

From: San Mateo Credit Union, Karen Niederkohr
Subject: Reg II - Debit card Interchange

Comments:

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Proposal: Regulation II - Debit Card Interchange Fees and Routing
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February 8, 2011 Jennifer J. Johnson Secretary, Board of Governors Federal Reserve System 20th Street and Constitution Avenue Washington, DC 20551
Subject: Proposed Debit Interchange Fee and Routing Regulations (Docket No. R-1404) Dear Ms. Johnson: In response to the Federal Reserve Board's call for comments pertaining to the proposed rule to regulate interchange fee income and debit card routing under the Dodd-Frank Act, San Mateo Credit Union (SMCU) respectfully submits the following comments. As background information, SMCU is a state chartered community based credit union in San Mateo County, California. As of December 31, 2010, SMCU had approximately \$605 million in assets serving over 68,000 members. As you will recall, the rules as proposed would cap the fees that merchants pay financial institutions for processing debit card transactions at 12 cents each with a safe harbor provision of 7 cents each. This is a significant decrease from the current national average of 44 cents each for signature debit and PIN debit transactions. Although the Act provides an exemption for small issuers with assets under \$10 billion from the interchange fee rate setting limitations that will apply to larger institutions, the rules do not include provisions specifically designated to enforce this designation. As a small issuer of debit cards, we are very concerned with this proposal, and we believe the Federal Reserve should implement reasonable interchange regulations that will allow small issuers like San Mateo Credit Union to continue to be exempted from lower interchange fees. If the small issuer exemption is not enforced, it is estimated that small issuers like us will lose up to 73% of our current interchange income. As a not-for-profit financial institution, San Mateo Credit Union relies on this interchange income generated to offset the costs of offering a debit card program to members. Although Visa indicated on January 13, 2011, that it will support a two-tiered system, Visa was also clear that they expect the payments landscape

to evolve quickly and for market forces (including merchant routing choices) to influence debit interchange in the future. In addition, Visa gave no assurances regarding the fees and charges that small issuers would pay under a two-tiered system. We believe that even if a two-tiered system is developed, we will pay additional fees and charges to offer and process our debit card program. We believe the Federal Reserve should consider all costs of operating a debit interchange system to the maximum extent allowable by law, including all fraud costs associated with offering a debit card program. As a result of these additional fee and charges, we will likely have to offset our reduced income by increasing other operational fees for our members. As a not-for-profit financial institution, we pride ourselves on offering affordable financial services to our members; however, the reduction in interchange income will leave us with few other options but to raise other fees. Further even if a two-tiered system is permitted and works in practice, small issuers will be disadvantaged if the provisions on routing and exclusivity that allow merchants to choose how debit card transactions are processed are not implemented properly. We therefore urge the Federal Reserve to adopt routing "Alternative A," which would only require issuers to provide debit cards that can be used over two unaffiliated networks, such as a PIN-based network and an unaffiliated signature-based network. Requiring more than two networks is inconsistent with statutory requirements and would place an unreasonable regulatory burden on our credit union. Finally, our greatest concern with the proposed interchange rule is the detrimental impact it will have on our members. In 2010, our members conducted 5.4 million transactions using our debit cards. Regardless of whether a two-tiered system is implemented, we will likely experience lower interchange income and additional costs to offer our debit card program through the Visa Network. As a result, we will likely have to re-coup this lost income by increasing fees in other areas of our operation. We believe this will be a disservice to our members who rely on our debit card program for a convenient and free way to pay their everyday expenses. We strongly urge the Federal Reserve to reconsider the proposed rules and ensure actual protections are carved out for small issuers. Should you have any questions, please feel to contact me at kniederkohl@smcu.org or 650.363.1795. Sincerely, Karen Niederkohl Director, Compliance & Legal Affairs San Mateo Credit Union cc: Congresswoman Jackie Speier Mary Dunn, CUNA Jeremy Empol, California Credit Union League