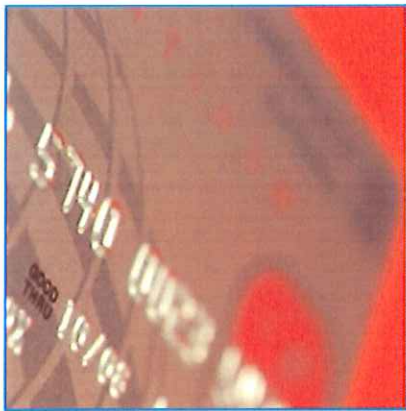


Report to the State of Iowa General Assembly

SF 2088 CONVENIENCE FEES STUDY



January 13, 2011

Department of Administrative Services
Information Technology Enterprise

Foreword

I am pleased to present this Report on Convenience Fees to the State of Iowa General Assembly.

This study was undertaken by the Department of Administrative Services Information Technology Enterprise, in the absence of a State Chief Information Officer, in an effort to present alternatives to the current procedures used to recover the costs of providing online payment service through assessment of convenience fees.

The topic of assessing an additional fee for online payment is controversial, but studies show that the citizens of Iowa recognize the need for such fees to cover the costs of providing the service. However, it appears the fees could be assessed in a more palatable manner.

The study points out the confusion associated with the concept of convenience fees, assesses current industry practices and various analyses, and provides the results of a survey of State agencies.

Finally, several alternatives to current practices are provided for Legislative consideration.



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Executive Summary

The subject of “convenience” fees for online payment prompts controversy. The term itself has many interpretations and the use of it by providers of credit card payment services has further complicated our understanding as they use it in reference to surcharges, discount fees, and any number of other terms. But, it appears that the *practice* of charging a fee for the convenience of securing a product or service online is at once both attractive and offensive.

A fee added to a product or service is acceptable because the online service provides for an efficient, time-saving method of receiving the online service. It saves the citizens of Iowa the trouble and cost of driving to a remote location, standing in line, waiting on payment confirmation, and driving a distance back home. “So, why not add a little charge to save time and aggravation?”

A counter argument would be that one of the roles of State government is to provide services in the easiest way possible. If that service is required, such as a license to practice a profession, should the people of Iowa have to pay further to secure that service online? “Isn’t that what we pay taxes for? Why pay an extra charge?”

The fact remains, providing a service, be it online or over-the-counter, involves costs – costs for staff, for equipment, for supplies – the cost of doing business. Those costs have to be paid for in some manner.

After reviewing payment card and commerce industry studies and literature on convenience fees and arriving at a working definition of “*convenience or other handling fees charged by state agencies by credit or debit card or other electronic means of payment,*” this paper explores nationwide and Iowa surveys addressing citizen and business view of such fees. There appears to be a grudging acceptance of such fees as necessary, but distasteful. The key to acceptance appears to be the manner in which such fees are presented to the citizen user.

Following analysis of the magnitude of fees and the impact of eliminating such fees within Iowa state government, this study presents alternatives to the current methods of collecting convenience fees, for consideration by the Legislature.

SF 2088 CONVENIENCE FEES STUDY

In the absence of an appointment of a State Chief Information Officer, the Department of Administrative Services, Information Technology Enterprise, has conducted a study of convenience fees charged by state agencies for online services, as directed by Section 22 of SF 2088:

Sec. 22. CHIEF INFORMATION OFFICER —— CONVENIENCE FEE STUDY. The chief information officer of the state shall conduct a study concerning convenience or other handling fees charged by state agencies by credit or debit card or other electronic means of payment. The goal of the study would be to encourage the elimination of such fees wherever possible. The department shall determine the extent and amount of the fees charged, revenues generated by those fees, and explore ways to reduce or eliminate the fees. The chief information officer shall submit a report to the general assembly by January 15, 2011, concerning the results of the study, including any recommendations for legislative consideration.

Background

Most local governments assess additional fees for credit card payments in order to cover the processing expenses because, unlike retailers, cities and counties cannot build processing costs into the amount charged. This is because most governmental fees are set by law and cannot be changed. In 1993, VISA and MasterCard realized that surcharging had become a widespread practice for governments and, because their rules prohibit surcharges, ordered them to stop the practice. Around the same time, Ticketmaster was emerging as a dominant provider of electronic ticket sales, and began charging a surcharge on its transactions. Because of the growth of companies like Ticketmaster, MasterCard and VISA changed their rules in 1994, to allow “convenience fees” for transactions done through a “truly more convenient” form of payment, such as the Internet, interactive voice response (IVR) and kiosks. The convenience fee rules were intended to encourage online payments with credit cards. ¹

Prior to 1994, VISA's rules prohibited a third party from assessing a convenience fee on the seller's behalf and required the fee to be fixed or flat regardless of the transaction size. That did not stop a now-flourishing group of third party vendors from offering online payment services to state and local governments with percentage-based convenience fees. Until late 2007, MasterCard and VISA's rules also required the convenience fee to be assessed equally for all types of payment. Initially, that worked well because credit cards were the only method of payment for electronic transactions. However, the emergence of e-check and automated clearing house (ACH) or electronic funds transfer (EFT) for online payments complicated the situation. ACH and EFT, terms used interchangeably, both refer to the manner in which funds are sent electronically through the banking system. ACH/EFT is prevalent for recurring bills because it usually costs less to process than credit cards. As a result, many local governments, or third parties on their behalf, began offering lower convenience fees for online e-check and ACH payments, and again, there was little enforcement by either MasterCard or VISA.

In response to those issues, MasterCard changed its convenience fee program in November 2007. The company's new convenience fee rules apply to government and educational entities for all payment channels with no restrictions on other forms of payment. The credit card company allows convenience fees to be assessed as a fixed or percentage-based fee by the local government or its third party provider.

American Express followed suit in March 2008, and Discover always has allowed a convenience fee surcharge. That meant that state and local governments that assessed percentage convenience fees and lesser fees for e-check and ACH were now compliant with MasterCard, American Express and Discover rules. More importantly, it also

¹ *Credit Card Confusion*, American City and County, September 1, 2009. Available at <http://americancityandcounty.com/admin/finance/government-credit-card-fee-rules-200909/>

meant governments could assess convenience fees for face-to-face transactions with the three card brands, something previously prohibited.²

Surcharge? Discount Fee? Interchange Fee? Assessment Fee? Convenience Fee?

Some merchants seek to impose a service fee for all credit card purchases. This may be termed a *surcharge*, *discount fee* or *convenience fee*, but they are not the same.

Surcharge

When a merchant gives a credit card slip to the credit card company or bank for processing, a percentage of each purchase—usually 1.5% to 5% of the purchase amount—is deducted. This "merchant discount fee" helps pay for the bank's services and for the credit card system.

The Federal Truth in Lending Act defined surcharging as, "any means of increasing the regular price to a cardholder which is not imposed upon customers paying by cash, check, or similar means". The Act further stated that, "no seller in any sales transaction may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check, or similar means." However, this prohibition expired in 1984 and was not renewed by Congress. Since then, 10 states have enacted laws prohibiting surcharges.

While surcharges are prohibited, a cash discount is permitted under all credit card companies' rules. A cash discount offers a lower price for cash payment than credit. For example, many gasoline stations offer cash discounts. There are a few state governmental agencies, including state tax offices and motor vehicle departments, which are permitted to itemize surcharges on the customer's receipt. However, retail merchants may not impose surcharges.³

Discount Fee

The discount fee is the fee charged for processing the credit card transaction. In a retail transaction, the total transaction amount is "discounted" by the amount of the fee. The State of Iowa receives the entire transaction amount and is billed on a monthly basis for the "discount fee". The majority of this fee, called the *interchange fee*, goes to the issuing bank; however, portions of it go to the processing network, the card brand (VISA, MasterCard, etc.) as an *assessment fee*, and to the acquiring institution.

Example: \$100 VISA or Master Card transaction with a discount fee of 2.5% plus 10 cents/transaction

The total discount fee = \$2.50 plus 10 cents = \$2.60

Distribution of the Discount Fee

Issuing Bank Transaction Fee:	\$.10
Interchange Fee:	\$2.05 ½ + \$.10 (Paid to the Issuing Bank)
Assessment fee:	\$.095 (Paid to Master Card or VISA)
Acquiring Bank Processing Fee:	\$.25 cents

² *Credit Card Confusion*, American City and County, September 1, 2009. Available at <http://americancityandcounty.com/admin/finance/government-credit-card-fee-rules-200909/>

³ *Financial Guide: Merchant Credit Card Abuses: What They Cannot Ask You to Do*, Financial Strategies Online, 2003. Available at http://fso.cpasitesolutions.com/Premium/LE/06_le_ic/fg/fg-merchants.html

