

Commerce Bancshares, Inc.
1000 Walnut Street
Kansas City, MO 64106

Via email at regs.comments@federalreserve.gov

August 11, 2021

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

RE: Docket No. R-1748, RIN 7100-AG15
12 CFR Part 235 – Debit Card Interchange Fees and Routing (Regulation II); Proposed Rule

Dear Ms. Misback:

Commerce Bancshares, Inc. (“CBI”) is a regional bank holding company with one bank subsidiary, Commerce Bank, (“Commerce”), and total assets of \$33.9 billion as of June 30, 2021. Commerce is a full-service bank, with more than 300 banking locations in Missouri, Illinois, Kansas, Oklahoma, and Colorado. A full line of banking services, including payment products, mortgage banking, investment management and securities brokerage, is offered. We take pride in providing over 600,000 customers convenient and secure access to their funds through the issuance of debit cards.

We appreciate the opportunity to comment on the proposed changes to Federal Reserve Regulation II.

The proposed amendment to Regulation II has been characterized as a clarification of existing language, to make clear, in part, that the requirement to process debit card transactions on two unaffiliated payment card networks applies to card-not-present (CNP) transactions. We believe the impact of that clarification is a substantive change that would introduce risk and confusion based on the points made below.

1. Risks associated with Card-Not-Present enablement and routing.

Within the proposal, the Board of Governors of the Federal Reserve System (the “Board”) points out that “most single-message networks are now capable of processing card-not-present transactions” along with a reference in the next paragraph to the “widespread adoption of these innovations.” The Board further states that, in the decade since the adoption of Regulation II, more networks have introduced capabilities to process CNP transactions, which have become an increasingly significant portion of all debit card transactions. At the same time, with this growth, CNP transactions have accounted for an increasingly significant portion of card fraud. As discussed in the Board’s Data Report, CNP fraud accounted for more than half of overall fraud in 2019.

The Board mentions developments among single-message networks which have allowed them to process CNP transactions, and states that “issuers have not consistently enabled single-message network for card-not-present transactions.” It’s important to note that issuers use several factors when deciding to enable certain payment networks, including current contractual term, payment network availability, payment network reliability, payment network security, varying payment network and chargeback liability rules, the availability and effectiveness of fraud detection and prevention tools, integration capabilities, and robust reporting.

Not all payment card networks are interchangeable and can be managed as if they were seamlessly interwoven. It is important for the issuer to have autonomy in selecting and enabling a payment network. This network evaluation and selection process is rigorous and expensive. It takes months to configure and stand up a network via a transaction processing platform, and years to refine the business processes so it can function optimally. Each payment card network has its own strengths and weaknesses, and it is the duty of the issuer (not the merchant) to make critical authorization decisions when allowing the customer to access their funds during the payment process. By requiring the use of single-message networks for CNP transactions, the Board’s amendment, as proposed, could have the unintended consequence of undermining the issuers’ critical decisions related to the rigorous network selection process and would place the cost and compliance burden squarely on the issuer. Without the ability to select only networks that meet the highest standards, issuers will no longer be able to ensure that their customers have an optimal payment experience. If issuers do not have the autonomy to do business with payment networks that meet the issuers’ standards, it will be more difficult for issuers to keep poorly engineered systems and bad actors at bay. Our interest in reducing fraud in the payments system could be thwarted by removing such options for mitigating controls. All participants, including consumers, could be harmed by that outcome.

Single-message networks have historically relied on the PIN as their primary means of cardholder verification and many have failed to invest in the infrastructure needed to prevent fraudulent PIN-less CNP transactions. As evidenced by the fact that more than half of fraud is attributed to CNP transactions, that infrastructure is necessary to protect consumers, issuers and merchants from the higher and rapidly increasing risks associated with CNP transactions. By requiring issuers to enable networks that are not prepared to adequately support all types of transactions, including CNP transactions, there is additional risk of fraud. This could also add stress to the payments system and to the consumers that could be negatively impacted when the predictability of the purchase process they have come to enjoy is disrupted. We believe that it’s important to fully consider the fraud risks associated with CNP transactions when processed by single-message networks.

For the above-mentioned reasons, we request the Board to consider withdrawing its changes that would identify CNP transactions as a “particular type of transaction” requiring two unaffiliated networks to be enabled. Alternatively, we ask the Board to consider confirming that any requirement to enable two unaffiliated networks does not supersede the issuers’ good faith efforts to mitigate risk, and/or establish standards to ensure the consistency of networks with regard to fraud prevention capabilities and chargeback liability rules.

2. The Board’s proposed language used to further clarify restrictions in 235.7(a)(2) introduces unintended consequences.

We believe that the wording in proposed paragraph 235.7(a)(2) is too broad and could be misinterpreted to require an unlimited routing requirement.

The proposal imposes a new substantive obligation on the issuer to ensure “at least two unaffiliated payment card networks” whenever a debit card can be used to process an electronic debit transaction. As explained in proposed comment 7(a) – 1, this issuer obligation must be “satisfied for every geographic area, specific merchant, particular type of merchant and particular type of transaction for which the issuer’s debit card can be used to process an electronic debit transaction.”

The proposal requires issuers to ensure that everywhere its debit cards can be used, every merchant will always be able to select among two debit card routing options. However, issuers have no way of knowing the networks selected by any given merchant, and those networks are subject to change without notification to the issuer. As a result, the issuer has no ability to ensure that there are two unaffiliated networks enabled for every specific merchant location where their debit cards might be used.

