



February 22, 2011

*Via Electronic Mail (submitted via Federal e-rulemaking portal)*

Jennifer J. Johnson, Secretary  
Board of Governors of the Federal  
Reserve System  
20th Street & Constitution Avenue, N.W.  
Washington, DC 20551.

**Re: Proposed Regulation II; Docket No. R-1404 and RIN No. 7100 AD63**

Dear Ms. Johnson:

This comment letter is submitted by Boku, Inc. ("Boku") in response to the Board of Governors of the Federal Reserve System's ("Board") request for comment on its proposed rule on Debit Card Interchange Fees and Routing identified by RIN No. 7100 AD63 ("Regulation II"). Regulation II was published in the Federal Register on December 28, 2010 at 75 Fed. Reg. 81722-81763 and implements Section 1075 of the Dodd-Frank Act to add a new section 920 to the Electronic Funds Transfer Act ("Durbin Amendment") regarding interchange fees and rules for payment card transactions.

Boku appreciates the opportunity to comment on this important subject. As a pioneer in the area of mobile payments, Boku plays an important role in advancing payment products and technologies. Boku's goal is to create a bank-grade mobile payments platform which provides a trusted, viable and accessible market for consumers, merchants and carriers. Based in San Francisco with offices in Europe and Asia, Boku currently reaches more than 2 billion consumers worldwide. Boku's founders include several pioneers in the emerging payment systems market, including the founders of Accept.com, one of the first successful internet payment startup companies. While Accept.com was eventually acquired by Amazon.com, the role that Boku's founders played in that startup enabled Boku to secure critical venture capital funding from five major venture capital firms.

Given its commitment to innovation in the payments industry, Boku hopes that its comment will serve to inform the Board's drafting of a final rule which excludes emerging payments systems from its coverage so as to allow such systems to evolve and mature before subjecting them to a host of regulations which present a very real risk of stifling their development. Drafting otherwise would undermine one of the primary objectives of the Durbin Amendment, namely, to improve and strengthen competition in the payments industry, which will ultimately benefit consumers by providing better and less costly payment alternatives.

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In pursuing his amendment, it is our view that Senator Durbin was clearly focused on the issuance and use of plastic debit cards by the four largest payment networks and, particularly, the two largest networks that currently account for approximately 75 to 80 percent of the debit market. In fact, the Board's surveys that helped inform the drafting of Regulation II also targeted these networks. This point, alone, highlights the dichotomy between traditional and emerging payment systems. While broader definitions of "payment card network" and "electronic debit transactions" would include emerging payment systems and transactions within emerging payment systems, respectively, we believe, based on the ample legislative history of the Durbin Amendment that this was never intended. Rather, the amendment's author and numerous supporting Members were focused on regulating networks and transactions in which small businesses and other merchants have no market power to negotiate the fees for the services they desperately require to continue to operate their businesses. Thus, we believe it is critical that the Board take the time and dedicate the resources to determine how to distinguish the networks clearly targeted by the Durbin Amendment versus emerging and other non-traditional networks, the existence and growth of which, will further the purpose of the Durbin Amendment.

In particular, we encourage the Board to further study how to exclude emerging payment systems from coverage of Regulation II. In the interim, we note that it is entirely appropriate for the Board to apply a narrow definition of the terms "payment card network" and "electronic debit transactions" consistent with the use of debit cards as generally understood in the marketplace, and the amendment's legislative history, as described more fully below. In this regard, this letter is in response to the following request for comment by the Board:

"The Board requests comment on whether other non-traditional or emerging payment systems would be covered by the statutory definition of 'payment card network.' For example, consumers may use their mobile phone to send payments to third parties to purchase goods or services with the payment amount billed to their mobile phone account or debited directly from the consumer's bank account. In addition, consumers may use a third party payment intermediary, such as PayPal, to pay for Internet purchases, using the consumer's funds that may be held by the intermediary or in the consumer's account held at a different financial institution. In both examples, the system or network used to send the payment arguably provide the 'proprietary services, infrastructure, and software for authorization, clearance, and settlement of electronic debit transactions.' Transactions involving these methods of payment typically are subject to rules and procedures established by the payment system. If such systems are not covered, the Board requests specific comment on how it should appropriately distinguish these payment systems from traditional debit card payment systems that are subject to the rule."

