

# City of Independence

## MEMORANDUM

City Council Office

DATE: July 25, 2018

TO: Honorable Mayor and City Council Members

FROM: Jordan C. Ellena, Management Analyst *JCE*



SUBJECT: Findings RE: Credit Card Fees Paid by the City and Proposed Changes

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### General Background

Paymentus Corporation is the City's chosen payment vendor for processing the City's eCommerce payment transactions. Any payments made through the City's website or the automated call-line (325-SERV) is considered eCommerce and will be processed by Paymentus Corporation once the vendor change is fully implemented. Any other payment made to the City whether in person by check or credit/debit card, by check through the mail, by automatic withdrawal (setup either through your bank or through City Utilities) are not considered eCommerce payments and are **NOT** processed by Paymentus Corporation. **Over the course of the next several months Technology Services will be in the process of switching eCommerce transactions from other departments over to Paymentus. City Utilities were the first department to be switched to Paymentus due to their new billing system.** It is important for customers to realize that they still have many payment options available that are free of user fees.

The decision to select Paymentus Corporation as the City's payment processing vendor was precipitated by the selection of Advanced Utility Systems as the new utility billing system. Advanced Utility Systems allows its clients to select from only two payment processing vendors, Paymentus and Invoice Cloud. In the City's case it made the most financial sense to select Paymentus because their software has a solution built into it to manage automated call-line transactions. Choosing Invoice Cloud would have necessitated the City to either discontinue the 325-SERV function or find another vendor to integrate that service at an additional cost and extended implementation timeline.

A payment processing vendor is selected by merchants in order to ensure personal and credit card information is safe and secure when payments are made through their websites. All merchants accepting credit card payments must ensure that their payments are processed in accordance with the Payment Card Industry Data Security Standard or PCI Compliance standard. **This new user fee covers the cost of the**

**technology needed to ensure the City's eCommerce payments meet PCI compliance standards.** Without a payment processing vendor the City is still subject to PCI compliance and has to employ network and data security staff to monitor PCI standards as well as designing and engineering secure systems in house to handle those transactions. The City currently has one and one-half staff persons working on PCI compliance.

In negotiating an agreement with Paymentus Corporation, the City had the option to continue to subsidize the fees charged by the credit card companies on eCommerce transactions through an "Absorbed Fee Model" or pass those fees on to customers through a "User Fee Model". **The decision was made by staff to pursue a "User Fee Model" with the thinking that the customers who utilize the eCommerce payment methods should pay for the service and not pass those fees on to the rest of the City's customers and taxpayers.**

The "User Fee Model" for eCommerce utility payments adds a \$4.95 fee to the amount being paid for both credit card and eCheck transactions. The maximum single utility eCommerce payment is \$750. A customer who needs to make a larger payment can make multiple payments, however they would be charged the user fee for each payment. There is a separate pricing structure for non-utility billing payments that will be discussed later. All user fees go directly to Paymentus and the City never holds any of those funds. Based on historical credit card payment data provided by the city's current acquiring bank, it was determined that Independence's average eCommerce utility payment amount is \$250 per transaction. **The vendor used that average to determine both the user fee and the maximum single payment amounts.** These amounts are outlined in a signed agreement between Paymentus and the City of Independence.

For non-utility eCommerce payments, the user fee is calculated as a percentage of the amount total payment per the credit card brand rules. The City's average non-utility eCommerce payment amount is \$100. The "User Fee Model" agreement for non-utility eCommerce payments was set at 2.95% of the total payment. For non-utility eCommerce eCheck payments, the user fee is \$0.50 per transaction. An Electronic Check or eCheck is simply a digital version of a paper check. It is not a new technology; the eCheck has been around for nearly twenty years. Simply put the eCheck is processed and secured the same way as a paper check. Because they utilize a tried and true transaction and verification system they generally cost less to process than credit cards.

Customers making a non-utility eCommerce payment (business license, building permits, or court fines) have the option to pay a smaller user fee with an eCheck. If a customer's payment is \$100, the credit/debit card user fee on that transaction would be \$2.95. An eCheck user fee would only amount to \$0.50. The maximum payment amount for non-Utility Billing is \$15,000. Multiple payments are allowed but again a user fee will be charged for each transaction.

**The card brands allow this differential in fees because the transaction volume for non-utility payments is not nearly as significant as for utility payments.** The major credit card brand rules dictate that when using the "User Fee Model" for heavy volume

transactions, preference cannot be given to an electronic payment method such as an eCheck. A utility billing payment is going to be a monthly recurring payment whereas; a business license, building permit, or traffic ticket is less frequent. If non-conformance is discovered, the card brands can and will penalize the merchant. For non-utility billing payments, credit card companies are less concerned due to the lower volume of transactions.

### **About the Decision**

Per Chris Wease, a Paymentus Corporation official, **the City has the right to move forward with either the “User Fee Model” or the “Absorbed Fee Model”.** There are **no consequences for not moving forward with the “User Fee Model”.** **Additionally, the City can choose to change from one model to the other at their choosing.** The main consequence of choosing to forgo the “User Fee Model” is that the adopted budget for Fiscal Year 2017-18 was completed with the saving to the City factored in. A budget hole of approximately \$550,000 would need to be addressed. Even with the implementation delayed until January of 2019, the City will have at account for at least a quarter million dollar shortfall.

### **Credit Card Fees Absorbed by the City**

Since at least 2002 the City of Independence has been accepting credit card payments both online and via an automated call-line (325-SERV). While processing credit cards first offered a convenience for the customer it is now seen a necessity for any business or service provider to offer. This service does not however come without expense to the City. Every credit card available on the market today charges the merchant (in the case the City) both interchange fees and gateway fees. The interchange fees vary between card types and the “extras” (miles, points, etc.) offered to the card holder often account for the differences.

