pay but “[n]either retailers nor consumers can influence.”²⁷⁶ Instead of allowing networks to set interchange fees, the European Commission will now study and regulate interchange fees, abolish traditional “honor-all-cards” practices, and establish rules for greater transparency.²⁷⁷

These regulations were prompted by a 2007 European Commission decision against MasterCard that deemed its cross-border interchange fees an unfair violation of European Union Antitrust rules for “inflat[ing] the cost of card acceptance.”²⁷⁸ That decision was affirmed in 2014 by a

273. See, e.g., Steven Semeraro, *The Reverse-Robin-Hood-Cross-Subsidy Hypothesis: Do Credit Card Systems Tax the Poor and Reward the Rich?*, 40 RUTGERS L.J. 419, 436 (2009); Martha C. White, *A 4% Surcharge for Using a Credit Card?! Now Legal—but Not Likely*, TIME (Jan. 25, 2013), <http://business.time.com/2013/01/25/a-4-surcharge-for-using-a-credit-card-legal-but-not-likely/>.

274. Credit Cards (Price Discrimination) Order 1990, SI 1990/2159 (U.K.).

275. Press Release, European Comm’n, Commission Welcomes Political Agreement Reached by European Parliament and Council on Capping Inter-bank Fees for Card-based Payments (Dec. 17, 2014), http://europa.eu/rapid/press-release_STATEMENT-14-2767_en.htm [hereinafter Commission Welcomes Political Agreement].

276. *Id.*

277. *Id.*

278. Press Release, European Comm’n, Antitrust: Commission Prohibits MasterCard’s Intra-EEA Multilateral Interchange Fees (Dec. 19, 2007), http://europa.eu/rapid/press-release_IP-07-1959_en.htm?locale=fr [hereinafter Commission Prohibits MasterCard’s Fees].

Similarly, in 2005, the United Kingdom’s Office of Fair Trade conducted a lengthy inquiry into the practices of MasterCard UK, resulting in a decision that MasterCard UK’s interchange fees violated both the European Commission Treaty Article 81 and the Competition Act of 1998. See Press Release, Office of Fair Trading, MasterCard Agreement Anti-Competitive, Rules OFT (Sept. 6, 2005), <http://webarchive.nationalarchives.gov.uk/>

European Court of Justice judgment,²⁷⁹ and the announcement of reforms to the entire industry followed shortly thereafter. Not simply curative or retributive, the European regulation also contains a preventative component that removes much of the uncertainty around interchange fees in emerging areas like online, mobile, and person-to-person transactions to prepare the market for technological innovation.²⁸⁰

IV. Surcharging Credit-Card Transactions in the United States After Landmark Changes

Currently, merchants may surcharge credit cards at the point of sale without violating federal law. Merchants may also surcharge without being in violation of contractual obligations with Visa and MasterCard provided that they (1) provide Visa and MasterCard thirty days' notice that they intend to surcharge; (2) disclose the surcharge at the point of sale; and (3) disclose the surcharge on the customer's receipt.²⁸¹ A surcharge cannot exceed the actual cost of the merchant-discount fee, and Visa and MasterCard prohibit merchants from setting any fee above 4%, even if the actual cost of acceptance exceeds 4%.²⁸² Merchants are also able to surcharge Discover and American Express credit-card transactions.²⁸³ As of date of publication, merchants cannot surcharge in Colorado, Connecticut, Kansas, Massachusetts, New York, Oklahoma, or Texas pursuant to state no-surcharge statutes. The following sections discuss arguments for and against surcharging and consider possible legislative action that would

20131101202531/http://www.offt.gov.uk/news-and-updates/press/2005/168-05, *See also* Decision No. CA 98/05/05, Office of Fair Trading, Investigation of the Multilateral Interchange Fees Provided for in the UK Domestic Rules of MasterCard UK Members Forum Limited, Case No. CP/0090/00/S (Sept. 6, 2005), http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.offt.gov.uk/shared_offt/ca98_public_register/decisions/mastercard.pdf?jsessionid=6FF02D2689FA2A679783A2BA941602CF.

279. Case C-382/12 P, *Mastercard v. Comm'n*, E.C.J. (Sept. 11, 2014), <http://curia.europa.eu/juris/document/document.jsf?text=&docid=157521&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=3927>.