As written, the proposed rule holds issuers responsible for the actions of other parties, over which issuers have no control. For example, if a single retailer decided to stop using a certain network, all issuers that have enabled that network as their secondary, unaffiliated network would immediately become non-compliant, because that “specific merchant” would no longer have two choices to process electronic debit transactions. Issuers should not be required to enable their debit cards to be used on any and all networks preferred by merchants or to ensure that two unaffiliated networks are always available at every specific merchant location.

Likewise, as written, the proposed rule could be interpreted to mean that issuers will be required to support any and all point-of-sale configurations designed by merchants regardless of whether the payment solutions are reliable, secure and ubiquitous. This could create significant risk to the stability and effectiveness of the payments system.

We request that proposed § 235.7(a)(2) and supporting Commentary be withdrawn. At a minimum, the proposal should be revised to reflect that the issuers’ responsibilities do not extend to decisions and actions of other parties involved in the transaction which are outside the issuer’s control. In addition, the rule should clarify that the requirements for an issuer only apply to the extent that payment card networks and payment solutions meet the issuer’s criteria for safely and securely processing transactions.

3. References to future capabilities in the proposal could be subject to misinterpretation, generate on-going confusion, and produce a climate of uncertainty that puts the stability of the payment system at risk.

We have yet to understand the implications of future technology to the payments ecosystem. The proposed language, combined with the introduction of the ambiguous term “means of access” and

the unlimited routing requirement for issuers, (as described in point 2, above) is a unilateral interpretation of policy which adds technical complexity before payment methodologies are even conceived. This could inhibit or delay innovation and/or the enablement of new compliant technology in the payments system. If the rule is interpreted to require the inclusion of unproven and complex technologies, this would have the potential to increase levels of fraud and ultimately impair the payment system.

We strongly urge the Board to strike the language referring to future capabilities. At a minimum, we ask the Board to consider making it clear that any method of cardholder authentication or means of access must be proven secure and “approved or allowed by the issuer, at the issuer’s discretion”, and any means of access must be “issued in connection with a card or authorized by the issuer”.

4. The proposed rule is connected to consumer protections.

In its Regulatory Analysis, the Board states that the “proposed rule does not relate to consumer protections, and therefore the Board cannot, at this time, determine whether the benefits to consumers exceed the possible costs to financial institutions”. We believe that the proposed rule does relate to consumer protections.

Banks have a responsibility to ensure consumers can securely access their funds during the debit card payment process. The proposed rule could put consumers’ sensitive data at risk by requiring issuers to enable CNP transactions on networks with the fewest tools for data security and fraud protection. In addition, the proposal would require issuers to support unlimited routing and even capabilities that do not yet exist. The primary concern is an increase in fraud losses, the cost of which will be borne primarily by issuers as they contract with networks that did not meet issuer standards because they do not have the infrastructure, rules or tools to prosecute fraud-related disputes in a satisfactory manner. The ripple effect of that will be felt by consumers in higher cost of access to the payments system and increased stress caused by disruption of the payments dispute process.

While it’s true that consumers are “typically unaware” of how their transactions are being routed, they trust the bank as an issuer to act in their best interest when it comes to choosing safe and secure payment networks and partners. The “clarifying” language the Board uses in the proposed rule could have severe negative consequences, potentially impeding our ability to deliver on access to funds, payment speed, accuracy and reliability, card security services, fraud liability, and affordable account fees. With our current and prospective customer relationships at stake, we ask the Board to reconsider the consumer protection implications.

Conclusion

For the reasons stated above, we respectfully request the Board to consider withdrawing the proposal. Should the Board decide to move forward with the proposal, we request the Board consider the following:

1. Withdraw changes that would identify CNP transactions as a “particular type of transaction” requiring two unaffiliated networks to be enabled. Alternatively, confirm that any requirement to enable two unaffiliated networks does not supersede the issuers’ good faith efforts to mitigate risk,

and establish standards to ensure the adequacy and consistency of networks with regard to fraud prevention capabilities and chargeback liability rules.

2. We request that the all-encompassing language in proposed §235.7(a)(2) and supporting Commentary be withdrawn. At a minimum, the proposal should be revised to reflect that the issuers' responsibilities do not extend to decisions and actions of other parties involved in the transaction which are outside the issuer's control. In addition, the rule should clarify that the requirements for an issuer only apply to the extent that payment card networks and payment solutions meet the issuer's criteria for safely and securely processing transactions.
3. We request the Board strike the language referring to future capabilities and instead, address future innovations as they develop. At a minimum, we ask the language make clear that any method of cardholder authentication must be proven secure and "approved or allowed by the issuer, at the issuer's discretion", and any means of access must be "issued in connection with a card or authorized by the issuer".
4. We request that the Board reconsider the consumer protection issues related to the proposal.

The changes required by the proposal are significant and would take substantial time, effort and investment to implement. Issuers need time to implement system changes and renegotiate network contracts. Single-message networks need time to address security and fraud issues. Due to the complexity involved with implementing proposed changes, we request that any final rule be phased in gradually over at least three years.

Again, we appreciate the opportunity to comment on the proposed changes to Regulation II. Please contact me with any questions.

Sincerely,

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