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## **I. Overview of Boku**

Boku's mission is to provide innovative alternative payment services to merchants and consumers in emerging and fast growing markets that did not exist when conventional debit systems were launched. Boku's alternative services, present and planned, focus on the special operating and marketing measures required to enable mobile phone users to purchase virtual and digital goods directly from their phones. In every sense of the concept, Boku is an "emerging payment system."

Boku's payment services are currently offered primarily to online merchants. These services permit the customers of online merchants to purchase virtual goods and services (e. g., those utilized by the customer in its participation in online games, such as FarmVille) through the use of their mobile phone. Currently, these online merchants typically offer online games that sell either (a) access to certain aspects of those games, or (b) digital or virtual goods or virtual currency that can be used to purchase digital or virtual goods. However, online merchants can include companies providing other types of digital goods or content - an important area of development for Boku in which we anticipate numerous opportunities and possibilities in the coming years.

Finally, from a consumer perspective, Boku is uniquely positioned to provide payment services to certain consumers not being adequately served by existing traditional payment networks. In particular, Boku's system provides the opportunity to reach consumers who are currently unbanked or underbanked and do not otherwise have access to a checking account, a branded payment card, or other traditional means to pay.

## **II. The Legislative Intent of the Durbin Amendment is to Increase Competition within the Payments Industry to Provide More Payment Options to Small Businesses**

Subjecting non-traditional and emerging payment systems to the Board's implementation of the Durbin Amendment under Regulation II would perpetuate the very problems that the Durbin Amendment was intended to address - lack of any meaningful competition resulting in too much market power concentrated in too few companies, a theme that was repeated throughout the Senate debates by the amendment's sponsor, Senator Durbin, and other Members. In discussing the legislative intent of the provisions of the Durbin Amendment during the Senate's consideration of the Conference Report for the Dodd-Frank legislation, Senator Durbin stated:

It should be noted that the intent of my amendment is not to diminish competition in the debit issuance market. I will be watching closely to ensure that the giant payment card networks Visa and MasterCard do not collude with one another or with large financial institutions to take steps to purposefully disadvantage small issuers in response to enactment of this amendment.

Senator Durbin was particularly concerned about the dominant market power of traditional payment systems to dictate their terms to those using and participating in these networks due to the lack of adequate competition in the payments industry. In his descriptions and statements on the amendment, market power and the lack of competition- and the resulting lack of market factors constraining the price of interchange fees - were often repeated themes. In a floor statement discussing opposition by credit unions and community banks to his amendment, Senator Durbin noted, "It is an indication to all of us of the power of these credit card companies to terrorize credit unions and community banks. They have become the messengers of the big banks and credit cards to kill the amendment we passed in the Senate." He further stated, "This duopoly, this power in the market, this ability to terrorize credit unions and small banks is an indication of too much power and too little competition." Finally, in the same statement he concluded, "It is obvious what is going on: Visa and MasterCard are making threats if this amendment becomes law, they will use their market power against small banks by voluntarily lowering their interchange rates."

As is evident in numerous other statements from its sponsor, the Durbin Amendment's real focus on market power and lack of competition is aimed at the impact of interchange fees and, specifically, at the lack of bargaining power - owing to too little competition - on small businesses. For example, in one discussion of the amendment on the Senate floor, Senator Durbin notes, "Unfortunately, over the years, small businesses across America have had little or no bargaining power with the major credit card companies." Also during this statement, the Senator comments, "Why would we give a monopoly - a virtual monopoly - situation here, where two major credit card companies can impose rules on small businesses which are so costly to them?" He further notes, "Visa and MasterCard - which control 80 percent of the debit market - set the debit interchange fee rates that apply to all banks within their networks." Finally, Senator Durbin observed, "Visa and MasterCard do not allow banks to compete with one another or negotiate with merchants over interchange rates, and there is no constraint on Visa's and MasterCard's ability to fix rates at unreasonable levels."