280. Commission Welcomes Political Agreement, *supra* note 275.

281. Settlement Agreement, *supra* note 12, ¶ 42(c).

282. *Merchant Surcharging Considerations and Requirements*, VISA USA, <https://usa.visa.com/dam/VCOM/download/merchants/surcharge-considerations-and-requirements.pdf> (last visited Oct. 28, 2015); *What Merchant Surcharge Rules Mean to You*, MASTERCARD, <https://www.mastercard.us/en-us/merchants/get-support/merchant-surcharge-rules.html> (last visited Oct. 17, 2015).

283. *See supra* notes 162-163 and accompanying text.

allow market forces to guide interchange fees while furthering consumer-protection objectives.

A. Arguments in Favor of Surcharging Credit-Card Transactions

1. Allowing Credit-Card Surcharging Will Reduce Consumer Indebtedness as Consumers Shift Purchases from Credit to Other Forms of Payment

The increase of consumer debt and bankruptcy filings “present[s] a new impetus to reexamine no-surcharge rules and their influence on consumer payment system choices.”²⁸⁴ Congress has recognized the negative effects of credit-card debt on individuals and the economy at large²⁸⁵ and has passed numerous pieces of legislation to reduce consumer debt and bankruptcies. These efforts include the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA),²⁸⁶ the Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009,²⁸⁷ and the Dodd-Frank Act of 2010.²⁸⁸ Commenting on consumer bankruptcy filing reforms under BAPCPA, Professor Charles J. Tabb noted, “[I]f Congress really wants to slow or even reverse the increase in bankruptcy filings, the real target should be the underlying cause—credit card debt—and not the bankruptcy law itself.”²⁸⁹ Signing the Dodd-Frank Act, President Obama called creditor practices “abusive” and noted that Americans often get “caught by hidden fees and penalties, or saddled with loans they can’t afford.”²⁹⁰ Senator Chris Dodd, the architect of the CARD Act, stated, “The whole business model of the credit card industry is not designed to extend credit but to induce mistakes and trap consumers into

284. Levitin, *supra* note 184, at 284.

285. *See, e.g.*, H.R. REP. NO. 111-88, at 10 (2009) (“The accumulation of large amounts of credit card debt can have profound implications on individual consumers and the economy more generally.”); S. REP. NO. 111-16, at 4 (2009).

286. Bankruptcy Abuse and Prevention Act of 2005, Pub. L. 109-8, 119 Stat. 23 (2005).

287. Credit Card Accountability Responsibility and Disclosure Act of 2009, Pub. L. No. 111-24, 123 Stat. 1734 (2009).

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

289. Charles J. Tabb, *Consumer Filings: Trends and Indicators* (pts. 1 & 2), 25 AM. BANKR. INST. J. 1, 1 (2006), 25 AM. BANKR. INST. J. 42, 100 (2007).

290. Press Release, The White House, Remarks by the President at Signing of Dodd-Frank Wall Street Reform and Consumer Protection Act (July 21, 2010), *reprinted in* 2010 U.S.C.C.A.N. S26, S27.

debt.”²⁹¹ Consumer credit-card debt leads to increased consumer credit defaults, increased bankruptcy filings, decreased savings, and decreased purchasing power from inflation.²⁹²

The CARD Act’s stated purpose was “to implement needed reforms and help protect consumers by prohibiting various unfair, misleading and deceptive practices in the credit card market.”²⁹³ Examples of protections include prohibiting creditors from unilaterally changing the terms of cardholder agreements governing outstanding balances,²⁹⁴ prohibiting increases in a cardholder’s interest rate for failing to make timely payments to a different creditor,²⁹⁵ and prohibiting creditors from charging multiple over-limit fees for multiple infractions within the same billing cycle.²⁹⁶

While these reforms largely provided debt relief at the credit-card-issuer level and reformed bankruptcy filings, controlling merchant restraints can ameliorate the problem at perhaps the most important level: the point of sale. This is achieved by discouraging credit card use in the first instance. “[A]vailable evidence suggests that consumers will likely respond to surcharges by using a less costly payment system.”²⁹⁷ For example, the 2010 study by the Reserve Bank of Australia found that almost half of consumers opted for a less expensive alternative when faced with a surcharge.²⁹⁸ After Australian credit industry reforms, “The rate of growth for credit card spending dropped to its lowest level since the RBA began gathering data in the early 1990s, while the rate of growth for debit card spending rose to its highest level since 1999.”²⁹⁹ A shift away from credit card use in favor of cash or debit card use to evade a surcharge can solve

291. 155 CONG. REC. SR5313, SR5314 (daily ed. May 11, 2009) (statement of Sen. Dodd).

