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AMERICA'S CREDIT UNIONS

Re: Regulation II - Debit Card Interchange Fees and Routing [R-1404]

Dear Sir or Madam:

The Georgia Credit Union League (GCUL) appreciates the opportunity to comment on the proposal issued by the Federal Reserve Board's proposed Regulation II to implement the interchange provisions of the Dodd-Frank Wall Street Reform and Financial Protection Act. See Pub. L. No. 111-203, § 1075, 124 Stat. 1376 (2010), which added new Section 920 to the Electronic Fund Transfer Act, codified at 15 U.S.C. § 1693o-2. As a matter of background, GCUL is the state trade association and one member of the network of state leagues that make up the Credit Union National Association (CUNA). GCUL serves 160 credit unions that have nearly 1.8 million members. This letter reflects the views of our credit unions and the Regulatory Response Committee, which has been appointed by the GCUL Board to provide input into proposed regulations such as this.

We acknowledge that the Board was given a very difficult assignment from Congress to implement the interchange provisions, and appreciate the fact that Board staff members worked diligently following the passage of the Dodd-Frank Act (Act) to develop the proposal. Based on feedback we've gotten from our member credit unions of all asset sizes, there are several reasons we believe implementing the rule as proposed at this time will cause harm to consumers and the credit unions that serve them.

Because of these concerns, we oppose the proposal and request that the Board instead of advancing this proposal work with Congress to support and achieve a reasonable delay of 24 months in the implementation of the interchange provisions. It is important to note that credit unions in Georgia do not categorically oppose interchange fee structure reforms that could benefit consumers without unduly harming issuers.

Such a delay would allow policymakers time to address unresolved issues, including how best to protect the interests of small issuers (which includes all but the three largest credit unions that provide debit cards to their members) as Congress intended, how to ensure consumers will share in any cost savings to merchants that may result from reduced interchange fees, and how to minimize disruptions in the processing and payment of debit transactions. We believe there is growing support for such a delay in Congress, and we believe it could be accomplished if the Board and Congress will work together to help achieve it.

Of particular concern in the proposal are the following issues:

The Dodd Frank Act directs the Federal Reserve to determine a "reasonable and proportional" fee for the amount a merchant is charged on each transaction to use the debit card payment network created by the financial services industry. The Board's rate caps are based on costs for authorization, clearing and settlement in connection with debit card transactions. Both of the Board's proposed alternatives would generally limit interchange fees for issuers to 12 cents per transaction, far less than the total costs issuers actually incur to provide debit card programs. Based on industry surveys of credit unions and on data from CO-OP Financial Services, credit union debit interchange fees have been between $0.35 and $0.44 per transaction for the last several years. The proposed 70-85% reduction in fees is neither reasonable nor proportional.

The proposed rule gives no consideration to the overall costs to maintain or improve the U.S. payment system, the full costs that financial institutions bear to provide the service, the costs of fraud and fraud prevention (the vast amount of which is borne by the financial services system). Specifically, Congress intended for fraud prevention costs to be included in the Federal Reserve's calculations and they are not included in this proposal. Not including those cost calculations at this time would implement a regulation that would require many issuers to provide debit transaction services at below their actual costs.

The proposed rule imposes a one-size-fits-all approach for both signature and PIN-based debit card transactions. The proposal, in effect, favors PIN-based transactions, and we do not believe regulations should favor one type of transaction over another. Consumers and merchants can choose which type of transaction they prefer, and there are different cost structures to issuers for each, which are not fully taken into account as proposed.

The Routing and Exclusivity Provisions Represent an Unreasonable and Costly Regulatory Burden on Credit Unions (Section 235.7)

Under Section 920(b) of the EFTA, the Board is directed to write rules to provide that an issuer or payment card network cannot restrict the number of payment card networks on which an electronic debit transaction may be processed to just one network or two if the networks are affiliated with the issuer. The Board is also required to write rules that allow the merchant to direct the routing of debit transactions over any network that is authorized to process the transaction. These proposed provisions would apply to all issuers, not just those with assets of $10 billion and above.

The Board proposes two alternatives to fulfill the prohibition on exclusive arrangements. Alternative A would require an issuer to provide debit cards that could be processed on one of two unaffiliated networks, such as one PIN network and one unaffiliated network using signature authorization. A card could also be authorized to be processed on two unaffiliated PIN networks or two unaffiliated signature networks.

Alternative B would require a credit union to issue debit cards that could be processed on at least two unaffiliated PIN networks and also on at least two unaffiliated signature networks. The Board is also proposing to implement the prohibition on restricting merchants' routing choices. Under the proposal, issuers and card networks could not restrict a merchant from choosing between the various networks that have been enabled for a particular debit card, but the merchant

could only route the transaction through a network associated with the debit card at the time of the transaction.

While the uncertainty regarding these provisions extends to large and small issuers, the implications of these provisions may be even greater for small issuers. While GCUL believes that either alternative to prohibit exclusivity would result in new costs and additional fees for issuers, of the two alternatives proposed for comment, GCUL finds Alternative A the better option. That is because Alternative A would likely be less costly and burdensome for all issuers than Alternative B since under that option, issuers would have to be involved with multiple networks, each with its own fees for services, some of which would be redundant.

Routing and Exclusivity Provisions Should Not Include ATM Transactions (Section 235.7)

The Board seeks comments on whether Regulation II should include ATM networks with respect to the routing and exclusivity requirements. (ATM transaction fees would not be covered under the rate restrictions currently because such fees are typically paid by the issuers to the ATM operators. However, the Board notes in Footnote No. 29 that the fee limits could apply in the future "if ATM interchange fees begin to flow in the same direction as point-of-sale debit card transactions, as was the case for interchange fees of certain PIN-debit networks in the 1990's.")

GCUL does not agree that either the rate limits or the routing and exclusivity provisions should apply to ATM transactions. First, Congress specifically addressed the transactions that the interchange rule should cover and did not include ATM transactions in any of the definitions of "debit card," "electronic debit transaction" or payment card network." *See* 15 U.S.C. § 1693o-2(c). Moreover, the definition of "interchange transaction fee" would specifically exclude ATM transactions. If ATM transactions are included under the routing and exclusivity provisions, issuers would have to provide ATM cards that are associated with at least two unaffiliated networks and the ATM operator would have the authority to select the network a transaction would be routed over, again raising concerns that small issuers will be disadvantaged. We strongly oppose changes in the proposal that would bring ATM transactions under the scope of the rule.

Also, we believe the consequences of not addressing these concerns and implementing the rule as proposed will provide merchants additional savings they are not required to pass on to their customers, while at the same time introducing the likelihood that financial institutions will have to charge consumers more or reduce the variety and value of benefits they offer.

The Board Should Reissue A Proposal For Additional Comments

Given the nature and number of deficiencies with the Board's proposal, we do not think the Board should proceed with the document it approved for comments December 16, 2010. Rather, as stated above, we urge the Board to work with Congress to obtain more time to address issues relating to debit interchange much more thoroughly, provide better analysis and develop a regulation that reflects better public policy, consistent with congressional directives and intent.

In closing, GCUL appreciates the opportunity to express our views on this important proposed rulemaking. If you have any questions about our letter, please do not hesitate to call me at 770-476-9625. Thank you for your consideration of our concerns.

Sincerely,

Cynthia A. Connelly
Sr. Vice President Government Influence