



February 22, 2011

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Docket No. R-1404
RIN No. 7100 AD63

Dear Board of Governors:

I am the CEO of the ATM Industry Association (ATMIA), a non-profit trade association that represents all sectors of the ATM industry, including owners and operators of over 200,000 non-bank ATMs in the United States which provide convenient access to cash to millions of US citizens largely in retail locations.

This letter is written in response to the Federal Reserve's request for comment on various aspects of the Electronic Funds Transfer Act (the EFTA). Our recommendations represent, in the spirit of democracy, the majority consensus of our U.S. membership but do not necessarily represent the views of all members.

As the only non-profit association dedicated exclusively to the whole ATM industry, we are especially concerned about the erosion of competitiveness among the U.S. ATM networks and the particular threat this represents to the business models of non-bank ATM operators, who operate an estimated 50% of the ATMs in America. It is precisely these independently-operated ATMs which bring access to banked cash closest to where citizens live, work and shop. The potential impact of allowing this erosion of competitiveness to continue unabated could have a severe impact on hundreds of non-bank ATM operators, their employees and their service-providers and could spell the beginning of the end for convenient cash access through non-bank ATMs for millions of cardholders. In addition, merchants appreciate the convenience of ATMs

that are located near their businesses because it provides increased availability to cash in their vicinity and boosts their sales. Further add-on effects could include a slowing down in the cash cycle and distribution of cash which has become crucial to the entire consumer economy.

As an integral part of the wider debit card industry, we are writing to respectfully urge you to ensure that subsection 920(b)(1) of the Electronic Funds Transfer Act (the EFTA) – which prohibits network exclusivity and limits network routing restrictions – applies to ATM networks and transactions. This is our principal recommendation.

In addition, we urge you to require issuers to offer at least two unaffiliated ATM networks on each card with ATM functionality.

Thirdly, we wanted to voice our support for the Federal Reserve's view (as stated in the proposed rule) that subsection 920(a) – the limits on interchange transaction fees – does not apply to ATM interchange. ATMIA believes this is the right and wisest viewpoint.

By way of background, since 1996, the number of non-bank, off-premise ATMs in the U.S. has grown from near zero to over 200,000 – all in response to consumer demand. Yet this impressive infrastructure and amazing entrepreneurial achievement – the largest non-bank ATM base on the planet – is now under threat from ATM network rules that are eroding competitiveness. Allow me to explain. The dominant ATM networks, namely MasterCard and Visa, have signed agreements and imposed network routing restrictions that force ATMs to direct routing onto the dominant networks. At the same time, these dominant networks have increased the fees they charge ATM operators and significantly reduced the amount of ATM interchange paid to ATM operators. This double blow has resulted in higher ATM transaction costs, creating upward pressure on consumer fees. In addition, it has resulted in fewer ATMs being deployed and even led to the removal of a number of deployed ATMs. It is in this context that non-bank ATMs struggle to compete and survive. Consumers, small issuing banks, and the economy would benefit if these ATM operators were free to direct routing in a manner that optimizes consumer access to cash at the lowest possible cost.

I. The Network Exclusivity Prohibition and Limits on Network Routing Restrictions Should Apply to ATM Networks.

The Federal Reserve has requested comment on whether the network exclusivity prohibition and limits on network routing restrictions (subsection 920(b)(1) of the EFTA) should apply to ATM networks.

The question is whether the dominant ATM networks should be allowed to continue to force ATM operators and storeowners to direct routing onto the dominant networks which have increased transaction costs, or whether ATM operators should be free to direct routing in a manner that reduces the ATM operators' transaction costs and thereby optimizes consumer access to cash at the lowest possible cost. This is a fundamental principle for non-bank ATMs which we wish to put before you for consideration. Enabling this greater degree of choice in routing would

benefit consumers, small issuing banks, and the economy. It would create the same economic incentives in the ATM industry that would be created in the point-of-sale industry: an incentive to lower transaction costs thereby reducing upward pressure on price. Moreover, the broad statutory language utilized in the exclusivity and routing provisions explicitly covers ATM networks and transactions.

