You’re Going to Need a Bigger Vault

Pain Ahead: Crossing the $10 Billion Threshold

The Durbin Amendment and Dodd-Frank Act contain provisions that raise the hackles of banks and credit unions of all sizes, but the most intense pain for financial institutions begins when it approaches $10 billion in assets. Above this threshold, institutions are subject to heightened regulatory scrutiny and face a highly restrictive cap on debit card interchange rates. For many, this latter impact can represent lost interchange fees worth millions of dollars.

Mergers and acquisitions are a typical cause of banks and credit unions moving beyond the $10 billion threshold, but even with a modest growth of five percent, an institution with $8 billion in assets can find itself on the cusp of reaching this mark in just four years. Typically, a financial institution’s primary regulator will begin working with an institution as it approaches $10 billion, encouraging careful evaluation to measure the impact of new requirements early in the process.

Even so, every management team we’ve spoken with wishes they’d started their planning process earlier because they learned it takes years, not months, to prepare for the regulatory realities associated with being a $10 billion asset operation. New compliance programs must be implemented, new staff with specialized skill sets must be hired, and perhaps most importantly, the management team must prepare for a “cliff event” on the top line.

Watching a Key Non-Interest Revenue Line Drop Out of Sight
Debit interchange typically runs neck-and-neck with nonsufficient funds (NSF) fees as the top source of a financial institution’s non-interest income. Crossing the $10 billion mark triggers a reduction of roughly 40 percent to that debit interchange revenue line. Relying on organic growth, it will likely take 24-36 months for interchange income to return to prior levels. This loss of revenue combined with the bank or credit unions asset growth means its operating ratios will be weaker than they were in the pre-$10 billion days.

Few management teams are content with allowing a revenue decline of this type to fall directly to the bottom line, regardless of its cause. Yet, there is no magic bullet to resolve this issue. All corners of the operation must be scoured for potential savings, including areas with no correlation to card operations; e.g. online banking, mobile payments, and consumer checks.

FACT SHEET

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Debit-card interchange fees, also called swipe fees, dropped sharply after the Durbin amendment’s price caps went into effect in October 2011.

Interchange fee generated by a $50 purchase

BEFORE DURBIN* 51 cents
AFTER DURBIN* 2.5 cents**

21 cents 23.5 cents

Total: 23.5 cents

Interchange-fee revenue at the financial institutions covered by the 2011 price cap

$15 BILLION

2011 12 13 14 15

Interchange-fee revenue at the financial institutions covered by the 2011 price cap

October-December

*Average amount per transaction during the first nine months of 2011
**0.05% of the transaction amount

Source: Federal Reserve

The Wall Street Journal, 2017
Ironically, one of the natural areas to turn to for cost relief poses risks. Rules governing "net zero compensation" – stating that a payment card network cannot pay incentives to an FI in excess of the amount payed by the FI to the network in a year – kick in at $10 billion. Additionally, this regulation also states that any contract signed after October 1, 2011 is subject to this statute, even if the FI was non-regulated at the time of signing, but achieved regulated status during the contract. Lastly, regulators also can require repayment of signing bonuses if they are deemed disproportionate to ongoing business. If these bonuses have already been recognized as revenue, financial statements for the FI will need to be refiled.

As if these matters were not daunting enough, there is an additional requirement that involves scheduling a “mock” audit with the Consumer Financial Protection Bureau (CFPB). This audit is not simply a tick in the box exercise, but rather another part of the process that demands a significant amount of time and focus.

What We Offer
We typically recommend that our clients start the evaluation of Durbin impacts at $8 billion rather than just before they arrive at the $10 billion mark. Areas that SRM considers in evaluation include:

- Restructuring vendor agreements to maximize economies
- Actively managing portfolio yields
- Developing project strategies to increase revenue

The key is to avoid sitting on the sidelines hoping these issues will take care of themselves. Complaining about the shortcomings of Dodd-Frank and Durbin and advocating for change does not eliminate the present-day need to comply with these laws. Getting ahead of the game and engaging in thoughtful planning is your best strategy.

Since 1992, SRM has grown a proven track record of success negotiating with the vendors and suppliers that financial institutions depend on across their operations. Our subject matter expertise and current market benchmarking data can help soften the blow of crossing the $10 billion asset threshold. We have added billions in value to the bottom line of hundreds of banks and credit unions, and welcome the chance to discuss what we can do for your institution.

If your institution is at or nearing assets of $8 billion or more, arrange to have SRM provide a no-cost assessment of the impacts and potential opportunities that can help you prepare for growth.

There are Billions of Ways We Can Help You
The work we have done to help more than 700 institutions add $2.2 billion dollars of value to their bottom line also identified that there is an acute need for a solution that allows banks and credit unions to track, audit, and benchmark the contracts they have. Combining our data and experience from over 25 years of financial services gives us the ability to deliver a solution that addresses this need. It is a very powerful combination.

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<th>Effects of Durbin on Major Bank Debit Cards*</th>
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<td><strong>Average Interchange</strong></td>
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<td><strong>Per Transaction</strong></td>
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<td>Signature Debit</td>
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<td>Pre 10/1/2011</td>
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*For covered issuers