

May 10, 2024

Submitted electronically via regulations.gov

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th St. and Constitution Ave. NW
Washington, DC 20551

**Re: Docket No. R-1818, RIN 7100-AG67
Notice of Proposed Rulemaking: Debit Card Interchange Fees and Routing**

Dear Ms. Misback:

On behalf of Ahold Delhaize USA, I appreciate the opportunity to submit comments to the Federal Reserve Board of Governors (“Board”) regarding the November 14, 2023 Notice of Proposed Rulemaking (“NPRM” or “Proposed Rule”) on debit card interchange fees.

Ahold Delhaize USA and its great local brands are leading omnichannel supermarket operators in the United States. The companies of Ahold Delhaize USA comprise the largest grocery retail group on the East Coast and the fourth largest grocery retail group in the nation. We operate more than 2,000 stores and 20 distribution centers across 19 states and the District of Columbia under the Food Lion, Giant Food, The GIANT Company, Hannaford, and Stop & Shop retail brands. Our stores serve approximately 14.5 million U.S. households, both in-store and online, and we provide communities with high-quality food options that are healthy, sustainable, and affordable. Our brands constantly strive to deliver value to customers, not only by competing vigorously to keep prices low but also by offering award-winning customer loyalty reward programs. We are proud that our loyalty programs at Food Lion, Giant, and Stop & Shop were named among America’s Best Loyalty Programs 2023 by Newsweek.¹ We also take pride in our workforce. The companies of Ahold Delhaize USA employ more than 200,000 full-time and part-time associates across the United States, reflecting a diverse, inclusive, and skilled workforce that is representative of the communities we serve. And the role our brands’ stores play in communities goes beyond shopping and hiring. Our retail brands’ stores serve as centers of community life and frequently partner with local community organizations and charities to support causes such as fighting hunger through financial donations and providing surplus food to food banks.

¹ Newsweek, “America’s Best Loyalty Programs 2023,” available at <https://www.newsweek.com/rankings/americas-best-loyalty-programs-2023>.

In recent years, the food retail industry and the consumers who rely on it have faced significant challenges including the COVID-19 pandemic and inflation. The pandemic led to dramatic changes in shoppers' purchasing habits, and our brands responded by accelerating the number of stores with online and curbside purchasing options as well as by adding hundreds of click-and-collect locations. Inflation has contributed to higher operating costs for our brands, especially on commodities, and we have been relentlessly focused on keeping prices as low as possible for customers despite the inflationary environment.

In the context of these challenges, it is extremely difficult for grocery stores to bear the soaring cost of interchange fees. In 2023, Ahold Delhaize USA brands paid a total of \$166,460,219 in debit interchange fees. This marked a seven percent increase from the amount of debit interchange fees we paid in 2022, even though our volume of sales made via debit transactions increased only four percent. While we recognize that there is some cost that card-issuing banks incur to process debit transactions, the dominant debit card networks, which centrally fix interchange fee rates on behalf of their issuers, have incentive to provide issuers with high fee rates that exceed the issuers' actual cost of transactions in order to motivate the issuers to issue more of their cards. When excessive interchange fees are charged, they inflate the retail cost of goods. This means consumers end up paying more for everything they buy, whether they pay with cash, check, or plastic. Ensuring an equitable interchange fee structure is therefore critically important to our business and to our customers.

That is why the role the Board plays is so important. In 2010, Congress on a bipartisan basis passed the Durbin Amendment to the Dodd-Frank Wall Street Reform and Consumer Protection Act, which tasked the Board with placing reasonable limits on debit interchange fee-fixing by card networks and with preserving a measure of competition in the card network market by stopping Visa and Mastercard from forming network exclusivity deals with debit card-issuing banks. This reform was enacted because it had become apparent that the interchange fee system was structured by the dominant Visa and Mastercard networks to insulate the fees from normal marketplace competition. Congress stepped in to address this market failure and gave the Board the authority and responsibility to rein in the dominant networks' fee-fixing within the debit system so the system can operate more fairly for all participants in our economy. We rely on the Board to ensure reasonableness, proportionality, and competition in the debit system for the sake of all American businesses and consumers who use it.

