



December 12, 2024

The Honorable Jerome H. Powell
Chair
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

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

Dear Chair Powell:

We are writing to reiterate our strong concerns with the proposed amendments to Regulation II (Reg II).¹ As you are aware, Reg II currently sets a cap on debit card interchange fees to a base component of 21 cents, an ad valorem component of 5 basis points multiplied by the value of the transaction, and a fraud prevention adjustment of 1 cent.² The proposed rule arbitrarily lowers the cap on debit card interchange fees to a base component of 14.4 cents, an ad valorem component of 4 basis points multiplied by the value of the transaction, and a fraud prevention adjustment of 1.3 cents. The proposed changes to the cap are based on 2021 survey data that is artificially skewed by negative externalities stemming from the COVID-19 pandemic, and the data does not consider subsequent routing restrictions imposed on card-not-present transactions.

It is our belief, and the belief of over 300 commenters, that the proposed amendments to Reg II are fundamentally flawed and should not be finalized. Attached to this cover letter is a report showing that nearly 80 percent of the comment letters submitted to the Board oppose the implementation of the proposed amendments to Reg II. Comments in opposition to the rule cited myriad issues, including:

- Ill-conceived methodology that fails to (i) account for allowable costs, and (ii) maximize cost recovery for covered institutions.
- Consumer harm—particularly for low- and moderate-income consumers—in the form of reduced access to affordable banking services.
- Failure to assess the impact that recent changes to the routing rules will have on fraud costs, which have increased for our members.
- Failure to account for the combined impact of proposed amendment and other recently promulgated bank regulations, which will, in aggregate, impair access to basic banking services by impacting a bank's ability to recuperate costs.
- Failure to account for the proposed amendment's impact on community financial institutions, despite an asset-based exemption that has proven ineffective.

¹ Debit Card Interchange Fees and Routing, 88 Fed. Reg. 78,100 (Nov. 14, 2023).

² 12 C.F.R. §§ 235.3 and .4(a).

Significantly, commenters reinforced that the proposed amendments to Reg II threaten the economic viability of offering Bank On accounts for low- and moderate-income households. The goal of the Bank On program is to provide banking services to the unbanked.

According to new data from the Federal Reserve Bank of St. Louis, the program is currently working as intended.³ Bank On accounts have been opened in nearly 90 percent of U.S. zip codes, and there has been a 16 percent increase in the number of monthly debit card transactions processed per Bank On account.⁴ Further, the most recent data from the FDIC shows that only 4.2 percent of U.S. households are unbanked—an historic low—and the FDIC credits the growth of the availability and use of these Bank On accounts with bringing this number down.⁵ Finally, in October, subsequent to the closing of the comment period, the US Treasury issued its National Strategy for Financial Inclusion, which endorsed private sector programs like Bank On and noted that “[g]overnment, nonprofit, and private sector actors should continue to collaborate on the Bank On initiative.”⁶

ABA believes the proposed amendments will reduce the availability and affordability of Bank On accounts for low- and moderate-income Americans, and the comment file demonstrates that our view is shared by civil rights leaders who are working to close the unbanked gap, among others.⁷

In addition, we note that even the minority of commentators that conceptually supported the proposal raised fundamental issues with the amendments as proposed. These comments, taken together with the comments opposing the proposed amendments, demonstrate that the proposal is fundamentally and critically flawed.

We encourage you to review this report and take the time to understand the detrimental impact the proposed amendments will have on community financial institutions, small businesses, and American consumers. In light of the wide range of comments in opposition and the substantive concerns raised, we would further urge the Board to withdraw the proposed amendments.

³ Federal Reserve Bank of St. Louis, Bank On National Data Hub: Findings from 2023 (Nov. 12 2024), available at <https://www.stlouisfed.org/community-development/bank-on-national-data-hub/bank-on-report-2023>.

⁴ *Id.*

⁵ Michael del Castillo, FDIC Boss Credits One Simple Technology for Helping More Americans than Ever Get A Bank Account, *Fortune* (Nov. 18, 2024), available at <https://fortune.com/2024/11/18/more-americans-than-ever-have-bank-accounts-fdic-boss-credits-this-key-technology/>.

⁶ US Treasury, National Financial Inclusion Strategy in the United States (October 2024), available at <https://home.treasury.gov/system/files/136/NSFI.pdf>.

⁷ Letter from Rev. Al Sharpton to the Board of Governors of the Federal Reserve System (Apr. 30, 2024), available at https://www.federalreserve.gov/SECRS/2024/May/20240507/R-1818/R-1818_050124_159038_278955250295_1.pdf; American Bankers Association, Federal Reserve’s Flawed Debit Card Proposal Harms Banks, Credit Unions and Consumers (May 10, 2024), available at <https://www.aba.com/about-us/press-room/press-releases/federal-reserves-debit-card-proposal>.



If you have any questions or need any additional information, please reach out to me at trosenkoetter@aba.com.

Sincerely,

A handwritten signature in black ink, appearing to read 'Tom Rosenkoetter', with a long horizontal flourish extending to the right.

Tom Rosenkoetter
Executive Director, ABA Card Policy Council
SVP, American Bankers Association

CC: Philip N. Jefferson, Vice Chair, Federal Reserve Board
Michael S. Barr, Vice Chair for Supervision, Federal Reserve Board
Michelle W. Bowman, Governor, Federal Reserve Board
Lisa D. Cook, Governor, Federal Reserve Board
Adriana D. Kugler, Governor, Federal Reserve Board
Christopher J. Waller, Governor, Federal Reserve Board
Susan M. Collins, President and Chief Executive Officer, Federal Reserve Bank of Boston
John C. Williams, President, Federal Reserve Bank of New York
Patrick T. Harker, President, Federal Reserve Bank of Philadelphia
Beth M. Hammack, President and Chief Executive Officer, Federal Reserve Bank of Cleveland
Thomas I. Barkin, President and Chief Executive Officer, Federal Reserve Bank of Richmond
Raphael W. Bostic, President, Federal Reserve Bank of Atlanta
Austan D. Goolsbee, President, Federal Reserve Bank of Chicago
Alberto G. Musalem, President and Chief Executive Officer, Federal Reserve Bank of St. Louis
Neel Kashkari, President, Federal Reserve Bank of Minneapolis
Jeffrey R. Schmid, President, Federal Reserve Bank of Kansas City
Lorie K. Logan, President and Chief Executive Officer, Federal Reserve Bank of Dallas
Mary C. Daly, President, Federal Reserve Bank of San Francisco

