

DOLLAR GENERAL

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February 22, 2011

BY EMAIL

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

Re: Docket No. R-1404 (Debit Card Interchange Fees and Routing)
RIN No. 7100 AD63

Dear Ms. Johnson,

Thank you for providing us the opportunity to comment on the notice of proposed rulemaking ("NPRM"), and we would like to express our appreciation for the time and hard work the Federal Reserve Board Payments staff has put into this proposed regulation. It is clear that the Board has worked diligently to lay the groundwork in establishing regulations that interpret and apply the Durbin Amendment within the timeframe required by the statute. On behalf of Dollar General, I submit the following comments.

Allowable Costs

The Board has requested comment on whether it should allow cost recovery beyond authorization, clearing, and settlement ("ACS") and whether it should limit allowable costs to include only authorization. The statute calls for the Board to (1) consider the functional similarity between debit and checking transactions and (2) consider the incremental cost incurred by the issuer in the ACS of a particular electronic transaction. With regards to the functional similarity to checking, the cost of authorization is the only comparable cost as checks clear at par and no costs (fixed¹ or variable) from the check-issuing institution are borne by the retailers. While we agree with your observation that with clearing and settlement there is no analogous fee for checks, we still believe that the language in the second consideration clearly states that the only cost which shall be considered is the incremental cost incurred by the issuer in the ACS of a particular electronic transaction. Therefore, with respect to allowable cost recovery, the proposal allowing only ACS costs incurred by the issuer for a particular debit transaction should be adopted. We believe that

¹ It has been suggested that fixed costs might be applied. Since fixed costs are non-ACS costs and authorization is the only comparable cost to checking transactions, this would be inappropriate and inconsistent with the statute.

the staff's recommendation is appropriate and consistent with Section 920. We agree with the Board's use of "average variable" costs in interpreting incremental costs for a particular transaction, as defined in the statute, and we agree it should not include fixed costs or marginal costs.

Proposed Interchange Fee Standards

Regardless of the final amounts set, we believe the concept of a safe harbor and a cap (Alternative 1) is best designed to reflect each issuer's variable costs while providing a safe harbor to make it easier to administer and enforce. By having a cap in place, there is an incentive to reduce costs. As compared to Alternative 2, Alternative 1 more closely aligns to the mandate of the reasonable and proportional language as it does incorporate actual costs for the issuer above the safe harbor up to the cap. However, for a safe harbor to be effective, it should be limited and should not be greater than the weighted average cost. We believe that the safe harbor should be no greater than the 4-cent weighted average ACS costs reported by the issuers, considering that number already has some upward bias with a portion of exempted prepaid cards included in that average. This would be more in line with the statute while still allowing a significant reduction in administrative costs.

We also strongly recommend against the two additional alternatives described in Section B.3 based on network/issuer averages as this will greatly penalize small merchants who would incur costs above the regulatory standard, resulting in blatant price discrimination. Finally, we agree with the Board that there should be no distinction between pin and signature debit, as it would otherwise be rewarding a less secure payment alternative.

Circumvention

In regards to circumvention, it is difficult to identify all the ways that issuers could circumvent these rules and how to address them. For example, we have concerns with how hybrid cards will be used to circumvent these rules. In addition, the exemption of prepaid cards from an otherwise non-exempt issuer could result in circumvention by transferring costs. We believe that it is important for enforcement mechanisms, including certification processes, to be put in place to identify and address those circumstances when they arise.

Exclusivity and Routing

In our opinion, this is one of the most critical areas of the rulemaking. We strongly favor Alternative B. This alternative meets the statutory requirements and provides competition with each authorization method, particularly for small merchants, many of whom do not have the capability to accept pin transactions. The idea that eliminating the market power that exists today will somehow result in a less competitive market is absurd. By choosing Alternative B for all debit payment methods, the Board will be promoting *more* competition. The results of a more competitive marketplace should ultimately reduce the use and need of the cap standard as increased competition will drive prices down over time. This is why we strongly urge the Board that all issuers, including small issuers, be subject to Alternative B since the small issuer's exemption was clearly limited to "regulations prescribed under paragraph (3)(A)" in the statute.

Multiple networks would not limit the cardholder's control and benefits any differently from the situation the cardholder faces today with a multi-bug card. Moreover, if the issuer (and the cardholder) deems the benefit a "true" benefit, then, for their card, they can choose the networks that offer it. Unfortunately, the perverse effect of the market failure that has plagued this industry is that these cardholder benefits are being paid for by all consumers. Dollar General serves low-income customers in communities across the country, and the soaring cost of interchange fees impacts the cost of goods and services they receive from us. These higher interchange fees are being borne by the consumer, in particular, the low income consumer who may not have any electronic payment card but will have to pay for cardholders' rewards and benefits. By adding competition to the debit market, the users will determine what benefits are worthwhile.

In addition, we strongly concur with the Board's conclusion that the merchant, not the issuer or network, must be able to designate preferences for the routing of transactions.

The Durbin Amendment and your proposed rules are important steps in eliminating this suppressing control of market power that banks have collectively displayed in centrally setting interchange. It is apparent by watching the response of the banking community how egregious and profitable these practices have been. We urge you to continue to move forward expeditiously to provide much-needed relief to the merchants and consumers across the country. Delaying this process is merely an attempt to circumvent the legislation passed and will continue to hurt consumers, retailers and the economy as a whole. While we have expressed certain differences with the NPRM in our comments, we believe the analysis is very thorough and generally agree with your interpretation of the statute. Implementation does not need to be delayed in the name of "getting it right" to address these endless criticisms. We believe you have faithfully and painstakingly worked to interpret the statute correctly. We appreciate your consideration of these requested comments.

Regards,



Wade Smith
Vice President & Treasurer