



HOLDING COMPANY

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May 10, 2024

Hon. Jerome Powell, Chair
Hon. Philip N. Jefferson, Vice Chair
Hon. Michael S. Barr, Vice Chair
Hon. Michelle W. Bowman
Hon. Lisa D. Cook
Hon. Adriana D. Kugler
Hon. Christopher J. Waller
Board of Governors of the Federal Reserve System
Washington, DC 20510

Re: Docket ID No. R-1818, RIN 7100-AG67; Proposed Revisions to Debit Card Interchange Fees and Routing

Dear Chair Powell, Vice Chair Jefferson, Vice Chair Barr, and Governors:

I am writing on behalf of FirstBank, a community bank with approximately \$28 billion in assets and over 100 branch locations, serving customers throughout Colorado, Arizona and California. Our core mission is “banking for good”, meaning we aim to do what’s best for our customers, communities and employees. That philosophy covers how we implement and service products, loans, and support our communities, and is the foundation of the feedback within this letter. As a concerned community banker and citizen, I recognize the Proposed Revisions to Debit Card Interchange Fees and Routing will cause undue harm to community banks as well as the customers and communities we serve. I am concerned that the Federal Reserve has not consulted debit card issuers in this two-party system before proposing these changes and is relying upon outdated information that fails to account for critical factors facing our industry in the decade-plus since Regulation II was enacted. While I recognize the agency’s responsibilities to follow the duties outlined within Regulation II and the importance of fair and balanced financial regulations, I have taken a comprehensive look at the justifications provided by the Federal Reserve to adjust the debit interchange cap and feel the agency continues to look for data to support an end goal while ignoring other information that should be considered. The proposal reflects an incomplete approach to debit card issuing and indicates an unclear understanding of the complexities within this industry.

I primarily urge the Board of Governors to pause any further action until there is transparent understanding into the real-world burden these proposed changes will create. I also respectfully request that the agency seriously consider the negative impacts this proposal will have on community

banks and issuers, and consider alternative viewpoints, in lieu of formalizing the debit card interchange cap changes as proposed. The proposed changes to the debit interchange cap will have detrimental consequences consumers. In addition, the proposal itself doesn't adequately consider applicable debit issuer costs. Finally, a consideration is needed to use a tiered cap approach based on bank asset size to mitigate against the harm the shift in methodology will cause to small and mid-sized banks.

Negative Impact on Consumers

Community banks offering debit card products provide an invaluable contribution to customers and merchants by maintaining the associated accounts and systems and supporting a safe, secure and ubiquitous payment experience. Consumers are directly benefitting from interchange revenue as this income has allowed banks to support a cost-effective and secure banking experience. However, this experience is threatened under the current proposal. As seen after the initial implementation of the Durbin Amendment in 2011, free checking product availability with large institutions fell below 20%, and free checking access have fallen by 15.5% with exempt institutions *originally assumed to be unaffected by the interchange fee adjustments*¹. This decline in free checking access is noted in the Federal Reserve Bank of Richmond studies, which found issuers of all sizes have greatly reduced free checking products and services since the original interchange cap was implemented.² These decisions were not made indiscriminately, but were necessary to retain a key source of revenue which enables ongoing funding in critical areas including: fraud prevention, security, customer authentication, customer support, and digital innovation.

Further reductions in the interchange cap will cause more institutions to make the difficult decision to eliminate free checking products in order to support continued growth and minimize fraud losses. My bank is included in the group that initially retained a free checking product sustained by interchange revenue, but after hearing of the Federal Reserve's announcement on the interchange cap reductions last fall in conjunction with the barrage of other regulatory changes, we made the difficult decision to eliminate free checking entirely. This was not a change we took lightly, but supporting debit card issuance requires investments far exceeding the limited scope of expenses currently considered within the Debit Card Issuer Survey. As the costs to access traditional banking accounts grow, we can refer to the impacts after the original Durbin Amendment was implemented to anticipate the impact of this proposal on consumers; those on the financial margins may be pushed out of the core banking industry and into more expensive and riskier financial services, such as payday lending and buy-now-pay-later facilities³ without experiencing any pricing reductions from merchants.