Congress passed Section 920 to restrain the exercise of market power in the debit market by dominant networks, largely Visa and MasterCard. It is important to note that Visa and MasterCard not only offer point-of-sale (POS) networks, they offer ATM networks which are branded as the Plus and Cirrus networks. In both the POS and ATM industries, the Visa and MasterCard networks have been signing exclusivity agreements with issuers and imposing network rules on merchants that *restrict routing*. Again, we come back to our fundamental principle of recommending a greater say for ATM operators in routing transactions in a more competitive ATM network system. By contrast, these exclusivity agreements and rules have led to higher transaction costs which are often passed on to consumers. Section 920 of the EFTA – which was included in the Dodd-Frank Act – is intended to address this problem and to give merchants a greater say.

To fully explain the benefit of applying subsection 920(b)(1) to ATM networks, we would like to provide some background. First, ATM interchange is not paid to issuers, it is paid by issuers. The issuer is compensating the ATM operator for a service: providing the issuers' customers convenient access to cash. Secondly, the non-bank ATM operator depends on two sources of revenue to pay all of its costs: (1) the ATM interchange which is set by the ATM networks and paid by issuers and (2) the convenience fee paid by consumers. The revenue from ATM interchange and the convenience fee is shared with the storeowner where the ATM machine is located. The division of these two revenue streams is based on the underlying contract between the ATM operator and the storeowner. In some cases, the contract provides for adding the two revenue streams together and dividing them between the parties in some ratio. In other cases, the ATM operator receives all or most of the ATM interchange while the storeowner receives most of the convenience fee. The storeowner often receives between 40 and 80% of the total earned from these two revenue streams. Thus, the ATM operator and storeowner are both the “merchant” in an ATM transaction. The ATM operator and storeowner are selling convenient consumer access to cash. The convenience fee is the price accepted by the consumer for that service.

Because they dominate the ATM industry, MasterCard and Visa have extensive power over ATM operators and storeowners alike. The networks can raise network fees charged to ATM operators (also known as network support fees) and decrease the amount of ATM interchange paid to ATM operators and storeowners by issuers. And, because they dominate the industry, the networks can do so without fear of losing volume. Therefore, it is no surprise that these networks have been signing exclusivity agreements with issuers and imposing routing restrictions that force ATM operators to route onto certain networks even if it is not beneficial to the ATM operator and storeowner to do so. This benefits issuers (and networks) at the expense of the merchant (the ATM operator and storeowner) and the consumer.

This power and its inextricable relationship to competition in the ATM market was on

display recently when MasterCard significantly raised the network fees for Cirrus ATM transactions by 260%, and reduced the interchange the large issuers would pay to non-bank ATM owners for such transactions by 62%.

As part of its strategy to enter into exclusive partnerships with the large debit issuers, Visa implemented similar, albeit less drastic, changes several years ago. These exclusivity agreements and network restrictions have restrained the ATM's ability to steer cardholders to networks who charge lower fees and pay higher ATM interchange. We provided evidence of these policies to the Federal Reserve in December 2010.¹

A. Consumers, Small Issuers, and the Economy Benefit if ATM Networks Cannot Limit Routing.

If the network exclusivity prohibition and limits on network routing are applied to ATMs, consumers could benefit from lower prices and greater access. The above-described actions taken by the dominant networks have increased the ATM operator's transaction costs and thereby created an upward pressure on the price of services (the price is the convenience fee consumers pay for convenient access to cash at non-bank ATMs).

In addition, the actions of the dominant networks have resulted in fewer ATMs being deployed and even led to the removal of a number of existing ATMs. A reduction of ATM deployment and removal from service negatively impacts access to cash and other ATM functions. In addition, a reduction in the number of non-bank ATMs forces consumers to rely more heavily on bank-deployed ATMs. On average, the convenience fee charged at bank-deployed ATMs is \$.75 - \$1.00 higher than at non-bank ATMs.

Consumers are not the only interest group to benefit. Small issuing banks have fewer bank-owned ATMs than larger banks. These smaller banks and their customers are more dependent on a robust system of consumer-convenient non-bank ATMs than big banks. If the exclusivity and routing provisions in subsection 920(b)(1) cover ATM networks, it will be easier for smaller issuing banks to continue competing with big banks for customers.