Lack of competition and too much consolidated market power are themes in numerous other statements on the Durbin Amendment. In one instance, Senator Durbin raised concerns that "These Visa and MasterCard credit card companies have reached the point where they have so much power and virtually no competition..." That same day, Senator Whitehouse rose in support of the amendment and noted, "It protects small businesses and consumers from gouging by the credit card companies and the monolithic monopoly power they bring to bear." In another statement on the amendment, Senator Durbin noted at length:

In a normal market, you see banks competing with one another to do business with the restaurants, shops, and the merchants. With that competition, things would be a lot better. But, in fact, the real world of credit cards with the two giants, Visa and MasterCard, is a world where there is little or no competition.

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The credit card and debit card markets are not normal. Visa and MasterCard unilaterally set interchange fee rates that apply to all banks within their card networks. There is no negotiation between the banks and merchants over reducing interchange rates. Individual businesses in New Hampshire, Illinois, New York, and all across America have no bargaining power with these giant credit card companies. They set the rules, they fix the fees, take it or leave it.

Visa and MasterCard have every incentive to continue to raise interchange fees because that additional revenue makes it more likely that banks will issue more cards.

What can businesses do to stop these rising interchange fees? Almost nothing.

In requesting comment on whether other non-traditional or emerging payment systems should be covered by the statutory definition of “payment card network,” the Board is presented with the issue of whether the statutory reference to “proprietary services, infrastructure, and software for authorization, clearance, and settlement of electronic debit transactions” should be narrowly or broadly construed. We respectfully submit that the appropriate construction is the one supported by the legislative intent of the drafter. In this regard, the legislative history of the Durbin Amendment is replete with a multitude of references suggesting the appropriate course of action for the Board is a narrow construction targeted precisely at the problem the amendment was intended to address - lack of competition and too much concentrated market power. In contrast, a broad construction that includes non-traditional and emerging payment systems undermines the very purpose the amendment was intended to address. Including non-traditional and emerging payment systems within the definition of “payment card network” will actually benefit traditional payment systems vis-à-vis their non-traditional counterparts by preserving their existing competitive advantages and effectively maintain the “status quo.” While distinguishing non-traditional and emerging payments systems from traditional payment systems presents certain interpretive challenges, we believe that this must be done for the Board’s rule to be consistent with the intent of the Durbin Amendment’s architect and sponsor, as well as the numerous Members that supported the amendment.

In sum, the legislative history of the Durbin Amendment provides a compelling case for excluding non-traditional and emerging payment systems from coverage of the Board’s implementation of the Durbin Amendment in Regulation II. Failing to exclude non-traditional and emerging payment systems will only serve to undermine rather than further the legislative intent of the amendment’s sponsor, Senator Durbin, and the many other Members supporting his amendment. Excluding non-traditional and emerging payment systems from coverage under Regulation II will inure to the benefit of small businesses by fostering the development of payment alternatives that will ultimately help to provide a more level playing field for competitive pricing of payment services. At the same time, it will provide access to payment options to unbanked and underbanked consumers who cannot access existing traditional payments networks. Based on the

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legislative history of the Durbin Amendment, Boku believes that emerging payment systems, in particular, must be excluded from the definition of payment card networks under Regulation II.

### **III. Subjecting Emerging Payment Systems to Regulation II Would Stifle Innovation**

The Board has historically refrained from regulating emerging industries out of concern that premature regulation of such industries could stifle their development and innovation. Instead, the Board has typically waited to regulate such industries until they mature and the Board has a better understanding of their operations and economics. For instance, in the interim final rule regarding payroll cards, the Board opted to exclude the coverage of general purpose reloadable cards from the definition of account by recognizing that “coverage of such products could impede the development of other card products generally” and that “the Board will continue to monitor the development of other card products and may reconsider Regulation E coverage as these products continue to develop.” Regulation II, as it currently stands, would capture a part of the payments industry that is very much in its infancy and the regulation of which, without a better knowledge and understanding of its economics and operation, could stifle innovation and perpetuate the existing market power of the traditional payment networks. As noted above, it may also result in curtailing access to payments options to unbanked and underbanked consumers who cannot access existing traditional payments networks.