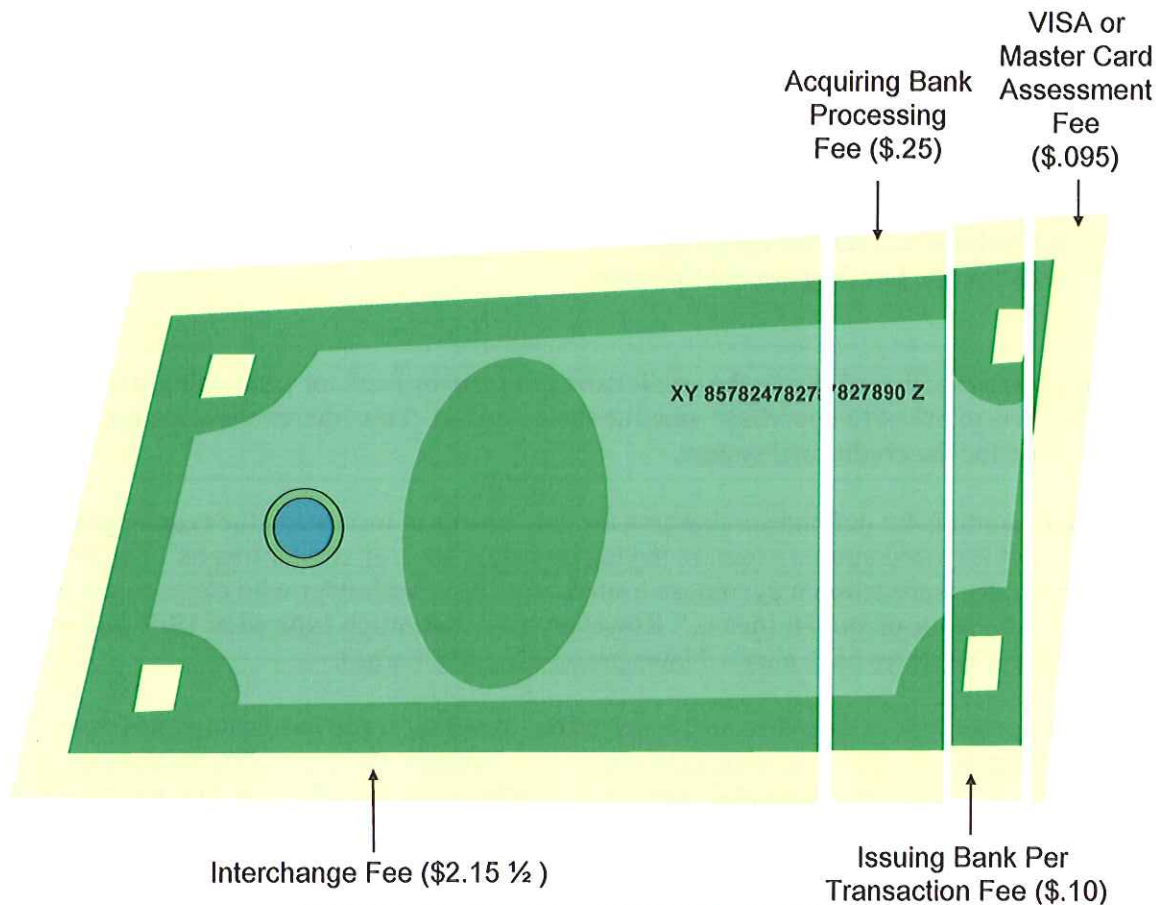


Figure 1 Distribution of the Discount Fee

Convenience Fee

For the purpose of this study, "convenience fee" means a fee charged for processing the credit card transaction, plus fees intended to cover actual costs for providing online payment.

Merchant Accounts

To understand merchant accounts and the flow of information and money involved in an Internet financial transaction, you must understand the functions of an Acquiring Institution and an Issuing Bank.

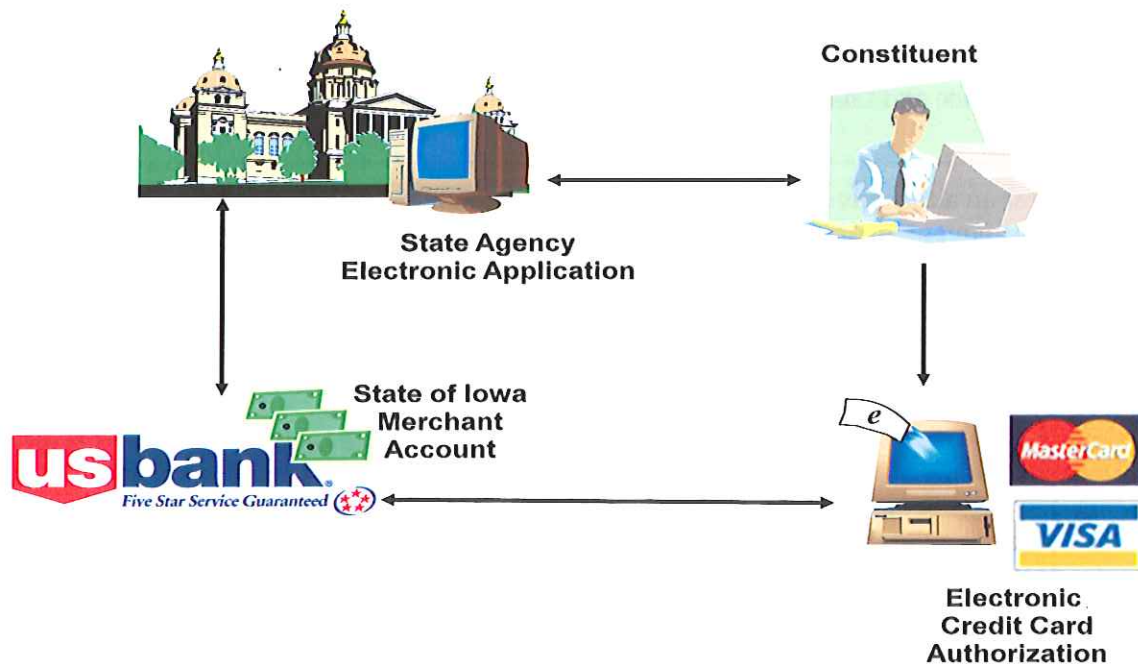
Acquiring Institution - A Bank that contracts with merchants or governmental entities to financially settle electronic transactions.

Issuing Bank - This is the bank that issued the customer's credit card and, upon approval of the transaction, makes funds available to settle the transaction with the acquiring institution. The issuing bank will then bill their customer for the debit on their card.

For a governmental entity to be able to accept credit cards for payment on the Internet, it must have a merchant account with an acquiring institution. When a credit card transaction is initiated by a constituent, the transaction information (i.e. credit card number; name and billing address; and transaction amount) is sent to an Internet authorization service (Elavon/USBank is used for most Iowa government transactions) who then forwards it to the issuing bank.

The acquiring institution ensures the funds are deposited into the appropriate State merchant account. Elavon/USBank acts as the channel for moving the credit card transaction from the State's web site to the acquirer's processing network, receives the results, and posts them back to the State's web application.

State agencies set up merchant accounts through the Office of the State Treasurer.



Fees Charged to the State

The charges related to credit card usage are multi-layered and somewhat complex. Discount fees from credit card companies are passed to the State by the bank and are based on manner of transaction and type of credit card used (consumer, corporate, reward cards, etc.). Below, in very general terms, are costs associated with credit card payments under the State of Iowa's current contract:

Card Type	Fee Charged
Consumer debit cards	0.80% + 25 cents to .90% + 20 cents per transaction
Consumer credit cards	1.43% + .05 cents to 2.70% + 10 cents per transaction
Corporate/purchasing credit cards	2.15% + 10 cents to 2.70% + 10 cents per transaction
"Reward" credit cards	1.55% + 10 cents to 3.25% + 10 cents per transaction
MasterCard assessment fee	0.11% of transaction amount
Mastercard Network Access and Brand Usage fee	\$.0185 per transaction
VISA assessment fee	0.11% of transaction amount
VISA Network Access charge	\$.0025 per transaction
VISA Acquirer processing fee	\$.0195 per transaction.
VISA Risk Identification service charge	\$.001 per transaction
Discover assessment fee	0.10% of transaction amount
Discover Data Transmission fee	\$.0025 per transaction
Discover Data Usage fee	\$.0185 per transaction
Other Credit Card Processing Charges:	Fee
Elavon merchant services processing fee	0.07% of transaction amount
Elavon chargeback fee	\$ 5.00 per transaction

Table 1 Sample Fees Charged to State by Credit Card Providers

Credit Card Providers' Views on Convenience Fees

The following is a comprehensive overview of various credit card providers' policies on convenience fees or surcharges.⁴ Different card brands have different rules on convenience fees, but VISA provides the most thorough guidelines.

VISA

(source: Card Acceptance and Chargeback Management Guidelines for VISA Merchants)

VISA states:

For merchant who offer an alternative payment channel (i.e., mail, telephone, or e-commerce) for customers to pay for goods or services, a convenience fee may be added to the transaction amount. If the merchant chooses to assess a convenience fee to its customers, the merchant must adhere to the following rules:

- The fee is being charged for a bona fide convenience of using an alternate payment channel outside of the merchant's normal business practice
- The Fee:
 - Must be disclosed to customers as a charge for alternate payment channel convenience
 - Is applied only to non face-to-face transactions (There is an exception - Please see VISA Tax Payment Program)
 - Must be a flat or fixed amount regardless of the amount of payment due
 - Is included as part of the total transaction
 - Cannot be added to recurring transactions
 - Is assessed by the merchant that provides goods and services to the cardholder and not by a third party
- The customer must be given the opportunity to cancel prior to the completion of the transaction

The convenience fee charged on a VISA transaction must be a flat rate fee regardless of the order dollar amount. This differs from, and is more restrictive than, the rules of other card brands.

VISA Tax Payment Program

VISA has a special program for merchants that are certified by their acquiring organization to participate in the *VISA Tax Payment Program*. According to the *VISA Tax Payment Program Guide*:

"The VISA Tax Payment Program allows participating merchants to assess cardholder fees on approved tax types. The program allows a fixed convenience fee - not to exceed \$3.95 - for VISA consumer debit products and a variable service fee solution for VISA consumer credit and commercial products. The program also offers an incentive interchange rate to participants on consumer debit tax payments."

