

August 9, 2021

Submitted via email to regs.comments@federalreserve.gov

Ms. Ann E. Misback
Secretary, Board of Governors
Federal Reserve System
20th Street & Constitution Ave, NW
Washington, DC 20551



RE: Docket No. R-1748, RIN 7100-AG15

Dear Ms. Misback:

On behalf of the members of the Kentucky Retail Federation, we ask that the Federal Reserve Board of Governors amend Regulation II to clarify the requirement that each debit card transaction must be allowed to be processed on at least two unaffiliated payment card networks for card-not-present transactions. Retailers' fees associated with accepting debit cards are untenably high and have resulted in increased operating costs that are ultimately passed on to consumers.

The Kentucky Retail Federation (KRF) is a non-profit trade association created to improve the retail business climate in Kentucky. As "The Voice of Retailing in Kentucky," KRF is a strong advocate for the retail industry with organizational roots going back to 1939 and today proudly represents over 6,000 member locations throughout the Commonwealth of Kentucky. Members are as diverse as the products they sell, from department and drug stores to hardware, apparel and building supply retailers.

All merchants rely on debit network routing options to help contain network costs. Networks competing for both banks' and retailers' business benefit all stakeholders in the merchant economy—most importantly the consumer. Retail is highly competitive and functioning on razor-thin profit margins. When they shop, consumers have a great number of choices in their community, and online. Price is often the only determining factor when a consumer makes a purchasing decision. The consumer has many choices on where and how to buy what they need; however, merchants have little to no choice when it comes to routing card payments used for online purchases.

The events of the past year placed previously unimaginable strains on the retail industry. Store owners pivoted from being ordered to close down their stores to keep people safe, to collectively investing millions of dollars into health and safety protocols and protective gear. In a matter of weeks, Kentuckians shifted a significant portion of their shopping to online and as a result went from paying with various tender forms to paying almost exclusively with debit and credit cards. In response to this shift, retailers have invested significant resources to accept, fulfill and deliver online orders to meet the increased consumer demand.

This shift has greatly increased Kentucky retailers' cost of doing business, placing further strains on the ability to keep prices low while also faced with rising inflation at such a critical time. The Federal Reserve Board of Governors can provide direct relief to retailers in Kentucky by enforcing the routing provisions in the 2010 debit reform law and reducing the regulated debit interchange rate commensurate with cost reductions.

While our members are overwhelmingly utilizing competitive routing for in-store transactions, they do not enjoy the same access to competitive debit networks when the card is used online and in mobile transactions. The Board's proposed clarification will do that, and simply clarify that banks and payment networks must compete for retailer business—just as retailers compete for consumers' business and loyalty—regardless of where the transaction occurs.

340 Democrat Drive - Frankfort, Kentucky 40601
www.kyretail.com - info@kyretail.com
(502) 875-1444 phone - (502) 875-1595 fax

Our members report that many banks already enable a second “PINless” network and can choose amongst service providers when the card is used online. Unfortunately, they report that some of the largest issuers with a vast majority of the debit business are not enabling a second network leaving the retailer with no options but to run across more expensive global networks.

The intent and language of the law is clear- retailers must have access to competitive networks for debit transactions. No network or issuing bank can remove that choice. The Board is entrusted to enforce the law, particularly when more dominant networks are benefiting at the retailer and other network expense due to lack of enforcement. As the Board notes, currently only 6% of online debit transactions are being processed by single-message networks. This marketplace distortion is clearly problematic and within the ability of the Board to rectify quickly. An open and competitive market benefits all stakeholders, most importantly the U.S. consumer.

Therefore, the Kentucky Retail Federation strongly supports the Board acting quickly to finalize the clarifications and enforce the debit routing provisions. Doing so will help ensure that retailers will have access to at least two unaffiliated debit networks before they head into the busy holiday season. In addition to providing merchants with the competitive choice to which they are entitled, the Board of Governors' proposal will help bring about the competition that is needed to bring debit interchange fees under control. Card processing fees ultimately increase prices for consumers and cannot be allowed to continue to grow.

The Kentucky Retail Federation also respectfully requests the Board act to reduce the regulated debit rate to reflect both the reduction in cost and fraud burden of the regulated issuing banks, pursuant to the survey that was released by the Board at the same time as this request for comment. U.S. merchants paid \$24.38 billion in debit interchange fees in 2019.¹ With the significant shift to online and card usage, we can only expect that number to have increased dramatically in 2020. The Board set the current regulated rate for covered issuers at 21 cents plus five basis points with an additional penny for fraud adjustment when the law was initially implemented ten years ago. However, even with issuer costs having reduced by half, the rate has never been adjusted. The Board, in its biannual survey of issuer costs and fraud losses, reports that it costs covered issuers less than four cents to process a debit transaction. Additionally, the Board noted “the percentage of losses from fraudulent transactions reported by covered issuers absorbed by merchants steadily increased from 38.3 percent to 56.3 percent...”² These two facts are clear indicators that it is time for the Board to reduce the regulated rate to bring it into alignment with the statutory requirement that is both reasonable and proportional to issuers actual costs.

Thank you for your consideration of our comments on this proposed clarification to the regulations. Our association and its members are hopeful that the Board will enforce the debit routing law and reduce the costs of transactions to retailers and consumers.

Sincerely,



Tod A. Griffin
President

¹ 2019 Interchange Fee Revenue Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions, May 2021.

² 2019 Interchange Fee Revenue Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions, May 2021.