

LEGAL UPDATES AND NEWS

Federal Reserve Board Adopts Final Rule Establishing Cap on Debit Card Swipe Fees

The Federal Reserve Board (“FRB”) has issued a final rule setting what it considers to be “reasonable” and “proportional” fees that can be charged by debit card issuers in connection with electronic debit card interchange transactions, *i.e.* so-called debit card “swipe fees.” The rulemaking was required by the Dodd-Frank Act and is effective on October 1, 2011.

The FRB approved a cap on an issuer’s base fee of 21 cents per transaction plus an additional five basis point charge (based on the value of the transaction) to defray losses due to fraud. The FRB also issued an interim final rule that authorizes an additional charge of one cent per transaction conditioned upon the issuer adopting certain fraud prevention policies. The final rule authorizes a total fee that is approximately twice as high as the FRB’s controversial proposed rule, which drew nearly 11,570 comments.

The Dodd-Frank Act contains an exemption from the interchange fee standards for any debit card issuer that, together with its affiliates, has less than \$10 billion of assets (the “Small Bank Exemption”). As a result, these small issuers are not subject to the FRB’s cap on debit card interchange fees contained in the final rule. However, many commenters on the FRB’s proposed rule expressed concern that the Small Bank Exemption would be ineffective because (i) payment networks would not be willing or able to institute a two-tier fee structure; or (ii) networks would discriminate against small issuers in favor of cards with lower interchange fees; or (iii) merchant routing choices and steering would depress interchange fees over time and ultimately erode any difference in interchange fees.

The FRB’s staff indicated that it lacks authority to take some of the stronger steps recommended by commenters in order to enforce the Small Bank Exemption, such as requiring payment networks to establish two-tier pricing. However, the FRB does plan to take certain limited steps to facilitate the exemption. Those include (i) publishing annual lists of issuers with under \$10 billion in assets to assist networks in ascertaining which issuers are not subject to the caps, and (ii) surveying networks annually and publishing a list of average interchange transactions fees each network provides to each of its covered issuers and its exempt issuers. The survey is intended to allow small exempt issuers to more readily compare the interchange revenue it would receive from different networks and provide Congress and the regulators with data to assess whether the Small Bank Exemption is operating as intended.

The Dodd-Frank Act also required the FRB to prohibit issuers and payment networks from restricting to one network, or multiple affiliated networks, the number of networks over which a debit card may be routed. The final rule addressed that issue by prohibiting issuers and networks from restricting the number of networks over which debit card transactions may be processed to less than two unaffiliated networks. That requirement is effective April 1, 2012 with respect to issuers and October 1, 2011 with respect to networks.

The Dodd-Frank Act also prohibits issuers from inhibiting the ability of merchants to direct the routing of debit card transactions over any network available to them. The final rule incorporates this restriction.

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