MasterCard

(Source: "MasterCard Rules" Section "5.9.2 Charges to Cardholders")

MasterCard doesn't go into as much detail about convenience fees as VISA. They simply state that:

A Merchant must not directly or indirectly require any Cardholder to pay a surcharge or any part of any Merchant discount or any contemporaneous finance charge in connection with a Transaction. A Merchant may provide a discount to its customers for cash payments. A Merchant is permitted to charge a fee (such as a bona fide commission, postage, expedited service or convenience fees, and the like) if the fee is imposed on all like

⁴ *Convenience Fee: Charging Convenience Fees for Credit Card Transactions*, Merchant Circle, Updated December 2009. Available at <http://www.merchantcouncil.org/merchant-account/operation/convenience-fee.php>

transactions regardless of the form of payment used, or as the Corporation has expressly permitted in writing. For purposes of this Rule:

- A surcharge is any fee charged in connection with a Transaction that is not charged if another payment method is used.
- The Merchant discount fee is any fee a Merchant pays to an Acquirer so that the Acquirer will acquire the Transactions of the Merchant.

While the rules for applying a convenience fee are in line with VISA, MasterCard allows a flat, tiered or percentage-based fee structure.

MasterCard also says:

"We allow a "convenience" to be charged by certain educational institutions and public sector merchants, including:

- *Elementary and secondary schools for tuition and related fees, and school-maintained room and board*
- *Colleges, universities, professional schools, and junior colleges for tuition and related fees, and school-maintained room and board*
- *Local, state, and federal courts of law that administer and process court fees, alimony, and child support payments*
- *Government entities that administer and process local, state, and federal fines*
- *Local, state, and federal entities that engage in financial administration and taxation*
- *Government Services; merchants that provide general support services for the government*

In addition, a merchant is permitted to charge a fee (such as a bona fide commission, postage, expedited service or convenience fees, and the like) if the fee is imposed on all like transactions regardless of the form of payment used. For example, a merchant that has a website that accepts MasterCard, VISA and direct debit to a checking account as its three forms of payment, may ask for a surcharge IF the fee is applied to all three methods of payment. The same applies to a merchant that has a physical store that accepts cash, checks, MasterCard and VISA. The store can charge a fee as long as the fee is applied to all four methods of payment."

Discover

(Source: "Discover Operating Manual", Section: "2.3 Surcharges")

Discover doesn't specifically mention convenience fees, but they do cover surcharges. For Discover, the two terms are interchangeable.

"You may assess a surcharge on a Card Sale conducted using a Credit Card provided that (i) the amount of the surcharge may not exceed the Merchant Fee payable by you to us for the Card Sale, and (ii) you assess surcharges on card sales conducted using other credit cards accepted by you. You may not assess a surcharge or other penalty fee of any kind on any other type of Card Transaction or for any Card Sale conducted using a Card other than a Credit Card."

Discover states that "you assess surcharges on card sales conducted using other credit cards accepted by you." With this Discover has effectively deferred to other card brands for rules governing surcharges. Therefore, to surcharge Discover you also have to surcharge the other card brands that you accept which will require you conform to VISA's more strict guidelines that differentiate between convenience fees and surcharges.

American Express

(Source: "American Express Operating Procedures for US Merchants" section: "1.7 Prohibited Use of the Card" and "8.5 Apartment Rentals")

American Express has a bit of confusion regarding surcharge in their operating agreement. AMEX doesn't specifically mention surcharges in the "Prohibited Use of the Card" section of their operating procedures but they make specific reference to this section from the "Apartment Rentals" section of the same guide stating that:

"The prohibition in subsection 1.7 "Accepting the Card – Prohibited Uses of the Card" against imposing restrictions, conditions, or disadvantages (e.g., fees, surcharges, "convenience" or "administrative" fees, penalties) when the Card is accepted will apply whether or not your Rental Establishments impose them on any Other Payment Products."

While there is no actual reference to surcharging in subsection 1.7, it is implied. In light of this, it would appear that American Express also generally rules against convenience fees. American Express says such fees are only allowed "in very limited industries, for example, taxes."⁵

Summary of Credit Card Providers' Views

- A convenience fee cannot be assessed in a face-to-face environment
- A convenience fee cannot be assessed for recurring payments. The convenience fee was designed for one-time payments and not for payments in which a cardholder allows his credit card to be periodically charged for recurring goods or services. Examples of recurring charges include, but are not limited to, insurance premiums, subscriptions, Internet service provider monthly fees, membership dues, and utility charges.
- The merchant must provide a true "convenience" in the form of an alternative payment channel outside the merchant's customary face-to-face payment channels, and the fee must be disclosed by the merchant to the cardholder as a charge for the alternative payment channel convenience that is provided.
- The convenience fee must be disclosed prior to the completion of the transaction, and the cardholder must be given the option to cancel the transaction if not wanting to pay the fee.
- The convenience fee must be included in the total amount of the transaction; it cannot be "split" out from the transaction amount.
- If a convenience fee is assessed it must be for all payments (V, MC, Discover, AMEX, ACH, Check) within a particular payment channel (mail, phone, internet).
- Since all convenience fees are required to be assessed equally, a merchant who accepts VISA is restricted to a flat convenience fee for all cards.

⁵ *More on Minimum Purchases, Surcharges, and Other Credit Card Merchant Agreement Violations, From the Companies Themselves*, The Consumerist, July 30, 2008. Available at <http://consumerist.com/2008/07/more-on-minimum-purchases-surcharges-and-other-credit-card-merchant-agreement-violations-from-the-co.html>

Citizen Views of Convenience Fees - Nationwide



Results of a 50-state survey suggest that states are becoming increasingly supportive of the use of electronic media for the receipt of payments from citizens.

An April 2007 nationwide study on the acceptance of electronic payments for state taxes and fees ⁶ found, “a potential barrier to expansion of electronic payments is managing the transactions costs associated with such payments.”

Currently, states have two principal options for addressing the issue of transaction fees, either direct state payment of such fees or passing the fees to taxpayers via a convenience fee or surcharge. In addressing this issue, states may make the distinction between required payments, such as taxes, and payments for services. Because states are typically required to collect 100% of the taxes owed, electronic transaction fees may have to be paid by the taxpayer, while the respective state agency may be able to absorb transactional fees for services such as licenses and registrations.

While electronic payments provide benefits and cost savings, the acceptance of electronic payments also involves costs such as specialized software and hosting services. If decisions are made to accept electronic payment, policies must be established to address how and by whom such costs will be covered.

Citizen Views of Convenience Fees - Iowa

In 2005, the IOWAccess Advisory Council (a 19-member citizen and agency representative board charged with advising the Director, Department of Administrative Services, on uses of IOWAccess funds) secured the services of Iowa State University’s Department of Political Science Public Policy and Administration Program to assess various aspects of online services. Among the areas surveyed were citizen impressions of convenience fees. An August 2005 report⁷ concluded that,

“The majority of Iowa citizens support user fees as the primary way of financing e-government information and services. An even higher level of support for user fees is evident when a service is said to be provided to a particular user group. The survey results indicate that Iowa citizens are willing to pay an average of \$3 per transaction for the convenience of online services after considering actual costs incurred in transactions with the government. Iowa citizens also place a premium on e-filing taxes with the state, application for state schools, and paying bills or fees online.”

A later survey⁸ conducted by the same group and reported in November 2005, also addressed user fees for e-government services:

⁶ *Acceptance and Use of Electronic Payments for State Taxes and Fees*, Dwight V. Denison, Merl M. Hackbart, Juita-Eleana (Wie) Yusuf, and Jay H. Song, University of Kentucky for the Council of State Governments, April 25, 2007. Available at <http://knowledgecenter.csg.org/kc/>

⁷ *Iowa E-Government Citizen Survey: Anticipating Demand and Understanding Financing Strategies*, Dr. Yu-Che Chen, Assistant Professor of E-Government and Public Management and Dr. Kurt Thurmaier, Professor of Public Policy and Administration Program, Department of Political Science, Iowa State University, August 12, 2005. Available at http://iowaccess.iowa.gov/forms_surveys/files/Iowa_eGovt_Citizen_Survey_FinalReport.pdf

⁸ *Iowa E-Government Citizen and Business Surveys: Final Policy Report*, Dr. Yu-Che Chen, Assistant Professor of E-Government and Public Management and Dr. Kurt Thurmaier, Professor of Public Policy and Administration Program, Department of Political Science, Iowa State University, November 23, 2005. Available at http://iowaccess.iowa.gov/forms_surveys/files/Chen_Thurmaier_eGovFinalReport.pdf

“Government should only develop online what users demand and are willing to pay for. Governments that develop e-transactions based on preferences of government agencies risk developing expensive service options for which there is little or no demand; the agency staff may be rightly proud of a state-of-the-art web portal with efficient services, but if the service provided does not meet user demand, then funds will not have been used in the most effective manner. ... we note that users retain the traditional “bricks and mortar” option to comply with regulations and so on. They are not compelled to use the e-transaction service for licensing, bidding, or other transactions with governments; if they use the e-transactions option it is because they choose to do so.

Citizens and businesses think differently about user fees as a general concept. About 47 percent of businesses prefer the principle of user fees and about 45 percent prefer the alternative of taxes to support e-government development. In contrast, about 67 percent of citizens support user fees as a general principle. In both cases, we find stronger support for user fees when specific beneficiaries are identified for a specific service. Support for fees by citizens is even stronger (83 percent) when they learn that it is for a specific group of people.