Ahold Delhaize USA appreciates the Board's recognition that Regulation II must be updated in order to comply with the requirements set forth in federal law. As we noted in comments we submitted to the Board on August 2, 2021,² the time has come to reduce the regulated debit rate to bring it into alignment with the statutory requirement that it be reasonable and proportional to allowable issuer costs. The Proposed Rule represents a meaningful step forward in this respect, but we urge the Board to make several modifications to the Proposed Rule to make it more consistent with the law's

² Comment letter from Ahold Delhaize USA to the Board of Governors of the Federal Reserve System, Aug. 2, 2021, available at https://www.federalreserve.gov/SECRS/2021/November/20211129/R-1748/R-1748_080221_139081_355755721020_1.pdf

requirements and to avoid unintended consequences. Our recommended improvements to the Proposed Rule are discussed below.

1. The Proposed Rule’s Base Component Fixed Multiplier Is Higher Than the Multiplier Used in 2011 and Must Be Reduced.

We agree with the Board that the current Regulation II base component rate of 21 cents must be reduced in order to comply with the statutory standard set out in the Durbin Amendment. The Durbin Amendment requires that when debit interchange fees are set by card networks on behalf of card-issuing banks with assets of over \$10 billion, the fees must be “reasonable and proportional to the cost incurred by the issuer with respect to the transaction.”³ In the NPRM, the Board notes that “the allowable costs incurred by covered issuers have fallen significantly since the original Regulation II rulemaking,” from an average of 7.7 cents per transaction to 3.9 cents.⁴ However, the NPRM’s proposed new rate of 14.4 cents does not reasonably reflect this decline in base component costs. Those costs declined by nearly half, yet the Proposed Rule’s rate represents a decrease of less than a third.

The NPRM produced its proposed 14.4 cent rate by identifying a fixed multiplier and applying that multiplier to allowable covered issuer costs. But the NPRM’s multiplier, which is proposed at 3.7 and which would be applied in perpetuity, is significantly higher than the multiplier that was effectively established by Regulation II, which has been 2.7 as long as Regulation II has been in effect. By increasing the base component multiplier even as allowable covered issuer costs have significantly decreased over time, the Proposed Rule would make future base component rates even more disproportionate to allowable costs than the current base component rate. This is unreasonable on its face, and the NPRM’s proposed justification for a 3.7 multiplier—that such a multiplier would meet a full cost recovery target of 98.5 percent of covered issuer transactions and reflect an efficiency gap of 5.2—relies upon target figures that themselves are inadequately justified. Further, by increasing the fixed multiplier and applying it in perpetuity, the Proposed Rule would actually incentivize issuers to coordinate with networks to increase certain allowable costs (such as the network fees that issuers pay to networks, which the Board treats as an allowable cost) because the issuers would receive 3.7 cents of higher interchange in return for every cent of higher network fees. Such inappropriate incentives should clearly be avoided.

We agree with the recommendation suggested by FMI in its December 2022 letter⁵ to the Board, which proposes that the Board maintain Regulation II’s current multiplier of 2.7 times the average per transaction allowable cost. This approach would be consistent with the statutory reasonable and proportional standard, and would produce a base component rate of 10.5 cents per transaction which would fulfill the Board’s obligation to revise the base component rate “to reflect the decline

³ 15 U.S.C. 1693o-2(a)(2).

⁴ 88 Fed. Reg. 78105 (Nov. 14, 2023).

⁵ Letter from FMI and NACS to Federal Reserve Chairman Powell, Vice Chairs Brainard and Barr, and Governors Bowman, Waller, Cook and Jefferson, Dec. 22, 2022, available at <https://www.federalreserve.gov/regreform/rr-commpublic/trade-association-letter-20221222.pdf>

since 2009 in base component costs.”⁶ We urge the Board to modify its Proposed Rule to preserve the current 2.7 multiplier and apply it to the average allowable covered issuer base component cost going forward.

2. The Proposed Rule’s *Ad Valorem* Fee Component Should Be Revisited in Light of Data Showing a Dramatic Reduction in the Share of Fraud Losses Borne by Issuers.

