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Subject: Reg I I - Debit card Interchange

Comments:

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Comments:
Thank you for the opportunity to submit a comment on the proposed Interchange rule. I realize that the Federal Reserve Board was constrained by some of the language in the original statute. They were constrained not only in what they could consider in setting the rate, but also severely constrained by time frame. While I won't rehash the litany of the most common issues you've likely heard from financial institutions on this issue, I do want to stress one significant concern I have: The flat-rate structure of the proposal seems, to me, to encourage the growth of debit card fraud by removing any incentive for merchants to take steps to help reduce fraud. Under today's interchange structure, it's my understanding that one of the ways merchants can "earn" their way into a lower interchange tier is by strengthening their own fraud prevention efforts and lowering the risk of transactions performed at their merchant site. For example, a merchant that processes a transaction with a card physically present is less risky than a merchant that takes a payment by phone. A merchant that confirms the 3-digit CVV/CVC security code on the back of the card is less risky than a merchant that does not. A merchant that settles their transactions very quickly is less risky than a merchant that does not. A merchant that inherently sells goods or services less subject to fraud is less risky than a merchant that does not (think the local barber shop vs a retailer that sells big screen TVs and portable electronics). Under today's structure, a merchant that takes additional steps to help the system protect everyone from fraud can receive a lower interchange rate in exchange for their lower risk. If the proposed flat-rate structure survives, what possible incentive does a merchant have to play any role in minimizing fraud? If they are going to be charged $.07 or $.12 or some other flat rate per transaction, why would it benefit them at all to take additional security precautions to prevent fraud? They receive no benefit from it in the form of lower interchange rates, so why do it? If the payment systems decided more fraud could be prevented if merchants installed upgraded terminals that support

biometrics or some other new security features, why would a merchant pay to install them? They're still billed a flat rate per transaction, so why should they even attempt to play a part in preventing fraud when they might have to foot an additional part of the bill? Or will it be yet another uncompensated cost that is fully borne by all financial institutions -- including credit unions and small community banks? Beyond the issues of the ineffectual exemption for small institutions, the fact that $.07 or $.12 per transaction is insufficient to make a debit card program simply a breakeven proposition for small institutions, the fact that $.07 or $.12 per transaction doesn't cover all fraud-related expenses as it is; it seems to me that the proposed flat-rate structure will actually INCREASE fraud losses. There's less incentive for merchants to participate in the process of minimizing fraud, and they are inherently one of the first lines of defense against fraud as it is. For those reasons and many more, financial institutions across the country will have no choice but to turn to consumers to generate additional income in other areas of banking services to subsidize what will soon be a net loss product. Consumers will pay more as a result of the proposed fee structure. Thank you again for the opportunity to submit a comment on this important issue. I hope you will seriously consider how a flat-rate structure may remove incentives for merchants to participate in the process of reducing fraud.