292. See Levitin, *supra* note 1, at 43-51.

293. S. REP. NO. 111-16, at 2 (2009). *But see* RENUART & KEEST, *supra* note 76, § 2.3.2.3.2 (2011 Supp.) (“The CARD Act was designed to rein in some of these abuses, but already creditors are finding ways to circumvent the Act’s limitations.”).

294. 15 U.S.C. § 1666i-1(c)(1) (2012).

295. *Id.* § 1666i-1(a)-(b) (excluding defaults on other credit accounts as a reason for increasing interest rates, effectively ending prior “universal default” rules). See Mary Beth Matthews, *The Credit CARD Act of 2009—Four Years Later*, 2013 ARK. L. NOTES 1488, <http://media.law.uark.edu/arklawnotes/2013/08/23/the-credit-card-act-of-2009-four-years-later/>.

296. 15 U.S.C. § 1637(k)(7) (2012).

297. Mann, *supra* note 36, at 222 (analyzing how check surcharges at the point of sale in Norway led to increased debit card use as a cheaper alternative).

298. Discussed at *supra* Part III.C.1.

299. Levitin, *supra* note 1, at 52.

many of the problems associated with the overuse of credit cards, strengthening the economy in the process.

2. No-Surcharge Rules Create a Cross-Subsidy, Forcing the Poorest Americans to Subsidize Rewards Programs

No-surcharge rules do not allow credit-card users to internalize the higher rates merchants pay, preventing reward cards users from “pay[ing] their own way.”³⁰⁰ “Price coherence” shows that retail prices generally remain the same at a retail location regardless of the payment method used.³⁰¹ The only relief for merchants who cannot or will not absorb these fees from profits is to pass on the costs of credit-card-interchange fees to all consumers by raising prices across the board. “To the extent that credit cards are a high-cost payment method to merchants, then all consumers supply the funds that are collected by merchants and paid as interchange fees.”³⁰² The current arrangement creates a “cross-subsidy of credit card consumers by non-credit card consumers, and of reward-card consumers by consumers not using rewards cards.”³⁰³ Because the poorest Americans do not have access to high-reward credit cards and tend to be cash-only customers, this cross subsidy is highly regressive.³⁰⁴ “In its worst form, food stamp consumers are subsidizing first-class frequent flier upgrades.”³⁰⁵ Professor Steven Semeraro labels this occurrence as “The Reverse-Robin-Hood-Cross-Subsidy.”³⁰⁶

A recent Federal Reserve Bank of Boston policy paper notes that “[o]n average, each cash buyer pays \$149 to card users and each card buyer receives \$1,133 from cash users every year, a total transfer of \$1,282 from the average cash payer to the average card payer.”³⁰⁷ The Senate committee hearings recognized the cross-subsidy in advocating against a federal no-surcharge law when considering the Cash Discount Act.³⁰⁸ The committee

300. Levitin, *supra* note 54, at 1356.

301. Frankel & Shampine, *supra* note 9, at 632.

302. *Id.*

303. Levitin, *supra* note 9, at 1356.

304. Levitin, *supra* note 1, at 35.

305. Levitin, *supra* note 9, at 1356. *But see* Semeraro, *supra* note 273, at 419 (criticizing Professor Levitin’s empirical analysis based on gasoline merchants, but nonetheless agreeing that a cross-subsidy does exist).

306. *See* Semeraro, *supra* note 273.

307. Schuh et al., *supra* note 2, at 3.

308. S. REP. NO. 97-23, at 12 (1981) (comments of Comptroller of Currency Homan) (“Recent testimony before the subcommittee indicated the existing ban on surcharges has the

stated that allowing surcharges “would provide a mechanism by which cash customers could be relieved of subsidizing credit-card users.”³⁰⁹

3. Surcharges Are Procompetitive, Facilitating a More Efficient Economy

Surcharge prohibitions disincentivize competition among acquiring banks (and ultimately networks) from setting interchange fees as low as the market will tolerate. Most merchants clearly must accept cards, as card use surpassed check use by 2003 and cash use long before that.³¹⁰ With surcharges in place, banks and networks have an incentive to keep their merchant-discount fees low. This incentive is absent today because these fees are concealed from consumers and therefore insulated from the competition in a free market. Surcharging “allows market forces to operate on the previously invisible (to customers) array of interchange fees, and will exert downward pressure on those fees by injecting a form of competition the current rules have prohibited.”³¹¹ This can eventually lower prices as merchants pass the savings from the embedded costs onto the consumer. As Professor Schmalensee notes, “In the short run, if you drastically reduce interchange fees retailers will make more money,” but customers will see embedded cost savings “passed through in the long run.”³¹² In addition to lowering prices, surcharging can lead to job creation as merchants are either able to recover the fees they once paid by surcharging or are relieved of the surcharge altogether when a customer uses another payment method that is less costly to the merchant.

