CITY OF MOUNTAIN VIEW

MEMORANDUM
Finance and Administrative
Services Department

DATE: April 28, 2015

TO: City Council

FROM: Suzanne Niederhofer, Assistant Finance and Administrative Services Director
Patty J. Kong, Finance and Administrative Services Director

VIA: Daniel H. Rich, City Manager

SUBJECT: Credit Card Processing Fees

PURPOSE

The use of credit cards, and therefore the costs associated with credit card processing, has increased with the use of accepting online payments. In the past, Council has stated the cost to do business online should not be more than the cost to conduct the transaction in person. Staff is seeking direction as to whether the City should implement credit card processing fees for online and/or on-site transactions.

BACKGROUND

On December 2, 2014, staff proposed an appropriation increase of $70,000 due to the projected increases in utility payment processing fees. At that time, Council requested staff to provide additional information as part of the budget process on alternatives for cost recovery and what other agencies are doing.

There are six locations in the City where staff accepts credit cards as a form of payment: City Hall Finance, Center for the Performing Arts (CPA), Library, Police/Fire Administration, the Community Center, and Shoreline Golf Links. In addition to on-site locations, the City also accepts online payments for utility payments, parking permits, CPA tickets, basic building permits (E-permits), recreation classes and camps, and Library fees and fines. All online transactions are done through a payment processor.

The fees charged for credit card transactions at on-site locations are charged to the City's general bank account at the end of each month. For Fiscal Year 2013-14, the total

credit card fees charged for on-site locations were $303,000 and approximately $100,000 for online transactions. The amount for utility payments is increasing as more customers choose to make payments online and is estimated to exceed $125,000 for the current fiscal year. About 50.0 percent of these charges are for credit card transactions at City Hall processed through Bank of America Merchant Services. It would be difficult to allocate on-site payment processing costs to different funding sources.

Other payment options are available. On-site locations accept cash and checks, and the City has long had an auto debit program and accepts home banking payments for utility payments. For online utility payments, debit and echecks are accepted. These types of transactions have a significantly lower transaction cost for the City.

Online credit card transactions require a payment gateway or processor. A payment gateway is an e-commerce application service that authorizes credit card payments for e-businesses and online retailers. It is the equivalent of a physical point-of-sale terminal. A variety of different credit card payment processors are used for online transactions primarily because each software application often partners with a particular payment processor. For example, the Shoreline Golf Links uses the EZLinks software system to book tee times, manage play at the course, and track payments. EZLinks partners with Electronic Transaction Systems Corporation (ETS) as its payment processor, which will interface smoothly with their system.

Although the City does not have to choose ETS as the payment processor, some of the automated functionality of the system does not work, or work well, without it. Where ETS as the credit card payment processor is fully integrated with EZLinks, staying with the City's current merchant services would require manual keying and less efficient processing. Although it may be beneficial to the City to only have one credit card payment processor, each software system partners with a payment processor to fully integrate with their system. Each payment processor sets up their fee schedule to recover all costs associated with credit card transactions.

The following are the payment processors the City currently uses:

Paymentus—online utility bill payments
Stripe—online parking permit payments
Tickets.com—online CPA ticket purchases
Cybersource—E-Permits (for basic building, electrical, mechanical, and plumbing permits)
Active—online Recreation class/camp payments
PayPal—online Library fee and fine payments

ANALYSIS

There are three different fees for each credit card transaction:

Interchange Fee: In a credit card or debit card transaction, the card-issuing bank deducts the interchange fee from the amount it pays the acquiring bank that handles the credit or debit card transaction for a merchant. This fee is passed on to the merchant.

There are many different interchange fee rates charged for various types of credit cards ranging from 1.43 percent to 2.65 percent for MasterCard and Visa. Commercial credit cards (which include cards that offer rewards such as air miles, cash back, etc.) have higher rates than basic (no rewards) credit cards. A payment processor will set their fees and charges to recover these interchange fees.

