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Subject: Reg I I - Debit card Interchange

Comments:

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Proposal: Regulation II - Debit Card Interchange Fees and Routing
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Comments:
I am very puzzled and perplexed by the consideration of the interchange price fixing plan that is being proposed. I work directly with our debit card program at our institution, and have since we implemented our very first program back in 1997. It is my belief that in giving thought to the current interchange rates being assessed to debit card transactions, the merchants and others who are in favor of the proposal are only taking one factor into consideration.the merchants cost per transaction and nothing else, when there are many other factors to evaluate. I understand that business owners have to be concerned with their expenses in order to be profitable, but I think the business owner has a false impression of interchange fees and why they are paying them. I believe they are under the assumption that the fee they pay is associated with solely routing their customer's transaction to complete the sale. I have spoke with 2 small business owners, just recently who have a very shallow interpretation of debit card programs due to their lack of knowledge of card issuance, transaction processing, and liability for un-authorized or fraudulent activity that could take place with a debit card account. I am very sure that they are not concerned with these factors, or applying this information to the current issue surrounding interchange rates, but I do believe that some basic comprehension is warranted to justify the issuer's cause for debate. Issuers of debit cards front the cost of providing and processing the plastic for the consumer to present for payment, which gets more expensive for the card issuer as time passes. Currently the processing expense for one card for a consumer is approximately $7.85. The issuer also incurs fees not only to "house" these issued card records, but to also maintain them and keep the records current in usually 2 to 3 databases. There are significant fees to the issuing bank to implement these databases, provide training on them, and to maintain them. Card issuers also absorb transaction routing and processing fees with each and every debit card transaction that is not only approved, but those that are denied as well. This would also include

transactions from the result of returned merchandise, and or goods and services, and for cash advances that are requested by the cardholder. If the transaction is a signature base POS transaction, there is an expense not only for the debit advice, (the transaction that debits the consumer's account) but also for the authorization transaction that guarantees these funds from the customer's account to the merchant. These two fees alone account for over half of the proposed .12 interchange fee cap per transaction. These fees are not just assessed by one entity involved with the approval, routing and settlement process but are more than likely, assessed by several entities such as Visa or MasterCard, a network "switch" and also a network processor. These fees do not include any annual, membership, or any other miscellaneous fees that may be charged by these entities for participation into their network. I would also like to comment on the liability that the issuers sustain for unauthorized activity that could be performed with a debit card. In most instances of fraudulent activity, the card issuer is responsible for the loss while at the same time the merchant is still guaranteed their payment, and is the party accepting the card for payment. So, although the merchant might suspect fraud in accepting the card for payment to secure the sale, they still don't have to concern themselves with a loss.the loss will still shift to the issuer if in fact, the accepted transaction is fraudulent. Let's give some consideration to some very common types of fraud. Our network reported in their research pertaining to debit card fraud, that counterfeit card fraud accounted for 35% of the fraudulent activity that occurred in 2010. Who becomes liable when transactions occur on a consumers account when this type of fraud occurs? The merchant is only required to check the back panel of a card plastic for a signature when accepting a debit card for payment. The merchant is not required to compare the signature with a signature on another form of ID provided by the consumer, doesn't have to match the signature with the embossed name on the front of the card, the signature doesn't even have to be legible for that matter. The signature panel just has to contain a signature in order for the merchant to accept the card for payment. If the accepted card is in fact a counterfeit card, the issuer becomes liable for the fraudulent activity. The only recourse that the issuer has if this type of fraud occurs on a cardholder's account, is to recover the counterfeit plastic and check the signature panel for a signature. If the signature is missing from the panel, then it's possible that the issuer can charge the transaction back to the merchant,
but nt without incurring fees for initiating the dispute of course. The chances of a counterfeit card plastic being recovered and routed back to a card issuer is slim to none. In fact, in the 14 years that we have supported a debit card program, we have received only one counterfeit card back that was used to commit fraud on one of our cardholder's accounts. The card was forwarded to us 11 months after the fraudulent activity occurred which exceeds the timeframe card issuers are given to dispute this type of activity. Most counterfeit card plastics that are created are the result of skimming devices that are sometimes attached to a merchant's electronic terminal that card plastics are swiped through for payment. Although it would seem reasonable that the merchants should be responsible for the inspection and security of their equipment, and liable for the fraudulent activity that could result from one of these devices being adhered to their terminals, they incur no loss for the
fraudulent transaction activity resulting from an event involving a skimming device. The loss resulting from this event is taken by the card issuer. Let's not also forget the violations of the Payment Card Industry's Data Security Standards that some of the merchants have been found in violation of in securing their databases and in the unnecessary retention of card account

