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Banks most reliant on interchange fees

By Maria Tor and Venkatesh Iyer *April 18, 2016*

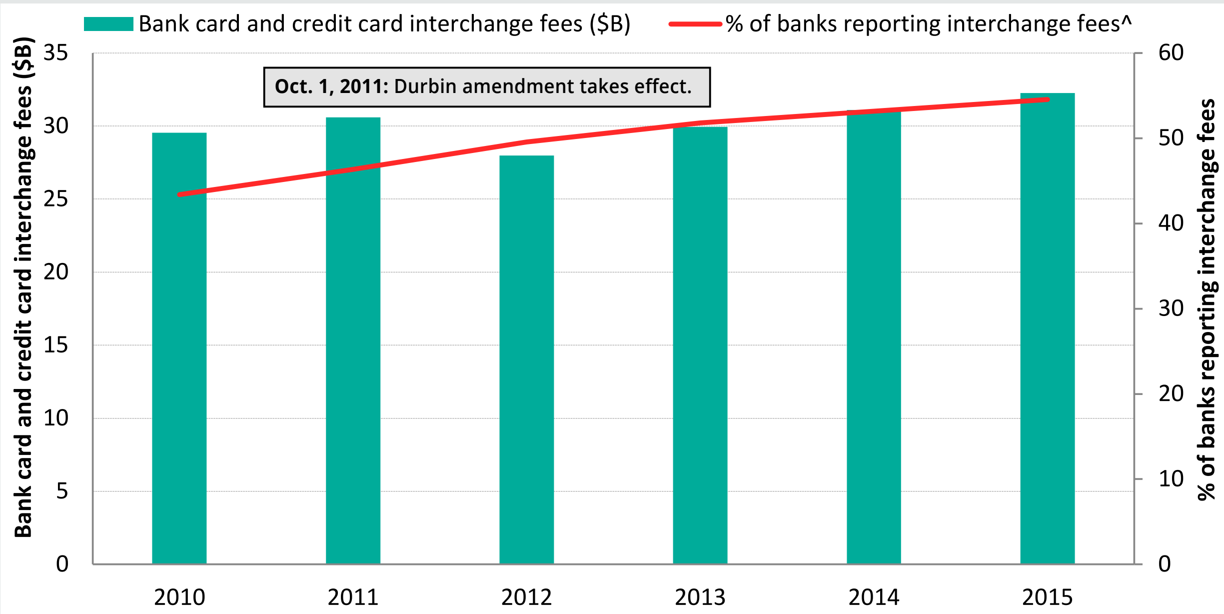
Despite earning a dismal rate on loans, the banking industry has grown profits in the years since the financial crisis, finding other ways to increase income. One of those ways is through interchange fees, or the fees paid by merchants to banks when bank customers use a debit or credit card to make a purchase. Interchange income has grown after new regulation imposed limits on debit card fees in late 2011.

The Dodd-Frank Act of 2010 included the "Durbin amendment," the more common name for Regulation II, which mandated that banking regulators limit the amount of debit card interchange fees that banks could charge merchants. The rule went into effect Oct. 1, 2011, and only applies to banks with assets above $10 billion. The regulation capped the maximum permissible interchange fee that an issuer may receive for an electronic debit transaction at the sum of 21 cents per transaction, plus 5 basis points multiplied by the value of the transaction, plus up to an additional 1 cent per transaction if the issuer implements fraud-prevention policies and procedures. The Fed said that for the average debit card transaction of $38, a debit card issuer above $10 billion in assets could charge no more than 24 cents. The rule does not apply to credit card or prepaid debit card transactions.

While the banking industry's interchange income took a hit in 2012 after the rule went into effect, the aggregate interchange income has risen back to pre-Durbin levels, according to regulatory data. Banks report "bank card and credit card interchange fees" in Form Y-9Cs and call reports. Data is somewhat limited because banks only have to disclose the line item if their interchange fees equate to more than 3% of "other noninterest income" and total more than $25,000; 54.5% of banks reported the figure for 2015, up from 43.4% who reported it for 2011.

To allow comparisons across years since 2010 in the above graph, the analysis excludes institutions from the aggregates that filed a thrift financial report for either 2010 or 2011. The thrift financial report did not require filers to break out interchange fees, and so including these companies causes an artificial increase in the aggregate figure in 2012 when thrifts had to begin filing call reports.