We also agree with the Board that Regulation II’s current *ad valorem* fee of five basis points is no longer compliant with the law. As the NPRM noted, “the issuer fraud losses on which the Board based the *ad valorem* component have fallen,” and accordingly the current rate is not reasonable and proportional to those covered issuer fraud losses.⁷ However, in light of data showing that covered issuers now bear only 33.5 percent of fraud losses, we believe that it is also no longer reasonable for the Board to require merchants to pre-pay covered issuers for anticipated fraud losses through the imposition of an *ad valorem* interchange fee component. The *ad valorem* fee component is not required by statute, and when the Board exercised discretion to create it in 2011, the Board did so based on data showing at the time that fraud losses on covered issuer debit transactions were borne 61.2 percent by issuers, 38.3 percent by merchants, and 0.5 percent by cardholders.⁸ However, since that time, the percentage of fraud borne by covered issuers has decreased by nearly half. In the Board’s most recent collected data, “covered issuers, merchants, and cardholders bore 33.5 percent, 47.0 percent, and 19.5 percent of fraud losses, respectively.”⁹

It is not reasonable for grocery stores and other merchants to be required to pay covered issuers twice for fraud losses—prepaying in advance for potential fraud losses through interchange fees that are deducted from the transaction amount and paying afterwards through chargebacks when fraud occurs. Because interchange fees are ultimately passed on to consumers in the form of higher retail prices, consumers as well as merchants bear the burden when issuers have their fraud losses subsidized by interchange. And as debit transactions increasingly migrate to card-not-present channels, issuers will almost certainly shift an even greater percentage of actual fraud losses onto merchants and cardholders, thus increasing the windfall that issuers receive when theoretical fraud losses are also paid in advance through interchange. Furthermore, the current *ad valorem* fee system that the Board created is not proving effective in reducing the occurrence and cost of debit fraud, as overall fraud on covered issuer transactions approximately doubled as a share of transaction value from 2009 to 2021.¹⁰ The current system of subsidizing fraud losses in advance through interchange and permitting issuers to also be compensated for fraud losses through chargebacks simply does not seem to be motivating issuers to reduce debit fraud.

It is important to note that Ahold Delhaize USA has invested significant resources in fraud reduction measures in our brands’ stores. These investments include costs for EMV support and hardware

⁶ 88 Fed. Reg. 78105.

⁷ 88 Fed. Reg. 78100.

⁸ 88 Fed. Reg. 78118.

⁹ *Id.*

¹⁰ *Id.*

and software upgrades to comply with PCI DSS requirements, and over the next four years, there will be a further \$10 million in costs to upgrade our stores' PIN pads to prevent fraud and tampering in accordance with the latest PCI requirements. With PCI DSS 4.0, Ahold Delhaize USA companies will also have significant costs in complete hardware and software upgrades, as well as ongoing PCI compliance costs such as annual assessments and annual PCI penetration tests. We take seriously our responsibility to reduce fraud, but we note that the Board's *ad valorem* fee is imposed equally upon all merchants including those who work diligently to reduce fraud. And, the fee is awarded equally to all covered issuers—even those who are not diligent in reducing fraud and who are focused instead on shifting fraud losses onto others.

Just as the Board exercised its discretion to create the *ad valorem* fee, the Board should exercise its discretion to change the fee. Unless and until the data show that covered issuers are once again bearing the majority of overall fraud losses on covered issuer debit transactions (as they did when Regulation II was established), the Board should suspend the *ad valorem* component of the interchange fee and allow responsibility for fraud losses to be allocated through chargebacks. Not only will this correct the disproportionate burden that the current system places on merchants for fraud losses, but it will also give all parties in debit transactions greater incentive to prevent fraud from occurring in the first place. And, of course, covered issuers are already receiving compensation for fraud prevention costs through the fraud prevention adjustment, so suspending the *ad valorem* fee component for anticipated fraud losses should not diminish issuers' ability to invest in effective fraud prevention steps. We urge the Board to revisit and update its approach to fraud losses as we have suggested, particularly before locking in any *ad valorem* formula that might be automatically applied to fraud loss data going forward.

3. The Fraud Prevention Adjustment Must Be Based Upon Issuers' Actual Measured Effectiveness in Preventing Fraud.

While we do not object to paying covered issuers a fraud prevention adjustment that funds effective fraud prevention steps, neither the current fraud prevention adjustment nor the modified adjustment in the Proposed Rule provide any assurance that covered issuers will use the funds effectively. The Board must not increase the fraud prevention adjustment without changing the Board's fraud prevention standards so that the standards comply with the Durbin Amendment, which mandates that the standards "require issuers to take *effective* steps to reduce the occurrence of, and costs from, fraud in relation to electronic debit transactions."¹¹ As far as we are aware, the Board has simply awarded every covered issuer the fraud prevention adjustment on every debit transaction without collecting sufficient data from issuers to assess whether an issuer's fraud prevention steps are effective. The Board's current practice of simply directing issuers to develop and implement fraud prevention policies and self-certify compliance does not ensure that the steps the issuers take are effective, and the Board's current Debit Card Issuer Survey does not collect data on how much any issuer invests in any particular fraud prevention activity and whether that activity has contributed to year-over-year reductions in fraud on the issuer's debit transactions. We urge the Board to revise its standards to require that issuers demonstrate that their fraud prevention steps are actually