General Preferences for User Fees or Taxes to Finance Egov Developments

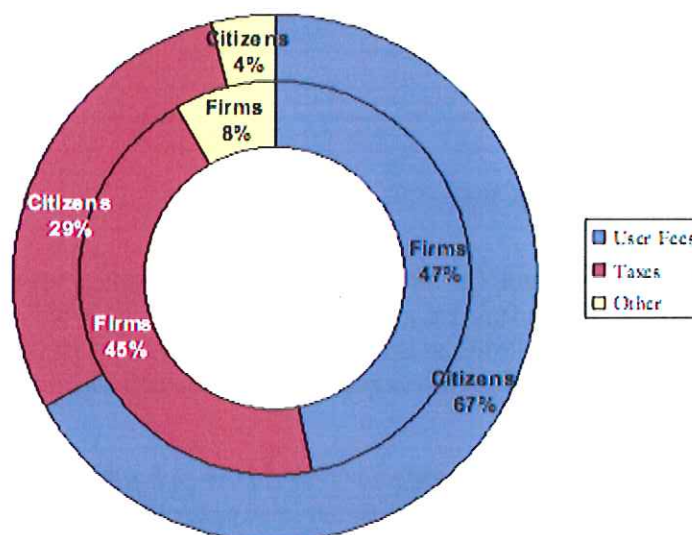


Figure 2 User Fees vs. Taxes

Willingness to Pay for Online Transactions

An important finding ... is that businesses and citizens are willing to pay for online services that directly benefit them. We define demand for services as both [1] a preference for a service and [2] the willingness to pay for that service. If a user (citizen or firm) is willing to pay something for a service, it is more likely that the user will adopt the service if it is available. Willingness to pay will be affected both by the preferences a user has for a specific service, and the price of that service relative to other service options.

To gauge how willing citizens and firms are to pay for online transaction with state agencies, respondents were first asked about the transactions that they would like to conduct online with a state agency. Against that backdrop, they were made aware that the full economic cost of conducting a transaction with state agencies offline may involve various costs such as travel expenses, travel time, waiting in line, postage costs, or mail delay.

The survey then asked whether they would be willing to pay \$1, \$2, and \$4 for the convenience of online transactions in general. They were then asked for the highest user fee they would be willing to pay to conduct their preferred transactions with a state agency online. This question also gave them the opportunity to indicate a value of less than \$1.

About 14 percent of citizens and about 20 percent of businesses do not want to pay any fee; these groups indicated a zero dollar fee is the highest amount that they are willing to pay for online transactions. That said, the demand curves in figure 3 generally suggest that online transactions exhibit a classic downward slope. The demand by firms for online transactions is less sensitive to increases in price than is the demand by citizens.

Firms (on average) are willing to pay more than citizens (on average) for online transactions that directly benefit them. While about 33 percent of firms are willing to pay \$2 per online transaction in a user fee, only 25 percent of citizens are willing to pay the same. If the demand is aggregated from \$2 or more, it appears that about 57 percent of the firms are willing to pay at least \$2/transaction compared to only 48 percent of citizens who are willing to pay at least \$2/transaction.

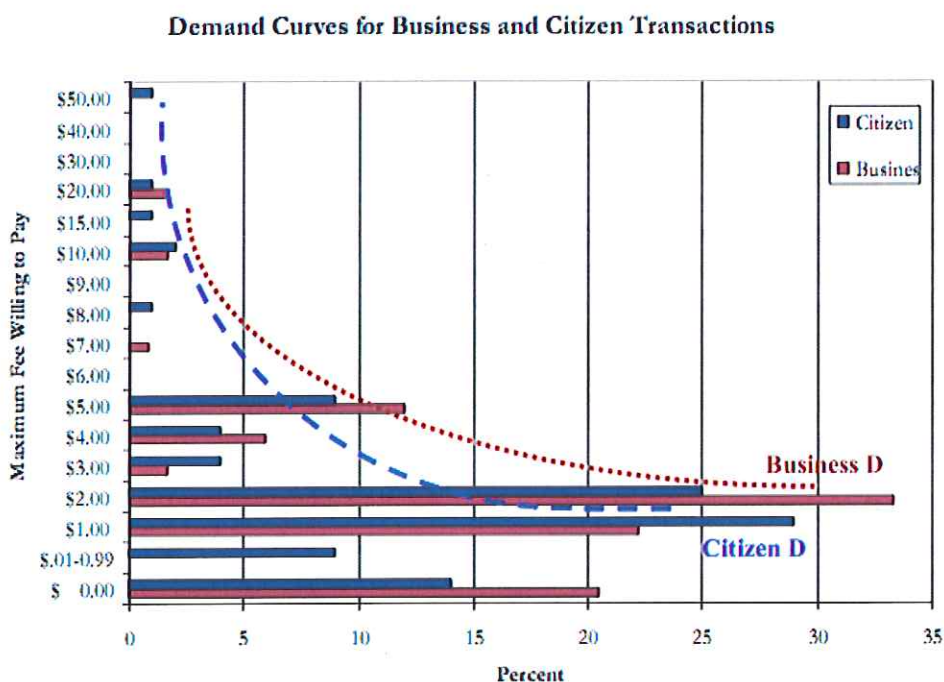


Figure 3 Willingness to Pay Transaction Fees

The demand curve analysis has important implications for the pricing structure of online transactions for state services. First, the user tolerance for a specific user charge is directly related to a specific service. Higher fees can be charged for services with a stronger demand by users. Second, determining the appropriate market fee requires market research about user preferences; the most important question is not what service does an agency want to develop online, but what online services do citizens and firms want to be developed.

Payment Methods and Surcharges

"It is important for the state to distinguish between the willingness of users to pay a user charge for an online service that directly benefits them and their willingness to pay a visible surcharge for a transaction (online or traditional paper) based on the method of payment for a service. Specifically,

payment method surcharges (such as a 1-3 percent credit card surcharge) are unpopular with both businesses and citizens. About 64 percent of citizens and 86 percent of firms would not want to be charged an additional 1% for a service fee."

It should be noted that both of the Iowa State University studies distinguish between fees charged to businesses and those charged to citizens. The IOWAccess Advisory Council, in considering fees to be imposed on online transactions, made no such distinction and considered online services to be used by either governmental entities or citizens. Fees approved by the Council were a mix of fixed fee and percent of the transaction, the latter usually due to fees charged by credit card providers.

The ability to charge fees is governed by the credit card provider member agreement, which varies depending on the card brand (VISA, MasterCard, etc.) The State conforms to the most restrictive agreement, which is typically VISA, which precludes a vendor (in this case the State agency) from charging customers a percentage of the transaction because of fees for imposed by the credit card services provider. This does not preclude an agency from charging a percentage of the total transaction which covers credit card services *and* actual direct and indirect agency processing costs. In other words, in order to comply with member agreements, a stated 4% convenience fee may be assessed if that percentage includes, for example, a 3.5% credit card charge *and* the calculated cost of staff processing time. However, an agency may not only charge a 4 % credit card processing fee.

Related Iowa Code

(Relevant portions highlighted)

The **Code of Iowa, Section 12.21, Accepting credit card payments**, states:

The treasurer of state may enter into an agreement with a financial institution to provide credit card receipt processing for state departments which are authorized by the treasurer of state to accept payment by credit card. **A department which accepts credit card payments may adjust its fees to reflect the cost of processing as determined by the treasurer of state. A fee may be charged by a department for using the credit card payment method notwithstanding any other provision of the Code setting specific fees.** The treasurer of state shall adopt rules to implement this section.

8A.221 IowAccess -- duties and responsibilities.

1. IowAccess. The department shall establish IowAccess as a service to the citizens of this state that is the gateway for one-stop electronic access to government information and transactions, whether federal, state, or local. Except as provided in this section, IowAccess shall be a state-funded service providing access to government information and transactions. **The department, in establishing the fees for value-added services, shall consider the reasonable cost of creating and organizing such government information through IowAccess.**

2. Duties. **The department shall do all of the following: a. Establish rates to be charged for access to and for value-added services performed through IowAccess.**

8A.222 FINANCIAL TRANSACTIONS.

1. Moneys paid to a participating agency from persons who complete an electronic financial transaction with the agency by accessing IowAccess shall be transferred to the treasurer of state for deposit in the general fund of the state, unless the disposition of the moneys is specifically provided for under other law. The moneys may include all of the following:

- Fees required to obtain an electronic public record as provided in section 22.3A.
- Fees required to process an application or file a document, including but not limited to fees required to obtain a license issued by a licensing authority.
- Moneys owed to a governmental entity by a person accessing IowAccess in order to satisfy a liability arising from the operation of law, including the payment of assessments, taxes, fines, and civil penalties.

2. Moneys transferred using IowAccess may include amounts owed by a governmental entity to a person accessing IowAccess in order to satisfy a liability of the governmental entity. The moneys may include the payment of tax

refunds, and the disbursement of support payments as defined in section 252D.16 or 598.1 as required for orders issued pursuant to section 252B.14.

3. In addition to other forms of payment, credit cards shall be accepted in payment for moneys owed to or fees imposed by a governmental entity in the same manner as provided in section 8A.125.

Section History: Recent Form

2003 Acts, ch 145, §25; 2006 Acts, ch 1030, §1
Referred to in § 12C.1, 12C.4

8A.125 BILLING -- CREDIT CARD PAYMENTS.

1. The director may bill a governmental entity for services rendered by the department in accordance with the duties of the department as provided in this chapter. Bills may include direct, indirect, and developmental costs which have not been funded by an appropriation to the department. The department shall periodically render a billing statement to a governmental entity outlining the cost of services provided to the governmental entity. The amount indicated on the statement shall be paid by the governmental entity and amounts received by the department shall be considered repayment receipts as defined in section 8.2, and deposited into the accounts of the department.

