Credit Union
ASSOCIATION
New York

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W., Washington, DC 20551
Docket No. R-1404

INTERCHANGE FEE CAP PROPOSAL

February 17, 2011

Dear Secretary Johnson;

On behalf of the Credit Union Association of New York, I would like to take this opportunity to comment on the Federal Reserve's proposed regulations implementing section 1075 of the Dodd Frank Wall Street Financial Reform Act of 2010. The Federal Reserve is, of course, obligated to promulgate regulations consistent with the relevant statutory provision. Unfortunately, in drafting these regulations, the Federal Reserve gave too little regard to the intent of the statute's drafters to minimize the impact of this legislation on credit unions and banks that have less than $10 billion in assets. Consequently, without substantial amendments and additions to this proposal, the proposed regulations will have a devastating impact on the ability of many New York credit unions to provide debit cards to their members.

The most important change the Federal Reserve should make to these proposed regulations, both in order to both fully implement the intent of the statue and insure adequate protection for small institutions such as credit unions, is to mandate that debit card networks provide interchange fees to institutions above the cap mandated for larger banks . The statute explicitly exempts institutions with less than $10 billion dollars in assets from the interchange cap (Section 1075(6) (A)). In addition, Senator Durbin, the chief sponsor of this legislation, has reiterated on the senate floor that the interchange cap is not intended to effect small banks and credit unions, indicating that it may violate the antitrust law for debit card networks to make credit unions subject to the interchange fee cap.(Congressional Record: December 22, 2010 S10995-S10997).

The Federal Reserve takes no steps to ensure that the provision is actually followed by debit card networks. There is nothing in this regulation preventing networks from simply making institutions with less than $10 billion subject to the same interchange cap schedule as larger institutions. Furthermore, even if networks exempt these institutions from interchange caps today, there is nothing preventing them from imposing interchange caps in the future. This eventuality can simply be avoided by mandating that debit card networks provide interchange fees to institutions of $10 billion dollars or less at a higher rate then those institutions subject to the cap.

The second major part of the statute, which applies to all financial institutions issuing debit cards, is a requirement that issuers provide merchants with at least two unaffiliated networks for processing debit charges. Nothing in the statue speaks to, let alone requires, two processing networks to be made available for each type of debit transaction service.

Consequently, there is nothing supporting the suggestion that credit union and bank issuers that provide both signature and PIN based debit transactions should have to obtain two networks for each type of payment process. In addition to the lack of statutory support for this suggestion, the Federal Reserve should consider the cost and time involved in contracting with additional networks. It will take most credit unions a minimum of 6 months to contract with additional providers and they will have to pay fees for each additional network.

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Even if credit unions are excluded -- in fact as well as in theory -- from the interchange fee cap, the amount at which these caps are set is sure to have an indirect impact on the interchange remuneration provided to credit unions. Consequently, there are other parts of this proposed regulation on which I wish to comment.

Most importantly, in proposing to implement the interchange cap, the Federal Reserve has proposed two options, only one of which is to be adopted. The first option would establish institution- specific interchange fees, based on the average daily usage of a given bank so long as such fees do not exceed 12 cents ($0.12). The second proposal is a 12 cent ($0.12) cap on all interchange transactions. Given the complexity of the first option, credit unions would favor a 12 cent fee for each debit card transaction. However, the proposed caps do not reflect the actual cost and expenses of interchange transactions.

Finally, the statute provides for the interchange cap to be adjusted to account for the cost of fraud. As currently drafted the Federal Reserve is interpreting its flexibility under the statute too narrowly. There are many expenses which have to be considered in order to get a full grasp on the cost associated with a fraudulent transaction, ranging from increased insurance costs to increased staff oversight of account activity to the time spent investigating fraud related claims.

The statue may very well have a devastating impact on the ability of credit unions across New York State to continue to provide debit card services to our members. The Association will continue to work with credit unions to amend the Dodd-Frank Act by making sure that our elected representatives are aware of the unintended consequences of this measure. However, even without further amendment, the proposed regulations implementing the Act do not adequately protect institutions with $10 billion or less in assets in a manner consistent with either the intent of the legislation or due regard for the burdens imposed on credit unions and banks by this proposal.

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