

**Supporting Statement for the
Recordkeeping and Disclosure Requirements Associated with Regulation II
(FR II; OMB No. 7100-0349)**

Summary

The Board of Governors of the Federal Reserve System (Board), under authority delegated by the Office of Management and Budget (OMB), proposes to extend for three years, without revision, the Recordkeeping and Disclosure Requirements Associated with Regulation II (FR II; OMB No. 7100-0349). Regulation II – Debit Card Interchange Fees and Routing (12 CFR Part 235) implements, among other things, standards for assessing whether interchange transaction fees for electronic debit transactions are reasonable and proportional to the cost incurred by the issuer with respect to the transaction, as required by section 920(a) of the Electronic Fund Transfer Act (EFTA) (15 U.S.C. § 1693o-2(a)).

Regulation II limits the interchange transaction fee that covered issuers (issuers that, together with affiliates, have assets of \$10 billion or more) can charge for electronic debit transactions. Under the rule, a covered debit card issuer is allowed to receive or charge an interchange transaction fee in the amount of 21 cents plus 5 basis points multiplied by the value of the transaction. In addition, a covered issuer may receive or charge an amount of no more than 1 cent per transaction (the “fraud-prevention adjustment”) for the costs associated with preventing fraudulent electronic debit transactions (fraud-prevention adjustment) if the issuer complies with the standards and requirements set forth in the rule. In addition to these interchange fee provisions, Regulation II prohibits any issuer (i.e., not just covered issuers) or payment card network from directly or indirectly restricting the number of payment card networks on which an electronic debit transaction may be processed to less than two unaffiliated networks, and from directly or indirectly inhibiting the ability of a merchant to direct the routing of electronic debit transactions for processing over any payment card network that may process such transactions. Finally, Regulation II prohibits any issuer from receiving net compensation from a payment card network with respect to electronic debit transactions or debit card-related activities within a calendar year.

Debit card issuers must retain records demonstrating their compliance with the requirements in Regulation II for at least five years after the end of the calendar year in which the electronic debit transaction occurred. In addition, any person (including an issuer or payment card network) subject to an investigation or enforcement proceeding involving Regulation II must retain records pertaining to the matter until the final disposition of the matter, unless an earlier time is allowed by court or agency order.¹ The Paperwork Reduction Act (PRA) classifies reporting, recordkeeping, or disclosure requirements of a regulation as an information collection.

¹ In addition, section 920(a)(3)(B) of the EFTA requires the Board to disclose aggregate or summary information, at least every two years, concerning the costs incurred, and interchange transaction fees charged or received, by issuers or payment card networks in connection with the authorization, clearance or settlement of electronic debit transactions as the Board considers appropriate and in the public interest. Thus, sections 235.8(a) and (b) of Regulation II impose a reporting requirement compelling the submission of information to the Federal Reserve (12 CFR 235.8(a) and (b)) and this reporting requirement is implemented in the form of two surveys collected by the Board (FR 3064a and FR 3064b; OMB 7100-0344). However, the reporting requirement contained in sections

The estimated total annual burden for the FR II is 22,294 hours.²

Background and Justification

Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act),³ which was enacted on July 21, 2010, amended the EFTA by adding a new section 920 regarding interchange transaction fees and rules for debit card transactions (15 U.S.C. § 1690-2).

Subsection 920(a)(3) of the EFTA requires the Board to prescribe regulations establishing standards for assessing whether the amount of any interchange transaction fee charged or received by a covered issuer is reasonable and proportional to the costs incurred by the issuer with respect to the transaction. Section 920(a)(5)(B) authorizes the Board to prescribe regulations to establish standards for the fraud-prevention adjustment. Section 920(a)(8)(C) authorizes the Board to prescribe regulations to ensure that a network fee is not used to directly or indirectly compensate an issuer with respect to an electronic debit transaction, and is not used to circumvent or evade the restrictions of EFTA section 920(a). Section 920(b)(1)(A) requires the Board to prescribe regulations providing that an issuer or payment card network shall not directly or indirectly restrict the number of payment card networks on which an electronic debit transaction may be processed to fewer than two unaffiliated networks. Section 920(b)(1)(B) requires the Board to prescribe regulations providing that an issuer or payment card network shall not directly or indirectly inhibit the ability of merchants to direct the routing of electronic debit transactions for processing over any payment card network that may process such transactions.

