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Signature Debit Not Going Away Soon, says Auriemma Consulting Group

NEW YORK, N.Y. Two years of massive overhaul of the payments industry came to a head on July 21, 2010 with the passage of the **Wall Street Reform and Consumer Protection Act**, popularly known as Dodd-Frank. As with the CARD Act of 2009 which preceded it, media attention focused primarily on credit cards, where issuers are now in the throes of implementation and retrenchment.

Meanwhile, debit card sales volume now outstrips credit cards and the gap is widening, even as issuers wait nervously for the second shoe to drop. The Durbin Amendment to Dodd-Frank gave the Fed 9 months to decide on “reasonable and proportionate” rates for debit card interchange. Banks are already facing a steep reduction in overdraft fees with the new opt-in requirement, and while no one knows until April of 2011 just what interchange rates will be, no one doubts the direction: down

At stake are millions of dollars riding on issues that are largely invisible to the consumer. Most shoppers who use debit cards know that they sometimes sign to authorize a purchase, sometimes enter a PIN, and don’t care which one they use as long as it works. But this distinction between signature and PIN authorization was such a major issue to Wal-Mart that it spent six years in court as the leader of a multi-billion dollar class-action lawsuit, ultimately winning in 2003 the right to reject signature debit in its stores.

How will the latest round of legislation and regulation affect this bone of contention between issuers and merchants? Some observers are predicting that the Durbin amendment will mean the end of signature debit, arguing that signature owes its dominant market position to the higher revenues it generates for the issuer (at the retailers’ expense, claim merchant coalitions). Reduce the price gap between the two, they reason, and PIN should become dominant by virtue of its lower incidence of fraud. But according to Auriemma Consulting Group (ACG, a management consulting firm serving the payments and lending industries), such predictions are too simplistic.

“The first mistake is thinking that all retailers embrace PIN debit,” says Ed Lawrence, Director at New York-based ACG. Certainly Wal-Mart, and a few other big players have exercised the ability they won in 2003 to accept only PIN-based debit. “But how many other stores stopped allowing customers to use signature debit altogether? Not many.”

Signature debit utilizes the same POS infrastructure and procedures as credit cards, Lawrence points out. “Customers are familiar with the process, there’s no extra training for cashiers, and critically, no extra hardware to buy.” The price gap between the two methods has narrowed in the last seven years, he noted, and the Fed’s actions may bring them to near-parity.

“The new laws will accelerate retailers’ use of software that automatically routes the transaction along the cheapest route,” says Lawrence. “Processing and interchange rates are already very complex, and likely to become more so. The simple distinction between PIN and signature that was so important ten years ago may cease to matter, especially as new technologies like contactless cards continue to grow.”

About Auriemma Consulting Group

Auriemma Consulting Group (ACG) is a full-service management consulting firm serving the payments and lending industries since 1984. Cardbeat® is ACG’s syndicated market research study of credit card holders, conducted monthly in the U.S. and quarterly in the U.K. With offices in New York and London, ACG consultants are experienced practitioners, drawn from the credit card, private label, auto finance, mortgage, and retail banking industries that we serve. For more information, contact Ed Lawrence at 212-323-7000 or ed.lawrence@acg.net.