B. Arguments Against Credit-Card Surcharging

1. Consumers May Turn Away from Merchants That Impose a Surcharge

Consumers may withdraw from merchants who surcharge credit-card transactions that were once not only free, but also accrued reward points. When confronted with a surcharge at the point of sale, consumers may direct their disapproval toward the merchant than toward the credit-card

effect of subsidizing credit-card users at the expense of cash paying customers, many of whom are low- and moderate-income persons who may not qualify for open-end credit.”).

309. *Id.*

310. Mann, *supra* note 36, at 16 (citation omitted).

311. *In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 986 F. Supp. 2d 207, 231 (E.D.N.Y. 2013).

312. Daniel Fisher, *Wal-Mart's 'Swipe Fees' Are a Political Weapon Against Visa*, FORBES (July 2, 2012), <http://www.forbes.com/sites/danielfisher/2012/07/24/wal-marts-swipe-fees-are-a-political-weapon-against-visa/>.

company, as most consumers lack a comprehensive understanding of the intricate credit-card networks and payment systems.³¹³ Consider a market wherein Target elects to surcharge credit-card transactions, but Wal-Mart opts to absorb the fees as operational costs or embed the cost and increase prices across the board. Wal-Mart's action would conceal the fees from consumer disapproval, while Target's fees would be transparent.³¹⁴ Merchants clearly take a competitive risk when deciding whether to impose a surcharge.

The consumer withdrawal objection entails another objection—that merchants will refuse to surcharge even given the opportunity. “[T]oday’s retail landscape is hypercompetitive, so many stores will be hesitant to risk alienating customers by charging extra for using plastic.”³¹⁵ Research in foreign markets provides mixed results. An article weighing credit surcharges on American Express’s small business Open Forum warns that up to 90% of New Zealand customers would “rather leave the store than pay more due to a credit card surcharge.”³¹⁶ A public relations firm, however, performed this study, and its sponsor was unnamed.³¹⁷ On the other hand, the official study performed by the Reserve Bank of Australia concluded that consumers would not altogether abandon their purchase from a merchant when presented with a surcharge, but half of consumers would simply elect a different form of payment at the point of sale that does not incur a surcharge.³¹⁸

These objections rely on the assumption that their solution is the continuation of surcharge prohibitions. However, that a consumer elects with her dollars a non-surcharging merchant should not preclude *all* merchants’ *freedom* to surcharge if they so decide. Since the consumer protection aims of no-surcharge prohibitions have largely lost their validity,³¹⁹ deference should be given to the business judgment of

313. See Schuh et al., *supra* note 2.

314. Wal-Mart and Target have actually both vowed not to impose a surcharge/checkout fee. See Nadine DeNinno, *New Credit Card Transaction Fees: List Of States Charging 4% Surcharge ‘Checkout’ Fee*, INT’L BUS. TIMES (Jan. 1, 2013), <http://www.ibtimes.com/new-credit-card-transaction-fees-list-states-charging-4-surcharge-checkout-fee-1042384>.

315. White, *supra* note 273.

316. Henry Helgeson, *Charging a Credit Surcharge Will Cost You Customers*, AM. EXPRESS OPEN F. (Oct. 20, 2012), <https://www.americanexpress.com/us/small-business/openforum/articles/charging-a-credit-surcharge-will-cost-you-customers/>.

317. *Kiwis Resent Credit Card Charge – Survey*, ONE NEWS (Apr. 9, 2012), <http://tvnz.co.nz/business-news/kiwis-resent-credit-card-charge-survey-4821797>.

318. Bagnall et al., *supra* note 271.

319. See *supra* Part III.A and *infra* Part IV.B.3-4.

individual merchants, given their knowledge of the unique demands of their industry. This is especially true in a marketplace wherein merchants must accept cards in order to operate, but are forced to pay artificially inflated interchange fees that are insulated from market discipline. The current prohibitions particularly harm small-margin merchants like those running grocery or convenience stores. In practice, some merchants will surcharge and others will not, but the *ability* to surcharge itself provides merchants with a powerful tool to combat the high credit-card-interchange fees that are currently insulated from market discipline.

