Proposal: 1748 (AG15) Regulation II - Debit Card Interchange Fees and Routing

Description:

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From: First National Bank Texas, Robert W. Hoxworth

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Subject: R-1748; Regulation II - Debit Card Interchange Fees and Routing

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Comments:

Date: Aug 11, 2021

Proposal: Debit Card Interchange Fees and Routing [R-1748]
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Your comment: August 11, 2021 Ann Misback Secretary Board of Governors of the Federal Reserve 20th Street and Constitution Ave Washington, DC 20551 Re: Proposed Changes to Regulation II- Debit Card Interchange Fees and Routing (Docket No. R-1748, RIN 7100-AG15OP-1747) Dear Ms. Misback, Secretary to the Board of Governors of the Federal Reserve: First National Bank Texas (FNBT) appreciates the opportunity to comment on the Proposed Changes to Regulation II- Debit Card Interchange Fees and Routing (Docket No. R-1748, RIN 7100-AG15OP-1747) and enumerate our concerns as enumerated below. The FNBT comments and recommendations contained herein are our independently comprised opinions and concerns regarding the aforementioned proposed rule. FNBT is a regional community bank with total assets of $3.7 billion as of June 30, 2021 and as such is a Regulation II exempt bank. Our concerns are primarily centered around and address the inadvertent and adverse operational and earnings effects on the exempt community banks as detailed below. We are hopeful the Board will recognize the legitimacy of our concerns as to the disproportionate impact of the additional and untimely regulatory burden the proposed change to Regulation II will have on exempt community banks especially considering the current environment and economic impact that all banks are facing as a result of the pandemic. Our attention in the current environment is prioritized on safety and soundness to our institution and to our customers, who ultimately will not benefit from this proposed rule, and may subsequently bear the burden of the Board's unanticipated consequential impact, while we, the community banks, continue to adapt to a developing new normalcy in all aspects of doing business. The proposed rule will affect the bulk of our compliance, technical, operational and accounting support operations detracting our resources and requiring us to redirect our immediate concerns and commitments to focus on proposed regulatory obligations with little preparation time to mitigate the entirety of the requirements and unavoidable reduced earnings. We ask the Board to reconsider imposition of this rule without an objective and comprehensive due-diligence report assessing the inadvertent and adverse impact that it will undoubtedly have on exempt community banks, or substantiating the Board's opposing position. Urgent and Critical Operational Concerns 1.