2. In addition to other forms of payment, a person may pay by credit card for services provided by the department, according to rules adopted by the treasurer of state. The credit card fees to be charged shall not exceed those permitted by statute. A governmental entity may adjust its payment to reflect the costs of processing as determined by the treasurer of state. The discount charged by the credit card issuer may be included in determining the fees to be paid for completing a financial transaction under this section by using a credit card. All credit card payments shall be credited to the fund used to account for the services provided.

Section History: Recent Form

2003 Acts, ch 145, §15
Referred to in § 8A.123, 8A.222

So Far

In summary, the term “convenience fee” is used in various ways to mean the fee imposed by credit card processors (more properly called the “discount fee”) or the total cost to a merchant for providing the convenience of paying by credit or debit card or other electronic means (discount fee plus cost overhead).

- The various credit card providers allow merchants, such as the State of Iowa, to charge an additional fee for the convenience of paying by a charge card, providing the fee is included in the cost of the purchase and not listed distinct from the article or service being purchased.
- The total amount of convenience fee as used in this study equals the fee charged by the charge card provider (discount fee) plus the costs of processing the online transaction.
- Convenience fees may be adjusted by the agency to reflect processing costs and merchants (agencies) may offer discounts for paying by cash.
- A fee equal to the charge imposed by the credit card provider (discount fee) may not be imposed on the customer in a face-to-face transaction.
- Users, i.e., citizens of Iowa, view convenience fees as necessary and are willing to pay these fees provided the value received for the fee-supported service is high.

Who Pays Convenience Fees?

The 2007 state and local government study⁹ on electronic payments surveyed reports on credit card usage within state and local governments. Of note was a 2003 survey by the Federation of Tax Administrators¹⁰ highlighting who paid fees associated with tax payments:

Responsible Party for Paying Fees Associated with Tax Payments

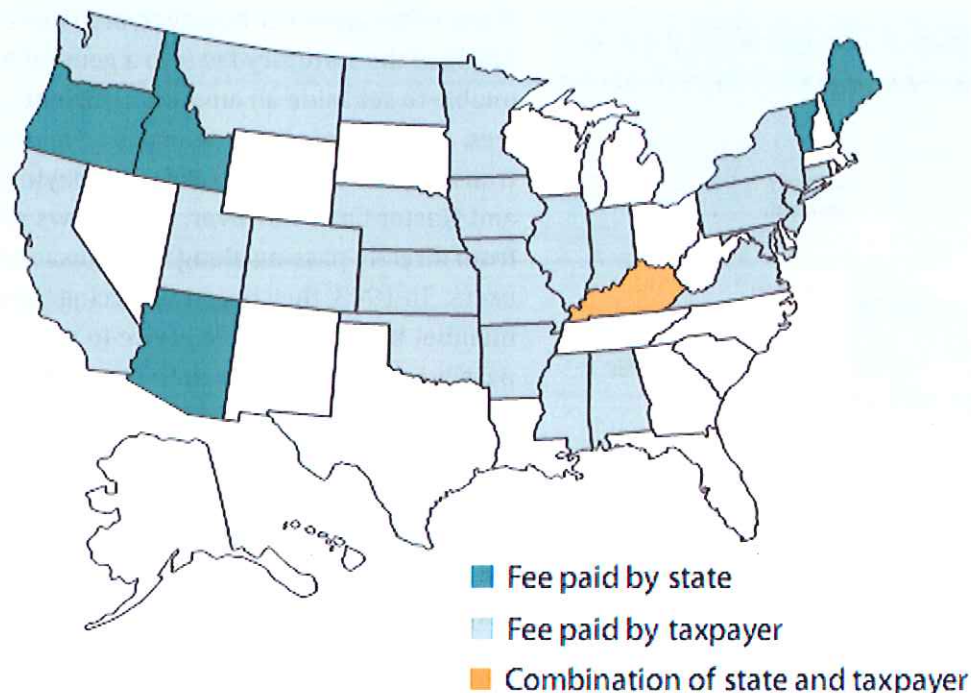


Figure 4 Convenience Fees for Taxes

The 2007 study noted that,

“One of the most significant obstacles to accepting credit card payments for government taxes is the per transaction cost of credit card use. Most public agencies are required by law to collect 100% of the tax or fee amount owed by the taxpayer. As a result, public agencies cannot pay the merchant discount fee that acquirers charge merchants for processing credit card payments.

For example, the 2003 NCSC survey found that the most commonly cited reason for state courts not accepting credit card payments were the transaction fees charged by the banks for processing credit cards.

The fee charged by banks to process credit card payments has typically been based on a formula that includes the interchange rates, anticipated sales volumes, average transaction amounts, and the method of authorization and settlement. In the 1991 Washington DC survey, most government agencies (69%) were charged a discount rate (a percent based on the dollar volume of credit card transactions) ranging from

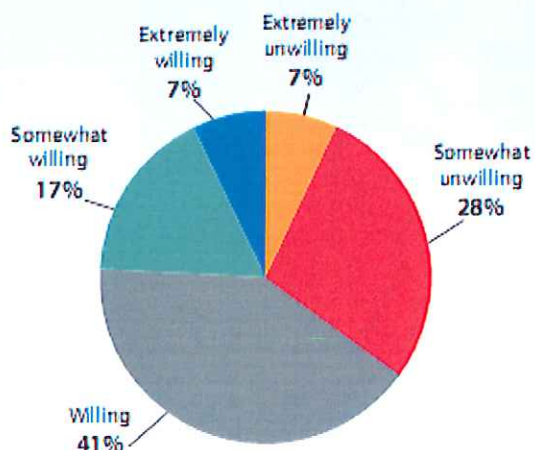
⁹ *Acceptance and Use of Electronic Payments for State Taxes and Fees*, Dwight V. Denison, Merl M. Hackbart, Juita-Eleana (Wie) Yusuf, and Jay H. Song, University of Kentucky for the Council of State Governments, April 25, 2007. Available at <http://knowledgecenter.csg.org/kc/>

¹⁰ *Results of 2003 FTA Credit Card Survey*, FTA Bulletin B-27/03, Federation of Tax Administrators (FTA), 2003. Available at <http://www.taxadmin.org/fta/rate/b2703.html>

1.4% to 5% (Kuhn 1992)¹¹. Other agencies, using a third party processor, paid a sliding scale of fees ranging from \$3 to \$60, depending on the amount of the payment being processed.

Private sector merchants can typically hide or bury the fees associated with accepting credit card payments into the price of the goods and services. Some government agencies have taken an approach similar to the private sector in absorbing the credit card transaction fees as part of the cost of doing business, but without an across-the-board rise in tax rates or fee structures.

States' Perceptions of Taxpayer Willingness to Pay Convenience Fees or Transaction Surcharges



Source: State Taxes and Fees E-payment Survey (Question 46).

Figure 5 Taxpayer Willingness to Pay Fees

Many other agencies, however, are constrained to deposit 100% of the statutory fee into a general fund and are therefore unable to set aside an amount sufficient to cover transaction fees. Most government agencies have passed on the transaction fee to those taxpayers paying by credit card. VISA and Master Card, however, had bylaws prohibiting merchants from directly passing along the transaction fees to credit card users. In 1993, they began enforcing these bylaws, ordering member banks to cut off service to those government agencies passing along the transaction fee. Despite extensive discussions with representatives of state and local governments, VISA and MasterCard were reluctant to change their position prohibiting passing along the transaction fees. As a result, government agencies have adopted various means for addressing the problem of passing on credit card fees to taxpayers.”

¹¹ “Charge it:” *Credit and debit cards come to the public sector*, Kuhn, Patricia, *Government Finance Review*. 8(3): 13–16, 1992.

SF 2088 Convenience Fee Survey

Methodology

In early October 2010, 57 State entities (Appendix A) were surveyed about their use of any convenience fee, the impact of such fees, and the effect on agency operations if the fees were altered. Detailed agency responses are shown at Appendix C.

**Convenience Fee = ePayment Fee + Provider Processing Fee +
Cost of Providing Online Payment**

Results

"...the extent and amount of the fees charged by state agencies... [and] revenues generated by those fees..."

State ePayment Service

In order to provide State agencies with an easy means for accepting credit cards, the State's Information Technology Enterprise provides a gateway to Elavon (a credit card provider) by offering an "ePayment Service". This allows agencies to add credit card acceptance capability to their online service. ITE charges \$0.32 (32 cents) per transaction for this service, which also creates appropriate transaction information for the State's I3 accounting system.

Agency	Annual ePay Charge	Annual ePay Charge for state agencies*
Board of Educational Examiners	\$1,0923	\$1,092.
Commerce Professional Licensing	\$3,240	\$3,240.
Inspections & Appeals	\$287	\$287.
Iowa Supreme Court Commissions *	\$5,526	
Iowa Workforce Development	\$9,024	\$9,024.
Natural Resources	\$10,154	\$10,154
Public Health	\$7,282	\$7,282
Public Health Iowa Board of Medicine	\$1,470	\$1,470
Public Health Nursing Board	\$4,651	\$4,651
Public Safety Department	\$8,953	\$8,953
Secretary of State	\$330.	\$330
Judicial -IT*	\$63,567	
Grand Total	\$115,582	\$46,487
<i>* not defined as "state agency" within scope of SF2088</i>		

Table 2 ITE ePayment Fee

Provider Processing Fee

The following table shows the annualized transaction values and associated fees. The figures have been projected to indicate probable 12-month transaction data based upon the first 9 months of usage date with a new vendor.

