



March 10, 2015

The Honorable Joe Jett
Chair
Revenue and Taxation Committee
Arkansas House of Representatives
572 County Road 101
Success, AR 72470

Re: HB 1775 - Interchange on State and Local Taxes or Fees

Dear Representative Jett:

I write on behalf of the American Financial Services Association (AFSA),¹ to register our serious concerns with House Bill 1775, which would prohibit the collection of an interchange fee on the portion of an electronic payment transaction representing state or local taxes or fees. If enacted, this bill would have serious unintended consequences for Arkansas consumers, financial institutions, retailers and the state itself.

Interchange is a value system, fundamental to the workings of electronic payments. It enables a fair balance to be struck between the interests of merchants, consumers, financial institutions and the card networks. It is interchange that allows merchants to derive the enormous value they receive from electronic payments. We are concerned that HB 1775 interferes with this careful balance and is likely to harm the very people it is intended to protect.

Card networks set interchange at a level designed to maximize this merchant value, while partially reimbursing card issuers for the value they create and the risks they take. This level of interchange is proportionate to the value received by merchants who receive electronic payments and recognizes product differences to reflect different market segments.

Merchant value is derived from increased sales, e-commerce, significantly reduced susceptibility to theft, faster payment, and simpler record keeping and tax preparation. Merchants also derive great value from the payment guarantee associated with the major card networks, which means the card issuer takes on the credit risk, not the merchant.

HB 1775 proposes to limit the interchange that is paid by the merchant's bank to the cardholder's bank on the proportion of the total transaction that represents a tax or fee levied by the state or local government. This would be an unwieldy process that fails to take into account the fact that the systems that process these transactions recognize only the total transaction amount, on which the merchant discount fee is based, and do not currently have the ability to subtract sales taxes or other fees from the purchase amount and levy an interchange fee on the remainder.

Compliance with this legislation would require the creation of new systems and operational mechanisms that could differentiate between different elements of the transaction. New payment systems would require a significant overhaul of retailer payments technology, with all of the costs and disruption that this

¹The American Financial Services Association is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA member financial institutions offer vehicle financing, cards, personal installment loans and mortgage loans. The Association encourages and maintains ethical business practices and supports financial education for consumers of all ages.

would entail. The increased costs for retailers associated with implementing new systems would likely result in higher costs at the register. If these mechanisms cannot be reconfigured, consumers would be required to pay a separate cash or check transaction for the sales tax portion of the sale, which would be especially burdensome for consumers when paying for large ticket items.

These additional costs would hit smaller merchants – those that need to keep overhead costs low to survive – the hardest. On top of this, a consumer’s bank would still bear the risk of default for the entire transaction, while being compensated only for bearing that risk for part of it. This additional risk could lead to higher costs for the merchant for each transaction, and diminish any value that lower overall interchange would bring them. Further, HB 1775 may act as a disincentive for smaller merchants to accept electronic payments. Multiple studies have shown that consumers value electronic payments and like to shop where they are accepted. If small retailers begin to shun electronic payments, it will put Arkansas out of step with the rest of the nation, at a time when new and innovative means of making electronic payments are becoming available. Consumers frustrated with having to pay separate transactions may also shift their purchases out of state.

We recommend Arkansas lawmakers study the potential unintended consequences of federal attempts to set government price controls on interchange, notably the Durbin Amendment to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which is widely considered to have resulted in a transfer of between \$1 billion and \$3 billion from poor households to the biggest retailers and their shareholders – while also pushing one million Americans out of the formal banking system, due to higher bank fees.²

States – most recently Colorado – have carefully considered similar proposals, but rejected them in the committee of reference due to the operational hurdles and harm to consumers, small businesses and financial institutions.

We respectfully request that you reject HB 1775. If you have further questions, I can be contacted by phone 952-922-6500 or email dfagre@afsamail.org.

Thank you for your consideration.

Respectfully,



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CC:

Representative Julie Mayberry
Senator Jeremy Hutchinson
Representative David Branscum

² The Economist, *Plastic Stochastic*, available at <http://www.economist.com/news/finance-and-economics/21621882-capping-fees-card-transactions-has-not-worked-out-planned-plastic-stochastic> (Oct. 4, 2014).