If added to the existing substantial barriers to entry that alternative payment providers like Boku already grapple with, the Durbin Amendment’s limits on Interchange Transaction Fees and Alternative Routing requirements would severely stifle market entry and sustained growth of creative and innovative solutions provided by emerging payment systems. Excluding emerging payment from the coverage of these provisions, however, would strongly support the purposes of the Durbin Amendment by providing more payment choices for merchants and their customers. Such exclusion will also further the goal cited by Chairman Bernanke in the Board’s public meeting to do “all we can to preserve the dynamism, competition and innovation in payments....” Fostering competition and innovation in the market for consumer services has been a recurrent theme in the Board rulemakings. For example, regarding implementation of Title IV of the Credit CARD Act, the Board noted “[t]he Board seeks comment regarding any approaches or solutions that could avoid potential impediments to innovation while still providing consumers clear and conspicuous disclosures.” Recognizing that the Board is tasked with staying true to the Congressional mandate in the Durbin Amendment, we note that the exclusion of emerging payment systems from the restrictions applicable to payment card networks is entirely consistent with the intent of Senator Durbin to improve competition for payment services by providing more choices for small businesses, other merchants and their customers.

### **IV. Emerging Payment Systems Provide a Market-Driven Solution for Dysfunctions in the Payments Market**

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Subjecting emerging payment systems to Regulation II would be counter-productive as it would constrain the development and proliferation of systems that create competition in an industry lacking meaningful competition. Emerging payment systems creating new ways to pay for goods and services hold promise for delivering value to merchants and consumers in a way that is both economical and convenient. However, these systems are emerging in ways that do not fit the assumptions underlying the Durbin Amendment. The Board's question regarding how emerging alternative payment services may be distinguished from traditional debit card systems under Regulation II poses a dilemma for alternative services (as well as for the Board in its regulatory role). Since the services sought to be excluded are by definition "emerging," their defining characteristics and resulting economics are not yet clearly known. A narrow definition of emerging or alternative payment services would inherently limit innovation as developing services try to fit their offerings into the definition instead of focusing on the needs of merchants and consumers. In our view, this would be a glaring weakness in an effort largely focused on increasing competition for payment services.

Senator Durbin's remarks throughout the Senate's deliberations suggest that the exclusion of emerging payment systems from the application of Regulation II would best serve the legislative intent. For example, in a Senate hearing on June 16, 2010, Senator Durbin noted, "Given the card companies' enormous market power and the rigid operating rules that they unilaterally mandate, it is extremely difficult for those who accept their cards, including the federal government, to influence how much Visa and MasterCard will make them pay." This legislative history makes it clear that the Durbin Amendment was aimed at the Visa and MasterCard four-party systems and the well-established American Express and Discover Card three-party systems. These systems in their traditional form are identified as those in which the interchange transaction fees are not constrained by market factors.

In contrast, emerging payment systems like Boku cannot force merchants to accept any aspect of their service. Instead, as a new market entrant, Boku can only gain acceptance with merchants and customers by continuously providing flexibility in its pricing and operating procedures. In other words, merchants have bargaining power because they do not view Boku as essential to market survival. This willingness and ability to adapt nimbly to its customers' needs and market forces is essential to the success of emerging payment systems like Boku. Moreover, by offering a payment means that can be conveniently integrated with the digital goods and services construct of existing online merchants, emerging payment players like Boku enable a tremendous expansion of existing lines of commerce, including currently unbanked and underbanked consumers. By intervening here, the Board may risk blocking the entry of other market players seeking to create alternative solutions not currently available in the payment industry. Boku, like other emerging alternative payment providers, seeks to overcome the "substantial barriers to entry" cited by Governor Raskin, and thereby improve competition in "a market that is working less than competitively."