In fact, the entire economy would benefit if the exclusivity and routing provisions in subsection 920(b)(1) apply to ATM networks. As discussed above, applying the exclusivity and

¹ Exclusive debit deals between Visa or MasterCard and large debit issuers include an ATM component because ATM functionality is a core feature of debit cards. As such, Visa and MasterCard can (and have) used their ability to drive superior ATM economics to debit issuers to help cement their debit exclusivity deals with issuers. Any attempt to unwind those deals must also deal with the way ATM fees and pricing can affect issuer incentives to favor Visa or MasterCard over competing networks.

routing provisions to ATM networks increases consumer access to cash. Merchants located near these non-bank ATM machines will see more foot traffic from consumers who have cash on hand. These merchants will likely sell more goods and services which leads to a more robust economy. Moreover, less market power will be concentrated in the hands of a few ATM networks. In addition, applying the exclusivity and routing provisions to ATM networks would help ensure that cash continues to be a viable alternative to credit and point-of-sale debit cards. Cash is less costly than credit. With healthy competition from the ATM industry, there is pressure to keep consumer prices down in the credit and debit industries.

B. The Economic Incentives Created in a Point-Of-Sale and ATM Transaction by the Exclusivity and Routing Provisions are the Same.

The Federal Reserve's concern that "coverage of ATM networks under the rule may result in very different economic incentives than coverage of point-of-sale debit card networks" is unfounded. **In both ATM and POS transactions, the prohibition on network exclusivity and limits on network routing restrictions would reduce the transaction costs of the merchant (which is the ATM operator and storeowner in the ATM transaction) and thereby reduce the need to increase consumer prices (which is the convenience fee in the ATM transaction).**

It is also important to note that POS merchants, such as grocers, are able to provide cash back to customers. These grocers will be able to take advantage of the exclusivity and routing provisions in subsection 920(b)(1) to the benefit of their customers. There is no reason that the ATM operator and storeowner should be treated any differently.

It is important to keep in mind that giving the ATM operator the freedom to route the transaction on the ATM network of choice will not lead to significantly higher ATM interchange rates. ATM networks set ATM interchange and issuers pay the ATM interchange. Each ATM network wants to set ATM interchange as low as possible in hopes that debit issuers (who pay that interchange) will enable cards with its ATM network.

C. The Broad Statutory Language Utilized in Subsection 920(b)(1) Covers ATM Networks and Transactions.

Congress passed Section 920 to restrain the exercise of market power in the debit market by dominant networks, largely Visa and MasterCard. ATM cards are included in the definition of a "debit card" which is defined as "any card, or other payment code or device, issued or approved for use through a payment card network to debit an asset account (regardless of the purpose for which the account is established), whether authorization is based on signature, PIN, or other means. ...". Similarly, an ATM transaction fits into the definition of an "electronic debit transaction" which is defined as any transaction using a "debit card." This is no surprise given the fact that competition in the POS market is inextricably linked to competition in the ATM market. After all, POS and ATM functionality reside on the same card and are usually provided through the same network. ATM transactions debit the same asset account as POS transactions and, in most cases, travel over the same networks.

Therefore, subsection 920(b)(1)(a)'s prohibition against networks or issuers restricting the number of networks "on which electronic debit transaction[s] may be processed" to less than two unaffiliated networks should apply to ATM networks. Moreover, subsection 920(b)(1)(b)'s prohibition against rules that "inhibit the ability of any person who accepts debit cards for payments to direct the routing of electronic debit transactions..." likewise should apply to ATM transactions. As discussed earlier, in an ATM transaction, the ATM operator and storeowner are the "merchant" accepting "debit cards for payment" of the convenience fee for the service being provided: convenient access to cash. There is no reason to distinguish between ATM operators and other merchants in terms of their ability to direct the routing of debit transactions.

We urge you to ensure that the various definitions used in the final rule help clarify that subsection 920(b)(1) applies to ATM networks and transactions. We urge you to clarify that a "payment card network" includes an ATM network, a "merchant" includes an ATM operator and subsection 920(b)(1) applies to ATM transactions. In the same vein, we urge you to avoid defining or clarifying terms in a manner that might imply that ATM transactions and networks are not covered by subsection 920(b)(1).

II. Issuers Should Offer More Than One Unaffiliated ATM Network on Every Debit Card with ATM Capabilities.

The Federal Reserve has requested comment on whether issuers should be required to offer at least two unaffiliated ATM networks (and more than one unaffiliated network of each type offered on the card) or whether it should simply require issuers to offer one POS network and one unaffiliated ATM network. We strongly urge the Federal Reserve to require issuers to offer two of each type of network enabled on the card including two unaffiliated ATM networks because it would benefit consumers, small issuers and the marketplace without putting a significant burden on issuers.