Finally, it's critical to acknowledge that the Durbin Amendment has not resulted in lower costs to consumers, and it's unrealistic to expect or assume that further reductions in interchange fees will benefit consumers. In fact, data supports the contrary; the 2014 study completed by the Federal

¹ Manuszak, Mark D. and Krzysztof Wozniak, "The Impact of Price Controls in Two-sided Markets: Evidence from US Debit Card Interchange Fee Regulation," Finance and Economics Discussion Series 2017-074, Washington: Board of Governors of the Federal Reserve System (2017), at 5-6, <https://doi.org/10.17016/FEDS.2017.074>.

² Wang, Zuh, "Price Cap Regulation in a Two-sided Market: Intended and Unintended Consequences," Working Paper No. 13-06R, The Federal Reserve Bank of Richmond (2015), https://www.richmondfed.org/-/media/RichmondFedOrg/publications/research/working_papers/2013/pdf/wp13-06r.pdf.

³ Sarin, Natasha, "Making Consumer Finance Work," Faculty Scholarship at Penn Carey Law, 2047 (2019), at 1537, https://scholarship.law.upenn.edu/faculty_scholarship/2047.

Reserve and Javelin Strategy & Research group identified 75% of merchants reported they made no change in prices to consumers after the implementation of Regulation II, and 23% reported they increased prices.⁴ Any further downward adjustments in interchange fee rates will ensure any savings will continue to feed merchant revenue, especially the large merchants, as guardrails to ensure these savings are passed onto consumers simply don't exist.

Assessment of Costs

The proposed adjustment to the interchange fee cap fails to ensure the cap “is reasonable and proportional to the cost incurred by the issuer with respect to the transaction”⁵. Since the inception of Regulation II, issuer-based fraud losses on a transaction-weighted average have increased 54% between the 2011 and 2021 surveys.⁶ Fraud loss trending within my bank follows that trajectory, particularly for the e-commerce/card-not-present transactions where losses have shifted from 5% of total debit card fraud in 2017 to nearly 55% of our debit losses in 2023. Losses continue to rapidly increase even in the last year, after the PIN-less routing amendments to Regulation II caused an increase in unauthorized fraud activity due to inferior fraud detection systems supported in the alternative networks, and from 2023 card network rule changes which shifted more of the burden of online financial fraud losses to issuers. Meanwhile, other costs directly tied to debit processing also continue to grow - expenses to enable and support tokenization, continuously advance customer authentication, prevent enumeration and ransomware attacks, and maintain card plastic EMV issuance expenses - and must also be considered in the assessment of allowable issuer costs. As an example, FirstBank's card reissuance costs alone have increased 299% between 2011 to 2023, growing to 12.4% of total expenses in 2023 from just 3.6% in 2011. This trending highlights how other direct issuance expenses must be considered in the net interchange cap calculation. Looking at these expenses holistically would ensure the Federal Reserve understands how these costs are directly bound to authorization, clearing and settlement expenses, and would acknowledge the innovation evolution within the card industry since the Durbin Amendment was first implemented.

Aggregate costs must also be considered in relation to resources and tools available by issuer asset size. Variations in fraud losses at the issuer level compared to the static data reviewed in the Debit Issuer Surveys does not indicate inefficient issuers as implied within the NPRM⁷. The Federal Reserve must recognize a mid-tier/regional bank issuer is substantially different than banks well over one trillion in assets, with substantially different access to technology and other resources to reduce allowable costs. As an example, JPMorgan Chase employs more engineers than Google or Amazon, with roughly 62,000 employed by the company.⁸ Those resources are impressive and highlight how comparing a bank of

⁴ Wang, Zuh and Schwartz, Scarlett and Mitchell, Neil, “The Impact of the Durbin Amendment on Merchants: A Survey Study,” Economic Quarterly – Volume 100, Number 3 – Third Quarter 2014, The Federal Reserve Bank of Richmond (2014), at 190, https://www.richmondfed.org/-/media/RichmondFedOrg/publications/research/economic_quarterly/2014/q3/pdf/wang.pdf.

⁵ 15 U.S.C. § 1693o-2(a)(3)(A).

⁶ Debit Card Issuer Surveys, 2011 – 2021; All covered issuers, Transaction-weighted average of Issuer fraud losses All Transactions; <https://www.federalreserve.gov/paymentsystems/regii-data-collections.htm>

⁷ Debit Card Interchange Fees and Routing, 88 Fed. Reg. 78100, 78105 (Nov. 14, 2023).

