HOLDING COMPANY

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July 25, 2021

Ann Misback
Secretary
Board of Governors of the Federal Reserve
20th Street and Constitution Ave
Washington, DC 20551

Re: Proposed Changes to Regulation II- Debit Card Interchange Fees and Routing (Docket No. R-1748, RIN 7100-AG15OP-1747)

Dear Ms. Mishback:

I strongly disagree with the Federal Reserve's proposed rule to make changes to Regulation II, as it will have a significant impact on banks like FirstBank. My bank is vulnerable to regulatory changes which combine new compliance costs with reductions in fairly earned revenue, as this revenue funds our core banking services including free checking and expanded digital banking services and accessibility. This expansion of the routing requirement to all card-not-present transactions and accompanying mandate that we accept PINless transactions effectively creates a price cap on the revenue community banks receive to participate in these transactions. It also results in extensive and recurring costs to comply with these new rules, while reducing my operational latitude to mitigate the higher fraud costs my bank directly incurs which are associated with these newly-covered transactions.

Any expanded requirements will only create new significant challenges for banks trying to provide the best financial products for customers and serve our communities. Debit revenue is particularly vital to offering affordable core deposit accounts, but the proposed rule does not acknowledge the harms that this intervention will cause to consumers in the two-sided debit card market. While as debit card issuers we care deeply for merchants in our community, this rule will largely benefit the most profitable national merchants who ship their products to customers. Merchants matter, but banking – particularly community banking – is also an essential part of the American economic landscape and should be equally valued in policymaking.

While presented as a clarification, my bank will experience the proposed rule as a material change in how we handle debit card transactions. Fundamentally, the rule shifts the compliance paradigm for Durbin by placing the technically infeasible burden on my bank to ensure merchants can enforce certain new rights across all geographies and transactions. Yet the proposed rule does not explain how an issuer can ensure these conditions are met, in a card system where we have no knowledge of or control over

merchants' transaction choices. In a nation this large, most merchants are located far from any given bank, making the all-geographies requirement particularly challenging. My bank has complied with the Durbin Amendment for a decade by issuing cards with two networks and ensuring we do our best to prevent fraudulent activity within the debit card ecosystem, and the merchant had to do their part by supporting cards that came across the checkout counter. It is beyond any reasonable technical expectation that I can issue a card that is guaranteed to support every merchant across the country who insists on an unsupported transaction configuration. The information to prevent such a violation would be literally incomprehensible since I do not have a business relationship with them, and thus it would be impossible to meet these compliance standards. Industry experts believe this would require elaborate technical builds, at a cost that would likely be born by community banks at the expense of supporting affordable banking services such as free checking, and potentially still fall short. The Federal Reserve incorrectly claims that there are solutions available today, yet then goes on to explain that these transactions are not used frequently enough for merchants' liking. There are legitimate operational reasons for these transaction trends, which, unfortunately, the proposed rule does not explore. Working through these myriad issues could crowd out and deprioritize discretionary investments I would like to make, including adopting faster payments systems, enhanced fraud prevention systems, and expanding digital accessibility to consumers and small businesses within our communities.

Secondly, it's important to address how this proposed rule could expose the payments ecosystem to more fraud and potentially reduce the overall level of security in the system, creating real consumer impact. Different networks and transaction types offer different protections against fraud, including the ability of issuing institutions to charge back fraud to the merchant, and not all fraud mitigation protections offered by the networks are created equal. Banks manage the transactions they support with these differences in mind and work to offer customers the most secure experience, minimizing fraud events. This proposal makes it even more difficult, if not impossible, for fraud-conscious financial institutions and consumers to manage how debit transactions are processed. Under the current rule (and if it were to be applied to card-not-present transactions) retailers, not consumers, choose how transactions are routed. Often the merchant may choose the lowest-cost routing option, regardless of the value that option provides to other parties in the transaction. Over time, this may undermine fraud protection benefits like zero liability protection and text alerts on potentially fraudulent debit transactions. Consumers expect all these benefits as part of my bank's brand promise, but when another party is given nearly-total control of how my banks' debit cards operate, they may not be sustainable to support based upon the increased operational and fraud expenses my bank would incur. At a time when the industry has worked so closely with the Federal Reserve to improve payments security, the proposed rule takes away key latitude and tools for financial institutions to do everything possible.

Additionally, if a retailer chooses a debit network and transaction type that lacks security and necessary fraud mitigation benefits and fraud occurs, they bear limited responsibility. This is particularly true of "PINless" transactions, which consumers assume to be signature transactions, but are entirely different. For instance, the world's leading online retailer says that refunds to consumers can take 2x to 3x longer via PINless transactions, leaving banks to pick up the slack and resolve the customer service problems that can result. PINless transactions are often difficult or impossible to decline when necessary and can be harder or impossible to reverse in the event of fraud or consumer error. As an example, as online debit card purchase activity has increased, online fraud losses at my bank have increased over 50% and PINless transactions have increased over 230%. These novel transactions did not exist in common usage when the Durbin Amendment was passed, so I am uncertain how they can be mandated upon card issuers now despite our reasonable reservations. By forcing us to take these less protected transactions, the proposed rule goes beyond the constrained routing rights merchants acquired in the Durbin

Amendment. It is banks like mine that cover the losses and reverse fraudulent transactions. We have the most incentive to ensure consumers are protected yet this proposal limits our ability to choose the best debit networks to route transactions and best serve and protect consumers.

Lastly, I am concerned the proposed rule would further suppress competition among debit networks and the required competition analyses were not completed. The rule could drive further consolidation among the debit networks, reducing choices for issuers and small businesses. There has already been significant vertical consolidation between bank technology vendors and payment networks. As proposed, the rule would benefit a handful of large merchants, potentially increasing their competitive advantage over Main Street stores. The proposed rule lacks a fulsome competition analysis and does not mention that the U.S. Supreme Court found in 2017 that the card market is a two-sided one, where policymakers must balance the commercial interests of issuers and merchants. The proposed rule still follows the one-sided market model where network dynamics will be tilted towards merchants who will not directly bear consequences if the cardholder experience offered by my bank is diminished. We should be encouraging an environment where debit networks compete on the quality of their network and whether they provide the best service for routing debit transactions, not by arbitrarily imposing government mandate that only account for one part of the picture.

The provisions of Regulation II have significant negative effects on consumers and banks and should not be expanded in any way. I would rather spend my resources offering customers new options like faster payments systems that are becoming available now than the distraction of revisiting my Durbin Amendment compliance posture. To enable a truly competitive marketplace, I strongly encourage the Federal Reserve to withdraw the proposed rule to expand routing controls to card-not-present debit transactions and the requirement to have two debit networks for routing.

Thank you for the opportunity to submit comments on this matter.

Sincerely,

Lavonne Heaviland
President – FirstBank Centralized Operations