2. Consumers May Reduce Credit-Card Spending, Harming Merchants

Some estimates indicate that consumers spend more when using credit instead of cash—sometimes almost twice as much.³²⁰ Merchants have an interest in minimizing the effect of interchange fees, but the interest in increasing sales may trump the interest in minimizing interchange fees. A customer's decision to purchase one \$100 item with cash or two \$100 items on credit certainly informs a merchant's decision of whether to implement a surcharge policy or not. This point requires a deviation from the general, merchant-based justifications discussed thus far in favor of social welfare and market efficiency justifications, though there are tangential benefits to merchants.

Arguments in favor of increased consumer-credit spending, of course, require as a premise that consumer credit-card debt is a positive component of the economy—a premise that many reject.³²¹ To the extent that merchants suffer a decrease in sales as consumers shift from credit to debit or cash purchases, merchants enjoy a stronger and more efficient economy overall. The economy as a whole benefits by surcharging because it disincentivizes credit purchases in favor of debit or cash purchases thereby decreasing consumer indebtedness.³²² Numerous acts demonstrate that Congress places an emphasis on reducing consumer indebtedness for the benefit of the overall economy.³²³

320. White, *supra* note 273.

321. See, e.g., RENUART & KEEST, *supra* note 76, § 2.3.2.3.2.

322. *But see* Evans & Schmalensee, *supra* note 5, at 131 (arguing that social welfare criticisms “have not been well substantiated”).

323. See *supra* notes 285-288 and accompanying text.

3. *Surcharge Prohibitions Protect Against Consumer Confusion and Frustration*

The initial consumer protection ambitions that existed upon the enactment of no-surcharge statutes may exist as possible objections to surcharging today—namely, that “consumers cannot be lured into an establishment on the basis of ‘low, rock-bottom price’ only to find at the cash register that the price will be higher if a credit card is used.”³²⁴ However, a customer should be no more surprised at the register by a surcharge than she is when she proceeds to the register with a \$5 item, only to discover that there is a \$10 minimum for credit-card purchases, as the Dodd-Frank Act now permits.³²⁵

Additionally, as surcharging becomes more common, the consumer-protection aims that were intended to protect against price differentials at the point of sale will dissolve. As consumers become more aware of surcharges for credit-card transactions, there will no longer be any “surprise” at the register. Just as consumers have become conditioned to accept varying state and local taxes, varying minimum transaction price rules under the Durbin Amendment, or “convenience” and other fees permitted on online and telephone purchases, consumers will undoubtedly learn to anticipate the possibility of a surcharge when they elect a credit card over another form of payment.

Furthermore, many of the state statutes that prohibit surcharging allow surcharges for some transactions, such as when a governmental entity,³²⁶ university,³²⁷ or utility company³²⁸ processes a payment. If consumers are being protected from seeing a lower price initially only to be informed of a higher credit-card price at the point of sale, this protection would seem to be of equal concern regardless of whether the customer is transacting with their government, utility company, university, or in a merchant’s store. The Eleventh Circuit recently employed this reasoning when it found Florida’s no-surcharge law unconstitutional: “If customers would be harmed by learning that they faced *surcharges* but not *discounts* from private

324. S. REP. NO. 97-23, at 3-4 (1981).

325. See 15 U.S.C. § 1693o-2(b)(3)(A)-(B) (2012).

326. See, e.g., ME. REV. STAT. ANN. tit. 9-A, § 8-509 (2014); TEX. FIN. CODE ANN. § 339.001 (West 2013).

327. See, e.g., COLO. REV. STAT. § 24-19.5-103(3) (2014); FLA. STAT. ANN. § 501.0117(1) (West 2014); 14A OKLA. STAT. § 2-417(C) (Supp. 2014); 14A OKLA. STAT. § 2-211(E) (Supp. 2014).

328. See, e.g., CAL. CIV. CODE § 1748.1(f) (West 2006); ME. REV. STAT. ANN. tit. 9-A, § 8-509 (2014).

merchants, creating an exception allowing the State to impose *convenience fees* betrays the frailty of any potential state interests.³²⁹ One may even feel more aggrieved or “taken advantage of” when she finds that the credit-card price differential at checkout was imposed by her own government or university.