On July 20, 2011, the Board implemented the information collection requirements contained in section 235.4 and section 235.8 of Regulation II.⁴ The recordkeeping standards in

235.8(a) and (b) is not the subject of this PRA submission, as the FR 3064a and FR 3064b surveys are separately reviewed and accounted for under the PRA.

² An entity's primary federal financial regulator is authorized to enforce compliance with the requirements of Regulation II (15 U.S.C. §§ 1693o(a) and 1693o-2(d); 12 CFR 235.9). However, for purposes of the PRA, the Board is estimating the burden of complying with the recordkeeping and disclosure requirements of Regulation II for the estimated 527 entities subject to the enforcement authority of the Board, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, and National Credit Union Administration (collectively, the federal banking agencies). Such entities may include, among others, state member banks, national banks, insured state nonmember banks, savings associations, branches and agencies of foreign banks, commercial lending companies owned or controlled by foreign banks, and organizations operating under section 25 or 25A of the Federal Reserve Act, and federally-chartered credit unions, if the entity issues a debit or credit card or authorizes the use of a debit card to perform an electronic debit transaction, and has consolidated assets of \$10 billion or more (hereinafter, issuers). The interchange transaction fee limitations, including the fraud-prevention adjustment, do not apply to (1) interchange fees charged or received by an issuer with assets of less than \$10 billion together with its affiliates, (2) electronic debit transactions made using debit cards issued pursuant to a government-administered payment program and (3) electronic debit transactions made using certain general-use, reloadable prepaid cards (12 CFR 235.5).

³ See Pub. L. No. 111-203, 1075, 124 Stat. 1376, 2068-74 (July 21, 2010).

⁴ See 76 FR 43394 (July 20, 2011) (adopting section 235.8 of Regulation II); 76 FR 43478 (July 20, 2011) (adopting section 235.4 of Regulation II as an interim final rule). On August 3, 2012, the Board adopted section 235.4 of Regulation II as a final rule, making various changes to the interim final rule. See 77 FR 46258 (August 3, 2012).

Regulation II help to promote compliance with its underlying substantive requirements. This information is not available from other sources.

Description of Information Collection

Sections 235.4(b)(1) and (2) – Develop and Implement Fraud-Prevention Policies and Procedures (fraud-prevention recordkeeping requirement). Section 235.4(b)(1) requires that, in order to be eligible to receive or charge the fraud-prevention adjustment, a covered issuer must develop and implement policies and procedures reasonably designed to take effective steps to reduce the occurrence of, and costs to all parties from, fraudulent electronic debit transactions, including through the development and implementation of cost-effective fraud-prevention technology. Specifically, section 235.4(b)(2) requires that a covered issuer's fraud-prevention policies and procedures address the following:

- Methods to identify and prevent fraudulent electronic debit transactions;
- Monitoring of the volume and value of its fraudulent electronic debit transactions;
- Appropriate responses to suspicious electronic debit transactions in a manner designed to limit the costs to all parties from and prevent the occurrence of future fraudulent electronic debit transactions;
- Methods to secure debit card and cardholder data; and
- Such other factors as the issuer considers appropriate.

Section 235.4(b)(3) – Review and Update Fraud-Prevention Policies and Procedures (fraud-prevention recordkeeping requirement). Section 235.4(b)(3) requires that a covered issuer must review its fraud-prevention policies and procedures, and their implementation, at least annually, and update them as necessary in light of:

- Their effectiveness in reducing the occurrence of, and cost to all parties from, fraudulent electronic debit transactions involving the issuer;
- Their cost-effectiveness; and
- Changes in the types of fraud, methods used to commit fraud, and available methods of detecting and preventing fraudulent electronic debit transactions that the covered issuer identifies from:
 - Its own experience or information;
 - Information provided to the issuer by its payment card networks, law enforcement agencies, and fraud-monitoring groups in which the issuer participates;
 - Applicable supervisory guidance.