Regulation II Debit Card Proposal: Public Comments Raise Substantive Concerns



TABLE OF CONTENTS

I.	Executive Summary	3
II.	Analysis of Comments	5
	A. OPPOSITION TO THE PROPOSAL	5
	B. SUPPORT FOR THE PROPOSAL	6
	C. GEOGRAPHIC DISTRIBUTION	7
III.	Summary of Arguments by Topic.....	8
	A. METHODOLOGY	8
	B. CONSUMER IMPACT	9
	C. LMI IMPACT	10
	D. FRAUD	10
	E. IMPACT TO COMMUNITY FINANCIAL INSTITUTIONS	11
	F. IMPACT TO SMALL BUSINESS	12
	G. COMPETITION	12
	H. CHANGES TO NETWORKS FROM JULY 2023 RULE	12
	I. BANK ON	13
IV.	Summary of Comments by Commentor.....	13
	A. BANK/CREDIT UNION INDUSTRY	13
	B. MERCHANTS	14
	C. ACADEMIC	15
	D. ACTIVISTS	15
	E. CONSULTANT/FINTECH	15
	F. GOVERNMENT	16
	G. INDIVIDUAL	16
	H. NON-PROFIT	16
V.	Conclusion	17

I. EXECUTIVE SUMMARY

On November 14, 2023, the Board of Governors of the Federal Reserve System (“**Board**”) published a Notice of Proposed Rulemaking (“**Proposed Rule**”) that would reduce the debit card interchange fee cap in Regulation II (12 C.F.R. pt. 235).

Currently, the interchange fee charged on a debit card transaction that does not qualify for an exemption can be no more than the sum of:

- 21 cents (the “**base component**”);
- 5 basis points multiplied by the value of the transaction (the “**ad valorem component**”); and
- For a debit card issuer that meets certain fraud-prevention standards, a “**fraud-prevention adjustment**” of 1 cent per transaction.

The Proposed Rule would update all three components of the interchange fee cap based on the 2021 data reported to the Board by non-exempt debit card issuers in the Debit Card Issuer Survey (“**Survey**”). Under the Proposed Rule:

- The base component would decrease to 14.4 cents from 21.0 cents;
- The ad valorem component would decrease to 4 basis points (multiplied by the value of the transaction) from 5 basis points (multiplied by the value of the transaction); and
- The fraud-prevention adjustment would increase to 1.3 cents from 1.0 cents.

The Proposed Rule would not amend the exemptions to the interchange fee caps, including the exemption for interchange fees charged or received by debit card issuers with less than \$10 billion in total assets (i.e., the “**small issuer exemption**”). The Proposed Rule would, however, amend some of the official staff commentary related to the small issuer exemption, as well as other aspects of Regulation II.

The Board also proposes to codify an approach for updating the three components of the interchange fee cap every other year going forward based on the latest data reported to the Board by covered issuers. The Board proposes to not seek public comment on such future updates.

Comments on the Proposed Rule were originally due on February 12, 2024; however, after numerous requests from the industry, the Board extended the comment period until May 12, 2024.

Of the 413 comments reviewed, 321—approximately 78 percent—of the commentors opposed the Proposed Rule, and 88—approximately 21 percent—of the commentors supported the Proposed Rule.¹ The remaining four comment letters did not express an opinion on the substance of the Proposed Rule but posed additional considerations and/or requests for the Board, some of which were unrelated to the Proposed Rule. For example, two comments requested that a rule be created to prevent businesses from surcharging. Another comment did not take a strong position in support or opposition of the Proposed Rule, but focused its entire narrative on the impact of banking-as-a-service accounts on low- and moderate-income (“**LMI**”) consumers in the wake of more inaccessible accounts at large institutions.

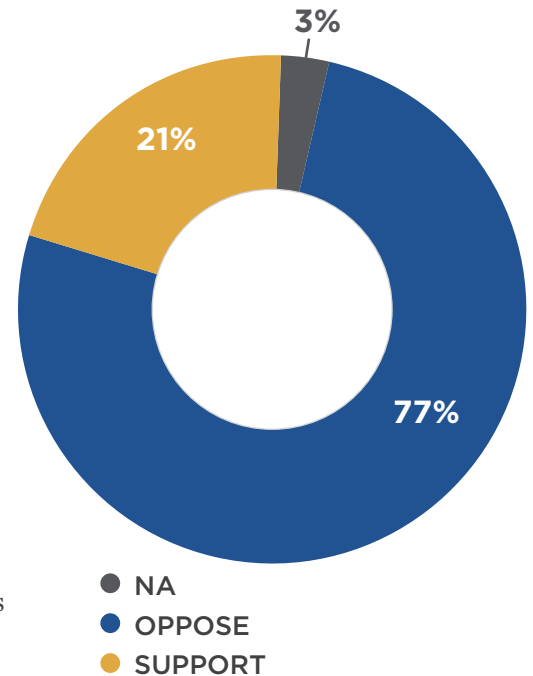
¹ The total number of comment letters reviewed reflects the comments posted by the Board to its public website as of November 26, 2024, excluding duplicate letters and letters that had no substantive content.

The comments were submitted by different constituencies, including:

- Academics
- Activists
- Banks and Credit Unions
- Consultants and Financial Technology Companies (“fintechs”)
- Government Officials
- Individuals
- Insurance Companies
- Merchants
- Non-profits
- Payment Card Networks
- Trade Associations²

There were letters submitted by commentators in each of the above listed constituencies that opposed the Proposed Rule. Letters in support of the Proposed Rule were submitted by activists, consultants and fintechs, government officials, individuals, merchants, and trade associations. The majority of the comments in support of the Proposed Rule were submitted by merchants or the trade associations that represent them.³

Comments that Support or Oppose Regulation II



As discussed in further detail throughout, the comment letters addressed a number of different concerns, including:

- The Board’s proposed methodology for calculating the interchange fee cap.
- Potential for consumer harm.
- The impact of the Proposed Rule on Bank On.
- The impact of the Proposed Rule on fraud prevention, as it affects both merchants and issuers.
- The impact of the Proposed Rule on small business.
- The impact of the Proposed Rule on community financial institutions, with a particular focus on non-profit credit unions.
- Concerns about competitive effects.
- The impact of July 2023 changes to the routing requirements.

