Maine Credit Union League

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

Re: Debit Card Interchange Fees and Routing

Dear Sir or Madam:

I am writing on behalf of the Maine Credit Union League (MCUL) to provide comments in response to the Federal Reserve Board's request for public comment on Debit Card Interchange Fees and Routing (Docket No. 2023-24034). MCUL **opposes the proposed rule** for the reasons discussed below.

Maine is home to 49 credit unions ranging in asset size from just over $1 billion to $6 million with a median asset size of $176 million. The Maine Credit Union League represents all Maine based credit unions in the state and two credit unions with a physical presence in the state that are headquartered elsewhere. Maine has an incredibly robust local, small financial services industry that focuses on service and community. Maine is a rural state of 1.3 million people with over 730,000 members at Maine-based credit unions. In our state, large financial institutions are the exception rather than the rule.

The basis for the Federal Reserve's calculation of the new interchange limit is based on a new transaction-weighted methodology and does not properly examine the effect on smaller, exempt issuers of debit cards. The calculation uses a fixed multiplier to correspond to a targeted portion of transactions to, in theory, allow issuers to recoup their costs of the base component over time.[1] This change in the algorithm reflects the experiences of large issuers but not that of small issuers. The largest issuers of debit cards can offer their programs at a lower cost because of their size and can reduce costs by automating systems, and cutting services around authorization, clearance, and settlement (ACS), and reducing transaction monitoring.

[1] 88 Fed. Reg. 78100, 78106.

In 2011, the original interchange calculation was made by looking at the average per-transaction cost for reporting issuers and set a cap on the base component based on the 80th percentile issuer's average per-transaction included costs.[2] Though smaller institutions were underrepresented in that initial survey, there was still some input from small issuers. The new proposal is solely based on the report of non-exempt issuers and focuses on per-transaction costs. Credit unions are not considered appropriately in the calculation. The cooperative, not-for-profit structure, limited fields of membership, and the limitations on business lending and investment of credit unions forces many of them to function on lean margins. In addition, because credit unions are usually small institutions, recouping their costs would take multiple years because they are not making enough transactions to cover the weighted per-transaction costs.

Though all of Maine's credit unions are exempt from the proposed rule, they will still be impacted by the changes proposed. The Federal Reserve Board's 2019 report on interchange fees indicated a 19.3 percent revenue loss on debit card interchange transactions processed on single-message networks between 2011 and 2019 for credit unions and community banks that are exempt institutions.[3] If the past is precedent, the change to the marketplace for exempt issuers will impact the overall card processing system and lead to the same shift in revenue that was seen in the last decade.

Further complicating the matter of costs, Regulation II's routing requirements have established a dual pathway for the authorization of debit payments by an issuer. The routing mandates have reduced revenue from debit card transactions for all issuers regardless of asset size. Significant differences exist between single-message and dual-message networks that raise operation and fraud costs for issuers. While merchants can select their network, they frequently opt for the most cost-effective solution without considering other factors, such as fraud.

Financial institutions are subject to the provisions of the Gramm-Leach-Bliley Act (GLBA) and are required to maintain robust cybersecurity and privacy systems to minimize the exposure of consumer data while retailers have no such provision. Retailers are expected to favor single-message networks for card not present transactions to the higher-fee, dual message networks. Credit unions rely on interchange revenue to improve security and reduce fraud. The funds also contribute to costs that are not covered in the interchange revenue calculation, such as insufficient funds losses, card-replacement costs, and international fraud losses. Fraud incidence has more than tripled from 2011 to 2021, and issuer fraud losses

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[2] 76 Fed. Reg. 43394, 43433 (July 20, 2011).

[3] Board of Governors of the Federal Reserve, "2019 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions" (2021).

have also increased. The loss of this income harms credit unions and puts at greater risk the private information of the member.

While non-exempt issuers can compensate for interchange losses through other business lines, credit unions have limited avenues where they can recoup costs of processing card transactions. By further contracting the revenue that credit unions can collect, the proposed rule would force credit unions to raise fees and interest rates for riskier consumers and reduce availability of products like free checking accounts.[4] A decrease in the availability of low- and no-cost accounts at exempt issuers will increase costs to consumers and make it harder for exempt issuers to serve their members at a low cost. The impact will be most acutely felt by low-income consumers, for whom banking may already be expensive. Credit unions with limited capacity to operate debit programs as loss leaders may face pressure to merge further reducing the competitive market and ultimately leading to fewer choices and higher costs for consumers.

Consumers will lose the benefits provided by interchange revenue and will not see increased savings in retail establishments. A study performed by the Federal Reserve Bank of Richmond in 2014, indicated that most merchants retained their pricing structures after the enactment of Regulation II, and 21 percent increased their prices.[5] The 2014 study indicated that enactment of the Durbin Amendment and Regulation II did not contribute to a meaningful decrease in consumer pricing. When this reality is paired with the loss of services and competitive options for consumers, it is difficult to see how this rule would result in a benefit to the average American.

For these reasons, the Maine Credit Union League urges the Federal Reserve Board to withdraw the proposed rule on overdraft lending. If you have any questions or need additional information, please do not hesitate to contact me.

Thank you for the opportunity to provide comments on this important issue.

Sincerely,

Robert Caverly
Vice President of Advocacy and Outreach

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[4] Mark D. Manuszak 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), htps://doi.org/10.17016/FEDS.2017.074.

[5] Wang, Zhu, Schwartz, Scarlett and Mitchell, Neil, "The Impact of the Durbin Amendment on Merchants: A Survey Study." (2014) Federal Reserve Bank of Richmond Economic Quarterly, Volume 100, Number 3.