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Via Electronic Mail

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

February 22, 2011

RE.: Docket No. R-1404 and RIN No. 7100 AD63

Dear Ms. Johnson:

SunTrust Bank submits this comment letter in response to the request for comments issued by the Board of Governors of the Federal Reserve System ("Board") regarding the implementation of the debit interchange fee and other modifications of the Electronic Fund Transfer Act.

Over the last few months, the Board has received a barrage of criticism concerning the proposed regulations. Like virtually every other financial institution, SunTrust Bank has read with alarm the proposed implementation of the law. In our view, the criticism is warranted and amply justifies an indefinite delay in the implementation of the proposed regulations pending a comprehensive review.

The criticism in question has focused on both the Board's interpretation of the intent of Congress in developing the proposed regulations and on the negative consequences of these regulations to consumers. After providing our comments to the Board's specific requests, this letter will only briefly summarize our concerns regarding the consequences of these regulations below. More importantly for SunTrust in addressing the Board, SunTrust urges the Board to reconsider its stance in light of the flawed, incomplete, and opaque nature of the regulations. The regulations are also oppressive in that if the financial industry chooses to continue offering debit card services, these services will be provided at a loss. Alternatively, the financial industry may discontinue offering debit card products altogether.

In order of importance, these are SunTrust's specific concerns with the Board's proposed regulations:

1. Congress asked for the Board to create standards that reflect the true cost of providing debit card services. The proposed regulations provide no such standards, but instead impose an inflexible cap on interchange fee per transaction and a one-size-fits all safe harbor that does not take into account the following differences: those between various issuers, and those between different types of debit transactions (i.e., PIN vs signature).

2. Fraud prevention (among other incremental costs) is an enormous component of true debit transaction cost. Congress wanted this cost to be included. Without the cost, the final regulation should not be issued since issuers would be forced to provide debit transaction services at below cost. This will discourage issuers from investing in fraud prevention measures, therefore placing the consumer at risk when using debit. Zero liability assurance will also necessarily be eliminated.

3. Historically speaking, any Congressional mandate for determining "reasonable and proportional costs" has always recognized the need to include a related percentage for return on investment. The proposed regulation provides no incentive for risks taken to the detriment of current and future investment and innovation.

4. Debit transactions may be either PIN or signature-based. These different types of debit transactions have very different cost structures. The proposed regulation does not address the distinct costs involved in each type of debit transaction and imposes a 'one-size-fits-all' for them both. As a result, and contrary to Congressional intent, PIN is favored over signature debit.

5. The proposed regulation creates a windfall to merchants and their acquiring banks since they are under no compulsion to pass on savings from a reduced interchange fee to consumers. Congress did not expect banks to shift the burden of the loss of reduced interchange fee income onto consumers through a return to per-transaction fee banking. Congress did not legislate a windfall for merchants. Similarly, Congress did not intend a cost increase to consumers for their banking services.

SunTrust Bank's responses to the Board's requested comments are as follows:

A. Regarding selective authorization cards, SunTrust would encourage the Board to consider these cards to be debit cards that are required to adhere to the Board's final regulations concerning debit card transactions. Merchants have already been given an enormous windfall through the interchange fee cap. Exempting merchant store gift cards from the final regulations will provide an additional windfall for merchants as they create more exempt cards to circumvent the interchange rules. Such cards will place financial institutions at a competitive disadvantage as consumers are driven to choose merchant-created selective authorization cards.

B. Concerning the interchange fee cap, it is important to point out that the Board's economic assumptions are based on a problematic analogy between debit transactions and paper check transactions. Debit transactions are a more evolved and faster payment method than paper check transactions. Debit transactions also provide the option of immediate authorization. Furthermore, debit transactions provide greater security, particularly regarding PIN-based transactions.

As a consequence of this misleading analogy between paper and plastic, the billions of dollars spent by the private sector to create and sustain the debit transaction network are completely disregarded. In addition, the cost of faster service, immediate authorization, superior fraud prevention, and other benefits are taken for granted.