² Most trade associations that submitted comment letters represented either banks and/or credit unions or merchants.

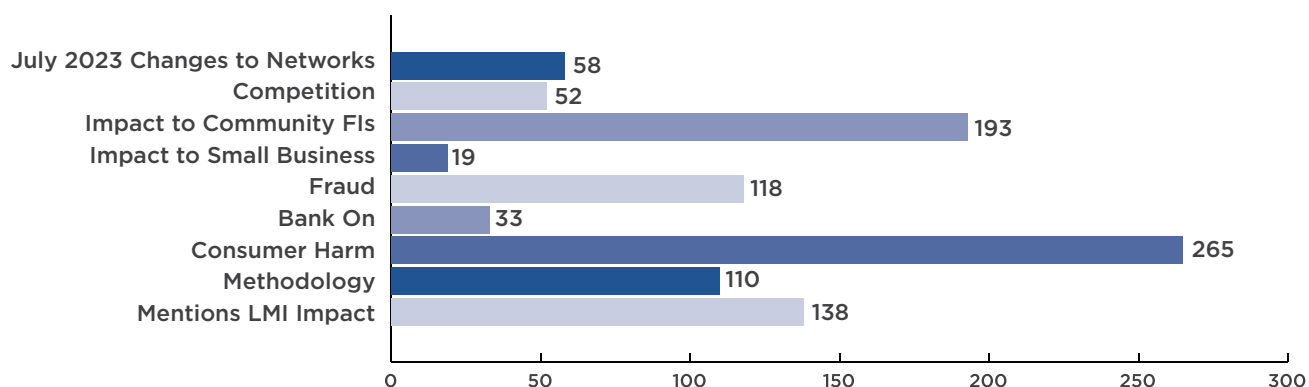
³ Overall, 64 comments or 73 percent of the comments in support of the Proposed Rule were submitted by merchants or merchant trades.

II. ANALYSIS OF COMMENTS

A. Opposition to the Proposal

A majority of comment letters—321 or 78 percent—oppose the Proposed Rule and either call for a withdrawal or re-proposal, or otherwise express significant concerns with the Proposed Rule or at least one of its key aspects.⁴ Members within each constituency that commented on the Proposed Rule submitted comments opposing the Proposed Rule. These comment letters covered a wide range of concerns, including:

Opposition to Updated Reg II by Concern



Methodology. Commentors opposing the Proposed Rule raised a range of concerns about the Board’s methodology, including:

- The failure of the Board to reconsider allowable costs, despite acknowledging in its 2011 rulemaking that certain costs may be included in the interchange fee calculation once the Board had sufficient data to analyze them.
- The Board’s proposed 98.5 percent cost recovery target.
- The Board’s proposed 3.7 multiplier.

Consumer Harm. Commentors, including prominent civil rights activists, raised concerns about consumer harm (particularly LMI consumer harm) that could result from the Proposed Rule. In particular, commentors focused on increased costs of banking services and failure of merchants to pass through savings to consumers.

July 2023 Regulation II Amendments. Commentors argue that the Board should wait until 2023 Survey data is available to establish a new interchange fee cap. This would allow the Board to assess the impact of new routing requirements on costs and fraud.

⁴ For example, the methodology the Board used to determine the interchange fee cap.

Competing Regulatory Schemes. As noted above, the Proposed Rule uses data from the 2021 Survey to inform the proposed interchange fee cap, despite the Board’s promulgation of new routing requirements under Regulation II that took effect in July 2023. Additionally, commentors noted that numerous federal banking agencies are currently proposing or finalizing regulations that will impact issuer income streams, including the late fee final rulemaking, proposed rules on NSF fees and overdraft fees, and Basel III endgame rules.

Impact to Community Financial Institutions. A number of community financial institutions submitted comments discussing the impact that the Proposed Rule would have on their operations if finalized. In particular, comments focused on the lack of bargaining power that smaller, and in some cases exempt, financial institutions have with card networks when establishing fees. This lack of bargaining power impacts the amount of interchange that these institutions can collect, even if they are otherwise exempt from the rule.

Additionally, small credit unions emphasized the differences between credit unions and other depository institutions. In particular, comments addressed the fact that credit unions are non-profit financial institutions that will be substantially impacted by decreased revenue streams, which they need to continue providing products and services (especially free products and services). Without interchange revenue, a number of credit unions noted that they would either have to eliminate certain services or start charging consumers for banking services that were previously offered for free.

B. Support for the Proposal

A minority of the comment letters—88 or 21 percent—supported the Proposed Rule’s efforts to decrease the interchange fee cap. The majority of comments in support of the Proposed Rule were submitted by merchants or the trade associations that represent them.⁵ Five of the letters (approximately 6 percent) in support of the Proposed Rule were submitted by government officials, including Senator Dick Durbin (D-Ill.), the namesake of Regulation II’s authorizing statute, and Letitia James, the Attorney General of the State of New York. Some of the topics addressed in comment letters that generally supported the Proposed Rule include:

⁵ 64 comments or 75 percent of letters in support of the Proposed Rule.

Larger institutions have more bargaining power with card networks and issuers, which allows them to negotiate higher interchange fees. When the caps for larger institutions are lowered, it creates a new benchmark for negotiation, leading to lower fees for all institutions, including smaller ones like ours.