Some argue that a new stratum of consumer confusion would be created under a surcharge regime because “different cards will have different surcharges, . . . customers will have to keep track of not only which stores charge them but also how much using each card would set them back.”³³⁰ This is, however, procompetitive almost by definition, and the industry can expect to see “credit card promotions touting low- or no-surcharge transactions to become part of banks’ marketing mix, similar to what we’ve seen with the gradual rollback of foreign transaction fees on many new card offers.”³³¹

4. Merchants Will Take Advantage of Consumers by Surcharging in Excess of the Actual Cost of Acceptance

Finally, proponents of surcharge prohibitions argue merchants will set surcharges such that they exceed the actual cost of acceptance and extracting a windfall from consumers.³³² In a footnote in *Expressions*, the Second Circuit even referred to this occurring in Australia when it legalized surcharging, though this is the only footnote for which the court provided no authority.³³³

A review of the briefs submitted in that case reveals that these arguments originated in the brief of the Attorney General of New York.³³⁴ Citing Australian sources, appellant argued, “sellers in places that permit credit-card surcharges have frequently recouped more than the fair cost of credit-card services by imposing surcharges that far exceed the merchant-discount fees.”³³⁵ Critically, and apparently unnoticed by the Second Circuit was the fact that the sources cited for these propositions predate Australia’s 2013 fee-regulation reforms. As discussed in Part III.C.1 above, the RBA

329. Dana’s R.R. Supply v. Att’y Gen., Fla., No. 14-14426, 2015 WL 6725138, at *10 (11th Cir. Nov. 4, 2015).

330. White, *supra* note 273.

331. *Id.*

332. Expressions Hair Design v. Schneiderman, No. 13-4533, 2015 WL 5692296, at *2 (2d Cir. Sept. 29, 2015).

333. *Id.* at *2 n.2.

334. Corrected Brief for Appellant Schneiderman at 6-8, *Expressions*, No. 13-4533, 2014 WL 12593069 (2d Cir. Mar. 18, 2014).

335. *Id.* at 7.

imposed reforms that eliminated surcharge gouging by allowing networks to limit surcharges to “the reasonable cost of acceptance.”³³⁶ While some merchants in the past may have been free to set surcharges at any amount, any surcharge over the actual cost of acceptance would now put merchants in direct violation of their contracts with credit-card companies.³³⁷ Apart from being based on outdated sources, this objection hastily and unfairly assumes that merchants will breach their contracts.

V. Actions That Permit Surcharging While Furthering Consumer Protection Objectives

With contractual no-surcharge rules lifted in *In re Payment Card Interchange Fee* and other agreements, and with federal law no longer prohibiting credit-card surcharges, the only legal restraints for merchants wishing to impose a surcharge are state statutes. The fact that we have wholly inconsistent court decisions indicates that the courts offer merchants no uniform and absolute relief from interchange fees. This is understandable, as courts reiterate that their role is simply to adjudicate the constitutionality of state statutes like these, and that “The *wisdom* of the policy choices animating [them] is not for us to judge.”³³⁸ Accordingly, the following methods can protect consumers and merchants alike by permitting limited surcharging.

The most complete and efficacious solution requires congressional action. With the CARD Act, the Durbin Amendment to the Dodd-Frank Act, etc., Congress has made clear that it has the ability and often the duty to intervene in the credit-card industry on behalf of merchants and consumers. Accordingly, Congress could protect the ability of merchants to surcharge credit transactions much as it protected merchants’ ability to discount in the 1980s with the Cash Discount Act³³⁹ or merchants’ ability to set minimum prices under the Durbin Amendment.³⁴⁰ The United States should look to foreign markets that permit merchant surcharging for guidance. Many of these countries regard network-established-interchange fees as antitrust

336. *Reforms to Payment Card Surcharging*, *supra* note 269.

337. *See, e.g., Merchant Surcharging Considerations and Requirements*, *supra* note 282 (Visa) (“The surcharge must not exceed your cost of acceptance for the credit card.”); *What Merchant Surcharge Rules Mean to You*, *supra* note 282 (MasterCard) (“The level of the fee that a merchant may charge a cardholder is capped in relation to the merchant’s cost for MasterCard credit acceptance.”).

338. *Expressions*, 2015 WL 5692296, at *19 n.9 (emphasis added).

339. *See supra* Part III.A.