information for extended periods of time. These violations have proved to be detrimental to issuers. Card issuers have sustained millions of dollars in losses from fraudulent transactions that have resulted from these data base breaches, not to mention their costs in statusing the compromised cards to protect their cardholder's accounts, and the costs associated with re-issuing these compromised card accounts. Card issuers also implement expensive fraud prevention tools and monitoring systems in their constant battle to mitigate fraudulent activity from occurring on their cardholder's accounts. I would also
like to take this opportunity to mention that the latest articles I have read on the topic of debit card fraud indicates that individuals, and groups engaged in this type of activity will be targeting US cardholder accounts now more than ever due to other countries implementing the EMV security feature that is embedded into the card plastic. This technology has not yet migrated to the United States. Experts in the field of debit card fraud and security are predicting that US card issuers could see a very evident increase in fraudulent activity on their cardholder's accounts due to the non-implementation of this new security feature which cannot be duplicated, unlike the current magnetic stripe that is placed onto the back of a card plastic. While countries who have rolled out this new technology has seen a drop of 46% in debit card fraud, debit card fraud in the United States continues to rise. These articles have indicated that it is far easier for fraudsters to shift their
operations to areas not protected by EMV technology rather than to make an attempt to compromise it. This theory was further emphasized by one of the Executive Vice Presidents of one of our Federal Reserve Banks in the United States. "We may become the only substantial economic power dependent on a payments standard that is less secure than that of the rest of the world. That means that criminals, with the intent of profiting from card fraud, will continue to migrate to the United States." Regulation E provides protection to the consumer in the event that fraudulent activity occurs on a debit card that becomes lost or stolen and limits the consumer's liability to 500.00. The amount of loss the cardholder takes depends on when they report a loss or theft of a card to their issuer. While most debit card fraud takes place within the first 24 to 48 hours from the time a card, or card account information is recovered by an unauthorized individual(s), Regulation E caps the consumer's liability at only 50.00 if the cardholder reports the loss or theft of their card to their issuer within a two business day time frame. The rest of the liability for the fraudulent activity falls onto the issuer. MasterCard and Visa both have 0 liability policies to the consumer in the event that un-authorized transactions post to a consumer's account. MasterCard's 0 liability clause does implement 3 provisions into their policy for this policy to be effective. Otherwise, all liability for un-authorized transactions shifts to the card issuer. It is my opinion then, that due to the extreme liabilities that the card issuers absorb, the card issuers are entitled to compensation for taking these risks and for sustaining the losses from fraudulent activity. These points should drive the current interchange rates home to those who might think that the current rates are not "reasonable or proportional" to the transaction costs incurred by the issuer. Let's now consider the proposed
.12 cap per tansaction. Is that rate "reasonable and proportional" to the issuers overall expense, (and let's not forget to consider the risk and liability that goes along with being an issuer of debit cards), in offering a debit card program to their customers and making it feasible and somewhat profitable? My point being.is that there is much more to be evaluated and reviewed from a card issuers stand point in determining a fixed and fair interchange rate for debit card transactions that is being grossly