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**V. Merchants View Emerging Payment Systems as an Attractive Competitive Alternative to Mainstream Debit**

In the view of Senator Leahy, the fundamental purpose of the Durbin Amendment was “to protect our small businesses from complicated predatory rules that big credit card companies could otherwise impose on [small businesses such as] Vermont grocers and convenience stores.” The same rationale was articulated by Senator Reed, who stated, “I am pleased that the [Dodd-Frank] legislation includes provisions from the Durbin amendment that will protect small business from unreasonable credit card company fees by requiring the Federal Reserve to issue rules ensuring that fees charged to merchants by credit card companies for debit card transactions are both reasonable and proportional to the cost of processing those transactions.” In the words of Senator Durbin, his amendment is entirely about improving competition and he specifically recognized that, “while [the] amendment will bring much-needed reform to the credit card and debit card industries, in no way should enactment of [the] amendment be construed as preempting other crucial steps that must be taken to bring competition and fairness to those industries.” Thus, the Board is tasked with implementing a law, based on its ample and clearly-stated legislative intent, that encourages competition in the payments industry and thereby provides more and better payment options for small businesses, merchants and consumers.

Merchants are extremely receptive to alternative payment options outside of traditional debit networks, particularly if the alternatives allow them to access a different mechanism for payment and a different target market. Merchants recognize that very few, if any, systems can provide such access and consequently merchants have willingly entered into agreements with companies like Boku that provide an attractive alternative to mainstream debit by opening up additional lines of commerce (i.e., mobile payments) and market segments (i.e., users of mobile payments which do not have access to traditional methods of payment, including unbanked and underbanked consumers).

Boku’s alternative payment service, like most emerging payment services, is not subject to the two-sided market structure that has increased pricing to merchants in four-party systems. In four-party systems, networks compete with each other for banks to issue cards in their networks, which causes upward pressure on compensation to issuers, much of which translates into interchange fee costs that acquirers routinely pass on to merchants. Emerging payment systems such as Boku will have to be particularly mindful of value delivered to merchants, because if they do not deliver additional value to merchants, their pricing to merchants will be constrained by the regulation of interchange fees in mainstream systems. Simply stated, if emerging alternative payment systems do not deliver more and better value to merchants, such as improved services or different customers, merchants will not pay more than they are currently paying for traditional systems.

In sum, evolving services provided by emerging payment systems offer alternative value propositions to merchants, promote competition, and fill specialized needs of a growing and potentially large market. Ultimately, the success of these non-

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traditional and emerging payment systems will allow for operating efficiencies and economies of scale that will drive down the cost of payments services to small businesses and merchants, and thereby benefit consumers.

**VI. Emerging Payment Systems are Distinguishable from Traditional Payment Systems Because Unaffiliated, Alternative Networks Often Do Not Exist for Emerging Payment Systems**

Compliance with Regulation II could potentially halt the operations of certain emerging payments systems for which alternative, unaffiliated routing networks do not exist. If the restrictions under proposed Section 235.7 were applied to an emerging payment system, debit cards issued by such network would be required to be capable of being routed through at least one unaffiliated payment card network in addition to the emerging payment network that issued the card (or analogous product covered by the definition of debit card). By definition, emerging payment systems are new and unique and are often the first of their kind in a particular industry. To require such systems to license alternative network providers to route transactions would require such systems to come to a standstill until a viable alternative network enters the market. Moreover, even if a potential licensee were to enter the market, there is no guarantee that such a licensee would be willing or able to dedicate resources and make investments that are necessary to support a parallel service, especially one that may have to continually evolve to offer merchants and consumers an attractive alternative value proposition.

Emerging payment services such as those offered by Boku usually require specialized network delivery systems in order to deliver truly innovative services. Innovation would be constrained by the need to develop and/or support an alternative network infrastructure. For example, an emerging payment service could be forced to license its technology to another network in order to provide an alternative processing path. Even in unusual situations where an alternative network can process today's innovative, emerging payment service, the alternative network is unlikely to keep pace with the development of the alternative service's processing requirements to introduce or refine emerging services. Either arrangement would cede control of the pace and nature of the product development to the alternative network provider. Furthermore, there is no indication that an alternative network would accept a license and invest in providing an alternative routing capability. Most concerning is that this creates the possibility that a traditional payment system could opt to fill the void by paying in to compete and, in effect, co-opt the innovative efforts of an emerging payment network.

Notwithstanding the foregoing, there are additional challenges presented by such a requirement, for example, licensing parallel unaffiliated networks would impair the ability to obtain investment financing because of (i) required disclosure of proprietary technology and planned enhancements and market strategies; (ii) loss of uniqueness; and (iii) loss of flexibility to meet market opportunities and requirements. While these negative implications for investment financing do not exist, or pose a much smaller consideration, for well-established mainstream transaction processing networks,

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investment financing serves as the lifeblood of many newer companies that rely solely on investment financing to fund their innovation.