340. 15 U.S.C. § 1693o-2(b)(3)(A) (2012).

violations, even after the laws changed to protect merchants' freedom to surcharge.³⁴¹

For a true solution to the interchange-fee problem, the freedom to surcharge must operate in tandem with federal regulation of credit-card-interchange fees. Inquiries into the regulation of credit-card-interchange fees in foreign markets along with inquiries into domestic-market performance after debit-card-interchange-fee regulation can inform these decisions. Regulation of debit-card-interchange fees in the United States now occurs as part of the Durbin Amendment,³⁴² which demonstrates that regulation of credit-card-interchange fees is an achievable aim. A Federal Reserve Board Study found that while the average debit-card-interchange fee was \$0.44, it only costs \$0.10 or less to process the transaction.³⁴³ Recall that these fees were insulated from market forces, and not even the federal government could convince networks to negotiate lower fees.³⁴⁴ A 2013 study by economist Robert Shapiro found that debit-card-interchange-fee regulation under the Durbin Amendment "saved consumers and merchants an estimated \$8.5 billion in 2012," with \$5.87 billion, or around 70%, passed along to consumers in lower prices.³⁴⁵ These lower prices led to more consumption, and Shapiro estimates that this consumption, coupled with higher retained earnings, supported the creation of some 37,501 new jobs in the United States in 2012.³⁴⁶ Federal legislation should expressly limit any surcharge to "the reasonable cost of acceptance" and mandate proper disclosure to consumers.

In lieu of federal action, state legislatures could repeal their respective no-surcharge statutes given the anticompetitive and arguably unconstitutional nature of no-surcharge statutes. States could also follow Minnesota's lead and permit surcharging conditioned upon proper disclosure.³⁴⁷ Minnesota's no-surcharge statute properly balances consumer and merchant protections by requiring merchants who decide to surcharge to clearly disclose the surcharge to customers. Section 325G.051(a) of the Minnesota Statutes provides that a merchant can surcharge provided (1) the seller informs the purchaser of the

341. See, e.g., Commission Prohibits MasterCard's Fees, *supra* note 278.

342. 15 U.S.C. § 1693o-2(a)(8); 12 C.F.R. § 235.1 (2015).

343. 157 CONG. REC. 2020-01 (2011) (statement of Sen. Durbin).

344. See *supra* note 98 and accompanying text.

345. Shapiro, *supra* note 25. But see David S. Evans et al., *The Economics and Regulation of What Merchants Pay for Cards*, COMPETITION POL'Y INT'L 41 (2011), <https://www.competitionpolicyinternational.com/assets/Hot-Tubs/Interchange-Fees-web.pdf> (arguing that the Federal Reserve Board's regulation will likely harm consumers because networks will recover from consumers the lost merchant revenue in the form of fees and reduced services).

346. Shapiro, *supra* note 25.

347. See MINN. STAT. § 325G.051 (2012).

surcharge both orally at the time of sale and by a sign conspicuously posted on the seller's premises, and (2) the surcharge does not exceed 5% of the purchase price. This statute gives merchants the freedom to surcharge but ensures that customers are fully aware when making a purchase. This customer awareness, in turn, brings to the surface the once-hidden surcharges so that customers can decide whether to incur the fee or not, de-insulating the higher fees from market forces. Further, the ability to surcharge gives merchants some degree of leverage, perhaps collectively, in negotiating interchange fees and merchant-discount rates.

Conclusion

The clear trend among the major credit-card networks, even if influenced by court order or class-action settlement, is in favor of allowing merchants to surcharge the reasonable cost of acceptance and conditioning surcharges on proper disclosure. The largest foreign markets permit surcharging and regulate credit-card-interchange fees. Merchants should be empowered to use their business judgment to determine whether to pass along the high costs of credit-card payments to those using credit cards instead of spreading the cost among all customers or absorbing them from their own profits. The ultimate solution likely requires the regulation of credit-card-interchange fees similar to the current regulation of debit-card-interchange fees.

Consumer protection should not be achieved in this area by state regulation at the merchant-level through no-surcharge statutes. These statutes punish merchants, not credit-card companies, and force merchants to incur artificially inflated interchange fees that are insulated from free-market principles. Regulation of this area should focus on the practices of credit-card companies and banks, whose conduct has already been considered antitrust violations in the United States and internationally. "There is nothing wrong with fees charged for services provided, as long as those fees are transparent and are set in a competitive market environment. Don't tell me you are for a free market and then say but Visa and MasterCard can fix prices."³⁴⁸

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348. 157 CONG. REC. 2020-01 (2011) (statements of Sen. Durbin).

