What the Age of Trump Means for Payments

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Generally, the prospects for overweening regulation and lawless intervention are dimmer, and that's a good thing.

A healthy and innovative financial-services and payments industry is vital for economic growth. Yet, for the last eight years, Washington's boot has been on its throat. It's been battered by the Card Act, Dodd-Frank (including the Durbin Amendment and the Consumer Financial Protection Bureau), Operation Choke Point, and an increasingly unchecked and lawless administrative state.

Despite the headwinds, a resilient payments industry has prospered and innovation flowered, particularly on the acceptance side of the network. But with less prescriptive and constrictive laws, and regulators narrowly tasked to implement and enforce the law, there would have been more growth, innovation, and value delivered to a broader spectrum of consumers and merchants.

The incoming Trump administration and 115th Congress could herald a sea change.

Before the election, Trump called for Dodd-Frank's repeal and decried excessive regulation of banks as the suppression of economic growth. His transition team declared the new administration will "dismantle" Dodd-Frank, noting it "does not work for working people."

This, of course, is true. And the statement is masterful political framing. Further, Trump's team said "bureaucratic and Washington mandates are not the answer"—not too thinly veiled criticism of the last eight years—and that they'll be replaced "with new policies to encourage economic growth and job creation."

Cautious Optimism

President Trump and the Republican Congress will attempt to make good on that pledge. Democrats will stonewall. And progressive heartthrob Sen. Elizabeth Warren will demagogue any and all efforts to roll back the regulatory chains on the financial-services industry. Nonetheless, there's cause for cautious optimism that the industry will be unshackled.

Treasury Secretary designate Steve Mnuchin promises "to strip back parts of Dodd-Frank," saying that it "will be the number-one priority on the regulation side." If, instead, former BB&T Co. chief executive and former chief executive and president of the libertarian Cato Institute John Allison or House Financial Services Committee chairman Jeb Hensarling were Treasury Secretary, either would use the position as a bully pulpit to push for gutting or repealing Dodd-Frank and reining in regulation of payments and financial services.

After meeting with Trump, Allison reported that, while the incoming administration wants to go further, Hensarling's Financial CHOICE Act is the baseline of financial regulatory reform Republicans will try to effect in 2017.

It would enable banks with sufficient capital to opt out of Dodd-Frank's most burdensome regulation, eliminate the Financial Stability Oversight Council and Title 2's backdoor politicized bailouts for too-big-to-fail banks, repeal the Durbin Amendment, end the rampant abuse of Operation Choke Point, and bring the unchecked and lawless Consumer Financial Protection Bureau to heel.

To pass the Financial CHOICE Act or pieces of it, Republicans will need a handful of Senate Democrats to overcome a filibuster. While in 2010 every Democratic senator but Russ Feingold voted for Dodd-Frank, some, perhaps many, can be persuaded to break ranks for its piecemeal dismantlement, if not the whole enchilada.

Few politicians of any stripe will cast high-profile votes decreasing their re-election prospects. In 2018, Senate Democrats face a daunting task. They'll be defending 25 seats, including 10 in states Trump carried. Trump carried West Virginia by 42 points, North Dakota by 36, Montana by 21, and Indiana and Missouri by 19. It's unlikely, therefore, that Democrat Sens. Joe Manchin, Heidi Heitkamp, Jon Tester, Joe Donnelly, and Claire

McCaskill, in particular, will want to tack too close to CFPB architect Warren or Senate Minority Leader Chuck Schumer.

Dumping Durbin

Most Congressmen would prefer to avoid a vote where they have to take sides between banks and merchants, which is the case with the effort to repeal the Durbin Amendment. However, if forced to vote, repealing Durbin's interchange price controls could attract Democrat support.

In 2011, Tester and McCaskill, along with Democrat Sens. Tom Carper, Chris Coons, Ben Nelson, Daniel Akaka, and Bill Nelson, co-sponsored a bill to defer implementing the Durbin Amendment pending a study of its effects. The 54 senators voting for it weren't enough to overcome a filibuster. Notably, however, they included Schumer, Manchin, and Democrat Sens. Mark Begich, Michael Bennet, Kirsten Gillibrand, and Mark Warner, and the bill's co-sponsors.

Durbin's price controls harmed the most important political constituency, consumers (voters). Debit interchange funds issuer innovation, including tax-advantaged health-care cards and reloadable prepaid cards with retail bank-account functionality, and expands availability of basic banking services for the disadvantaged.

