South Dakota BANKERS ASSOCIATION
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February 22, 2011

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Dear Ms. Johnson:

Thank you for the opportunity to comment on the Federal Reserve System's proposed "Debit Card Interchange Fees and Routing" rule (Docket No. R-1404 and RIN No. 7100 AD63). The South Dakota Bankers Association is a trade association which represents the interests of a full range of banking institutions including very small community banks, larger regional community banks and branches of large money center banks. Only 13 of the SDBA's 88 member banks exceed $500 million in assets and 53 are under $100 million in assets. But for all of the differences in size and scope of business among SDBA members, they all agree on one thing. Senator Durbin's amendment to the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act puts the Federal Reserve's Board of Governors in an untenable position. Implementation of the Durbin interchange amendment in the manner contemplated in the Board's notice of proposed rulemaking will immediately make debit cards into an unprofitable venture for our nation's largest banking institutions. Because the Durbin amendment doesn't allow the Federal Reserve to consider all costs associated with the issuing and maintaining debit cards and their associated demand deposit accounts, covered issuers will not be able to recover their costs, let alone generate a fair profit on that segment of their business.

But covered issuers are not the only banking institutions which would be negatively impacted by the Board's proposed rulemaking. Market forces within the banking, retail, and payment system sectors will ultimately work to eliminate any short term benefit which institutions under $10 billion may initially derive from the Durbin amendment's safe harbor provisions . Economic forces will eventually force smaller banks to migrate toward Durbin's interchange pricing restrictions or risk losing market share to large, covered institutions.

Further, despite the Durbin's amendments admonitions against retailer discrimination for and against cards issued by any specific institution, pricing differentials between cards will give merchants a strong incentive to steer customers to use cards of the larger institutions and to partner with large institutions to move their accounts to the larger institutions.

Because the Board's regulatory proposal does not permit banks to cover the full cost associated with providing debit cards, bank customers could very well be faced with new maintenance and other fees on checking accounts. Low and moderate income customers will find it more difficult to maintain a bank account and will have to turn to more expensive, less convenient, non-traditional banking services.

Because of the very limited amount of scrutiny afforded Senator Durbin's interchange amendment during congressional debate on Dodd-Frank, many of the banking industry's practical concerns regarding its impacts are only now being understood by many members of Congress. More members are beginning to understand why government price controls do not work, especially where debit card interchange fees are concerned. Price controls will lead to inefficiencies in the payment system and will stifle innovation and improvements.

While it is the banking industry's hope that Congress will take affirmative action to stay the Federal Reserve's implementation of this restriction on interchange pricing, in the event that Congress fails to act, the members of the SDBA strongly urge the Federal Reserve to rethink several specific components of its proposed rules.

We strongly urge the Board to exercise discretion to the maximum degree permitted under the statute. Specifically we believe the Board should include more debit card-related costs in its calculation of the allowable fee, including: network fees; costs of inquiries and disputes; fraud losses and fraud prevention costs; fixed costs, including capital investments; and a reasonable profit.

We also urge the Board to consider the fact that debit transactions are fundamentally different from checks. In calculating the permissible interchange fee, the proposal does not recognize important differences between debit cards and checks. This includes the fact that in transactions where the card is present, merchants are guaranteed payment and the issuer suffers the loss in the event there are no funds or a valid account. In contrast, checks may be returned unpaid and merchants will suffer the loss.

We also strongly suggest that the Board should adopt alternative A in implementing the routing requirement. Alternative A limits the expense of managing unneeded relationships with additional networks and increases the number of PIN network routes available for merchants. Alternative B would require banks to have and manage multiple PIN network relationships, creating costs with little benefit. In addition, Alternative B would require re-issuance of cards in many cases, an unnecessary expense and an inconvenience to customers.

In summary, the membership of the South Dakota Bankers Association is opposed to capping interchange fees at 7 or 12 cents as the Board has proposed. Such caps would create significant effects on banks and bank customers. If the Board ultimately must adopt some form of this regulatory proposal, the SDBA also opposes the adoption of Alternative B for routing debit transactions. Alternative A is a more practical approach.

Sincerely,

Curtis A. Everson

Curtis A. Everson, President
South Dakota Bankers Association