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The Merchant Advisory Group (MAG) appreciates the opportunity to comment on Maine House Bill 1544, An Act Regarding Credit and Debit Card Merchant Fees.

Founded in 2008, MAG represents merchants in the payments field dedicated to driving positive change in payments through multi-stakeholder collaboration. The MAG represents 165 U.S. merchants which account for over $4.8 Trillion in annual sales at over 580,000 locations across the U.S. and online. Roughly $3.5 Trillion of those sales and over 100 Billion card payments are electronic which represents approximately 62%[1] of total U.S. card volume. MAG members employ over 14 million associates.

The purpose of this statement is to help alleviate any misconceptions which might exist in implementing a procedure in which sales tax can be removed from any merchant fee calculation. While the MAG is supportive of any reduction in the cost of payments for merchants, we will let our other colleagues take up those points.

Once all of the rhetoric is removed from the conversation, the calculation to remove sales tax from the merchant fee is a simple equation which needs to take place before fees are applied: Net sales amount equals total sales amount minus sales tax. Once this amount is known it can be used to calculate the new merchant fees and follow the current process in how these fees are deducted from the final settlement amount.

Now that we have defined the needed calculation, let's discuss how it can be achieved. The total amount of the sale is already known and used in the process today which means the only additional information needed is the sales tax. In certain transactions today merchants are already required to pass the sales tax information to the networks in the transaction message. The networks created this process for business cards so they could provide this information back to the business that uses these cards. Merchants who do not provide the information are actually penalized by the networks and are required to pay a higher interchange when an amount is not provided.

Besides this example, the industry also works on an ISO standard format known as 8583. All of the current electronic card payments are conducted on this standard which prescribes how data is transferred between the parties. Field 54 within this standard is currently used for the purpose of sending alternative amounts within the transactions. For instance, when a merchant provides the customer cash back as part of the transaction, it must include the specific portion of the transaction which is cash in this field.

[1] *Source of Total U.S. card volumes: Federal Reserve Payments Study 2019*

Another process already in place that would simplify this effort is when an issuer only approves the transaction for less than the requested amount. This may happen when an account only has a limited amount of funds remaining in it. As an example, the merchant requests $100 in order to complete the purchase. On receiving the request, the issuer identifies that only $65 is available for purchase in the customer's account. The issuer sends back the message with the field indicating only $65 was available, and the merchant needs to collect another tender for the remainder of the transaction. As a result, interchange is now only applied to the $65 and **not** the full $100 originally requested.

As you can see by this example, there is currently a process in place by which the amount of the purchase is reduced in order to recalculate a new merchant fee amount. We know through these examples the industry has both a process to collect sales tax information and the ability to run an alternate amount through the merchant fee calculation. To remove sales tax from the interchange calculation as simple as possible, a new indicator could be added to Field 54 specific to sales tax which can then be deducted before the merchant fee calculation.

Clearly, the process of removing sales tax from the total transaction amount for a purchase before applying merchant fees is technically feasible and can be done with minimal programming. In this case, changes can be made to result in lower prices for merchants. Historically, the networks have imposed fees changes which were greater in complexity and resulted in higher fees to merchants. A sample of those fees changes is below.

International Card Transactions Fees

In an international card transaction, not only do networks have to recognize the card type and amount, but they also need to convert the currency to the proper fiat. In addition to calculating one of the hundreds of interchange rates to apply to the transaction, they are also able to collect **three** additional fees: an additional network fee because it is an international card, a fee for the currency conversion, and a fee for the acquirer.

Fixed Acquirer Network Fee

When Federal Regulation II took effect, the networks created an array of complicated fees to retain their debit volume, which required payments system stakeholders to put new procedures into place. They never once raised a concern about the burden the new fees and procedures placed on the industry. In this situation, networks created a fee based on the number of locations which accepted a card brand. A "by location" fee had never been created before, and networks reap the rewards of higher profits at the expense of merchants with this fee in place.

Premium Card Interchange

Several years ago, the networks and the issuers created new levels of interchange based on the status level of a card. Yet again, all parties faced additional burdens to create systems that recognize the card type and pass it through the transaction process. Merchants pay higher fees due to the increased complexities the new levels of interchange created.

To add insult to injury, the issuers complained that the new levels of interchange required them to issue new cards in order to upgrade the amount of interchange charged. As a result, the networks added an indicator within the ISO specification in order to allow the higher interchange amount to be charged without requiring the reissuance of a card. Networks required merchants to implement this new indicator in settlement so the new interchange amount could be applied. The irony of the situation is while the merchants were required to do the work their only reward was paying a higher interchange rate to the issuers.

Conclusion

The removal of interchange from the sales tax portion of transactions **IS** technically possible, can be accomplished easily, and should be implemented without networks charging merchants new fees. This is not a matter of the ability to not charge interchange on sales tax but, instead, the desire of those who benefit from charging the merchants an additional amount to retain profits. MAG supports LD 1544 and the efforts of the Maine legislature to remove interchange from the sales tax on transactions.

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