**Kellie LeTexier,
Kitsap Credit Union**

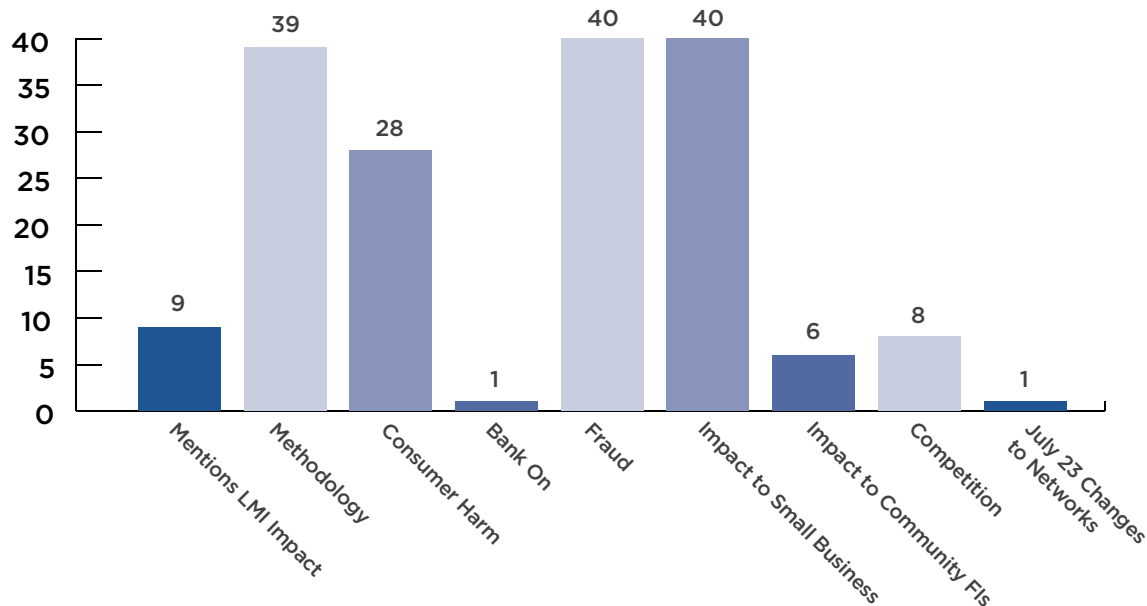
As you know, these negative impacts will not affect Credit Union stock prices or shareholder equity—it will affect interest rates, more robust debit card systems, and the ability to serve more in the community.

**Chris A. Leggatt,
LGE Community Credit Union**

For these reasons, Corner Post, NDRA, NDPMA, and Linney’s Pizza urge the Board to reject the proposed rule and instead adopt a standard that (1) does not include the third, non-statutory category of allowable costs and (2) does not use a fixed multiplier.

**Bryan Weir, Frank H. Chang, et al.,
Consovoy McCarthy PLLC**

Opposition to Updated Reg II by Concern



Methodology. Despite supporting the Board’s efforts to lower the interchange fee cap, comments submitted in support of the Proposed Rule nevertheless argued that the methodology used by the Board was flawed and should be revised. In particular, these comments asserted that the Board’s methodology should yield a lower interchange fee cap than is proposed, including by eliminating the ad valorem and fraud-prevention adjustment components. Additionally, a number of comments argue that the Board should have excluded costs that were not explicitly addressed in the statute.⁶

Debit Card Issuer Survey. Supporting commentors also raised numerous suggestions regarding the biannual Survey. First, some supporting comments suggested that the Board collect data annually to avoid issuers from cost shifting to maximize costs within the reportable period every other year. Second, the majority of supporting commentors asked the Board to consider audit mechanisms to ensure that issuers are accurately reporting the data requested, due to the data’s impact on further revisions to the interchange fee cap.

Fraud. Merchants in support of the Proposed Rule nevertheless criticized the Board’s inclusion of the ad valorem component and fraud-prevention adjustment, arguing that merchants are financially responsible for the bulk of fraud-related losses. As such, they argue that the ad valorem component is an unnecessary inclusion in the methodology, because it compensates issuers for costs that may be borne by merchants. Merchants also argued that the Board should confirm that issuers comply with fraud prevention standards to be eligible for the fraud-prevention adjustment, rather than just certifying compliance.

C. Geographic Distribution

Comments were submitted by commentors in 44 states, the District of Columbia, and Puerto Rico, including several comments submitted by commentors located in various states.

⁶ These costs are often referred to as the Board’s third category of costs, which the Board determined may be included in the interchange fee calculation in certain circumstances.

III. SUMMARY OF ARGUMENTS BY TOPIC

A. Methodology

Of the 413 letters reviewed, 149 letters — or 36 percent of comments—discussed the methodology the Board employed in the Proposed Rule. This includes 110 comments in opposition to and 39 comments in support of the Proposed Rule. These comments ranged all industries.

Letters opposing the Proposed Rule that discussed methodology include letters from academics, activists, banks and credit unions, consultants and fintechs, individuals, non-profits, payment card networks, and trade associations. Letters generally supportive of the Proposed Rule that discussed methodology include letters from consultants and fintechs, government officials, merchants, and trade associations representing merchants. Comments regarding the methodology employed by the Board were vast and covered numerous topics.

Those opposed to the Proposed Rule argued, among other things, that:

- The Board’s proposed methodology does not capture costs that are “reasonable and proportional” to the costs incurred by an issuer in processing electronic debit transactions.
- The Board failed to reconsider allowable costs when determining the new interchange fee cap, despite acknowledging in its 2011 rulemaking that certain costs may be includable when sufficient data was available.
- The cost recovery target of 98.5 percent and the proposed 3.7 fixed multiplier are arbitrary and capricious and would prevent a large number of issuers from recovering their costs.
- The Proposed Rule violates the Takings Clause by not allowing issuers to recover costs at a reasonable rate of return.
- The data used by the Board to establish the interchange fee calculation is unreliable and outdated. Some commentators also argue that the reporting in the Survey is inconsistent on an issuer-by-issuer basis because of poor instructions.
- The biannual automatic adjustment to the interchange fee violates the notice and comment requirement and is not consistent with the “good cause” exemption for avoiding notice and comment requirements.

