

Proposal: 1818(AG67) Debit Card Interchange Fees and Routing

Description:

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Comment ID: 159859

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Comments:

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Dear Federal Reserve Board:

I am writing on behalf of Space City Credit Union in response to the proposed amendments to Regulation II issued by the Board of Governors of the Federal Reserve System.

The Regulation II proposal is based on flawed methodology that disregards the cost experience for most issuers, especially smaller credit unions. Space City Credit Union opposes any reduction in the interchange fee cap.

The Federal Reserve Board of Governors should withdraw the proposed rule for the following reasons:

1. This proposal will increase profits of big box retailers and merchants while harming credit unions and consumers.

1. 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. Further reducing the fee cap and by extension debit interchange revenue will only exacerbate these issues.

2. This directly impacts consumers.

1. The Electronic Fund Transfer Act (EFTA) requires the Federal Reserve to consider the impact of its regulations 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 Federal Reserve reduces the fee cap as proposed.?

3. This affects credit unions of all asset sizes.

1. The Board has not adequately considered the impact of its proposal on exempt issuers &ndash; credit unions that have assets of less than \$10 billion. 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.

4. The Federal Reserve's transaction-weighted methodology is flawed. Credit unions that lack scale would be unfairly penalized, as would many other issuers denied full recovery of their costs.

5. Regulatory pressure on sources of fee income and the high cost of growing debit fraud will put pressure on credit unions to consolidate or eliminate critical programs that low and moderate-income populations rely on to end a cycle of debt and reach their financial goals.

Further:

\* Credit unions, as non-profit financial cooperatives founded on communal ties and relationship banking, reinvest in the communities they serve. The revenue generated from interchange fees often supports community-oriented projects, grants and programs.

\* More than 50% of covered credit unions indicate fewer community grants and scholarships are likely if the interchange fee is reduced.

\* Interchange fees support affordable access to credit. Reducing fees hinders the ability to serve Main Street small businesses and low-income communities.

\* Small business owners and entrepreneurs rely on credit unions to secure credit cards and capital to

launch and grow their businesses.

\* Additionally, when a small business chooses to accept credit cards, it opens opportunities: Consumers spend twice as much when using a credit card compared to cash purchases. Combined with the safety and security provided by the current credit card payments system, accepting credit cards pays off for small businesses.

Credit unions are less able to absorb reductions in interchange revenue due to their unique, not-for-profit structure. Credit unions with limited capacity to operate debit programs as loss leaders may face pressure to merge, especially in an environment where there is a regulatory agenda to limit fee income.

A proposed reduction in the debit interchange fee cap could disproportionately affect low-income and minority households 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 at the time of electronic payments as most current 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:

\* America's Credit Unions' data 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.

The proposed amendments to the debit interchange fee cap will harm credit unions and their members because the Durbin Amendment affects all debit card issuers, even those considered "exempt" (issuers below \$10 billion in total assets).

## REGULATION II DATA

From 2012 to 2022, issuers collectively lost nearly \$106 billion in interchange revenue, a figure that largely represents what merchants kept in their own pockets.

\* The Federal Reserve Bank of Richmond research reveals the vast majority of merchants did not pass along any of their regulatory savings onto consumers.

A Government Accountability Office (GAO) 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 noninterest checking accounts offered by exempt financial institutions declined by 15.5 percent.

A 2022 study found that fees including minimum balance requirements and maintenance charges fall disproportionately on low- and moderate-income (LMI) communities and majority-minority neighborhoods compared to non-LMI areas.

Among the 21 covered credit union issuers directly subject to the fee cap, the NCUA designates 10 as low-income.

The Board's historical data shows that after introducing the fee cap, debit interchange revenue from single-message network transactions declined 29 percent for exempt issuers.

In closing, the Board's proposal for the new fee cap is both unnecessary and premature. They lack crucial data on the recent changes to CNP routing rules (2022) and rely on a flawed method that could deny full cost recovery to up to one-third of issuers. Additionally, the Board has excluded relevant expenses from the fee cap calculation and significantly underestimated the impact on exempt issuers,

particularly small credit unions serving low-income and rural communities. For these reasons, we strongly urge the withdrawal of the proposed rule.

Thank you for the opportunity to provide comments in response to the proposed rule. If you have any questions, please do not hesitate to contact me.

Thank you,