The table below shows the breakdown of credit card fees subsidized by the City of Independence in FY 15/16, FY 16/17 and the first 11 months of FY 17/18. It is no surprise that utility billing makes up the vast portion of the credit card fees subsidized by the city. The numbers below include all credit card fees both those made online and those made in-person at a customer service location. All other fees include but are not limited to things like business licenses, building permits, and transactions at historic and park sites. The City receives a statement each month which outlines the credit card transactions and fees associated with each type of transaction. In reviewing several monthly statements I find that the fees outlined are consistent with the yearly budgeted amounts. For example, in April 2018 the total amount of credit card fees paid by the City was \$49,705.67, of that \$43,247.28 or 87% of that was for eCommerce utility payments. The \$43,247.28 is in line with last year’s average monthly budgeted amount of \$42,646.17 ( $\$511,754/12 = \$42,646.17$ ).

	FY15/16	FY16/17	FY17/18 YTD (5-31-18)
Credit Fees (Utility Bills)	\$612,529	\$511,754	\$511,566
Credit Fees (All Other)	36,678	\$38,748	\$38,862
Total	\$649,207	\$550,502	\$550,428

These fees are budgeted for each and every year. The utilities' portion of the fees is accounted for as part of the utility customer service budget. The bulk of the other credit card fees (\$28,575 for FY17/18) are budgeted from the general fund to support the departments there. Those would include Community Development, Health, and Finance. The remainder would come from other governmental fund for transactions made with those departments. Because these fees are budgeted for every year the city's annual independent financial auditor reviews our handling of them for compliance with Generally Accepted Accounting Principle or GAAP. In reviewing the audit findings of the annual independent financial audit, I do not find any concerns noted or changes recommended to management related to these credit card fees or the handling of them. **My own review of these credit card fees find management's handling of them consistent with GAAP and financial management best practices. The credit card fees charged by the card companies per transaction are billed to the city as the merchant.** The city has budgeted appropriate sums of money to cover these credit card fees which include interchange and gateway fees.

**Comparison of User fees Charged by Peer Municipalities**

It is often beneficial to look at peer communities and how they handle the same issue. In this case I have collected information regarding user fees charged by several peer communities for online transactions. The table below illustrates my findings. While the proposed \$4.95 user fee is higher than peer communities identified, it is not unreasonably higher. The \$4.95 user fee proposed for Independence was calculated based on the average credit card payment made online or via 325-SERV of \$250 per utility payment. This average is attributable to two factors, 1) an Independence utility bill includes charges for three utilities (electric, water, and sewer) while other communities have fewer and 2) Independence utility customers pay a higher average bill overall than others customers. The latter could be attributed to a number of factors not explored in this audit.

	<b>User fee Passed on to Customer per Online Transaction</b>
<b>Independence</b>	\$4.95
<b>Blue Springs</b>	No Fee
<b>Columbia</b>	\$3.55 Residential
	\$4.25 Commercial
<b>Lee's Summit</b>	No Fee
<b>Raytown</b>	\$4.25
<b>Springfield</b>	\$4.00

We can also look more specifically at the City of Columbia as they have a similar population to Independence, more utilities on a regular bill, and in fact have the same utility billing system and vendor for online payment processing as Independence.

Based on information provided by the City of Columbia, they charge different convenience fees to residential than commercial customers for web and IVR payments. For residential they charge \$3.55 per credit card and eCheck transactions with a \$750 maximum payment. For commercial the convenience fee is \$4.60 for both credit card and eCheck with a \$1,000 maximum payment. They use Advanced Utility Systems as their utility billing system and Paymentus as the online payment processor just like we do. Their utility service includes electric, storm water, sewer, water, and trash. Their average credit card payment is \$210. This is the key difference in convenience fee. Their average credit card payment is \$40 less than ours and those numbers are the basis for Paymentus's calculation of the user fee to pass along to the customer.

For non-utility services Columbia is able to charge 2% which is similar but lower than the 2.95% of the amount Paymentus is charging Independence customers. Columbia does not offer an eCheck option for non-utility service online payments which allowed Paymentus to agree to a lower 2% fee per transaction.

### **Business Licenses as Further Example**

As further illustration of this I also compared data from peer communities dealing with business licensing. This allows for additional comparison regarding the impacts on non-utility billing customers. The table below shows that comparison. In this case the maximum allowable online payment in Independence is \$15,000 per transaction, while at the same time the maximum business license fee is \$30,000. This could force an online payer to split their payment and be subject to two user fees. While that is a possibility, records from calendar year 2017 showed only a single online transaction the whole year greater than \$15,000. Presumably with this change that payer would choose an eCheck in the future, pay in person, or by physical check.

	<b>Business License Fees</b>	<b>User fees for Non-Utility Online Transactions</b>	<b>Business License Fee *</b>	<b>User fee on Business License</b>
<b>Independence</b>	\$75 for first \$25,000 of gross receipts + \$0.29 for each \$1,000 over \$25,000 (\$30,000 max)	2.95% card \$0.50 eCheck (max payment \$15,000)	\$111.25	\$3.28 card or \$0.50 eCheck
<b>Blue Springs</b>	\$50 + \$2 per employee (no max fee)	N/A	\$70	\$0
<b>Columbia</b>	\$47 app and background fee +	2% card only	\$84.50	\$1.69
	gross receipts < \$25,000 = \$15			
	\$25,000 – \$100,000 = \$25			
> \$100,000 = \$0.25 per \$1,000				
<b>Lee's Summit</b>	\$50 flat fee	N/A	\$50	\$0

\* Assuming \$150,000 in gross receipts and 10 employees