Those in support of the Proposed Rule argued, among other things, that:

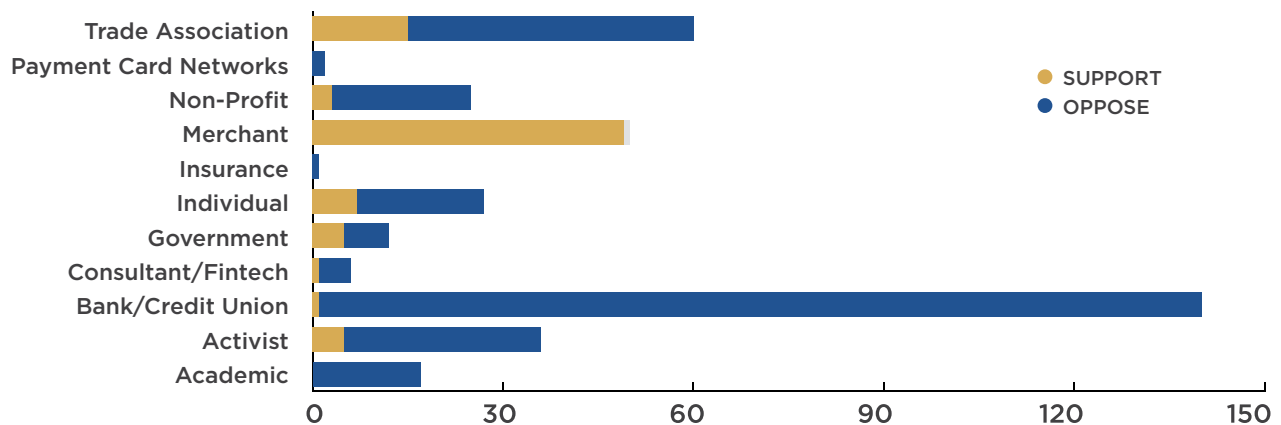
- The data has shown that issuer costs have dropped by half and the reduction in the cap is only one-third.
- The Survey should be completed on an annual basis and the Board should audit the submissions to ensure that they are accurate and do not inflate or cost-shift prices.
- The Board’s 3.7 fixed multiplier is arbitrary and could result in increased interchange fee caps during the adjustment period.
- Generally, those in support of the Proposed Rule argue that the ad valorem and fraud-prevention adjustment components of the calculation should be eliminated. Alternatively, numerous commentators argued that if the fraud-prevention adjustment is retained, the Board should audit issuer compliance with the fraud prevention standards.
- Some commentators argue that the Board should evaluate a tiered approach.

Across both supporting and opposing comments, the Board’s methodology was largely criticized.

B. Consumer Impact

Overall, 274 letters—or approximately 67 percent—discussed the impact of the Proposed Rule on consumers. Commentors opposing the Proposed Rule and discussing consumer impact came from a variety of industries, including academics, activists, banks and credit unions, consultants and fintechs, individuals, non-profits, payment card networks, and trade associations. Of the 274 comments that considered the consumer impact, only 28 comment letters were written by commentors that support the Proposed Rule. These commentors were an activist, a fintech, four merchants, a non-profit, and three trade associations representing merchants.

Consumer Impact Breakdown



Comments opposed to the Proposed Rule raised numerous potential consumer harms, including:

- Increased cost of banking services that resulting in decreased access to banking for certain populations. Commentors argue that this could have the effect of pushing consumers out of the banking system in some instances. For example, customers who cannot meet checking account minimum balances may be subject to account fees that they cannot afford.
- A number of community financial institutions (and in particular, credit unions) argued that decreased revenue will impact their ability to provide community services and free checking accounts.
- Data suggests that despite lower interchange, merchants will not pass through savings to consumers in the form of lower prices.

Enough Black Americans became at risk of becoming unbanked after the 2011 price cap. This problem will only increase in size and scope if the Fed makes the price cap more severe today.

Ronald J. Stephens,
Purdue University

Comments in support of the NRPM generally argued that the Proposed Rule would result in lower consumer costs.

C. LMI Impact

Overall, 148 letters—or approximately 36 percent—discussed the impact of the Proposed Rule on LMI consumers. Commentors were from all industries, with a large number of comments coming from banks and credit unions, the trade associations representing banks and credit unions, and non-profits. Of the 146 letters, only nine were written by commentors that otherwise supported the Proposed Rule.

General criticisms of the Proposed Rule expressed concern that if finalized, the Proposed Rule would decrease access to banking services for LMI consumers due to the likelihood of increased fees associated with banking services. Comments in support of the Proposed Rule generally argued, but without specific data, that the reduced interchange fee cap will help reduce pass-through costs to consumers and will serve to discourage monopolies that can inflate costs and harm consumers.

D. Fraud

Overall, 158 or approximately 38 percent of the comment letters discussed fraud. Of the 158 letters, 118 were submitted by commentors opposing the Proposed Rule, and 40 were submitted by commentors that generally support the Proposed Rule. The vast majority of letters discussing fraud rates were submitted either by banks, credit unions, and payment card networks (which oppose the Proposed Rule) or merchants (which support the Proposed Rule).

A study conducted by the Richmond Federal Reserve in conjunction with Javelin Strategy and Research concluded that current Regulation II has had limited positive effects for consumers. According to the study's authors:

- 77 percent of merchants did not change prices following the implementation of debit card price caps.
- 22 percent of merchants chose to increase prices; and,
- 1 percent passed on savings to customers.

Andrew Morris,
America's Credit Unions

The current fraud prevention adjustment proposal significantly underestimates the actual costs associated with combating increasingly sophisticated fraud, thereby increasing the risk of all debit card users becoming victims of fraud.

Bill Cheney,
SchoolsFirst Federal Credit Union

The requirement that issuers allow merchants to access two unaffiliated networks now affords merchants a means of routing transactions over their preferred network. Unsurprisingly, when provided a choice merchants tend to select the lower-cost network. This recent change in the routing of debit card transactions came with its own implications. Perhaps most notably, lower-cost networks can be more vulnerable to fraud. Consequently, giving merchants the option of choosing their preferred network means that as CNP fraud has increased the routing of those CNP transactions over lower-cost, single-message networks has led to a decline in the percentage of fraudulent debit transactions that issuers can recover.