⁸ https://www.finextra.com/newsarticle/43548/jpmorgan-faces-45-billion-hacking-attempts-a-dav?utm_medium=newsflash&utm_source=2024-1-17&member=126100, “JPMorgan faces rising number of hacking attempts”

FirstBank's size with a multi-trillion-dollar asset bank to validate the proposed changes is unfair and unjustified.

Finally, the Federal Reserve must acknowledge the 2021 issuer data, including data submitted by FirstBank, was skewed by pandemic-related variables outside of our control, which included an artificial and unprecedented drop in fraud losses as this activity shifted to focus on stimulus funding, as well as abnormally low ACS expenses due to significant staffing vacancies during the Great Resignation. Considering these variables and the impacts to cost shifts in the 2023 Survey, I again urge the Board to pause on implementing the current proposal.

Community Bank Impacts

FirstBank, as a local lender, was able to be a top Paycheck Protection Plan lender during the height of the pandemic, booking over 20,300 PPP loans totaling over \$1.5 billion in our communities. Approximately 80% of those loans were less than \$1 million, and directly served small business owners. We believe strongly in lifting up the communities we serve. Since 2020, FirstBank has invested over \$500 million in affordable housing projects across Colorado and Arizona. We've also developed our Providing Access to Homeownership (PATH) grant program, which has helped more than 200 Black/African American families become first time homeowners. I mention these examples to emphasize how interchange revenue enables a diverse banking system. Interchange revenue is a key source of non-interest income, keeping all bank asset sizes healthy, and ensuring all communities are well served. Community banks like ours rely upon interchange income to continue to serve customers and communities throughout the nation, including those in rural areas where local banks are a lifeline. This change as proposed will threaten the safety and soundness of banks, forcing some institutions to merge or sell to survive, especially those banks near the asset threshold of \$10 billion, and negatively impacting how and if banks can continue to serve our customers and communities.

Considering the impact to community banks and recognizing how the Debit Issuer survey data is skewed by the largest banks in the nation, the Federal Reserve needs to implement a tiered asset approach to the debit interchange cap methodology. I speak from experience as FirstBank is considered a "Top Tier" issuer with over 100 million debit transactions per year. However, from an economies of scale and cost efficiencies perspective, one cannot logically consider our \$28 billion bank to have the same access to tools and technology available to a \$4 trillion bank such as JPM Chase⁹, especially considering we are less than one percent their asset size. Banks with over \$1 trillion in assets are over one thousand times larger than banks with \$1 billion in assets, have substantial resources to minimize overhead and fraud losses that are not available to community banks, yet the data these banks produce has the greatest influence over the economic debit card trends evaluated by the Federal Reserve. The Federal Reserve must acknowledge the distorted impacts the trillion-dollar asset financial institutions have when aggregating their data with smaller issuers and respond by separating smaller asset issuers into a separate interchange fee determination tiers to enable reasonable cost recovery targets. Doing so will enable the safety and soundness of these financial institutions which provide critical financial services to the American populace and mitigate against further distorting the debit issuer landscape by disadvantaging institutions that fall well below the "Too Big To Fail" framework.

⁹ JPMorgan Chase First Quarter 2024 Earnings Presentation, <https://www.jporganchase.com/ir>

Conclusion

I will close by stating the Federal Reserve is under no legal obligation to respond to merchant demands to rewrite Regulation II requirements, or to finalize the proposal and trigger the consequences anticipated in this letter. In addition, a federal agency further regulating interchange to below break-even rates is inconsistent with the free market in place today which enables appropriate pricing strategies through competition. I hope that with this information, you will agree that the wiser and more appropriate course is to pause on implementing the proposal until more is known on the widespread impacts to consumers and community banks, or at a minimum, for the Fed to reassess the proposed interchange cap rule before proceeding further.

I appreciate your attention to this matter, and considering feedback to support informed and equitable decisions that serve the best interests of the public. I am confident that by addressing these concerns, the Federal Reserve can proceed with a more inclusive and well-informed rule-making process that safeguards the integrity of our financial sector, and also contribute to a more robust and secure financial system.

Thank you for your consideration of our comments. If you have any questions or need clarification on any issues raised, please contact me at (303) 235-6590 or David Kelly, Chief Risk Officer at (303) 235-1321.

Sincerely,

A handwritten signature in blue ink that reads "Lavonne Heaviland". The signature is written in a cursive, flowing style.

Lavonne Heaviland

FirstBank, President – Centralized Operations