overlooked. I am confident that the proposed cap of .12 per transaction, will undoubtedly drive up costs for consumers who use debit cards as their preferred choice of payment options, and card issuers may even have to consider eliminating these programs altogether. If the proposed interchange rate results in the elimination of debit card programs, consumers who have become accustomed and dependent on the use of debit cards will not understand and will become frustrated with the
issuer. This could mean not only potential losses in revenue for the card issuer, but the loss of the relationship with the consumer altogether to other entities that find favor with the proposed interchange rates. My last statement drives me to elaborate on my standpoint on this issue from a consumer's point of view. Nothing frustrates me more as a consumer than being "swayed" by a merchant to use one form of payment over another. I am the customer and that should entitle me to choose the form of payment which is most advantageous and convenient for me. In a few instances over the last several months, I have found myself being pressured by a merchant to use a check or cash instead of my debit card. When I reflect on these incidents, I as a consumer have come to the conclusion that those particular merchants were only concerned with what was in their best interest at the time, other than what was in mine as their customer. Has the role playing reversed from customer satisfaction to merchant satisfaction? The merchant that is pressuring their customer to pay with something other than a debit card when they are presented with one, are only frustrating and embarrassing their customers, run the risk of losing the sale due to the fact that their customer has no other form of payment to offer the merchant, and are deterring that customer from doing business with them in the future because of the merchant's reluctance to honor the customer's debit card for payment. Debit cards have become the consumer's choice of payment options. Checks can be expensive and inconvenient for the consumer, and it can be not only risky, but also dangerous for a consumer to carry cash. With the popularity of shopping online and our growing electronic payment system, many merchants and service providers are requiring a debit card for payment and consumers are considering debit cards a "must have" in managing their daily financial affairs. Debit card acceptance by the merchant benefits them in many ways. They are not only guaranteed their funds, but they also eliminate their risk in accepting a fraudulent, or an insufficient item for payment. The merchant can push big ticket items and can increase their sales without worrying about, or questioning the availability of funds unlike if they had been presented with a check for the same item. This is turn, saves them time and the expense that they would incur in the collection of unavailable funds, and no relationship with a collections provider is needed to help them to collect funds from these items. Their risk and liability for fraudulent and un-authorized activity is very minimal. These beneficial factors alone have to be of some value to the merchant. Paying with a debit card is faster and more convenient for both the consumer and the merchant. The merchant can move customers through their checkout process faster and customer satisfaction and convenience means repeated business activity. Processing returns becomes less complicated for the merchant, and less cash can be kept on hand as reimbursement for returned merchandise can be processed by crediting the debit card account the merchandise was originally purchased with. The merchant is under no requirement to request an ID when presented with a debit card, nor do they have to check a database for derogatory payment history. Their only requirement is checking the back panel of the card for a signature. Acceptance also saves them the time it takes to process items for daily deposits, and the number of trips to their financial institution to deposit paper items and cash to their business accounts are greatly reduced. The 10 billion dollar asset rule that is being proposed, and Visa's proposed two

tiered system segregating large and small issuers will not protect consumers who prefer to use their debit card issued to them by their community bank. The large retailers will take control over what networks they route their transactions through, anwill inevitably route their debit card transactions through the least expensive networks thereby avoiding Visa's two tiered system. Large retailers will also discriminate against small card issuers and their cardholders by swaying these cardholders to use cards that are issued by large financial institutions. In the end, the large retailers will benefit from maximizing their profits and minimizing their costs at the consumer's expense. The consumer will undoubtedly have to pay fees that they have never had to pay before to use their debit card, or their community bank will have to eliminate issuing debit cards altogether due to their expense in supporting a debit card program. The proposed .12 per transaction cap eliminates the opportunity for these programs to be in any way profitable for community banks. Large retailers will be the ones to reap the benefits of the proposed interchange rates. But in my opinion, they should be careful of what they wish for. The cardholders of community banks will hold their bank responsible for the implementation of fees assessed to debit cards not knowing or comprehending why their issuer has suddenly started to charge fees for usage. It's very possible that the cardholder will form the impression that the banks are charging new fees to increase their own profits. This change will impair our community banks and will compromise, or could even possibly dissolve the relationships that they work so hard to build with their customers. In conclusion, I truly value the opportunity to voice my opinion regarding this issue as a supporter of our community banks, and as a consumer who utilizes a debit card daily. It is my sincere hope that the content of this letter will help to warrant some consideration from the stand point of our community banks pertaining to this issue. It is also my hope that before any final revisions are implemented to the existing debit card interchange rates, that much more discussion, evaluating and research is completed to ensure that debit card interchange rates are reasonable, proportionate and fair to the small community banks and the customers they serve. Sincerely, Jennifer J. Wingerter Buena Vista National Bank