

**Communication between Federal Reserve staff and
William Trezza at the Sacramento Regional Bankers Forum
September 9, 2010**

Participants: Steve Walker (Federal Reserve Bank of San Francisco) and
William Trezza (Bank of Agriculture and Commerce)

Summary: After presentations by Federal Reserve Bank of San Francisco staff at the Sacramento Regional Bankers Forum had concluded, William Trezza sought out Steve Walker to express some of his views regarding the interchange fee provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Act”). Mr. Trezza expressed his view that there should be no government interference in open-market pricing mechanisms. He also expressed his belief that the Act favors retailers over bankers. Additional details regarding Mr. Trezza’s views are provided in the attachment below.

Delivered Via Fax

June 14, 2010

Representative Gerry McNerney
Representative Dennis Cardoza
Representative John Garamendi

Re: Interchange Amendment

Dear Sirs:

I am personally writing to you as I represent a community bank in each of your districts which employs 135 people. The Interchange Amendment as proposed in the Senate version of Financial Reform is bad legislation, and I feel compelled to personally advise you why the House of Representatives should reject it. If the House feels that it would be imprudent to reject the amendment, then it should be removed from the bill and given thorough review and consideration. There are several meaningful issues which support my opinion, and I will share them below.

Congress initiated Financial Reform legislation for two reasons. One is to insulate the banking industry from future financial crises that may arise as a result of imprudent activities such as sub prime mortgage lending. The other is to protect consumers from the damage and/or fraud that occurred relative to irresponsible mortgage lending. Interchange fees were never considered relevant to the mortgage crisis, and are in fact a retail merchant issue, not a consumer issue. Our economy is a free market operation, and interchange functions in that mode. Having a government agency set pricing parameters is contrary to sound economic modeling. The retail merchant lobby which has initiated this proposal claims that it will generate a savings which can be passed on to the consumer. If the retailers and Senator Durban feel so strongly about the consumer, why doesn't the proposed regulation require the savings to be passed through. This is a rhetorical question to illustrate the lack of depth and clarity in the design of this amendment. Government interference in open market pricing mechanisms is bad policy.

Forgotten in the interchange dialogue is the fact that this payment process provides a great benefit to retail merchants...instant delivery of cash via use of the card and the interchange payment system. Visa, MasterCard, and the banking industry have invested enormous amounts of capital to provide an expedient and convenient process to enable consumers to fulfill needs and let merchants run their businesses efficiently. Just recall how critical the payment system was when airplanes sat on the tarmac and checks did not reach their intended destinations after September 11, 2001. So critical that Fed and Treasury implemented "Check 21".

There is an exemption for community banks such as that relating to the CFPB. That is a wonderful gesture, however it will not work. For one the payment system does not recognize the class or size of a paying bank. It only recognizes if the funds are available and where the payment should be applied. Even if such a determination could be made, it would create a split playing field with larger institutions having superior pricing because of volumes and efficiencies. Retailers would certainly gravitate to the lesser cost and the purpose of the community bank exemption would be defeated. The authors of this amendment did not research the subject adequately, nor did they confer with the banking industry for its advice and consent.

The banking industry absorbs large losses each year on debit card transactions because of the consumer protections provided by Regulation E. Banks receive a portion of the interchange fees collected from merchants. A significant reduction in interchange income would force many banks to eliminate this service because the margins would be thin or non-existing. The only alternative to offsetting losses would be to assess fees on bank customers which is contrary to the purpose of this amendment.

I am hopeful that the insights of a local businessman will convince you and your colleagues that the Interchange Amendment is fraught with weaknesses and contradictions and does not belong in the final Regulatory Reform bill. I intend to copy this letter to the entire California Congressional membership with the hope that the House will give this matter serious attention. Thank you for your service and please feel free to contact me or the California Independent Bank Association with any questions you may have.

Sincerely,

William R. Trezza
Chief Executive Officer

cc: California Independent Bankers Association
California Bankers Association
California House Membership