American Financial Services Association

February 22, 2011

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

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

The American Financial Services Association ("AFSA") is the trade association for the consumer credit industry, protecting access to credit and consumer choice. We appreciate the opportunity to comment on the Notice of Proposed Rulemaking on Debit Card Interchange Fees and Routing ("Proposed Debit Card Rule"). We focus our comment not merely on the poor public policy of price controls, but on the fact that imposing a $.12 price cap on debit card usage spells the end of free checking and other innovations for consumers.

Though costs imposed on the industry are almost always borne by the consumer, it has perhaps never been truer than in this instance. Make no mistake about it: the cap of $.12 per transaction on debit cards will push modest-to-middle income consumers out of traditional banking relationships and into the "unbanked." And for what? To shift billions of dollars of the cost of doing business from merchants to consumers.

Reasonable and Proportional

Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") requires that the cost of interchange be "reasonable and proportional to the cost incurred by the issuer with respect to the transaction." This language requires the fee to be "reasonable and proportional" to the issuer's cost, but it does not require the Federal Reserve Board ("Board") to set a hard fee as it has done in the Proposed Debit Card Rule. It requires the Board to establish guidelines for pricing – not to set a price.

In establishing the guidelines, the Board should consider the totality of the costs involved—including the broader cost of doing business, the enormously high cost of fraud control and a return on investment for both issuers and payment systems. Not to consider a return on investment in these transactions is fundamentally unfair, since nobody would object to the argument that a merchant is also in business in order to make a profit.

Further, when a hard (and very low) price cap is set, there can be no recognition of the variable costs that go into widely varied transactions. We associate ourselves with the suggestion of others that card network associations are allowed to set their own reasonable rates, depending on transaction variables, and that they undergo regulatory examination for "reasonableness."

Price Controls

Setting hard one-price-fits-all limits on fees charged from one business to another should be avoided whenever possible. Government rate caps on interchange choke innovation and are hostile to the very notion of a free market system. As Rep. Blaine Luetkemeyer (R-MO) said at House Financial Services Subcommittee on Financial Institutions and Consumer Credit hearing on the Federal Reserve's Interchange Proposed Regulation and Debit Card Transaction Fees on February 17, 2011, "A government entity [setting] prices on the private sector is unconscionable. We're taking a huge step down a road we don't want to go. Suddenly we're starting to treat the banks and the people who do the interchange fees . . . as a utility company instead of a private sector entity." He added that this was, "Just like telling a pizza place that delivers pizzas, 'we're not going to allow you . . . to put into your cost [in]to your pizzas – the person who drives the car or the car itself. All we're going to let you do is charge for the gas.' And that's what we're doing here. And that's wrong."

The Federal Reserve was founded by Congress in 1913 to provide the United States with a "safer, more flexible, and more stable monetary and financial system." It strains the imagination to conceive of something more antithetical to a "flexible" financial structure than price controls in our payment systems. The Board should reverse course on its proposed price control and adopt a plan that is true to the requirement that fees be "reasonable and proportional" without being overly prescriptive.

Pushing Consumers Out of Free Checking

One policy argument for imposing this cap was that cash consumers subsidize the cost of good for payment card consumers. However, that argument does not make sense since retailers could always give a discount for cash. And the alternative is much worse: now the cost of processing debit cards will be borne entirely by the consumer.

Institutions are not "saber-rattling," as some have suggested, when they discuss the very real fact that all free checking and free online banking programs have real costs associated with them. These programs cost money, and changes to these programs are simply unavoidable when all revenue associated with debit card interchange is gone. This will hit moderate-to-middle income consumers the hardest, as banks will no longer be able to offer free checking to consumers who do not generate other income by holding large deposits or other behaviors associated with higher-income consumers. Rep. James Renacci (R-OH), who has been involved with banks, has been a retailer, and has been a CPA that audited both, said at the same interchange hearing on February 17 referenced above, "If I was sitting on the retailer side, and even if prices were able to come down, I know that the bankers have to make these dollars up somewhere and those fees will wind up going to the consumer. And, today, I'm sitting on the side of the consumer and the American -- and wondering who really wins in all of this." If the

Proposed Debit Card Rule is not modified, the Board is going to cause millions of more people to be unbanked.

Conclusion

The Proposed Debit Card Rule is very troubling for consumers and business alike. We urge you to reconsider the proposed price controls, and adopt instead a more flexible plan that still upholds the letter and spirit of the Dodd-Frank Act.

Please do not hesitate to contact me at (202) 296-5544 if I can be of further assistance in this matter, or to discuss any of the specifics herein.

Sincerely,

Chris Stinebert
President and CEO