No two debit transactions are the same. Some debit transactions require greater servicing and/or fraud investigation costs, whereas other transactions do not. As a result, all debit transaction costs are variable costs, and must be considered to continue offering the basic service. This cost analysis does not take into consideration a proper return on the billions of dollars already invested, and likewise does not conceive of maintenance costs or the cost of future innovations. Regarding innovation, it is important to emphasize that the proposed cap on fees will inevitably reverse our nation's positive trend away from paper-based and credit card transactions. Consequently, this shift backward toward cash and checks will decrease the innovation and efficiency of our financial system while increasing potentially the debt burden and safety risk of U.S. consumers.

As a result of the above criticisms, the Board's proposed "reasonable and proportional" method for arriving at cost reimbursement is neither reasonable nor proportional. The inflexible cap does not take into consideration the variable costs within a single issuer or the variation of average costs among different issuers. The Board should seriously consider jettisoning the cap in favor of a total cost approach for each individual issuer.

C. If forced to choose between the Board's two options, SunTrust would be less unhappy with alternative 1. In 'choosing' alternative 1, it is essential to register our strong objection to the dramatically flat allowable transaction cost that will force us to provide service at a loss without the prospect of future innovation in this payment method. Another objection is that the proposed cap was hastily arrived at using incomplete data. In addition, the one-size-fits-all fee cap provides no incentive to lower costs.

D. Regarding the Board's request for comment on the two possible Fraud Cost Adjustment approaches, SunTrust is in favor of the non-prescriptive approach. However, it will still be important to provide a regulatory incentive for technological innovation since, as mentioned above, the proposed fee cap will remove market-based incentives for technological innovation.

The Board should make the fraud adjustment fee reimbursement dependent on the adoption of a minimum level of fraud prevention. The Board should also allow for additional interchange fee fraud adjustment amounts for additional fraud prevention technology. This approach will guarantee a minimum level of security for all issuers and consumers while simultaneously encouraging technological innovation in fraud prevention. In this way, the resulting innovations may eventually become the new standard security features of the future. Furthermore, such innovations may lead to the creation of future payment methods.

Below are SunTrust's comments to the Board's ten specific requests on the merits, costs and benefits of the fraud adjustment approaches:

(i) Fraud costs comprise approximately 20-25% of debit card transaction costs and are the highest single item in our total cost. If the Board uses a flat rate fee for fraud cost reimbursement, then the entire fraud-loss risk burden falls on the issuer. Additionally, the flat rate fee removes issuer incentives to continue allowing consumers to use this payment method. A sensible and flexible alternative to a flat rate fee would be risk based pricing, which SunTrust strongly supports.

(ii) As for the type of technology that should be required, SunTrust understands the question as what should be the absolute mandatory minimum that all issuers should meet. Ideally and eventually, we should aspire to a Chip and PIN approach that will significantly reduce fraud. Specifically, Chip and PIN will reduce counterfeit transactions, cloning and fraud created by stolen payment devices. In the meantime, and without mention to a specific technology, the minimum *procedural* requirements must allow issuers to positively identify the owner of the payment device. The process of making the positive identification should preferably be automatic, but it may take time to reach a fully automated identification authorization method.

(iii) The effectiveness of certain fraud prevention technologies would serve as the basis for an increased fraud fee adjustment. The amount of the fraud fee adjustment may be assessed by making an objective determination of the effectiveness of the technology.

The Board should use a common process to set fraud fee adjustment standards by creating an application process similar to PCDISS (Payment Council Data Industry Security Standard). The Board could expand its current mission to include both minimum *procedural* standards and fraud prevention *technology* standards or engage a third party to set procedures and certify technological advances. The Board could institute a tiered rate adjustment structure based on the implementation of additional effective fraud prevention technologies. If the non-prescriptive approach is used, merchants must be required to participate since one-sided fraud prevention is ineffective.