Interchange fees at US banks & thrifts



Date compiled April 8, 2016.
Analysis based on call reports filed by commercial banks, savings banks and savings and loan associations.
Companies that filed thrift financial reports for 2010 or 2011 are excluded, since the thrift financial report did not require disclosure of interchange fees.
^ Under call report filing rules, banks report credit card and debit card interchange fees if the amount is greater than $25,000 and exceeds 3% of "other noninterest income," a subset of noninterest income.
The Durbin Amendment, part of the Dodd-Frank Act of 2010, mandated that the Federal Reserve limit debit card interchange fees. The final rule stated that banks above $10 billion in assets could receive an interchange fee of up to about 24 cents for the average debit card transaction. Banks below $10 billion in assets are exempt from the rule.
Source: SNL Financial, an offering of S&P Global Market Intelligence

Top 20 holding companies most reliant on interchange fees in 2015

Ranked by credit and bank card interchange fees/operating revenue (%)

Company (top-level ticker)	City, state	Total assets ($B)	Bank interchange fees: Amount ($M)	Bank interchange fees: YOY change (%)	Bank interchange fees: % of operating revenue
American Express Co. (AXP)	New York, NY	161.17	19,297.0	-1.01	58.75
Green Dot Corp. (GDOT)	Pasadena, CA	1.69	196.5	10.38	28.34
The Bancorp Inc. (TBBK)	Wilmington, DE	4.77	47.5	25.05	24.89
Woodforest Financial Group Inc.	The Woodlands, TX	4.69	120.8	8.37	22.64
First Community Bancshares Inc.	Killeen, TX	1.66	60.8	9.15	21.10
Independent Bankers Financial Corp.	Farmers Branch, TX	2.57	21.4	2.15	15.16
Dickinson Financial Corp. II	Kansas City, MO	2.05	24.0	-3.16	14.16
Commerce Bancshares Inc. (CBSH)	Kansas City, MO	24.63	148.5	3.24	13.57
Barclays Delaware Holdings LLC (BARC)	Wilmington, DE	28.00	341.2	18.01	13.24
Discover Financial Services (DFS)	Riverwoods, IL	86.94	1,117.0	14.09	12.82
First National of Nebraska Inc. (FINN)	Omaha, NE	18.35	162.1	7.11	12.11
Arvest Bank Group Inc.	Bentonville, AR	15.86	76.1	9.77	9.78
Capital One Financial Corp. (COF)	McLean, VA	334.18	2,235.0	10.57	9.54
Comerica Inc. (CMA)	Dallas, TX	71.98	261.2	NM*	9.50
Central Bancshares Inc.	Lexington, KY	2.19	9.9	5.61	9.31
INTRUST Financial Corp.	Wichita, KS	4.43	16.8	-0.11	9.02
Emprise Financial Corp.	Wichita, KS	1.57	6.0	6.01	8.65
Bangor Bancorp MHC	Bangor, ME	3.31	11.4	13.28	8.49
United Bank Corp.	Barnesville, GA	1.14	4.7	14.99	8.48
Charter Financial Corp. (CHFN)	West Point, GA	1.01	4.2	15.24	8.37
Industry median^		**2.16**	**2.55**	**8.09**	**3.18**