Merchant Account Holder	Sales Revenues	Fees	% of sales	#Sales
IA State Fair Foundation	\$149,275	\$3,111	2.08%	671
Iowa Judicial Branch	\$295,733	\$6,110	2.07%	5,072
Iowa Judicial Branch 2	\$27,614,476	\$376,024	1.36%	200,072
IA CSR Examiners Brd	\$36,853	\$674	1.83%	497
Iowa Judicial Branch 3	\$20,713	\$409	1.97%	204
IWD Unemp Ins Tx Pymts	\$39,563	\$747	1.89%	288
State Hist Soc Iowa Arts	\$25,179	\$585	2.33%	455
Museum Store-Histor	\$66,676	\$1,293	1.94%	2,260
Trails West Gift Shop	\$15,201	\$314	2.06%	583
IDPH Prof Licensure	\$1,817,811	\$32,434	1.78%	22,453
IDPH Plumb Mech Brd	\$974,653	\$17,575	1.80%	5,067
IA Education Examiners	\$266,000	\$4,317	1.62%	3,167
IA Criminal Record Checks	\$491,155	\$13,589	2.77%	12,963
IA Criminal Hist Rec Ck	\$0	\$2	0.00%	-
Iowa Dept Pub Safety SING	\$481,977	\$13,249	2.75%	13,815
IA DPS Elect Exam License	\$940,883	\$18,862	2.00%	9,765
IA DPS Elect Exam Permits	\$744,501	\$15,603	2.10%	7,232
IA Public Def Training	\$633,703	\$12,194	1.92%	11,264
Prof Lic-Engineers	\$445,040	\$9,262	2.08%	4,547
Prof Lic-Real Estate	\$825,953	\$14,985	1.81%	4,576
Prof Lic-Accountants	\$333,033	\$7,089	2.13%	3,672
Prof Lic-Architects	\$219,411	\$4,723	2.15%	1,017
Prof Lic-Engineers1	\$50,387	\$1,078	2.14%	411
Prof Lic-Real Estate1	\$105,799	\$2,000	1.89%	839
Prof Lic-Accountants1	\$38,440	\$794	2.07%	295
Prof Lic-Architects1	\$28,971	\$588	2.03%	121
Iowa Board of Nursing	\$1,564,115	\$24,104	1.54%	14,779
Iowa Board of Medicine	\$2,127,727	\$43,952	2.07%	4,787
IA Secretary State	\$2,489,412	\$61,604	2.47%	72,805
IA Dept Insp and Appeals	\$478,236	\$10,108	2.11%	1,100
IA Communications Network	\$448,504	\$12,178	2.72%	97
IA College Aid Comm	\$136,326	\$1,794	1.32%	701

LegServ Capitol Gift Shop	\$6,140	\$138	2.25%	240
DNR State Forest Nursery	\$178,034	\$3,866	2.17%	704
DNR-Geo Survey	\$3,465	\$84	2.43%	108
DNR-Iowa Outdoors	\$15,185	\$358	2.36%	792
DNR ESD wastewater fees	\$1,587	\$39	2.47%	19
DNR-Customer Service	\$132,914	\$3,022	2.27%	833
DNR-Cedar Rock	\$4,725	\$92	1.94%	133
DNR Sales	\$84,777	\$1,855	2.19%	609
DNR Boat Docks	\$0	\$0	0.00%	-
DNR Park Reservations	\$1,833,453	\$28,712	1.57%	24,519
DNR Banner Shooting Range	\$35,175	\$797	2.27%	1,819
DNR Special Events	\$19,859	\$545	2.75%	992
Office Prof Regulation (Judicial)	\$2,003,373	\$40,196	2.01%	20,705
TOTAL for State Agencies	\$48,224,395	\$791,057	1.64%	457,047

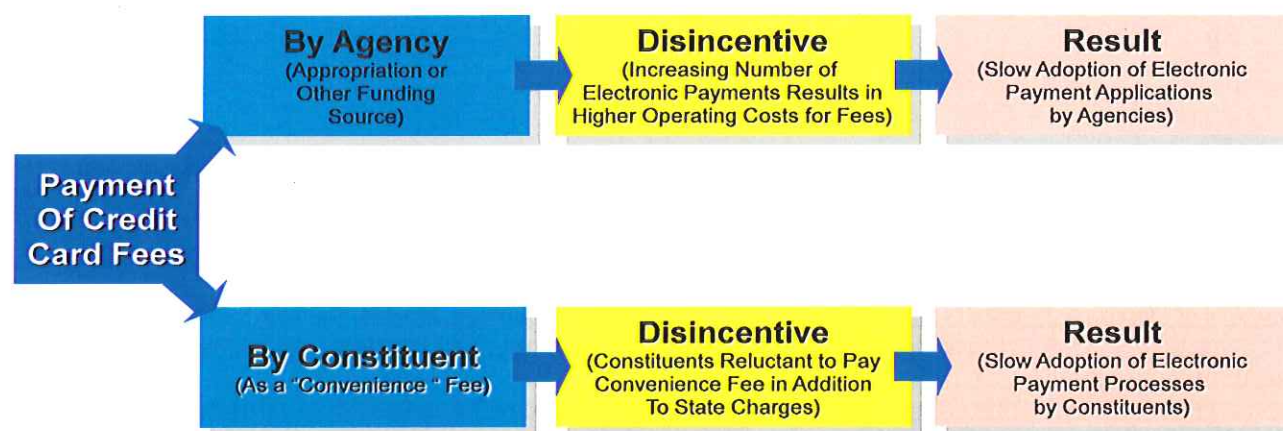
Table 3 Annual Processing Costs for 2010

The Iowa Department of Agriculture and Land Stewardship utilizes another provider, Kelly Registration Systems, Inc.

Alternatives to Convenience Fees

"...ways to reduce or eliminate the fees."

Consistent with the intent of the General Assembly to encourage the use of electronic transactions, it is necessary to eliminate disincentives to a) the development of electronic payment options by governmental entities, and b) the adoption of electronic payments by government's constituents. The most significant disincentive appears to be the fees associated with the use of credit cards.¹²



¹² *State Government E-Commerce Study-Encouraging the Use of Electronic Financial Transactions With the Citizens of Iowa* Department of Administrative Services, State of Iowa, Des Moines, Iowa, January 2006. Available at <http://publications.iowa.gov/3318/>

The 2007 Council of State Governments survey¹³ determined six basic policies and practices that states identified as “best” or “effective” policies. These include:

1. Marketing the credit and/or debit card payment option and educating citizens and taxpayers on the availability of these payment options;
2. Refraining from charging convenience fees or surcharges that may detract from the use of credit or debit cards;
3. Using a third party service provider and contracting with one primary service provider for all agencies;
4. Maintaining a standardized payment processing system or platform across all agencies;
5. Providing citizens and taxpayers with the option to pay online using credit or debit cards; and
6. Making credit and debit card payment options available across a variety of taxes and fees.

The charging of convenience fees continues to be a probable citizen complaint, largely due to the presentation of such fees in a manner that makes them appear to be an additional taxpayer burden.

With the exception of the first two items, Iowa has adopted most of the above recommendations. The marketing of payment options has not been addressed in a comprehensive manner outside of the actual online service portal. The charging of convenience fees continues to be a probable citizen complaint, *largely due to the presentation of such fees in a manner that makes them appear to be an additional taxpayer burden.*

A May 2010 report¹⁴ on surcharges noted that, Merchants have pricing options other than point-of-sale surcharges that avoid the problem of unannounced price increases at the checkout counter. They can build the out-of-pocket expenses associated with bank card expenses into the prices of their products, as they do with other business expenses, thereby providing consumers with a single price and avoiding surprises at the point of sale. Also, bank card network rules and federal law allow retailers to offer discounts to customers who pay with cash. In that instance, retailers would post a single price for all customers and then make reductions in that price at the point of sale for customers who use cash.

Recently, legislative proposals in other states have appeared that would explicitly negate no-surcharge rules by preventing credit card companies from ‘inhibit[ing] the ability of any merchant to direct consumers to the merchant’s preferred form of payment.’¹⁵ Some of the nation’s largest retailers have expressed support for this approach and opposed additional state bans on bank card surcharges.

Economists at the Federal Reserve Board¹⁶ developed a basic model to explain the relationship between the fees merchants pay to banks for processing credit card payments and retail pricing. They found that retailers set a price for an item purchased by credit card using the following formula.

¹³ *Acceptance and Use of Electronic Payments for State Taxes and Fees*, Dwight V. Denison, Merl M. Hackbart, Juita-Eleana (Wie) Yusuf, and Jay H. Song, University of Kentucky for the Council of State Governments, April 25, 2007. Available at <http://knowledgecenter.csg.org/kc/>

¹⁴ *Point-of-Purchase Bank Card Surcharges: The Economic Impact on Consumers*, Allen Rosenfeld, Ph.D., for the New America Foundation, May 2010. Available at www.Newamerica.net.

¹⁵ Credit Card Interchange Fees Act of 2009 (H.R. 2382), Section 193(c).

¹⁶ *Interchange Fees and Payment Card Networks: Economics, Industry Developments, and Policy Issues*, Prager R., M. Manuszak, E. Kiser, and R. Borzekowski, Finance and Economics Discussion Series. Federal Reserve Board, Divisions of Research & Statistics and Monetary Affairs, 2009.

$$\begin{aligned}
 & \text{The Retail Price for a Cash Purchase} \\
 & + \text{Credit Card-Related Costs Paid by the Retailer, Including Bank Fees} \\
 & \quad + \text{Processing Costs} \\
 & - \text{The Benefits to the Retailer for Accepting the Credit Card Rather than Cash or Check} \\
 & = \text{Retail Price for Credit Card Purchase}
 \end{aligned}$$

In other words, the retail price for a credit card purchase is not simply the price that would be charged by the retailer in the absence of credit card use plus the cost of bank card fees. Rather, calculating the full net costs to the retailer of accepting credit cards, instead of cash, *after accounting for the benefits of the credit card transaction to the retailer*, is the key to the retail pricing. If the benefits of credit card acceptance for retailers are greater than the costs associated with the acceptance of the cards, then the credit card price should be **less than**, not **higher than**, the cash price. This outcome would overturn a key assumption that underlies arguments for allowing retailers to impose a customer surcharge.