(iv) The decision to adopt any fraud prevention measure must be based primarily on its objectively-determined effectiveness. Accordingly, the most important criteria in selecting a fraud prevention measure should be its effectiveness, but other criteria must also be considered. Other criteria may include consumer-friendly considerations (e.g., forgetting a PIN, equipment malfunctions and power outages, etc.).

(v) Fraud impacts consumers, merchants, and issuers alike. Even if the fraud impact on each of these parties could be distinguished, doing so would be counterproductive.

Focusing on the impact only on merchants will eventually give rise to policies and activities that will shift the burden of fraud losses onto consumers and issuers. Consequently, fraud prevention measures must be considered holistically and not piecemeal in order to remain effective for all parties.

(vi) If no adjustment is made, issuers will naturally be forced to scale back their fraud prevention measures. Issuers will make region-by-region decisions regarding the risks and rewards of issuing debit cards and will stop issuing debit cards in areas of high fraud.

(vii) Recoverable costs cannot be measured accurately through current cost accounting systems since such systems do not fully capture total costs. A neutral third party must be responsible for assessing the effectiveness and permissible fee adjustment for implementing additional fraud prevention technologies.

(ix) If the Board takes the prescriptive approach as proposed, then the Board should review the standards at least annually from the date of implementation. However, the Board should be prepared to review standards more frequently if and when new technologies become available. There should be an ongoing submission process and annual review to track results.

(x) SunTrust has addressed this issue above in comment number (v).

E. Regarding the timing of the fraud adjustment, the importance of this adjustment in addition to all of the other abovementioned concerns amply justify delaying the issuance of the final regulations pending further dialogue and investigation.

F. SunTrust does support a process to review additional applications for product exemption claims. Granting such product exemptions may allow solutions for the unbanked and the underbanked. However, we must reiterate the fact that the proposed regulation will have a tendency to add to the ranks of the unbanked and underbanked.

G. SunTrust recognizes the Board's responsibility to prohibit circumvention and evasion any final regulations. However, an overzealous series of restrictions will have an unintended impact on network financial incentives given to banks for product development and marketing purposes. Issuers receive compensation incentives from networks based on volume; however, many also receive incentives in a lump sum or in the form of service credits for marketing and product development to further debit use. We believe those incentives directed at marketing, consumer education, and product development should not be limited. The non-circumvention and evasion rules should not be so overbroad as to cause network incentives to be more controlled.

Concerning signing bonuses, such bonuses encompass not only an issuer's debit business, but the total banking portfolio. Removing signing bonuses will penalize issuers for having other financial products with a payment network.

H. Regarding the two payment network proposals for implementing EFTA section 920(b)(1)(A), SunTrust supports alternative (a) since it more faithfully reflects the will of Congress.

I. If the Board only allows nationwide networks, every PIN network in the U.S., regional and start-up networks will be unfairly penalized. All networks began as regional networks at one time, and favoring the more established national networks would create a de facto monopoly or duopoly by forcing smaller networks either to go out of business or consolidate and concentrate. In addition, the Board would be forcing regional banks like SunTrust to assume additional unnecessary costs to receive service from one of the national networks. As competition decreased, costs for issuers would increase as a virtual monopoly network would result on a national level.

J. SunTrust asks that the Board make exempt from the final rules special or limited use cards (e.g., HSA, employee benefits cards, etc.) that require special technology to limit expenditures. Otherwise, the existence of multiple rules creates the possibility of conflicts between other regulations governing these products.

In closing, the proposed regulations will harm much more than banks. It will harm consumers of financial services and will weaken our payment system. With a projected loss of over 73% of interchange fee income, the proposed rules will cause the industry to compensate by reducing or eliminating debit card products. The availability of debit products will also decrease as banks offer such products on a more limited basis. The increased cost of banking will force many consumers to leave banks and join the ranks of the under-banked and unbanked. These consumers will increasingly resort to the unregulated financial industry, where opportunities for criminal activity will increase while the Board's control diminishes.

Once again, these facts amply justify urgent Board action to delay the issuance of the final regulations.

Sincerely,

James M Wells III
Chairman and Chief Executive Officer
SunTrust Banks, Inc.