In addition to the resources necessary to support the development of an alternative service delivery network, an emerging payment service provider would likely be required to finance (or facilitate the financing of) the development of an alternative network path. This would involve either directly paying for development or through establishment of a pricing structure, at least until economies of scale are realized sufficiently to fully support profitable development and maintenance of the separate network. This increased cost would intensify the already daunting risks of introducing alternative payment systems, and almost certainly inhibit financing for such services. The Board, in essence, would be creating artificial but effective restraints on growth and innovation of emerging payment systems by requiring that for every unique payment system out there, another alternative must exist. In effect, this would force emerging payment systems to surrender the very competitive advantage needed to position and propel them as effective competitors in their industry.

While Boku recognizes that the Board views the statute as not providing “any apparent basis for excluding three-party systems from the scope of the provisions of EFTA Section 920(b),” Boku believes that emerging payment systems, which are distinguishable from established three-party systems, should be excluded from coverage of Regulation II for the very reason the Durbin Amendment was enacted - to encourage competition in the payment systems industry. This is not only an entirely defensible statutory position, but is arguably compelled by the legislative history of the Durbin Amendment, which Proposed Regulation II would implement. Again, this view was stated most succinctly in Senator Durbin’s words, “the intent of my amendment is not to diminish competition in the debit issuance market. I will be watching closely to ensure that the giant payment card networks Visa and MasterCard do not collude with one another or with large financial institutions to take steps to purposefully disadvantage small issuers in response to enactment of this amendment.” Similarly, the Senator expressed the view that, “my amendment contains much needed reforms that will help increase fairness, transparency and competition in the debit card and credit card industries.”

In our view, it would stand the Durbin Amendment “on its ear” for the Board to subject emerging and other non-traditional payment systems to the provisions of the Durbin Amendment and Regulation II discussed herein. Rather than the giant payment networks colluding to disadvantage small issuers, the Board would be doing it for them. It is difficult to imagine a result that would be further from the intended purpose of the Durbin Amendment than to require the very entities that offer the most promise of restoring competition to the payments industry to abide by a series of regulatory requirements that would ultimately ensure their failure to establish alternative payment networks that could compete with the currently existing, traditional payment networks.

**VII. Unlike Traditional Payment Systems, What Constitutes an Interchange Fee in Emerging Payments Systems is Uncertain due to the Unique Economics and Evolving Nature of Such Systems**

As the Board observes in its proposal, it is difficult to determine whether any portion of the fees charged by emerging payment systems can accurately be characterized as interchange transaction fees. Even where such fees may be characterized as interchange, it appears inappropriate to cap such fees based on market information regarding interchange fees in the traditional debit context. The Durbin Amendment requires that “[t]he amount of any interchange transaction fee that an issuer may receive or charge with respect to an electronic debit transaction shall be reasonable and proportional to the cost incurred by the issuer with respect to the transaction.” This requirement, however, does not cover fees (a) which may not be appropriately characterized as interchange transaction fees and (b) the reasonableness and proportionality of which cannot be fully ascertained.

The Durbin Amendment defines “interchange transaction fee” as “any fee established, charged or received by a payment card network for the purpose of compensating an issuer for its involvement in an electronic debit transaction.” It is not entirely clear what portion of the merchant discount constitutes such a fee in the emerging payment systems context. Most often, such systems resemble a three-party construct more closely than a four-party construct leading to issues in isolating the interchange transaction fee, as the Board itself notes in Regulation II. In its discussion regarding three-party systems, the Board distinguishes the four-party network structure that typifies bank-issued debit cards and acknowledges the difficulty of applying the definition of interchange fee to a three-party network, i.e., one in which one organization serves as both the card issuer and merchant acquirer and contracts with all of the cardholders and merchants who may pay with or receive payments through the network in which there is no explicit interchange fee. Importantly, the Board points out:

“If a three party network apportioned its entire merchant discount to its roles as network or merchant acquirer, however, the interchange fee would, in effect, be zero. This outcome, coupled with the fact the statute does not restrict fees an acquirer charges a merchant, may present practical difficulties in limiting the amount of a merchant discount charged in a three-party network. The Board requests comment on the appropriate way to treat three-party networks and on any specific clarifications with respect to such fees that should be provided in the regulation.”