To put it another way, if retailers incurred lower, not higher, net costs (i.e., benefits minus costs) when accepting card payments instead of cash, and if card purchases dominate sales, the difference between those costs would represent the amount by which retailers in competitive markets could lower, not raise, prices to account for the savings produced by credit card use. Those price decreases should occur despite the fact that retailers are being charged bankcard fees. This would contradict the assumption that bank card use leads to higher retail prices, thereby undermining the claims of retailers advocating for the right to add surcharge fees to posted retail prices.

Recommendations

"...including any recommendations for legislative consideration."

At this time, we resubmit our primary recommendation from the 2006¹⁷ DAS report, plus several additional alternatives:

Alternative 1: Make an appropriation to the State Treasurer's Office for the estimated amount sufficient to cover the annual cost of all potential executive branch credit card fees (estimated to be \$15.8 million annually). The FY10 credit card fees for merchant accounts set up through the Treasurer's Office totaled \$791,057. This is estimated to be approximately 5% of the payments eligible to be remitted by credit card if all eligible payments were made electronically.

In exchange for this appropriation, all executive branch "convenience" fees currently being charged to constituents to defray credit card fees would be eliminated. The Department of Revenue, Board of Regents and its' institutions, and the Judicial Branch would be exempted from this arrangement. In requesting this appropriation, it must be understood that a) the amount requested is an estimate, based on historical data and projections of future credit card use, which should be reevaluated annually; b) an increase in the use of credit cards for payments to the State of Iowa results in a corresponding increase in the amount of the credit card fees (approximating 1.64% of total revenues collected by credit card).

Alternative 2: Allow agencies to build transactional fees into the cost of goods or services so that the price charged reflects the statutory amount to be charged plus calculated, supportable value-added fees, e.g., credit card charges, ITE ePayment fees, processing costs, the system providing the online service, etc. Periodic adjustments will be permitted through Administrative Rules or some other pre-defined process that allows for transparency and public comment.

For example, a professional license may have a statutory amount of \$100. Agency costs for transactional fees total \$4.50 making the online price \$104.50. The agency would deposit the statutory fee into the General Fund and retain the additional funds in order to pay the credit card and other transactional expenses.

The agency would periodically review the added fee in relation to actual costs and propose adjustments to maintain break-even operation. Upon approval, the new rate would be implemented. Agencies could consider offering a cash discount that reflects the reduced transactional costs. Alternatively, a lower transactional fee could be charged on all transactions, removing the cash discount and spreading the cost to all.

Option: Charge more for not using online service. The Board of Medicine, in years past, considered charging a fee for those license applicants who did not apply online. The rationale was that it took longer to personally attend to a walk-in applicant, enter data from a hard copy application, collect payment, and issue a receipt than it would to process the application electronically. In the above example, parity between online and face-to-face applications could be achieved so either method costs the same.

¹⁷ *State Government E-Commerce Study-Encouraging the Use of Electronic Financial Transactions With the Citizens of Iowa* Department of Administrative Services, State of Iowa, Des Moines, Iowa, January 2006. Available at <http://publications.iowa.gov/3318/>

Appendix A: State of Iowa Government Entities Surveyed

ABD	Alcoholic Beverages Division (Department of Commerce)
AG	Agriculture
AOS	Auditor
BLIND	Department for the Blind
BON	Board of Nursing
DAS	Department of Administrative Services
DCA	Department of Cultural Affairs
DHR	Department of Human Rights
DHS	Department of Human Services
DIA	Department of Inspections and Appeals
DNR	Department of Natural Resources
DOC	Department of Corrections
DOT	Department of Transportation
DPD	Department of Public Defense
DPS	Department of Public Safety
DVRS	Vocational Rehabilitation (Department of Education)
ED	Education
HSEMD	Department of Public Defense
IANG	National Guard
IBM	Board of Medicine
IBOP	Board of Pharmacy
ICN	Iowa Communications Network
ICRC	Civil Rights Commission
ICSAC	Iowa College Student Aid Commission
IDA	Iowa Department on Aging
IDALS	Department of Agriculture and Land Stewardship
IDB	Dental Board
IDCU	Credit Union Division (Department of Commerce)
IDED	Iowa Department of Economic Development
IDOB	Iowa Division of Banking
IDOM	Department of Management
IDPH	Department of Public Health
IDR	Department of Revenue
IDVA	Veterans Affairs
IECD	Ethics and Campaign Disclosure Board
IFA	Iowa Finance Authority
IGOV	Office of the Governor
IID	Insurance Division
ILEA	Iowa Law Enforcement Academy
ILOT	Lottery
IPERS	Iowa Public Employee Retirement System

IPTV	Iowa Public Television
IRGC	Racing and Gaming Commission
ISAC	State Association of Counties
IUB	Utilities Board (Department of Commerce)
IVH	Veterans Home
IWD	Iowa Workforce Development
JB	Judicial Branch
LEGIS	Legislature
LIB	Library
ODCP	Governor's Office on Drug Control Policy
OEI	Office of Energy Independence
PERB	Public Employment Relations Board
RIO	Recovery Iowa Office
SOS	Office of the Secretary of State
SPD	Public Defender
TOS	Office of the Treasurer
	Iowa Interactive, LLC (State Website Contractor)

Appendix B: Glossary

Acquiring Bank/Merchant Bank

The bank that does business with merchants who accept credit cards. A merchant has an account with this bank and each day deposits the value of the day's credit card sales. Acquirers buy (acquire) the merchant's sales slips and credit the tickets' value to the merchant's account.

Clearing

The process a check goes through to validate and transfer funds between banks. An electronic check will clear in the same manner as a paper check.

Discount Rate

A percentage rate that is charged by the acquiring bank for processing a merchant's transaction. The type of business and/or how the credit card is processed usually determine this rate. Retail based transactions, also known as Card Present transactions are assigned lower discount rates than MO/TO, also known as Mail Order/Telephone Order, Internet, or Card Not Present transactions.

Interchange Fee

A fee paid by the acquiring bank/merchant bank to the issuing bank. The fee is meant to compensate the issuer for the time after settlement with the acquiring bank/merchant bank and before it recoups the settlement value from the cardholder. The interchange fee is a percentage applied, according to VISA/MasterCard regulations, to the dollar value of each transaction. There are multiple categories of interchange, and VISA and MasterCard each have their own criteria for their own categories. A transaction must meet the specified criteria for a category in order for that category's rate to be applied. Each transaction is evaluated individually, so various interchange rates may apply within one batch of merchant transactions.

Internet merchant

A business owner who sells products or services over the Internet.

Issuer

The bank that extends credit to customers through bankcard accounts. The bank issues the credit card and receives the cardholder's payment at the end of the billing period. Also called the issuing bank or the cardholder bank.

Online Store

A web site that accepts direct payments in exchange for goods and services.

Merchant Service Agreement

A contract that outlines the terms for accepting and processing credit cards between an acquiring bank and/or payment gateway company, and the merchant.

Payment Processor

A financial institution distinct from the bank that processes data from credit card transactions. Providing pre-authorization, post-authorization, and refund services to businesses accepting credit cards. They are responsible for the distribution of funds between consumers and businesses. Sometimes also referred to as a Transaction Processor.

Processor

A transaction processor, distinct from the bank, that processes data from credit card transactions and then distributes funds from the merchant's bank account.

Settlement

A process in which an electronic transaction (credit cards) is accepted for financial settlement between the acquiring and issuing banks.

Transaction

The process that takes place when a cardholder makes a purchase with a credit card.

Transaction Fee

A per transaction amount charged by the bank for processing each transaction. This amount is in addition to the discount rate. For example: a discount rate of 2.25% plus 15 cents per transaction.

Appendix C: Responses from Agencies that Charge Convenience Fees

Agency: Department of Inspections and Appeals

Agency Comments: The two online services conducted approximately 614 transactions during SFY 10, which generated \$1,639 in convenience fees. The cost to the Department of offering online services to its customers amounted to approximately \$7,800 during this same period of time.

Name of Online Service: Social and Charitable Gambling License Application

Convenience Fee Charged Per Transaction: Sliding scale dependent upon total cost of licenses purchased by the customer. System calculates the convenience fee as 4 percent of the total transaction, excluding any bank/credit card fees.

Number of Annual Transaction: During State Fiscal Year 2010, a total of 2,039 licenses were issued by the Social and Charitable Gambling Unit. The online licensing system did not become fully operational until January 2010, so we have yet to complete either a full fiscal year or full calendar year with the online application. The Social and Charitable Gambling online system has generated a total of \$1,617 in convenience fees since January 2010.

Basis for Fee: Fee is used to offset costs associated with ITE's hosting and maintenance of the website, as well as to offset charges from the issuing bank/credit cards.

Impact To Department Of Reducing Or Eliminating Fee: Reducing or eliminating the convenience fee would result in the Department reallocating additional scarce resources to fund the hosting and maintenance of the website.

Name of Online Service: Targeted Small Business Certification

Convenience Free Charged Per Transactions: Only applications for renewals can be processed through the online system. Initial applications must be submitted by mail or hand-delivered as extensive documentation is required to start the certification process. The convenience fee charged for a renewal is \$0.60, which also is calculated by the system as 4 percent of the renewal fee (\$15).

