The Wisconsin Credit Union League

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Submitted via email to: regs.comments@federalreserve.gov

May 9, 2024

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

Re: Debit Card Interchange Fees and Routing
(Docket No. R-1818; RIN 7100-AG67)

Dear Secretary Misback:

On behalf of Wisconsin's credit unions® and their 3.8 million members, the Wisconsin Credit Union League ("The League") appreciates the opportunity to comment on the Federal Reserve Board's (the "Board's") proposal to amend Regulation II, lowering the maximum interchange fee that a large debit card issuer can receive for a debit card transaction.

Specifically, the Board's proposal:

- Includes a reduction in base fees from 21 cents to 14.4 cents, a decrease in the ad valorem component from 5 basis points to 4 basis points, and a fraud adjustment increase from 1 cent to 1.3 cents; and

- Would automatically, without notice and comment, update each component of the cap every two years, based on reported issuer costs.

Wisconsin's credit unions strongly oppose this amendment. We believe that it is misguided, and we respectfully ask the Board to withdraw it, for several reasons:

- The changes would only serve to line the pockets of large retailers;

- The changes would disproportionately harm credit unions, which, as not-for-profit institutions, are less able to absorb reductions in interchange fees than for-profit banks;

- The changes would impact all credit unions that issue debit cards, regardless of size; and

- The changes would lead to fewer financial services options for credit union members, especially in low-income areas.

The changes would only benefit large retailers

We believe that this proposal would simply line the pockets of big box retailers and merchants while harming credit unions and their member-owners.

Research and history have shown that following the introduction of the current fee cap, the availability of free and low-cost accounts for consumers declined while merchants saved money. From 2012 to 2022, issuers collectively lost nearly $106 billion in interchange revenue, a figure that represents what merchants kept. The Federal Reserve Bank of Richmond research reveals that the vast majority of merchants did not pass along any of their regulatory savings to consumers. Further reducing the fee cap will cut debit interchange revenue for issuers, exacerbating these issues.

The changes would harm credit unions disproportionately, driving more credit union mergers

Unlike banks, credit unions are non-profit financial cooperatives, owned by their members. The difference between for-profit banks and not-for-profit credit unions is critical because credit unions would be less able to absorb reductions in interchange revenue than banks, due to credit unions' unique, not-for-profit structure. And with limited capacity to operate debit programs as loss leaders, credit unions could face increasing pressure to merge, (especially in an environment with an apparent regulatory agenda to limit fee income.)

The Board should not take steps that would accelerate the ongoing consolidation in the credit union movement. Increased regulatory burdens and compliance costs are driving credit unions to merge. The Board's proposal is likely to fuel this trend, given that the only way for debit card issuers to reduce transaction costs is to achieve scale. (When the current fee cap was adopted in 2011, only two out of 7,386 credit unions were subject to the debit interchange cap. The number of credit unions has decreased by 37.6%, but 21 credit unions are now directly subject to the cap. Among those 21, the NCUA designates 10 as low-income.) Credit unions that lack scale would be unfairly penalized, as would many other issuers denied full recovery of their costs.

Increasing mergers would result in fewer sources of responsible financial services for U.S. consumers, and that cannot be what the Board intends.

The changes would impact all credit unions that issue debit cards, regardless of size

The proposed amendments to the debit interchange fee cap would harm credit unions of <u>all</u> sizes, because the Durbin Amendment affects <u>all</u> debit card issuers, even those considered "exempt" (issuers below $10 billion in total assets).

Two national credit union trade associations released a study last summer showing that government-mandated interchange price caps disproportionately harm local, community financial institutions. Among other things, the study found that these "exempt" institutions saw a 31% revenue decline, adjusted for inflation, in the decade after its implementation.

The Board has not adequately considered the impact of its proposal on exempt issuers. The Federal Reserve's data, along with research examining the initial effects of the 2011 fee cap, show that even smaller, exempt issuers were harmed when debit interchange rates were reduced for larger issuers. The Board's historical data shows that after introducing the fee cap, debit interchange revenue from single-message network transactions declined 29% for exempt issuers.

The changes would lead to fewer financial services options for credit union members, especially in low-income areas

Lowering the interchange caps would hurt credit unions, as explained above. This would inevitably lead to harm for the communities and members that credit unions serve, especially in low-income communities. As discussed earlier in this letter, the proposal would be another driver of consolidation in the credit union movement. The potential closure or scaling down of low-income credit unions would exacerbate financial exclusion for low-income communities, leaving them with fewer options for accessing basic financial services.

The federal government's own data reflects this risk. A Government Accountability Office study ranked the Durbin Amendment among the top five laws and regulations most cited as having significantly affected the cost and availability of basic banking services. Research on the initial effects of the current debit interchange fee cap adopted in 2011 showed the resulting decline in debit interchange revenue translated into reduced access to free accounts, higher fees, and a rise in the number of unbanked consumers. A study by Federal Reserve economists showed that following the 2011 fee cap, free non-interest checking accounts offered by exempt financial institutions declined by 15.5%. A 2022 study found that fees – including minimum balance requirements and maintenance charges – fall disproportionately on low- and moderate-income communities and majority-minority neighborhoods compared to other areas.

The Electronic Fund Transfer Act requires the Board to consider its regulations' impacts on consumers, and research shows that consumers were harmed when the debit interchange fee cap was introduced in 2011 as costs were passed on by issuers. Similar harm is likely to occur if the Board reduces the fee cap as proposed.

It is not difficult to predict how else the proposed Regulation II amendments would impact credit unions' members and communities. For example:

- Regulatory pressure on sources of fee income and the excessive cost of growing debit card fraud would put pressure on credit unions to eliminate critical programs that low- and moderate-income populations rely on to end a cycle of debt and reach their financial goals. Founded on communal ties and relationship banking, credit unions have a strong history of reinvesting in the communities they serve. The revenue generated from interchange fees often supports community-oriented projects, grants, and programs. But more than 50% of covered credit unions indicate that fewer community grants and scholarships are likely if the interchange fee is reduced.

- A reduction in the debit interchange fee cap could disproportionately affect low-income and minority households the hardest – by reducing the availability of free and low-cost accounts and services. After the Durbin Amendment capped interchange fees, consumer checking account fees grew to cover lost revenue. Low-income households faced challenges maintaining the required minimum balances. Cash being the preferred choice among low-income households creates problems because most payment methods require linkage to a financial institution's account, debit card, or credit card.

- Further reduction in interchange revenue could also threaten credit unions' ability to return savings and benefits to their members. Data from our national counterpart, America's Credit Unions, shows more than 3,500 credit unions offer free checking accounts. The cost of preventing and mitigating fraud is growing for credit unions. However, the proposal adopts a limited fraud prevention adjustment which would deny full cost recovery for actual fraud losses for half of covered issuers.

Conclusion

The Board's proposal to lower the maximum interchange fee under Regulation II would serve only to line the pockets of large retailers. It would impact all institutions that issue debit cards, regardless of their size, and that harm would fall disproportionately on not-for-profit credit unions, which are less able to absorb the loss in interchange fees than for-profit banks. This harm would drive further consolidation in the credit union movement, resulting in fewer sources of responsible financial services for consumers across the country. The communities and members that credit unions serve, especially in low-income communities, would be especially hard hit if these changes take effect.

For all these reasons, we urge the Board to withdraw this proposal.

Thank you for taking the time to consider The League's comments. If I can be of any further help, please do not hesitate to contact me. I can be reached at pguttormsson@theleague.coop or 608-640-4052.

Sincerely,

Paul Guttormsson
Senior Vice President & General Counsel
The Wisconsin Credit Union League