May 10, 2024

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

RE: Notice of proposed rulemaking on Regulation II; Docket No. R-1818, RI 7100-AG67

Dear Ms. Misback:

We are writing on behalf of **Consumers Credit Union of Kalamazoo, Michigan**, to comment on the Notice of Proposed Rulemaking to amend Regulation II ("NPRM") issued by the Board of Governors of the Federal Reserve System ("Board"). The Board should not amend Regulation II as proposed in the NPRM because it will have a negative effect on all financial institutions and consumers.

Consumers Credit Union was founded in 1951 and now serves members throughout Michigan with 27 locations and growing. We employ over 400 passionate and dedicated people to serve our members with over-the-top service, financial wellness and easy-to-use technology. In addition to our banking services, we dedicate ourselves to eight (8) core charities through volunteer hours and monetary donations.

We are submitting these comments to the Board to make it aware of the harm that Regulation II has and will continue to cause on institutions of all sizes. As a smaller issuer in the ecosystem, we do not have the same ability to scale services and reduce costs to offset the loss of interchange income. Since the pandemic, we have experienced 48% growth in our Card Not Present (CNP) transactions which have the highest rate of fraud, causing our fraud costs to climb. These increased costs will not be covered by the 0.3 cents increase proposed.

In 2023 alone, Consumers Credit Union lost 9.62% of revenue to fraud losses and processing, which equates to one million, two hundred and thirty-four thousand, three hundred and fifty-seven dollars and thirty-five cents ($1,234,357.35). Continued fraud losses will cause smaller institutions, like ourselves, to rethink our Free Checking product as it will operate at a loss. This in turn negatively affects our members who will be forced to pay for banking services that are today free.

Interchange fees are vital to credit unions as they help offset the growing costs associated with credit card fraud detection, credit monitoring and, most importantly, they allow credit unions to shield members AND merchants from fraudulent charges via zero-liability protection policies when fraudsters take advantage of members, merchants and institutions alike. A reduction in interchange strikes at the very heart of data security, as it takes away our budget to protect our members.

The original intent of these proposals was for the merchant savings to be passed to the consumer. Multiple studies have been conducted to discover where these billion-dollar savings ended up. Unfortunately, it was not with the

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consumer. Studies conducted by Richmond Federal Reserve in conjunction with Javelin Strategy & Research concluded that:

- A majority of merchants raised prices,
- Many merchants implemented minimum purchase amounts or surcharges for card usage,
- 77% of merchants did not change prices after debit price caps, and
- Only 1% of merchants passed any savings to consumers.

The Board proposes to decrease the interchange fee cap under Regulation II by approximately 30%. We know from experience the $10 billion exemption is hollow and the proposal will worsen Consumers Credit Union's financial position and harm our customers, comparable to our experience following the introduction of Regulation II in 2011. Changes to any part of this ecosystem will cause substantial ripple effects throughout the card network because the costs of managing card programs will only increase and those costs will be passed down to other system participants. This means those with the least bargaining power (credit unions, community banks, small businesses & consumers) will be the most impacted.

As Governor Bowman has cautioned, finalizing the NPRM will harm us and other exempt financial institutions even though it does not directly target our business. As a result, we will have to take action to mitigate the detrimental effect on Consumers Credit Union and how we are able to serve our members. To offset these negative consequences, we will have to consider:

- Eliminating Free Checking account options,
- Eliminating or reducing our rewards programs for credit and debit programs,
- Reducing our local community support of businesses and core charities,
- Reducing deposit rates,
- Cutting loan & limit availability to members, and
- Tightening underwriting criteria, thus reducing the number of members who can borrow.

Many of these unintended consequences will be detrimental for lower income households and will grow our unbanked population in the United States. Our current banking model allows financial institutions the ability to offer Free Checking and debit card options to give members safe access into the banking ecosystem. The reduction in revenue will also lead to further consolidation of smaller community-based financial institutions, minimizing competition and thus, banking options for members.

Additionally, the automatic updating of the interchange fee cap, without notice and comment, will be near impossible for acquirers. This change creates operational burdens and adversely affects issuers as it is difficult to account for costs for in-year changes. Most importantly, making such a substantial change WITHOUT NOTICE AND COMMENT raises legal concerns about the Federal Reserve's regulatory authority to take such a negatively impactful automatic action.

Finally, the NPRM comes at a time when **Consumers Credit Union** and the industry more generally are still trying to adjust to the most recent amendment to Regulation II, which went into effect on July 1, 2023. That amendment did not directly affect the interchange fee cap, but it did impose additional routing restrictions on debit card issuers, including institutions like us, supposedly exempt from the interchange fee cap. As the Board's own data shows, average interchange per exempt debit transaction is much lower for single-message networks than for dual-message networks. The most recent amendment forced us to enable a PINless single-message network for ecommerce transactions, reducing our revenue. This requires additional program costs to manage a second network in addition to the loss in revenue. Although the effects of the July 1, 2023 amendments are still being implemented by acquirers, we expect it will reduce our revenue and urge the Board to pause implementation of the pending proposal to ensure small financial institutions are not disproportionately harmed. Additionally, PINless networks do not have the security features of other networks, and therefore we are also likely to face increased costs from fraud losses. If the Board also finalizes the NPRM, it will negatively impact our financial institution and customers, which may imperil access to basic financial services and drive further consolidation in the industry. None of these predictable outcomes will benefit consumers or promote the safety and soundness of our financial system.

consumers credit union

If you have any questions regarding our comments, please contact the undersigned at **1-800-991-2221** or **see below for their email addresses.**

Sincerely,

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