Bankrate.com's 2009 survey reported 76% of banks offered free checking. By 2015, only 37% of banks surveyed offered free checking with no conditions. Thank Sen. Durbin for that. Increased fees and reduced benefits hurt debit card holders and pushed less affluent consumers—whom Democrats profess to be concerned about—out of the banking system.

Promoted as pro-consumer, repeal of Durbin should pass. Debit interchange would rise, fueling the return of free checking and rewards, issuer innovation, and perhaps decoupled debit. Debit-routing determination would revert to issuers, networks, acquirers, and merchants jockeying in the market, where those who influence payment share—Bank of America, Costco, and ultimately consumers—reign.

Regulatory Absolutism

In terms of an administrative state on steroids suppressing availability, innovation, and new entrants in financial services, the CFPB and director

Richard Cordray are ground zero. Before Congress moves to clip the CFPB's wings, President Trump is likely to ask for Cordray's resignation.

This fall, the D.C. Circuit Court of Appeals ruled the CFPB's structure unconstitutional and required that the President be able to fire its director at will. The Bureau, however, appealed the decision for an en banc review, putting at-will firing on hold. Cato's Thaya Brook Knight argues, nevertheless, that President Trump could act boldly and fire Cordray for cause, as the director has violated due process and been abusive in exercising the powers he was granted.

In 2017, or at the latest in 2018, there'll be a Trump-appointed CFPB director. He won't be as hostile to the industry or as cavalier in flouting the law as Cordray.

Notwithstanding the CFPB's failure to uncover Wells Fargo's fraudulent account-opening scandal, Democrats used the scandal to circle the wagons around the Bureau. Additionally, the Pied Piper of anti-bank rage, Elizabeth Warren, will put pressure on many members of Congress in their districts.

Still some Democrats should be receptive to replacing a Trump-appointed CFPB director with a bipartisan board. And, some should want to protect Congress's institutional power-of-the-purse prerogative, rather than having the Fed fund the Bureau.

Republicans must make the case the D.C. Circuit's decision made that the CFPB as constructed is unconstitutional, and further that the CFPB hurts consumers by suppressing availability and innovation in consumer financial services, and that Warren is no champion of the little guy. Rather, she and the CFPB believe enlightened Washington mandarins know best and that Joe and Sally Sixpack are not competent to manage their own affairs.

Just maybe, eight or more Senate Democrats will support curbing the CFPB because they want to keep their seats, don't believe in a paternalistic omnipotent administrative state directing financial-services markets and consumers' lives, or a bit of both.

Regulatory absolutism is an increasing menace to a healthy and innovative financial-services industry that is vital for economic growth, and the threat is epitomized by Operation Choke Point. Hensarling warns: "To wake up one morning and find out that your bank account, your access to funds have been choked off by an oppressive federal government, lawlessly, has to be stopped.”

Bullying Tactics

In March, 2013, the U.S. Department of Justice unveiled Operation Choke Point, a program ostensibly to curtail illegal activities by cutting off their access to banking and payments. But regulators, including the DoJ, Federal Deposit Insurance Corp., the Office of the Comptroller of the Currency, and New York State’s Department of Financial Services, have used it to bully banks and payment processors into not serving industries the regulators don’t approve of, notably payday lenders, gun dealers, coal producers, pawnbrokers, and tobacco retailers.

Trump’s cabinet appointments matter. Attorney General-designate Jeff Sessions is not Loretta Lynch or Eric Holder. He won’t countenance lawless intimidation of banks and processors into not serving politically out-of-favor industries.

There’s a move for a legislative fix. Congressman Blaine Luetkemeyer’s Financial Institution Customer Protection Act would prohibit regulators from preventing banks and payment processors from refusing to serve businesses based solely on reputational risk. It would also ban agencies from using their subpoena power on fishing expeditions. It passed 250-169. Ten Democrats voted for it.

Senators Cruz and Lee introduced a companion bill in the Senate which went nowhere. Luetkemeyer’s remedy is included in the Financial CHOICE Act.

A Deep Moat

Dodd-Frank and the reign of Washington regulators created a deep moat around large established firms, deterring bank, fintech, and payments startups. That’s not good for anybody except regulators and perhaps giant incumbents.

Still, there’s a good chance that, in 2017, U.S. retail payment networks will revert to being less regulated, payment processors will be free to serve legal businesses, and—so long as they disclose the material facts about their products and aren’t deceptive—financial-services providers will succeed or fail based on whether enough consumers see value in and buy their products, rather than on whether Washington regulators bless them.

Meanwhile, the payments and financial-services industry should be four-square for gutting Dodd-Frank, repealing the Durbin Amendment, and reining in the CFPB and regulatory absolutism.

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