Sections 235.4(c) and (d) – Annual Fraud-Prevention Compliance Notification and Change-in-Status Notification (fraud-prevention disclosure requirements). Section 235.4(c) requires that, to be eligible to receive or charge a fraud-prevention adjustment, a covered issuer must annually notify its payment card networks that it complies with the standards under section 235.4(b). Section 235.4(d) requires, no later than 10 days after a covered issuer determines or receives a notification from the appropriate agency under section 235.9 that the covered issuer is substantially non-compliant with the standards set forth in section 235.4(b), a covered issuer must notify its payment card networks that it is no longer eligible to receive or charge a fraud-

prevention adjustment. The covered issuer must stop receiving and charging the fraud-prevention adjustment within 30 days after providing such notification to its payment card networks.

Section 235.8(c) – General Compliance Records Retention (general recordkeeping requirements). Section 235.8(c)(1) requires that any debit card issuer subject to Regulation II (i.e., not just covered issuers) shall retain evidence of compliance with the requirements in Regulation II for a period of not less than five years after the end of the calendar year in which the electronic debit transaction occurred. In addition, section 235.8(c)(2) requires that, where any person subject to Regulation II (e.g., an issuer or payment card network) receives actual notice that it is subject to an investigation by an enforcement agency, they must retain the records until final disposition of the matter. Compliance with this general recordkeeping requirement involves retaining records to demonstrate fulfillment of the other requirements in Regulation II. The burden associated with generating the records that must be retained under this general recordkeeping requirement have already been accounted for under other information collection requirements. In particular FR 3064a requires debit card issuers to submit summary data regarding its debit card transactions each year. The incremental burden (not already accounted for under other information collection requirements) associated with retaining these generated records is minimal.

Respondent Panel

The FR II panel comprises state member banks, national banks, insured nonmember banks, savings associations, and federally-chartered credit unions.

Time Schedule for Information Collection

The recordkeeping requirement associated with the initial development and implementation of fraud-prevention policies and procedures under section 235.4(b)(1) and (2) of Regulation II occurs on a one-time basis. The recordkeeping requirement associated with an issuer's ongoing review and implementation of its fraud-prevention policies and procedures under section 235.4(b)(3) occurs on a continuous basis and must occur at least annually. Documentation associated with these fraud-prevention recordkeeping requirements is maintained by each issuer; therefore, such records are not collected or published by the Federal Reserve System.

The fraud-prevention compliance notification required under section 235.4(c) must be provided by an issuer to its payment card networks annually. The fraud-prevention change-in-status notification required under section 235.4(d) is event-generated and must be provided by an issuer to its payment card networks within 10 days of the issuer determining on its own, or receiving notification from the appropriate federal banking agency, that the issuer is substantially non-compliant with the standards set forth in section 235.4(b). These fraud-prevention disclosures are not collected or published by the Federal Reserve System.

The general recordkeeping requirement in section 235.8(c)(1) of Regulation II requires issuers to retain records that demonstrate compliance with the requirements of Regulation II for not less than five years after the end of the calendar year in which the electronic debit transaction occurred. Section 235.8(c)(2) states that if an issuer or payment card network receives actual

notice that it is subject to an investigation by an enforcement agency, such person shall retain the records until final disposition of the matter, unless an earlier time is allowed by court or agency order. Documentation associated with these general recordkeeping requirements is maintained by each issuer or payment card network; therefore, such records are not collected or published by the Federal Reserve System.

Public Availability of Data

There is no data related to this information collection available to the public.

Legal Status

The Recordkeeping and Disclosure Requirements Associated with Regulation II are authorized by section 920(a)(3) of the EFTA.⁵ The fraud-prevention and disclosure requirements are additionally authorized by section 920(a)(5) of the EFTA.⁶ Regulation II's general recordkeeping requirement for issuers is mandatory. Regulation II's fraud-prevention recordkeeping requirements and disclosure requirements are required to obtain a benefit.