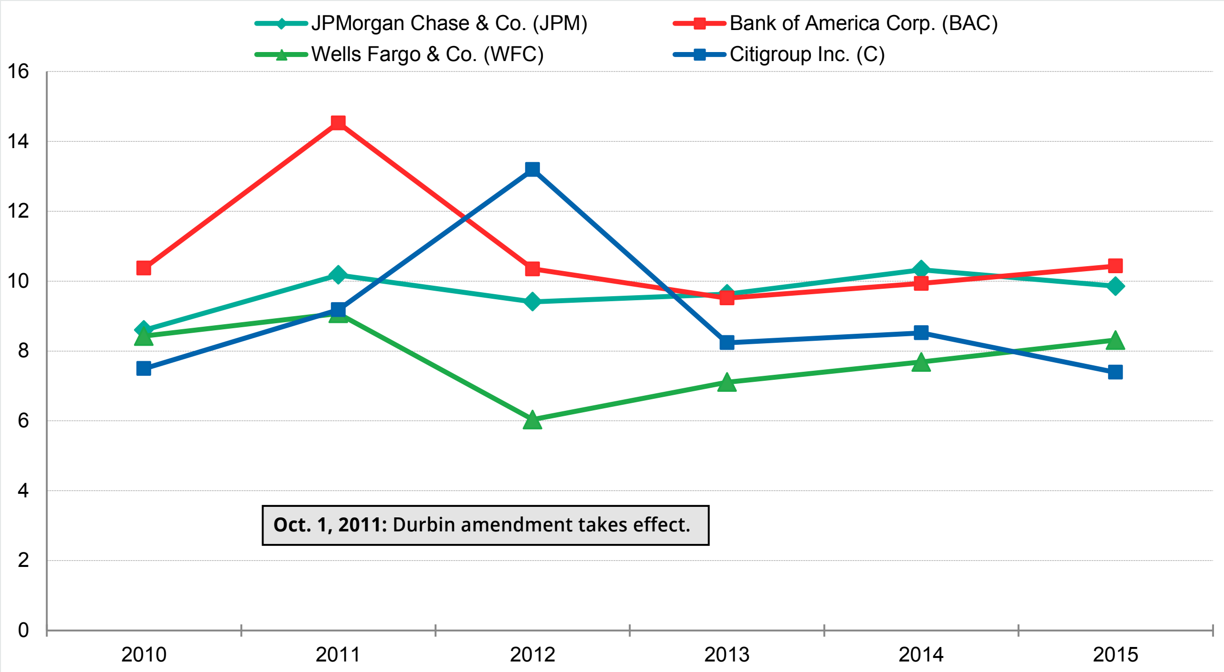
Data compiled April 8, 2016.
Analysis is based on bank and thrift holding companies that filed Form Y-9Cs for 2015.
^ Under Form Y-9C filing rules, holding companies report credit card and debit card interchange fees if the amount is greater than $25,000 and exceeds 3% of "other noninterest income," a subset of noninterest income. Therefore, the industry median cannot include banks whose interchange income was not high enough to be reported.
* Not meaningful. Starting in 2015, Comerica Inc. changed its accounting presentation for card fees, according to the company's 2015 Form 10-K. Without this change, the bank's card fees were "stable" year over year.
Tickers based on top-level entity's home country stock exchange.
Source: SNL Financial, an offering of S&P Global Market Intelligence

Excluding these former thrifts, aggregate interchange fees from debit and credit card transactions fell to $27.97 billion in 2012 from $30.58 billion in 2011. But since then, interchange fees rose to $32.25 billion in 2015, an increase of 15.3% from 2012 levels, while overall operating revenue for banks, excluding former thrifts, grew by only 1.7% over the same time period.

The potential loss of interchange income is a major reason banks approach growth above $10 billion in assets with caution. Banks that earn significant income from debit card interchange fees will almost certainly see a decline after they become subject to the Durbin amendment. Credit cards and prepaid debit cards are not subject to the interchange cap, so it's not surprising to see American Express Co. and Green Dot Corp. at the top of the ranking of holding companies most reliant on interchange income as a percentage of operating revenue. Twelve of the top 20 banks most reliant on interchange income have less than $10 billion in assets.

At the largest four U.S. banks, which hold nearly 40% of the country's deposits, growth in interchange income has been mixed. JPMorgan Chase & Co. saw its 2015 interchange

Card interchange fees/total noninterest income at top 4 US banks (%)



Date compiled April 8, 2016.
Data based on credit card and debit card interchange fees reported in the Form Y-9C.
The Durbin Amendment, part of the Dodd-Frank Act of 2010, mandated that the Federal Reserve limit debit card interchange fees. The final rule stated that banks above $10 billion in assets could receive an interchange fee of up to 24 cents for the average debit card transaction. Banks below $10 billion in assets are exempt from the rule.
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income fall to $4.89 billion in 2015 from $5.31 billion in 2014, or to 9.9% of noninterest income from 10.3% of noninterest income. Bank of America Corp., on the other hand, reported interchange income rose to $4.34 billion in 2015 from $4.30 billion in 2014, or to 10.4% of noninterest income from 9.9% of noninterest income.

Regulatory data is not yet available for the first quarter of 2016, but some of the early reporters have seen positive trends in card purchase volume. Wells Fargo & Co. CFO John Shrewsberry said during the company's earnings conference call April 14 that debit card purchase volume was $72.4 billion, up 9% from the year-ago quarter, and credit card purchase volume was up 13% from a year ago to $17.5 billion. Bank of America CFO Paul Donofrio also said April 14 during the company's earnings call that credit card spending was up 8% in the first quarter compared to the year-ago quarter, adjusted for the divestiture of a $1.6 billion credit card portfolio to U.S. Bancorp.