Bill Thomas, United Nations Federal Credit Union

Commentors opposed to the Proposed Rule argue that (1) less interchange fee revenue will result in less investment in fraud prevention measures (e.g., cybersecurity), (2) the Proposed Rule fails to consider the impacts of the July 2023 Regulation II amendments on fraud (e.g., merchants can route payments on less secure networks, potentially resulting in increased fraud losses), and (3) fraud rates are generally on the rise following increases in contactless payments.

Commentors in support of the Proposed Rule generally argued that issuers and payment card networks shift the burden of fraud losses onto merchants, and therefore should not recover fraud costs through the ad valorem component of the interchange fee calculation. Certain commentors argued that the Board should require issuers to compensate merchants for fraud losses, while others argued that the Board should ban issuers from shifting fraud losses to merchants if issuers are compensated for fraud under the interchange fee calculation. Commentors in support of the Proposed Rule also argued that if the Board maintains the fraud-prevention adjustment, it should audit compliance with fraud prevention requirements instead of permitting issuers to certify that they are eligible for the adjustment.

E. Impact to Community Financial Institutions

Of the 413 letters reviewed, 199 letters—approximately 48 percent of comments—addressed the impact of the Proposed Rule on community financial institutions. Nearly all of the comments addressing this issue were opposed to the Proposed Rule.⁷ The bulk of the comments were submitted by banks and credit unions or the trade associations that represent them.

These comments focused on the fact that community financial institutions (both exempt and non-exempt) are more likely to be harmed by the Proposed Rule because these institutions are unable to generate revenue through other streams like larger financial institutions can. In particular, a substantial number of credit unions and credit union trade associations submitted comments highlighting the differences between traditional banks and credit unions, and how lower interchange could negatively impact the non-profit credit union model. Most financial institution commentors suggested that they will have to cut free banking services and charge additional fees in order to compensate the income lost through interchange.

Many commentors flagged that community financial institutions have less bargaining power, which impacts their ability to negotiate pricing. This is true even where the institution is exempt from Regulation II. Many exempt institutions commented that the promulgation of Regulation II has nonetheless impacted their interchange fee revenue since 2011.

Credit unions, unlike larger financial institutions, operate on a not-for-profit basis and focus on returning value to our members in the form of enhanced products and services as well as investments in our communities, many of which qualify as low income designated. This means these communities have limited access to financial services. Additional changes to debit interchange could have a significant impact on a credit union's ability to continue providing products and services to these already disadvantaged members.

Amy Ciciliot,
Lookout Credit Union

Regulators need to recognize the impact of their decisions on America's community banks that serve the full range of banking needs across a wide spectrum of consumers, small businesses, and communities. We do not have the capacity to offset this revenue source and the lower income communities which we serve will be unable to pay service charges on their current free checking accounts.

Mark J. Cvrkel, Kish Bank

⁷ Only six of 199 letters supported the Proposed Rule.

F. Impact to Small Business

Overall, 59 of 413 letters (approximately 14 percent) address the impact the Proposed Rule may have on small businesses. Of these, 40 of the comments were submitted in support of the Proposed Rule, and 19 were submitted in opposition.

The majority of the supporting comments are submitted by merchants and the trade associations that represent them. Comments in support of the Proposed Rule generally expressed that decreased interchange fees will help level the playing field between large merchants and small businesses and will help to decrease operating costs. However, a number of letters nonetheless expressed concerns about the impact of the Proposed Rule on small ticket purchases, which tend to collect disproportionately more in interchange fees.

Comment letters opposing the Proposed Rule note that because small merchants cannot scale their costs as well, they will not receive a windfall of profits like larger merchants. Commentors opposed to the Proposed Rule also noted that an unintended consequence of the proposal may be that small businesses end up paying more money in bank account fees.

G. Competition

Approximately 60 letters, or approximately 15 percent, discussed the Proposed Rule's potential impacts on competition. The large majority of these letters were submitted in opposition to the Proposed Rule.⁸ Some comments addressed concerns that fintechs partner with exempt institutions to take advantage of higher interchange revenue, which disadvantages competing institutions and consumers that get less direct access to banking services. Others noted that debit card issuers compete with the Board's own FedNow product, which did not exist when Regulation II was originally promulgated in 2011.

The marginal benefit small businesses might receive from a reduction in their swipe fee liabilities would be far outweighed by the massive windfall that the mega-retailers will receive. Small companies simply cannot scale their costs as well. Flush with billions of more dollars from Regulation II, Costco and Walmart will put tens of thousands of more small and medium entrepreneurs, including minority-owned businesses, out of business.

David Byrd,
Former National Director
of the Minority Business
Development Agency

When Regulation II was first written, the Fed did not operate a payments system (FedNow) that directly competed with debit cards. Now it does, through FedNow. There is concern in the industry that by using its regulatory power to cap the revenue that banks may earn from private sector debit cards, there may be an unfair advantage given to the Fed's own payment services.

Clark A. Hervert, First National Bank in Ord

H. Changes to Networks from July 2023 Rule

Overall, 59 comments (approximately 15 percent) addressed the 2023 amendment to Regulation II and its impact on the Proposed Rule. All but one comment was submitted in opposition to the Proposed Rule.

Commentors argue that the Proposed Rule should not be finalized until the Board's data covers a time period for which changes to the routing requirements in Regulation II were in effect. Commentors argue that

⁸ 52 of the comments.

this data should be considered because, among other things, it is yet to be seen whether increased fraud resulted from the rule. Many comments also address other rulemakings, in addition to the 2023 routing amendments, that may impact issuer costs. For example, the Consumer Financial Protection Bureau has finalized a rule governing late fees, and has proposed rules governing non-sufficient fund and overdraft fees. Commentors argue that the cumulative impact of all of these rules must be considered.

Regulation II would impose a cut of nearly 30% on interchange fees collected by banks and credit unions, which would surely result in fewer funds to support Bank On initiatives. The proposed cap would close doors that have only recently been opened and turn back the clock on equality and access in the U.S. banking system.

I. Bank On

Overall, 33 comments—approximately 8 percent of letters—addressing Bank On were submitted. Every comment addressing Bank On was submitted in opposition to the Proposed Rule, and numerous of the comments were submitted by civil rights leaders.