As difficult as it may be to identify an analog to the interchange fee in a well understood, mature three-party network, Boku wishes to highlight that it would be highly speculative to attempt in the emerging payments context to fairly identify costs that are purely meant to compensate the “issuer” as opposed to costs incurred in delivering the service to merchants and the network clearing and settlement functions. The cost elements are not easily identified because the elements of services provided by emerging payment systems, such as Boku, are still evolving. As these systems mature, it may become apparent that the interchange fee pass-through concept does not apply

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at all, let alone ever pose the type of market imbalances that Senator Durbin identified as the legislative target. Alternatively, if it appears that such interchange fees do exist, the Board will have sufficient opportunity to inform its decision in the regulation of such fees.

The Board's determination of the average fees associated with interchange was based on surveys distributed to "networks believed to process debit card transactions," which naturally excludes emerging payment networks that currently do not process such transactions but may wish to build out systems to process analogous transactions in the future. The concern here is due to the broad definition of payment card network, such transactions would be captured by Regulation II. This is problematic because the cost structure for many emerging payment systems is still evolving and any cap could potentially act as a barrier to entry and limit any sort of meaningful market penetration. In other words, by failing to exclude emerging payments systems from the interchange fee restrictions, the Board here may unwittingly regulate the caps for fees on transaction models which have not yet come to fruition and, given the direction of Regulation II, may never have that opportunity. This would be unfortunate as it would deprive customers of the competition and alternative options that the Board has emphasized as a priority in its rulemakings. Furthermore, for many unbanked and underbanked consumers, this could mean not being able to access any meaningful payment options.

Finally, there is another important point regarding the unique cost structure of emerging payment systems that is relevant to the Board's request for comment on Regulation II. The Board solicited comment on whether costs beyond the direct costs of authorization, clearing and settlement should be considered in the definition of "incremental costs" under the proposal. While Boku believes that emerging non-traditional payment systems should be excluded from the interchange fee restrictions altogether, the consideration of indirect costs shows that Boku's cost structure is different in many ways from the traditional networks and that these factors also are still evolving. As previously noted, there are many indirect costs associated with a payment transaction involving an emerging payment system that are unique and/or quite different from those of a traditional payment network. These include customer support systems and infrastructure, merchant onboarding and monitoring, and numerous other costs. In the event that emerging non-traditional payment systems are not excluded from the interchange fee restrictions altogether, Boku believes that such costs should be considered allowable costs for emerging payments systems by the Board.

## **VIII. Conclusion**

Boku respectfully requests that the Board consider clarifying proposed Regulation II to exclude emerging alternative payment services such as Boku's. This exclusion will ensure that the final regulation best serves the intended purpose of the Durbin Amendment by providing opportunities for the market to provide innovative competitive alternatives to small businesses and other merchants that will also better serve consumers. Such alternative services hold the potential to provide payment services to large consumer groups who may now be underserved and thereby also

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expand merchants' markets for their products and services. Applying regulations aimed at the practices and resulting market conditions of entrenched payment services to Boku and other innovators of payment services would undermine the very purpose of the Durbin Amendment - to promote meaningful competition in the payments systems industry. Ultimately, this would perpetuate the status quo that Senator Durbin and other Members were trying to rectify and, in effect, only serve to further entrench the conventional debit payment services.

For all of the reasons articulated herein, we strongly encourage the Board to implement Regulation II consistent with the legislative intent of its sponsor and the many other Members that supported his purpose in introducing the Durbin Amendment. In this regard, we believe it is entirely appropriate, if not compelling, that emerging payment systems be excluded from the provisions of the Durbin Amendment discussed herein. Boku would also support a determination at this time by the Board that further study is required before the Durbin Amendment is applied to emerging payment systems. Thank you.

Sincerely,

/s/

Javier Martell  
General Counsel, Boku