The proposed rule will not benefit consumers. The Board does not imply expected consumer benefit from the proposed rule, however it is a critical concern to community banks. As proposed, the rule will subsequently result in consumers bearing the burden of the Board's unanticipated consequential impact to community banks in reduced interchange revenue all while being tasked with the expenses of fighting an ever-increasing amount of card related fraud. It is important to reference the enactment of Regulation II in 2011 and the Board's assertion that the interchange fee standards would transfer into consumer savings via lesser merchant expenses. There is no evidence of fact that this materialized. The proposed rule now has significant potential to adversely impact consumers as the cost of the proposed rule inevitably transfers to community banks whose commitment is to deliver safe and efficient consumer financial services. It is our concern that the Board is unduly expediting the imposition of this rule without appropriate due-diligence. 2. The Board's references to the 2019 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions report issued by the Board in May 2021 is not sufficient to determine the potential adverse impacts to the exempt community banks. The 2019 data referenced by the Board to support the Board's expected effects of minimal impact is not realistic, as there is no deliberation of the costs of implementation and support, as well as the shift of interchange fee income as merchants choose the least costly and least secure routing option that would be more available for card-not-present (CNP) transaction routing. As proposed, we can reasonably expect the rule will result in an inequitable impact to exempt community banks. Prior to imposing the rule, we urgently request the Board to conduct an objective impact assessment separate from its 2019 report addressing each of our concerns. The exempt banks have complied with the current expected standards for a decade while the Board has had the responsibility in that same period to conduct an assessment every two years and, for each report conducted, has issued no interchange fee or network standards adjustments to date. It is insupportable of the Board without more notice and quantification to expedite the proposed rule change without additional appropriate due-diligence and sufficient mitigation opportunities for community banks. 3. The proposed rule does not provide sufficient substantiated standards and requirements. The ambiguity of the proposed rule language predicates conflicting interpretation by banks, networks and merchants alike, as opposed to establishing substantiated standards and requirements. The absence of substantiated standards will be a root cause of misapplications and misinterpretations of the rule, and create unnecessary resource and cost burdens. 4. The proposed rule places additional and untimely regulatory burdens on community banks, and does not contemplate the effect of the rule on the banks' network dependencies. It is our opinion and interpretation that the required rule, as proposed, without clear standards and requirements, and without an assessment and evidence to support the proposed rule, places the preponderance of burden on community banks. This includes but is not limited to, technical, security, operational and compliance requirements; and therefore creates a predictable consequential negative revenue impact on community banks to implement and support such rule and at a cost disproportionate to networks and merchants who are not subject to the Board's rule-making. In addition, the timing of this proposal has critical consequences to community banks who continue to adapt to a developing new normalcy in all aspects of doing business during and post-pandemic. This proposed rule affects the bulk of our compliance, technical, operational and accounting support operations and detracts our resources, and would require us to redirect our immediate concerns and commitments to our customers to focus on proposed regulatory obligations with little preparation time to mitigate the entirety of the requirements and perceivable reduced earnings. The Board's intent to "clarify" Regulation II disregards the current economic and payments innovation environment where non-regulated entities and networks are not bound by the same regulatory requirements as banks, nor do the banks' have any authority or control of interchange rates set but are dependent on the competitive market between the networks. In addition to banks' multi-regulatory requirements, we are also subject to partner networks' operating rules and mandates and who represent their merchant client interests. The partner network rules affect banks' rights in processing disputed transactions. Without substantiated standards and requirements, banks can expect to incur more implementation and support costs as well as losses due to fraud. E-commerce CNP transactions are predominantly processed today through the known, more secure dual-message network that provides protections for both banks and its customers. As merchants will choose the least cost routing option, the proposed rule requirement potentially expands the volume of e-commerce CNP processed through a single-message network without PIN authentication. It is an urgent concern that the transactions will be more susceptible to fraud, and without substantiated standards and requirements, the banks will absorb additional losses in conjunction with reduced interchange income. 5. The Board states the proposed rule does not directly address interchange fees. The Board states that the proposed rule does not directly address interchange fees. An additional concern is the potentially expanded e-commerce CNP transactions availability where again merchants will likely choose the least costly routing option which could effectively reduce community banks' average interchange income to levels only somewhat higher than the regulated fee cap imposed on $10 billion banks. It is our opinion that the rule, as interpreted, to require and ensure two unaffiliated networks have been enabled for CNP, will have a significant earnings impact, with reduction of interchange fee income and costs related to the implementation and support of the proposed rule. Our interpretation is based on the following: "the rule requires card-not present transactions to be applied to the current written rule, that each debit card transaction must be able to be processed on at least two unaffiliated payment card networks, and also requires debit card issuers to ensure that at least two unaffiliated payment card networks have been enabled for debit card transactions." 6. We respectfully request the Board conduct an objective and comprehensive assessment prior to imposing the proposed rule change on banks. It is imperative of the Board to reassess the consequences of the proposed rule. We ask the Board to conduct a comprehensive payments eco system assessment and provide evidence of substantiated standards and requirements while considering the potential impact to community banks, and consequently, and most importantly, to consumers. There is no historical evidence or reasonable belief that merchant savings from the proposed rule will pass to the consumer while banks are committed and obligated to providing safe, secure and sound banking environment while investing in the future of payments services as well as other innovative financial services. We respectfully oppose and appeal to the Board to withdraw the Federal Reserve Board's proposed changes to Regulation II-Debit Card Interchange Fees and Routing (Docket No. R-1748, RIN 7100-AG15OP-1747) due to the consequences to exempt community banks, the absence of consumer benefit and without an objective and comprehensive due-diligence assessment that considers all of the urgent and critical concerns as stated above. Sincerely, Robert W. Hoxworth