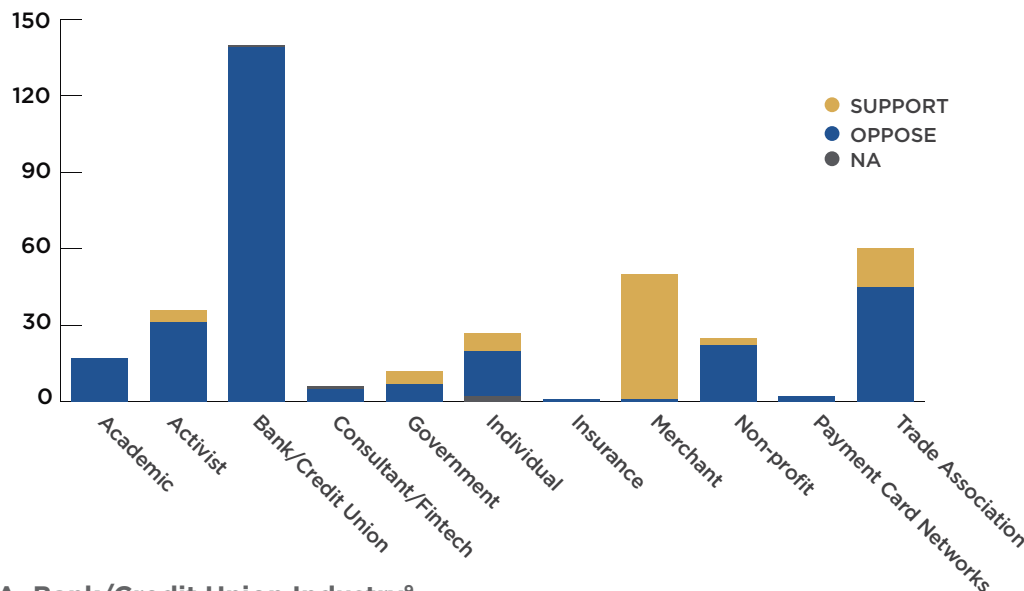
These comments focused on the threat that decreased interchange revenue could face to availability of Bank On accounts. Commentors fear that the Bank On program may not be able to continue if the rule is finalized in its current state, as interchange revenue funds Bank On and similar programs that promote access to banking. Commentors highlight that lack of access to Bank On accounts will hurt LMI consumers and underbanked communities.

Rev. Al Sharpton

IV. SUMMARY OF COMMENTS BY COMMENTOR

A breakdown of comments by industry is below.

Comments by Industry



A. Bank/Credit Union Industry⁹

On the whole, the banking industry opposed the Proposed Rule. Almost 184 of the 413 letters reviewed—approximately 46 percent of comments—were from individuals affiliated with financial institutions (or the trade associations that represent them) and they uniformly opposed the Proposed Rule. A single letter was

⁹ Including trade associations.

submitted in support of the rule by an exempt institution that clarified that it supports the Proposed Rule so long as it is not applicable to it.¹⁰ Many of these criticisms are discussed in further detail in Section IV, but we highlight some concerns specific to the banking industry below.

Exempt vs. nonexempt financial institutions. There was not a substantial difference between the letters submitted by exempt and non-exempt institutions. Exempt institutions generally highlighted that more and more institutions are becoming subject to the Regulation II, and even where they are not, market influences typically impact their ability to charge interchange at any rate.

Methodology. The banking industry focused on a number of the methodology concerns raised in opposition to the Proposed Rule that are discussed in Section IV.A above. For example, both trade associations and financial institutions critiqued the Board’s allowable costs, and encouraged inclusion of costs not currently covered in the Proposed Rule, including cardholder inquiries, compliance fees, non-sufficient funds handling, and research and development.

Impact of rule on smaller financial institutions. Credit unions and community financial institutions wrote to discuss concerns unique to their institutions. For example, when discussing the small issuer exemption, banking industry commentators pointed out that the competitive disadvantage faced small financial institutions may force them to abandon their debit programs. Additionally, small financial institutions expressed concerns about their ability to offer free or low-cost debit cards.

Dozens of credit unions wrote to the Board to highlight the impact of Proposed Rule to the credit union structure specifically. Credit unions are not-for-profit, so any loss in revenue from the Proposed Rule would mean loss of services to members.

General harm to consumers. Specifically, the banking industry noted that interchange income assists in financing of free or reduced cost services to low-income communities. With substantially reduced interchange income, financing of these programs may no longer be feasible.

No regulation required. Numerous institutions argued that nothing in the Durbin Amendment requires the Board to reconsider the interchange fee caps set forth in Regulation II at this time. Further, institutions point out that Congress has not otherwise compelled the Board to amend its prior rulemaking.

Supreme court rulings. Several banking institutions also commented on ongoing litigation in *Corner Post, Inc. v. Board of Governors of the Federal Reserve System* and *Loper Bright Enterprises v. Raimondo*. At the time the Board published the Proposed Rule, neither of these cases had been decided by the Supreme Court of the United States, and commentators emphasized that those decisions would have a substantial impact on future rulemaking.

B. Merchants¹¹

Merchants and their representative trade associations submitted 64 letters in response to the Proposed Rule. All but one of the letters submitted by merchants supported the Proposed Rule. The last letter opposed the Proposed Rule on the grounds that is “meaningless”—the commentator expressed that this cut in interchange would have no practical effect on businesses its size because issuers would compensate losses through other fees.¹² Some of the themes found throughout merchant comment letters are highlighted below.

¹⁰ See [Comment letter](#).

¹¹ Including trade associations.

¹² See [Comment letter](#).

Small businesses. 31 of the 50 merchant comment letters were submitted by small businesses. These letters highlighted that interchange fees represent one of small merchants' largest operating expenses. As such, these entities generally support lowering the interchange fee cap.

National merchants. The remaining 19 comment letters were submitted by national merchants. National merchants generally agreed with small businesses that the Proposed Rule does not go far enough in cutting interchange fees, criticizing the methodology utilized by the Board in establishing the new cap.