Discount Rate: The rate charged to a merchant by a bank for providing debit and credit card services. The rate is determined based on factors such as volume, average transaction amount, risk, and industry. The discount rate charged can be different for each bank. A payment processor will set their fees and charges to recover the discount rate charged by the bank they use.

Bank Fee: A fee that is charged when daily credit card transactions are settled (also known as a batch fee). This fee is very minimal, less than $100 per month. Although there is not a bank fee, per se, when using a payment processor, there are still bank charges for the Automated Clearing House (ACH) deposit transactions. The cost is similar.

Previously, Council has supported not charging additional fees for online payment services by having the City absorbing all the payment processing costs associated with online payments. Our neighboring cities of Palo Alto and Sunnyvale do not currently charge a fee for credit card transactions either online or on-site. However, as online payments are increasing, these fees have increased substantially and staff has identified three types of fees that the City could charge its customers for the use of credit cards for payments (on-site or online):

Convenience Fee: The charge levied for the privilege of paying for a product or service using an alternative payment channel or a payment method that is not standard for the merchant (i.e., online payments). Each payment network's (Visa, MasterCard, etc.) policy on convenience fees varies. For example, Visa restricts the fee to a flat or fixed amount, not a percentage, and requires the fee to be applied to all means of payment that are accepted by the alternative payment method. This

fee would be applicable only to online transactions and are typical on commercial sites when purchasing tickets for events (e.g., theatre, sports, concerts, etc.).

Surcharge: A cost added for the privilege of using a credit card. California law (Civil Code Section 1748.1) prohibits retailers from adding a surcharge when a customer chooses to use a credit card. However, California law excludes public agencies from the definition of a retailer and expressly allows cities to impose a fee for the use of a credit card so long as it does not exceed the City's cost to accept the credit card and is approved by City Council (Government Code 6159). In addition, payment networks' policies on surcharge requirements vary. It is unclear if these would be applicable to both on-site and online credit card processing.

Government Fee Programs: Both Visa and MasterCard appear to have programs available for government entities that authorize a service fee for the use of a credit card. It is unclear if these would be applicable to both on-site and online credit card processing. Each payment network has their own rules, but both require preregistration with the network amongst additional requirements. Although more information about these programs is needed, such programs are an option available for further evaluation.

Staff from the Finance and Administrative Services Department and the City Attorney's Office have researched information available online and believe outside assistance (such as the City's Merchant Services provider) would be needed to determine how a fee(s) can be set. Should a fee or some cost recovery be desired, setting these fees can be complicated. Things to be considered are as follows:

• Each payment network has their own rules about how much can be charged as well as other requirements with which the City needs to comply. Generally, a fee must be the same across all card payment networks.

• The type of card used determines the interchange fee charged (see above about Interchange Fees); however, the amount the City can charge generally cannot be more than the cost to the City for transacting the payment. For a surcharge, the fee can be imposed at the product level, but it is unclear how staff would be able to identify what type of card is presented for payment to determine the fee.

• The City has different payment processors that charge for services differently. It is unclear if the set fee has to be the same across all payment processors, or if it could be set based on each payment processor.

• A convenience fee can only be applied to payments made by alternative payment methods (online, over the phone, etc.), not on-site transactions. However, it must

be imposed on all like transactions regardless of form of payment used for that payment channel.

SUMMARY/CONCLUSION

There is a cost for accepting credit cards for payments whether on-site or online and these costs are substantial and increasing. The City is currently incurring over $400,000 in credit card processing fees. Online payments require a payment gateway which is provided by a payment processor. A convenience fee may be added on to a credit card payment transaction if using an alternative payment method (i.e., online payments), or a surcharge may be added to a credit card payment transaction but must not be more than the City's cost. Finally, government fee programs provide another option but more information is needed to evaluate.

Staff is requesting direction from Council if they would like staff to research and develop options for fees for credit card charges. If so, general policy direction on whether full cost recovery or something less is desired would be helpful. If Council directs staff to research and provide alternative fees to be implemented, due to the complex nature of complying with each payment network's rules and ensuring that the fee is being applied correctly, staff will require outside assistance.

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