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STATE OF MICHIGAN
OFFICE OF FINANCIAL AND INSURANCE REGULATION
DEPARTMENT OF ENERGY, LABOR & ECONOMIC GROWTH
STEVEN H. HILFINGER, DIRECTOR

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COMMISSIONER

March 29, 2011

The Honorable Ben S. Bernanke, Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington DC 20551

Subject: Debit Interchange Transaction Fees

Dear Chairman Bernanke:

I am requesting the Federal Reserve Board reconsider its approach in implementing debit interchange fee rules pursuant to Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act). Despite congressional intent to exempt institutions under \$10 billion, which includes over 450 banks and credit unions headquartered in Michigan, questions remain regarding the potential adverse impacts of the proposed rule. Further, the Dodd-Frank Act requires rule implementation meant to establish standards for assessing whether the amount of any interchange fee is "reasonable and proportional to the cost incurred by the issuer." It does not mandate the setting of a specific fee limit.

Michigan's depository institutions have been operating in a stressed economic environment for a prolonged period of time that predates the national recession by several years. The cumulative impact has been most pronounced during the past two years. Since October 2008, eleven banks have been closed in Michigan due to safety and soundness concerns, with the state's economic stressors playing an integral role in each case. Only eight banks were closed in Michigan during the preceding 38 years.

The economic difficulties faced by our institutions have reduced the number of state-chartered depository institutions not only via closures but also as a result of mergers necessitated by stressed financial condition. Since December 2008, the number of state-chartered banks and credit unions has declined nearly 13 percent from 352 to 307 total charters, with the vast majority of this reduction driven by viability concerns.

The interdependence between economic conditions and lending institutions is clearly evident. Economic hardships over the past few years, notably high unemployment, left many borrowers unable to repay loans. Loan defaults, coupled with significant declines in real estate values, produced significant related expenses for Michigan's banks and credit unions. These expenses all too often led to net operating losses for our institutions, which eroded capital and, in some

cases, forced mergers and closures. Many Michigan institutions have had to curtail lending to shore up capital ratios and liquidity in order to weather the storm.

Michigan's economy remains distressed but improvements are evident. Unemployment is on a downward trend, with recent data revealing a rate of 10.4% versus a high 14.1% reported in September 2009. Building permits are up, reversing a declining trend. The pace of reductions in real estate values has slowed.

Now is an untoward time to place an additional burden on community banks and credit unions, which largely didn't cause the problems sought to be addressed by the Dodd-Frank Act. Asset quality indicators generally reveal stable to improving trends for the industry, and 65 percent of Michigan banks reported earnings gains for 2010 versus 2009. However, on aggregate, Michigan's depository institutions continued to report a net loss for 2010.

While stability appears upon us, recovery for Michigan is fragile. Any additional earnings pressure on our banks and credit unions – including reduced ability to recoup interchange-related expenses – will undoubtedly have a negative effect on capital levels. The net result of lower capital at our institutions is necessarily less lending.

I am concerned the proposed rule will further hinder efforts to extract ourselves from the financial malaise of which we've been working our way out.

Therefore, I urge you to seek congressional authority to delay implementation of the final rule until a comprehensive evaluation of its impact on the industry can be completed and fully considered.

Sincerely,

A handwritten signature in black ink, appearing to be 'K. Ross', with a long horizontal flourish extending to the right.

Ken Ross
Commissioner