Trade associations. Much like the individual letters from merchants, merchant trade groups submitted 14 comment letters reiterating their desire for lower interchange rates and dissatisfaction with the lack of competition in interchange.

The Retail Industry Leaders Association and Retail Litigation Center, Inc and National Retail Federation advocated for the evaluation of a tiered interchange structure, which would create different interchange fee caps for the largest issuers with the lowest costs than for all other regulated issuers.

Fraud. The comments included a number of arguments for eliminating the ad valorem and fraud-prevention adjustment components of the interchange fee cap. The merchants argue that these components are not necessary because merchants shoulder the bulk of fraud costs. In the alternative, merchants argue that the Board should validate compliance by issuers with the fraud-prevention requirements in order for them to be eligible for the adjustment, as opposed to retaining the "check-the-box" certification currently utilized.

Debit card issuer survey. Additionally, the comments typically argued for annual (as opposed to biannual) Survey reporting, to ensure that issuers cannot allocate costs across the two-year reporting period in a manner that would serve to increase interchange. Additionally, merchants requested that the Board audit the data in the Survey to ensure accuracy.

Automatic adjustment to the interchange fee cap. While merchants typically supported automatic updates to the interchange fee cap on a biannual basis, some argued that merchants should be able to submit comments prior to the adjustment where the data will support an increase in the interchange cap.

C. Academic

All 17 academic commentators opposed the Proposed Rule. These comments included general criticisms of a government price cap, particularly as it relates to a policy that did not lower consumer prices as intended when attempted in 2011.

D. Activists

Overall, 31 of the 36 letters submitted by activists opposed the Proposed Rule. Approximately one quarter of these letters raised arguments related to Bank On, as discussed above in Section III.I. Activist commentators also discussed access to banking services, generally. These comments pointed to the observed effects of the Durbin Amendment (i.e., increased costs of banking services) as evidence in support of their opposition to the Proposed Rule.

E. Consultant/Fintech

Five of the six letters submitted by consultants and fintechs opposed the Proposed Rule. These comment letters varied widely, and included concerns about the timing of the proposal, the small issuer exemption (e.g., one comment argued that it should be increased to \$20 billion to account for inflation), and the reliability of the data relied upon to promulgate the Proposed Rule.

F. Government

Nine of the fourteen letters submitted by government officials opposed the Proposed Rule. A summary of some of the letters submitted by government officials is below:

- **U.S. Congress:** Senator Richard Durbin, who is the namesake of the Durbin Amendment that required promulgation of Regulation II, supports the rule.
- **U.S. Congress:** Representatives Nikema Williams (D-Ga.) and Blaine Luetkemeyer (R-Mo.) submitted a bipartisan letter signed by 38 members of Congress stating that the proposal to lower debit interchange fees could undermine recent progress in bringing low- and moderate-income (LMI) consumers into the mainstream banking system.
- **U.S. Congress:** Rep. Luetkemeyer, a member of the House Financial Services Committee, submitted two comment letters opposing the rule that discussed his concerns over the ability of the proposed rule to “survive independent judicial review.”
- **State Government:** Attorney General of the State of New York Letitia James supported the Proposed Rule because she believes that savings from decreased interchange fees will be passed from merchants to consumers. Attorney General James also argued that lowering the cap on debit interchange could incentivize debit acceptance and help those without access to credit cards or other alternative payments.
- **State Government:** The President of the Ohio Legislative Black Caucus, State Representative Terrence Upchurch, opposed the Proposed Rule due to its potential impact on the availability of Bank On.
- **State Government:** Illinois State Senate and House of Representatives members supported the Proposed Rule but argued that the proposed 17.7 cent per transaction rate should be lower.
- **Local Government:** Comments from two members of the government of Oakland County, Michigan refused to support the Proposed Rule, citing that they are concerned with its potential effect on LMI communities and Bank On.
- **Local Government:** The Mayor of the City of Prior Lake, Minnesota wrote in support of the rule on small business grounds.

G. Individuals

Overall, 20 of the 30 letters submitted by individuals opposed the Proposed Rule. While these comments varied, the most consistent topic discussed by individuals was consumer harm, which was discussed in 13 of the 30 letters. In particular, these comments suggest that the Proposed Rule could exacerbate consumer harms that emerged following the 2011 rulemaking, including decreased access to banking services.

H. Non-Profit

Nearly all—22 of 25—of the letters submitted by non-profits opposed the Proposed Rule. The general focus on these letters was consumer harm. Seven letters discussed Bank On specifically, 17 letters discussed LMI impact, and 18 discuss consumer harm at large.

Rather than doubling down on a policy that has been proven to fail, we should learn from our mistakes.

Stephen W. Robinson

We are concerned that the proposed nearly 30% cut in debit interchange rates could upend the economics that enable financial institutions of all sizes to offer Bank On-certified accounts

Reps. Nikema Williams (D-Ga.) and Blaine Luetkemeyer (R-Mo.)

V. CONCLUSION

In summary, the Proposed Rule elicited extensive feedback from commentors in a vast array of industries and locations. The vast majority (78 percent) of commentors opposed the Proposed Rule, and even those commentors in support of the Proposed Rule raised specific concerns about the methodology employed by the Board to arrive at its proposal. Commentors consistently questioned the Board's methodology in arriving at the proposed interchange fee cap, including the allowable costs considered by the Board, and the cost recovery target and multiplier used in the interchange fee calculation.

Commentors also focused heavily on the data relied upon by the Board in establishing the interchange fee cap. Many commentors highlighted that the Board is relying upon stale data from 2021—a year which is not generally representative as a result of the COVID-19 pandemic—when more current data will be available shortly and will reflect recent amendments to Regulation II. Other commentors questioned the Board's data collection cadence and cautioned reliance upon the data without proper auditing.

Finally, across different constituencies, commentors expressed concern about the potential impacts of the Proposed Rule on LMI communities, especially as it relates to the availability of Bank On. Civil rights activists and government officials encouraged the Board to consider how the Proposed Rule will impact the availability of banking services to historically underbanked communities, and pointed to the decrease of free banking services following the 2011 final rule implementing Regulation II.