The ATM operator and storeowner cannot avoid the increased transaction costs posed by a network if they do not have a choice between at least two unaffiliated ATM networks. The long list of benefits to consumers, small issuers, and the marketplace that were discussed above would not materialize unless issuers are required to offer at least two unaffiliated ATM networks.

In addition, if issuers are required to offer at least two unaffiliated ATM networks, consumers who currently have debit cards which are enabled on only one ATM network likely will find that their card will be accepted at more ATMs.

Moreover, it would not be burdensome on issuers to require them to offer at least two unaffiliated ATM networks on every card enabled with ATM capabilities. In virtually all cases the same networks that offer POS debit functionality also offer ATM functionality. The issuers already will be contracting with more than one of these networks in order to comply with the regulations. Requiring an issuer to contract with those networks for both POS and ATM capabilities should not add a significant cost.

III. The Limits on the Interchange Transaction Fee in Subsection 920(a) Do Not Apply to ATM Interchange.

As noted in the proposed rule, Section 920(a) – which limits the “interchange transaction fee” – does not apply to ATM interchange because ATM interchange is paid by issuers, not to issuers. In other words, ATM interchange is clearly not included in the definition of “interchange transaction fee” which is defined 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.” Moreover, as discussed above, it would not benefit consumers, small issuers, or the marketplace to limit ATM interchange. Limiting ATM interchange would create an incentive to increase the convenience fee charged to consumers.

On a side note, the Federal Reserve asked for comment on whether the exemption for small banks should apply to ATM transactions. Because the small issuer exemption does not apply to subsection 920(b)(1) (the exclusivity and routing provisions), we do not believe the small issuer exemption is relevant to the analysis of whether subsection 920(b) applies to ATM transactions. The small issuer exemption only applies to subsection 920(a) (limits on the interchange transaction fee) and, as mentioned in the proposed rule, subsection 920(a) does not apply to ATM interchange.

IV. The Federal Reserve Should Regulate Network Fees Paid by ATM Operators if these Network Fees are Intended to Compensate Issuers for the Cost of Complying with the Limits on the Interchange Transaction Fee.

The Federal Reserve should regulate other network fees, including fees charged to ATM operators, if those fees are part of an overall effort to compensate issuers for compensation lost due to the limits on the interchange transaction fee in subsection 920(a). Subsection 920(a)(8) allows the Federal Reserve to regulate other “network fees” -- which are defined as “any fee charged and received by a payment card network with respect to an electronic debit transaction fee” -- if these network fees are an attempt to circumvent the limits on the interchange transaction fee.

We are concerned that networks will try to compensate issuers for compensation lost due to limits on the interchange transaction fee by changing ATM policies to the issuers’ benefit. In fact, the ATM support fees (charged and received by networks and paid by ATM operators) have been increasing, particularly the fees charged by MasterCard which increase by 260% in 2010. We believe this increase may have helped to fund the networks’ agreements with large issuers. We are concerned that network fees charged to ATM operators may continue to fund such agreements. We urge you to make clear in the final rule that such fees can be regulated by the Federal Reserve if those network fees are used to circumvent subsection 920(a).

V. Do Not Delay Implementation of Subsection 920(b) beyond 2011.

The Federal Reserve proposes to delay implementation of the subsection (b) of section 920, including the prohibition on network exclusivity and limits on network routing restrictions. We believe subsection (b) should be implemented as soon as practicable so the rule can address the current problematic policies that are being imposed by the dominant ATM networks. We see no reason subsection (b) should not take effect in 2011.

Conclusion.

As discussed above, subsection 920(b)(1) of the EFTA – which prohibits network exclusivity and limits network routing restrictions – should apply to ATM networks and transactions. In addition, issuers should be required to offer at least two unaffiliated ATM networks on each card with ATM functionality. Moreover, subsection 920(a) – the limits on interchange transaction fees – do not apply to ATM interchange. However, if the network fees charged by ATM networks and paid by ATM operators are increased in order to help compensate issuers for revenue lost pursuant to Section 920(a), the Federal Reserve should regulate those network fees. And, finally, subsection 920(b) should take effect in 2011.

We thank you for your kind attention and consideration. We are committed to fair, competitive ATM networks in what is the world's largest ATM market, so that our 200,000 plus non-bank ATMs can continue providing convenient access to cash for millions of consumers daily.

Sincerely,

A handwritten signature in black ink that reads "Mike Lee". The signature is written in a cursive, slightly slanted style.

Mike Lee, CEO
ATM Industry Association