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Subject: Reg I I - Debit card Interchange

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Comments:

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Proposal: Regulation II - Debit Card Interchange Fees and Routing
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Comments:
Thank you for the opportunity to comment on the proposed implementation of the Durbin Amendment of the Dodd-Frank Wall Street Reform and Consumer Protection Act. I am confused by the need for this regulation. Under the terms of the settlement of what has been called "The WalMart" lawsuit, merchants gained two things in 2004: 1) the right to not honor all cards-merchants can now accept debit and credit, credit only, or debit only and, 2) lower debit interchange fees. One of the concerns after the settlement of this lawsuit was that merchants would stop taking debit cards. To my knowledge, that has not happened with any merchant; certainly not with any major retailers. One can assume from this outcome that merchants find value in accepting debit cards and have been willing to pay the merchant discount rate (which includes the interchange fee) in order to offer this means of payment to the consumer. Interchange fees are set by Visa and MasterCard and are included in the discount
rate that a merchant pays to merchant acquirers for the processing of the merchant's card transactions. The intent of the interchange fee is to cover, for the issuing financial institution, the cost and the risk of issuing a card. Debit and credit interchange fees vary based on type of merchant, how the card is being processed, and retailer volume. According to the proposed new Regulation II, Debit-Card Interchange Fees and Routing, it "would establish standards for determining whether a debit card interchange fee received by a card issuer is reasonable and proportional to the cost incurred by the issuer for the transaction." Yet, the Board is offering two alternative interchange fee standards that only consider the cost of authorization, clearing, and settlement of a transaction. Notable costs that are not being considered include card issuance, processing costs, network fees, fraud prevention costs, and fraud losses. The Board is asking for comment on a framework for an adjustment to interchange to reflect certain costs associated with fraud prevention. My response is that there is a framework for adjustments to

interchange in existence today, e.g. MasterCard and Visa, and that framework takes into consideration all costs associated with issuing and maintaining a card account. That framework for interchange adjustment does include one cost factor that one could argue should not be recovered from the merchant and that is the rewards associated with the card. Card rewards do increase purchases made with the card as the cardholder tries to maximize rewards, but do not necessarily increase purchases by the cardholder. The Board is also asking for comment on a proposed rule to prohibit restricting the number of networks for card transaction routing. One would require at least two unaffiliated networks per card; the other would require at least two unaffiliated networks per card for each type of cardholder authorization method, e.g. signature or PIN. Under either alternative, issuers and networks would not be allowed to inhibit the ability of a merchant to direct the routing of a debit card transaction. Let's discuss the easiest first. Merchants have the ability and the authority to direct the routing of a debit card transaction today. That is why the consumer is prompted to select "Debit" or "Credit" at the point-of-sale. If the consumer is using a debit card and selects "Debit", they will then be prompted for a PIN and the transaction will be routed over the online or PIN network where, today, interchange rates are lower than for signature-based debit transactions. (Of course, this assumes that the merchant has made the financial investment in a PIN pad and accepts PIN-based debit cards.) If the consumer is using a debit card and selects "Credit", they will not be prompted for a PIN and the transaction will be processed over the credit card network as a signature-based debit card transaction at a higher interchange rate. Financial institutions benefit from a higher interchange fee if the consumer selects "Credit". The consumer benefits from a much larger number of merchants that will accept their debit card if they select "Credit". The merchant benefits from the lower interchange rates for online or PIN debit if they have made the investment in PIN pads at the point-of-sale and, for those that have, they are steering consumers to PIN debit. There are two alternatives to the prohibition on restricting the number of networks. Alternative one requires at least two unaffiliated networks per card. This is the case for most cards today. The exceptions would be Visa cards with an Interlink mark and MasterCard cards with a Maestro mark. For example, my Visa debit card has a NYCE logo on it. It really doesn't matter which network. The signature networks, Visa and MasterCard, compete. The PIN networks, Interlink, Maestro, NYCE, STAR, etc., compete. And, does it really matter since te base of $0.07 with the safe harbor of $0.12 or the stand-alone cap of $0.12 basically regulates interchange rates for signature and PIN debit as the same? Alternative two requires at least two unaffiliated networks per card for each type of cardholder authorization method (signature and PIN). I'm not sure what is to be gained with this alternative other than increased costs for issuers, confusion for consumers and merchants, and contradiction of an existing law/regulation that prohibits an issuer from issuing both Visa and MasterCard debit cards as state's attorney generals thought that if an issuer issued both Visa and MasterCard debit cards that it would be anti-competitive. Of course, I'm sure that they never dreamed that there could be a future scenario where a Visa and a MasterCard logo on the same card could be required. Finally, I think that the proposed regulation ignores the fact that this is a competitive industry that is on the brink of becoming even more competitive with mobile payment. No harm is being done. There is competition. Merchants have the option to not accept debit. They have the right to try to steer consumers at the point-of-sale. If enough merchants decide to not accept debit, the market will respond-the consumer market and the networks.