

United States Senate

WASHINGTON, DC 20510

December 16, 2013

Dear Colleague,

I write to draw your attention to the attached article from the December 11 edition of the *American Banker*. This article summarizes a new study from the Federal Reserve Bank of Kansas City examining the availability of free checking accounts after interchange fee regulation took effect in late 2011. In stark contrast to the predictions of some that interchange reform would bring about the end of free checking, the Kansas City Fed's study concluded that free checking became more widely available for consumers after interchange fee regulation took effect.

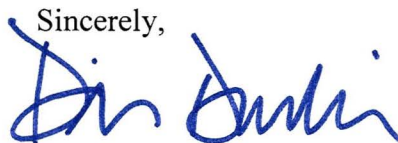
The study analyzed an extensive sample of banks, including large banks that were subject to interchange fee regulation as well as small banks that were exempted from it, and found that "on net consumers actually had increased access to free checking after the debit card regulations went into effect." The study revealed that the share of checking account balances in banks that offer free checking increased from 19.4 percent of all balances in 2011 to 21.6 percent in 2012. The study noted that "consumers' net increase in access to free checking stemmed mainly from the greater availability of free checking at exempt banks," and found that "access to free checking has expanded most in cities and regions where banks are engaged in vigorous competition." The full study, entitled "The Impact of Debit Card Regulation on Checking Account Fees," can be found at <http://kansascityfed.org/publicat/econrev/pdf/13q4Sullivan.pdf>.

The Kansas City Fed's study comes after another Federal Reserve study, issued on May 23, concluded that the small bank exemption in interchange fee regulation "is working as intended" and that small banks have received roughly the same average per-transaction interchange fee before and after the regulation took effect. This study can be found at <http://www.federalreserve.gov/newsevents/press/bcreg/20130523a.htm>.

These studies demonstrate that interchange reform not only has successfully protected small banks' ability to offer competitive checking account and debit card products, but it has actually enhanced their ability to compete against giant financial institutions for consumers' business. By reining in the big banks' collective price-fixing of interchange fees and by promoting transparency, competition and choice in the debit system, this reform has provided benefits for Main Street banks in addition to benefitting Main Street merchants and consumers.

Thank you for your consideration of this matter. If you have any questions please feel free to contact Dan Swanson on my staff (daniel_swanson@judiciary-dem.senate.gov, 224-2152).

Sincerely,



Richard J. Durbin
United States Senator

AMERICAN BANKER.

Free Checking Increased After Durbin: Study

by Kevin Wack
DEC 11, 2013 4:57pm ET

Many in the banking industry predicted that the arrival of price caps on debit card swipe fees would spell the end of free checking.

But free checking isn't dead, according to a new study from the Federal Reserve Bank of Kansas City. In fact, the product actually became more widely available after the so-called Durbin Amendment took effect than it was before, the study shows.

The findings aren't a complete surprise. It's been clear for a couple of years that many banks with less than \$10 billion of assets, which are not subject to the swipe fee price cap, would continue to offer free checking.

But the Kansas City Fed study, which relies on data from a sample of 281 banks, offers the most comprehensive analysis of the issue to date. The study looks at the prevalence of free consumer checking in early 2011 and then again in 2012, after the price caps took effect. Free checking was defined as an account with no monthly fee and no monthly balance requirement.

Banks with more than \$10 billion of assets, after experiencing a sudden decline in their swipe fee revenue in late 2011, became much less likely to offer free checking. The percentage of larger banks that offered free checking fell from 51% to 27% a year later.

Among smaller banks, though, the percentage offering free checking rose from 37% to 44%. The study's author, economist Richard Sullivan, suggests that the smaller banks may have lowered their fees in a competitive move to attract customers.

The cap on interchange fees was championed by Sen. Richard Durbin, D-Ill., and was among the provisions included in the 2010 Dodd-Frank Act. It took effect in October 2011.

The study also found that the percentage of checking account balances that were in banks that offered free checking rose slightly by the end of 2012 — from 19.4% to 21.6%.

"Elimination of free checking accounts at larger, regulated banks was more than offset by an increase in free checking accounts at smaller, exempt banks," the study concluded, while acknowledging that factors other than the Durbin Amendment might have had an impact.

The retail industry, which lobbied Congress to enact the swipe fee price cap, crowed Wednesday about the study's findings.

"The bottom line is that consumers win and competition is strengthened when debit fees are reduced," Doug Kantor, a lawyer for the Merchants Payments Coalition, said in a news release.

Apart from the findings about the Durbin Amendment's effect on the availability of free checking are questions about whether or not banks should offer the product. Consultants to community banks are divided on that issue.

Steven Reider, president of the consulting firm Bancography, says that much of the supposed value to banks from free checking involves the opportunity to cross-sell other products to new customers, but he argues that most small banks aren't good at doing that.

"My belief is if you give a product away, you are telling a customer you believe it has no value," he says.

But Jeff Platter, vice president of business intelligence at consultancy Haberfeld Associates, is a fan of free checking at small banks. He estimates that small banks can add new customers for only about \$28 annually, and says that cost can easily be recouped through swipe fees and other revenue.

When small banks compete with larger institutions, "they don't have the ability to compete without good products, and those good products include free checking," Platter says. "I think it's almost a necessity."