Walgreen Co.
1399 New York Ave NW, Ste 725
Washington, DC 20005
Walgreens.com

May 9, 2024

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

Re: Regulation II; Docket No. R1818 Debit Card Interchange Fees and Routing

Dear Ms Misback:

On behalf of Walgreens, we respectfully submit the following comments in response to the Notice of Proposed Rulemaking published by the Federal Reserve Board ("Board") in the Federal Register on November 14, 2023 - Debit Card Interchange Fees and Routing, 12 CFR Part 23 RIN 7100–AG67 Fed. Reg. 78,100. Walgreens appreciates the diligent work of the Board as reflected in the NPRM. The Board has made good progress toward establishing a methodology that will begin to address changes in issuer costs more quickly and allow merchants and consumers to benefit from lower costs.

Walgreens is included in the U.S. Retail Pharmacy and U.S. Healthcare segments of Walgreens Boots Alliance, Inc. (Nasdaq: WBA), an integrated healthcare, pharmacy and retail leader with a 170-year heritage of caring for communities. WBA's purpose is to create more joyful lives through better health. Operating nearly 9,000 retail locations across America, Puerto Rico and the U.S. Virgin Islands, Walgreens is proud to be a neighborhood health destination serving nearly 10 million customers each day. Walgreens pharmacists play a critical role in the U.S. healthcare system by providing a wide range of pharmacy and healthcare services, including those that drive equitable access to care for the nation's medically underserved populations. To best meet the needs of customers and patients, Walgreens offers a true omnichannel experience, with fully integrated physical and digital platforms supported by the latest technology to deliver high-quality products and services in communities nationwide.

Walgreens strongly supports the Board's proposal to reduce the cap on debit interchange fees imposed by Regulation II. These comments generally explain our support while providing evidence from the Board's own data that would encourage setting a cap that is lower than currently proposed in order to generate cost reductions that can be passed through to consumers as savings on every retail transaction.

Congress intended the Durbin Amendment to create a cost-recovery regime where issuers should have limited (if any) profits from debit interchange. However, the current system leaves a massive allowance in place, particularly for the largest issuers. The Board's proposed change begins to trim that allowance, representing a clear improvement on the status quo. But we believe a true cost-recovery regime remains a long way off and that the Board has an opportunity to go further toward rectifying a grossly asymmetrical relationship between issuers, merchants, and consumers. We believe the Board should recognize this gap and pursue ways to improve the alignment between the regulatory design and the Durbin Amendment's statutory text, which limits "an issuer" to debit charges that are "reasonable and

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proportional to the cost incurred *by the issuer*." 15 U.S.C. §1693o-2(a)(2). A system where a very large subset of issuers continues to reap a very large profit falls outside of what Congress intended or enacted.

The Board's proposal seeks to set the base interchange fee such that 98.5% of transactions would provide 66% of issuers with an interchange fee that would cover their authorization, clearing and settlement (ACS) costs. While this percentage is lower than the 80% covered in 2011, this approach ignores the fact that the average covered debit transaction costs much less than the 98.5 percentile transaction. If the new regulated rate was cut in half to $0.105 to mirror the actual reduction in weighted average costs, it would still cover 95% of transactions.

A maximum debit interchange fee cap of $0.105 cents (instead of $0.144 cents) is justified because it: (1) represents a cap that is proportionate to revised costs and the original cap of $0.21; (2) still creates incentives for banks to lower their costs; (3) further incentivizes the use of enhanced technology that is less prone to fraud; and (4) would still allow the most efficient issuers to benefit from the spread between costs and the cap.

Approximately 66% of Walgreens customers use debit cards when picking up their prescriptions or making retail purchases. Further, roughly 66% of those debit transactions are subject to the regulated rate, which means the Board's proposal to lower that rate is of significant consequence to us. As a primarily small-ticket merchant, interchange fees make up a disproportionately large percentage of nearly every Walgreens transaction and, in a retail business like ours that operates on razor-thin margins, such costs must often be passed through to the consumer to avoid actually losing money on each sale. On average, every dollar of sales equates to only $0.02 in net earnings attributable to Walgreens, as our adjusted net earnings margin was 2% for the fiscal year ended August 31, 2023. Thus, reducing the base interchange fee represents an opportunity for the Board to take an action that could result in lower retail costs for consumers, as merchants like us would likely be able to share the benefits of this saving with our shoppers. This is particularly impactful at a time when the rising cost of goods is having a notable impact on all consumers.

Additionally, the Statute directs the Board to consider all parties that bear the cost of fraud and not to reimburse issuers for all fraud losses. Merchants invest in many types of fraud prevention, but our costs are not quantified nor considered by the Board for either fraud losses or fraud prevention costs. For example, with card-not-present transactions, we consistently bear nearly all of the fraud risks through burdensome chargeback rules imposed by the payment networks and by extension, card issuers. Further, merchants are charged fees for every chargeback we represent, and we pay additional fees if the chargeback is not reversed upon representment. Moreover, appealing lost chargeback disputes is cost-prohibitive since the "loser" is required to pay $500 for arbitration.

Chargebacks are disputes between three parties: the issuer, the merchant, and the cardholder. But the network rules, which heavily favor issuers, determine who bears the liability. If issuers were responsible for all fraud, it might be appropriate to provide a fraud adjustment to help them cover the fraud losses incurred due to authorizing transactions at merchant locations. However, if merchants and cardholders end up being responsible for more than two-thirds of fraud, it doesn't make sense for issuers to collect an adjustment for that fraud. For the fraud adjustment to be more equitable, the Board should change the fraud adjustment to better reflect the reality of how disputes are arbitrated today.

Because we do not have a guarantee of payment when a debit card is used, we face increased risk liability as the transaction amount goes up just as issuers do. For this reason, a fraud adjustment fee paid to issuers is inappropriate for addressing fraud losses since network-mandated, issuer-centric chargeback rules prevail in the marketplace.

By continuing its biannual reporting and making commensurate reductions in the weighted average cost, the Board will continue to incentivize banks to lower their costs and to develop and use technology that is less prone to fraud while still allowing for the most efficient issuers to benefit from the spread between costs and the cap. This will generate the further benefits of greater parity in the relationship between issuers and merchants and increased savings for American consumers.

Thank you in advance for your attention to the comments in this letter. If you have any questions, please feel free to reach out to me at Maria.Smith@Walgreens.com.

Respectfully,

MSmith

Maria Smith

Vice President, Payments & Financial Services