TABLE 1: STATE NO-SURCHARGE STATUTES
(Current Jan. 2015)

STATE	STATUTE	SURCHARGE	NOTES
California	CAL. CIV. CODE § 1748.1(a) (West 2006).	“No retailer in any sales, service, or lease transaction with a consumer may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check, or similar means.”	Permits utility company surcharging. Held unconstitutional and enforcement enjoined in <i>Italian Colors Rest. v. Harris</i> , No. 2:14-CV-00604-MCE, 2015 WL 1405507 (E.D. Cal. Mar. 26, 2015), <i>appeal filed</i> , Case No. 15-15873 (9th Cir. Filed Apr. 30, 2015).
Colorado	COLO. REV. STAT. § 5-2-212 (2014).	“[N]o seller or lessor in any sales or lease transaction or any company issuing credit or charge cards may impose a surcharge on a holder who elects to use a credit or charge card in lieu of payment by cash, check, or similar means.”	
Connecticut	CONN. GEN. STAT. § 42-133ff(a) (2013).	“No seller may impose a surcharge on a buyer who elects to use any method of payment, including, but not limited to, cash, check, credit card or electronic means, in any sales transaction.”	CONN. GEN. STAT. § 42-133ff(b) (2013) provides a statutory “Honor-all-cards” rule; CONN. GEN. STAT. § 42-133ff(d) (2013) permits a minimum credit-card purchase amount.
Florida	FLA. STAT. § 501.0117(1) (2014).	“A seller or lessor in a sales or lease transaction may not impose a surcharge on the buyer or lessee for electing to use a credit card in lieu of payment by cash, check, or similar means, if the seller or lessor accepts payment by credit card.”	Permits “convenience fee” for payments to an eligible college institution. Found unconstitutional in <i>Dana’s R.R. Supply v. Att’y Gen., Fla.</i> , No. 14-14426, 2015 WL 6725138 (11th Cir. Nov. 4, 2015).

STATE	STATUTE	SURCHARGE	NOTES
Kansas	KAN. STAT. ANN. § 16a-2-403 (West 2010).	“No seller or lessor in any sales or lease transaction or any credit or debit card issuer may impose a surcharge on a card holder who elects to use a credit or debit card in lieu of payment by cash, check or similar means.”	
Maine	ME. REV. STAT. ANN. tit. 9-A, § 8-509 (2014).	“A seller in a sales transaction may not impose a surcharge on a cardholder who elects to use a credit card or debit card in lieu of payment by cash, check or similar means.”	Permits a governmental entity to impose a surcharge.
Massachusetts	MASS. GEN. LAWS ch. 140D § 28A (2012).	“No seller in any sales transaction may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check or similar means.”	
Minnesota	MINN. STAT. § 325G.051(a)(1)-(2) (2012).	“A seller of goods or services may impose a surcharge on a purchaser who elects to use a credit card in lieu of payment by cash, check, or similar means, provided (1) the seller informs the purchaser of the surcharge both orally at the time of sale and by a sign conspicuously posted on the seller’s premises, and (2) the surcharge does not exceed five percent of the purchase price.”	
New York	N.Y. GEN. BUS. LAW § 518 (McKinney 1984).	“No seller in any sales transaction may impose a surcharge on a holder who elects to use a credit card in lieu of payment by cash, check, or similar means.”	Found constitutional in <i>Expressions Hair Design v. Schneiderman</i> , 803 F.3d 94 (2d Cir. 2015).

STATE	STATUTE	SURCHARGE	NOTES
Oklahoma	14A OKLA. STAT. § 2-417(a) (2014).	“No seller in any sales transaction may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check or similar means.”	
Oklahoma	14A OKLA. STAT. § 2-211 (2014).	“No seller in any sales transaction may impose a surcharge on a cardholder who elects an open-end credit card or debit-card account instead of paying by cash, check or similar means.”	
Puerto Rico	P.R. CODE LAWS tit. 10, §§ 11 (2008).	“No merchant shall impose a surcharge on a consumer who chooses to use a credit card instead of cash, check or any similar means of payment in any transaction that involves the sale or lease of products and services.”	
Texas	TEX. FIN. CODE ANN. § 339.001 (West 2013).	“In a sale of goods or services, a seller may not impose a surcharge on a buyer who uses a credit card for an extension of credit instead of cash, a check, or a similar means of payment.”	Held constitutional in <i>Rowell v. Pettijohn</i> , No. 1:14-cv-00190 (W.D. Tex. Mar. 4, 2014), <i>appeal docketed</i> , No. 15-50168 (5th Cir. Feb. 26, 2015).
Utah (Allowed to sunset)	UTAH CODE ANN. 1953 § 13-38a-302 (West 2010).	A seller may not impose a surcharge on a transaction for \$10,000 or less that is paid for by using a credit card.	Sunset Provision: UTAH CODE ANN. 1953 § 63I-1-213(2)(West 2015): Sections 13-38a-301 and 13-38a-302 are repealed June 30, 2014. Proposed Legislation repeals surcharge prohibition.