¹¹ 15 U.S.C. 1963o-2(a)(5)(A)(ii)(II) (emphasis added).

effective in reducing the occurrence and cost of fraud on debit transactions in order for an issuer to be able to continue receiving the fraud prevention adjustment. We also urge the Board to conduct meaningful data collection and oversight of the fraud prevention adjustment and to deny the adjustment to issuers who have not presented the Board with adequate data demonstrating that the issuer is using the adjustment to fund fraud prevention steps that show effectiveness.

4. The Board Must Ensure the Ongoing Accuracy and Integrity of Data Reported by Issuers Before Automatically Updating the Regulated Fee Rate Based on Such Data.

We support the Board's proposal to provide for future adjustments to the regulated debit interchange rate every two years, as it has taken far too long for the rate to be adjusted since Regulation II's initial establishment in 2011. However, if the Board plans to apply formulas to automatically update the fee component rates when data is collected going forward, it is critical that the Board both apply appropriate formulas (for example, by applying a fixed multiplier for the base component that is no higher than the current 2.7) and that the Board ensure the accuracy and integrity of the data reported by issuers before using that data in its formula methodologies. The Board should modify the Proposed Rule to make clear that the Board will conduct periodic audits of issuer-provided data to ensure that the data accurately reflects allowable costs and does not misstate those costs or include costs that are not allowable.

We believe the above recommendations will align the Proposed Rule with the Durbin Amendment's statutory requirements and will reduce the unreasonably high current debit fee rate while incentivizing issuer behavior that will strengthen the security of the debit system. Such updates to Regulation II will not only benefit grocery stores like ours, but they will also benefit our customers. Food retailers like Ahold Delhaize USA operate on tight profit margins in a fiercely competitive market sector. When we are able to save on costs such as interchange, that enables us to better compete for consumer business through lower prices and through consumer rewards programs. Our award-winning loyalty programs provide customers with meaningful and personalized discounts tailored to their needs and wallets, and reduced interchange costs enable us to put more resources into these programs. American consumers care deeply about their ability to buy healthy, quality groceries at affordable prices, and reducing excessive interchange fees and incentivizing better fraud prevention helps grocery stores like ours deliver on that goal.

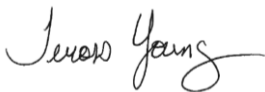
Before concluding, we would like to raise two additional points for the Board's consideration. The first is that Ahold Delhaize, the parent company of Ahold Delhaize USA, also operates brands within European Union (EU) countries where interchange is capped and tightly regulated, and the implementation of interchange regulation in the EU has had numerous positive outcomes of which the Board should take note. For example, EU interchange regulation has fostered competition and innovation in the payment industry by reducing barriers to entry for new players and enabling smaller firms to compete more effectively with established incumbents. It has enhanced transparency in the payment ecosystem, allowing for a better understanding and management of costs associated with accepting electronic payments. And it has contributed to lower costs for merchants, thereby enabling merchants to compete to offer lower prices for consumers.

Importantly, the European experience demonstrates that comprehensive interchange regulation can effectively lower debit interchange rates without compromising the integrity or efficiency of the payment system. Despite initial concerns raised by some industry stakeholders, the regulated environment in the EU has proven to be conducive to the development of robust and cost-effective debit systems with low fraud rates. It is noteworthy that despite the reduction in interchange fees, instances of fraud have significantly decreased in Europe, indicating that effective regulation can concurrently enhance security measures while reducing costs.

The second point is that while interchange fees are constrained by Regulation II, network fees imposed on merchants are not, and those fees are constantly increasing. In recent years merchants have seen new or increased switch fees, license fees, infrastructure fees, and network security fees, among others, imposed on them by networks for debit transactions. As the Board finalizes its rulemaking, we urge the Board to keep in mind the growing burden merchants bear when both excessive interchange and network fees are deducted from debit transaction amounts—particularly because both types of fees may affect the retail prices consumers ultimately pay.

Thank you for your consideration of this comment letter. We urge the Board to act expeditiously to finalize the Proposed Rule with the modifications we have recommended.

Sincerely,

A handwritten signature in black ink that reads "Teross Young".

Teross Young
Vice President Government Affairs