Number of Annual Transactions: During State Fiscal Year 2010, a total of 178 renewals were handled by the Targeted Small Business Certification Unit. Not all renewals, however, were processed through the online application system. The Targeted Small Business Certification online system has generated a total of \$16.20 in convenience fees during SFY 2010.

Basis for Fee: Fee is used to offset costs associated with ITE's hosting and maintenance of the website, as well as to offset charges from the issuing bank/credit cards.

Impact To Department Of Reducing Or Eliminating Fee: Reducing or eliminating the convenience fee would result in the Department reallocating additional scarce resources to fund the hosting and maintenance of the website.

Agency: Iowa Department of Agriculture and Land Stewardship

Agency Comments: Roughly 2.4% plus 20 cents per transaction is paid to the Credit Card Processor... that's pretty much standard for internet transactions where the credit card is not physically present. The balance of the convenience fees are not based upon a specific amount for staff, hosting, etc... We calculate that based upon what is fair and reasonable, and what our experience tells us people will pay to optimize the adoption rate, but at the same time ensure that we make money. So, we don't have a breakdown for staff, hosting, etc. Obviously larger dollar amounts will pay a higher percentage, but we usually use a sliding scale, so the percentage may be lower for higher dollar amounts.

Name of Online Service: Commercial Meter License Renewals

Convenience Fee Charged Per Transaction: 10% convenience fee for total transaction

Number of Annual Transaction: During State Fiscal Year 2010, a total of 186.

Basis for Fee: Roughly 2.4% plus 20 cents per transaction is paid to the Credit Card Processor_(Kelly Registration Systems, Inc.)

Name of Online Service: Scales

Convenience Free Charged Per Transactions: 6% convenience fee for the total transaction

Number of Annual Transactions: During State Fiscal Year 2010, a total of 483.

Basis for Fee: Roughly 2.4% plus 20 cents per transaction is paid to the Credit Card Processor_(Kelly Registration Systems, Inc.)

Impact of Reducing/Eliminating Fee:**Name of Online Service: Pesticide Dealers**

Convenience Free Charged Per Transactions: 7% convenience fee for the total transaction

Number of Annual Transactions: During State Fiscal Year 2010, a total of 278.

Basis for Fee: Roughly 2.4% plus 20 cents per transaction is paid to the Credit Card Processor_(Kelly Registration Systems, Inc.)

Name of Online Service: Meat and Poultry

Convenience Free Charged Per Transactions: 10% convenience fee for the total transaction

Number of Annual Transactions: During State Fiscal Year 2010, a total of 37.

Basis for Fee: Roughly 2.4% plus 20 cents per transaction is paid to the Credit Card Processor_(Kelly Registration Systems, Inc.)

Name of Online Service: **Scale Servicers**

Convenience Fee Charged Per Transactions: \$2.00 per transaction

Number of Annual Transactions: During State Fiscal Year 2010, a total of 79.

Basis for Fee: Roughly 2.4% plus 20 cents per transaction is paid to the Credit Card Processor (Kelly Registration Systems, Inc.)

Agency: Department of Natural Resources

Name Of Online Service: **Parks Reservation**

Convenience Fee Charged Per Transaction Type: \$4 per on-line transaction and \$6 per telephone reservation collected by the vendor

Number Of Annual Transactions: 31,314 reservations--this number does not include walk-in registrations which account for 50-65% of camping business

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): Fees set by the contracted vendor through a formal RFP process

Fees remitted to a vendor \$4 per on-line transaction, \$6 per telephone reservation, \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per transaction fee to ITE

Impact To Department Of Reducing Or Eliminating Fee: Significant annual costs to the State Parks and Reserves operational budget which could impact the level of service provided to the Citizens of Iowa.

Name Of Online Service: **ELSI**

Convenience Fee Charged Per Transaction Type: \$5 plus 2.5% per transaction collected by the vendor

Number Of Annual Transactions: 1.4 Million transactions annually

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): Fees set by the contracted vendor through a formal RFP process

Fees remitted to a vendor \$5 plus 2.5% per transaction collected by the vendor

Impact To Department Of Reducing Or Eliminating Fee: Significant annual costs to the Fish and Wildlife Trust Fund which could impact the level of service provided to the citizens of Iowa.

Name Of Online Service: **NPDES**

Convenience Fee Charged Per Transaction Type: None

Number Of Annual Transactions: 164 annual transactions of \$85 per.

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.):

Fees remitted to a vendor \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per trans

Name Of Online Service: **Water Use**

Convenience Fee Charged Per Transaction Type: None

Number Of Annual Transactions: 1918 items for a total collected amount of \$349,174.44 collected in FY '10; plus 3,115 annual users totaling \$425,980.00 in FY '10

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.):

Fees remitted to a vendor \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per trans

Name Of Online Service: **State Forest Nursery**

Convenience Fee Charged Per Transaction Type: Undecided

Number Of Annual Transactions: 2,850 average annual sales number over the past three years for an average revenue of \$699,781.50

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): considerations include: amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.

Fees remitted to a vendor \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per trans

Name Of Online Service: **Op-Cert**

Convenience Fee Charged Per Transaction Type: Undecided

Number Of Annual Transactions: Averaging 10,357 transactions annually.

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): considerations include: amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.

Fees remitted to a vendor \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per trans

Name Of Online Service: **Special Events**

Convenience Fee Charged Per Transaction Type: none

Number Of Annual Transactions: FY '11 Year to date transactions as of 11/9/2010 is 38. This system is new and expected to be seasonal and increase significantly over time and with enforcement efforts.

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.):

Fees remitted to a vendor \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per trans

Name Of Online Service: **Storm Water**

Convenience Fee Charged Per Transaction Type: Undecided

Number Of Annual Transactions: Approximately 6,000 transactions in Fiscal Year 2010

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): Considerations include: amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.

Fees remitted to a vendor \$95 monthly maintenance and reporting fee to US Bank, \$0.27 per transaction fee to US Bank, \$0.31 per trans

Agency: Secretary of State

Comments: Charged for credit card transactions only

Name Of Online Service: **Biennial Report**

Convenience Fee Charged Per Transaction: Our office charges up to \$2.00 per credit card transaction. In FY 2010, the Secretary of State's office collected \$46,713 in convenience fees

Number Of Annual Transactions: This varies by year. Biennial reports are filed every other year. The number of entities (LLC's, corporations, etc.) filing reports with our office varies by year as well. In FY 2010, there were approximately 52,450 entities

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): Our office collects the amount paid to Elavon through the State Treasurer's office

Impact To Department Of Reducing Or Eliminating Fee: Our office would need to pursue one of the following options; 1) secure an increase in appropriation to cover the costs associated with credit card transactions, 2) reduce one or more full time employees which reduces the effectiveness of the agency's ability to provide excellent customer service, or 3) increase other fees associated with the biennial report process.

Agency: Iowa Board of Medicine

Name Of Online Service: Online license renewal

Convenience Fee Charged Per Transaction Type: \$12.50

Number Of Annual Transactions: Approximately 4,600

Credit card charge, ITE fee, and staff time.

This would be a significant amount of money that our agency would need to cover. It would put us in a position of to raise our licensure fees to cover the expense or look at reducing other items in the office to offset the cost which in turn would affect staff efficiency and productivity. This would also impact the future of other services going online.

Name Of Online Service: On-line license renewal

Convenience Fee Charged Per Transaction Type: \$5

Number Of Annual Transactions: \$2 to reimburse credit card fees from the Treasurer's Office, \$3 to reimburse ITE hosting costs

Impact To Department Of Reducing Or Eliminating Fee: Loss of approximately \$75,000 revenue annually

The Department of Revenue is separate from other surveyed as they are able to assess surcharges for tax-related transactions.

Name Of Online Service: Tax payments

Convenience Fee Charged Per Transaction Type: Credit Card – 2.5%

a. Debit Card - \$3.95

b.

Number Of Annual Transactions: Number of annual transactions:

The tables below reflect FY10 credit card data. Debit card usage was not authorized until FY11.

Payment Counts and Dollars:

Card Type	Total Count	Total Amount
American Express	756	\$1,038,672.05
Discover	802	\$403,157.89

Master Card	9,114	\$2,830,134.22
VISA	19,696	\$5,424,936.12
	30,368	\$9,696,900.28

Payment Method:

	Telephone		Web	
	Count	Amount	Count	Amount
American Express	170	\$299,818.25	586	\$738,853.80
Discover	251	\$134,717.62	551	\$268,440.27
Master Card	4,553	\$1,356,036.23	4,561	\$1,474,097.99
VISA	9,693	\$2,550,750.45	10,003	\$2,874,185.67
	14,667	\$4,341,322.55	15,701	\$5,355,577.73

Basis For Fee (i.e., amount to credit card provider, amount for internal resources such as staff time, amount for external resources such as web hosting, etc.): The Department of Revenue does not accept payment by credit or debit card for purposes of PCI/DSS. Taxpayers who want to pay by credit card are referred to Official Payments Corporation (OPC). OPC processes one transaction for the amount the taxpayer wishes to pay and a separate transaction equal to the processing charge. The tax payment is remitted to IDR by OPC and the transaction fee is retained by OPC.

Impact To Department Of Reducing Or Eliminating Fee:

If the fee were eliminated the cost of processing the card transactions would have to be paid directly from tax receipts. Eliminating the fee would likely be very attractive to many payors, particularly businesses and individuals who pay their balance in full each month and who use credit cards primarily for convenience and rewards. The increased cost to the state could very likely be many millions of dollars.