The Recordkeeping and Disclosure Requirements Associated with Regulation II are generally not submitted to the Board or to any of the federal financial regulatory agencies. In the event that the Board obtains such information, it may be kept confidential under exemption 4 of the Freedom of Information Act (FOIA) to the extent that it contains commercial or financial information both customarily and actually treated as private.⁷ If such information is obtained through the examination or enforcement process, it may be kept confidential under exemption 8 of the FOIA.⁸

Consultation Outside the Agency

There has been no consultation outside the Federal Reserve System.

Public Comments

On December 3, 2021, the Board published an initial notice in the *Federal Register* (86 FR 68667), requesting public comment for 60 days on the extension, without revision, of the FR II. The comment period for this notice will expire on February 1, 2022.

Estimate of Respondent Burden

As shown in the table below, the estimated total annual burden for the FR II is 22,294 hours. The number of respondents is based on the Board's list of debit card issuers that have

⁵ 15 U.S.C. § 1693o-2(a)(3) (authorizing the Board to prescribe regulations regarding interchange transaction fees and require issuers or payment card networks to provide to the Board such information as deemed necessary).

⁶ 15 U.S.C. § 1693o-2(a)(5) (permitting the Board to allow for the fraud-prevention adjustment and condition it upon compliance with fraud-related standards promulgated by the Board).

⁷ 5 U.S.C. § 552(b)(4).

⁸ 5 U.S.C. § 552(b)(8).

assets, together with their affiliates, of \$10 billion or more, and thus are covered issuers. The list is generated from the set of institutions in existence on December 31, 2020, according to available data.

While the Board does not anticipate many, if any, new covered issuers, it is estimated that there may be one per year, and that each new issuer would take, on average, 160 hours (i.e., one month) to develop and implement the fraud-prevention policies required by section 235.4(b)(2), and to train staff to comply with the recordkeeping provisions under section 235.4(b)(2) and 235.8(c) of Regulation II. Thus, the one-time initial burden for one new covered issuer is estimated to be 160 hours (total).

These recordkeeping and disclosure requirements represent less than 1 percent of the Board's total paperwork burden.

FR II	<i>Estimated number of respondents⁹</i>	<i>Annual frequency</i>	<i>Estimated average hours per response</i>	<i>Estimated annual burden hours</i>
Recordkeeping				
Section 235.4(b)(2) Implement policies and procedures (one-time)	1	1	160	160
Section 235.4(b)(3) Review and update policies and procedures	527	1	40	21,080
Section 235.8(c) General recordkeeping	527	1	1	527
Disclosure				
Sections 235.4(c) and (d) Annual notification and change in status	527	1	1	<u>527</u>
<i>Total</i>				22,294

The estimated total annual cost to the public for these collections of information is \$1,318,690.¹⁰

⁹ Of these respondents, none are considered small entities as defined by the Small Business Administration (i.e., entities with less than \$600 million in total assets), <https://www.sba.gov/document/support-table-size-standards>.

¹⁰ Total cost to the public was estimated using the following formula: percent of staff time, multiplied by annual burden hours, multiplied by hourly rates (30% Office & Administrative Support at \$20, 45% Financial Managers at \$73, 15% Lawyers at \$72, and 10% Chief Executives at \$95). Hourly rates for each occupational group are the (rounded) mean hourly wages from the Bureau of Labor and Statistics (BLS), Occupational Employment and Wages May 2020, published March 31, 2021, www.bls.gov/news.release/ocwage.t01.htm. Occupations are defined using the BLS Occupational Classification System, www.bls.gov/soc/.

Sensitive Questions

These collections of information contain no questions of a sensitive nature, as defined by OMB guidelines.

Estimate of Cost to the Federal Reserve System

The estimated cost to the Federal Reserve System for collecting and processing this information collection is negligible.