

State of Ohio

Governor's Council on Electronic Commerce
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e-Payments Automation Project

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1. Background

The State of Ohio has been one of the national leaders in the receiving of electronic payments. In 1992 the Department of Taxation in partnership with the State Treasury created an electronic tax collection environment that served two purposes. The primary purpose of the Electronic Funds Transfer (EFT) system was to streamline the tax payment process. Taxes would flow into the state electronically, which would reduce the float associated with paper based payment environments such as check remittance processing. Secondly, the EFT process enabled the submission of tax remittance information in the same EFT transaction as the payment, which had a dramatic effect on the processing of remittances and the updating of taxation systems. The EFT program is administered by the State Treasury and includes the following tax types:

- Employee withholding tax.
- Corporation franchise tax.
- Sales tax.
- Motor vehicle tax.
- Public utilities tax.

In fiscal year 2001 the EFT program was responsible for the collection of over \$10 billion dollars in state revenue. The primary transactions of the EFT program are Automated Clearing House (ACH) credits and debits.

The first credit card acceptance in the state began with the Department of Natural Resources (DNR) and the Bureau of Motor Vehicles (BMV). The DNR use of credit cards was limited to state parks and lodges. Customers staying in a lodge or campground could use their Visa or MasterCard to pay for their expenses. The BMV use was for motor vehicle registration, and was limited to mail-in renewals. Customers could use their Visa or MasterCard to renew their vehicle license tags through mail remittance processing. BMV included an additional fee for the transaction that was used to cover the cost of the discount fee associated with credit card transactions. The inclusion of a fee associated with credit card transactions became a watershed event for the state because it resulted in Visa issuing a cease and desist order to Huntington Bank, the BMV processing bank, for allowing the fee to be passed to Visa cardholders. Visa and MasterCard have internal rules that state that their customer cannot be assessed a surcharge for the use of their product. The result of the order was that BMV had to discontinue their credit card program, and the state encountered its first obstacle in the electronic payments environment.

In 1998, after a period of managing a couple of separate credit card relationships with separate banks the State Treasury embarked on a project that would consolidate the states credit card processing into a single relationship. The advantages that the Treasury hoped to realize from a single card processing relationship were a reduction in administrative time associated with managing multiple card processing relationships, economies of scale when negotiating card discount rates, and reduction in duplicate processes within state agencies. The Treasury proposed legislation that

centralized the card processing relationship within the state, and authorized the charging of convenience fees to customers for credit card transactions. The legislation was passed in 1999 and is now section 113.40 of the Ohio Revised Code ([Attachment A](#)).

Once the legislation was in place for centralized credit card processing the Treasury issued a Request For Proposal (RFP) to secure the services. The central processor award was made to Fifth Third Bank. The Treasury worked with the State Accountancy Board and in December of 1999 the first Internet based credit card transactions were received. Some of the other applications that have gone live that accept credit cards are:

- Accountancy Board – License Renewal.
- Bureau of Workers’ Compensation – Dolphin.
- Department of Public Safety – OPLATES.
- Department of Commerce - BUSTR
- Department of Natural Resources – Watercraft.
- Department of Taxation – Various applications.

The integration of ACH payments into some of these applications is the next logical step to be taken. ACH, also known as electronic check, is a cost effective way of transferring funds from a customer. While the ACH transaction is cost effective, the greatest efficiencies to be gained can only be achieved by increasing the number of transactions that are using the ACH method of payment.

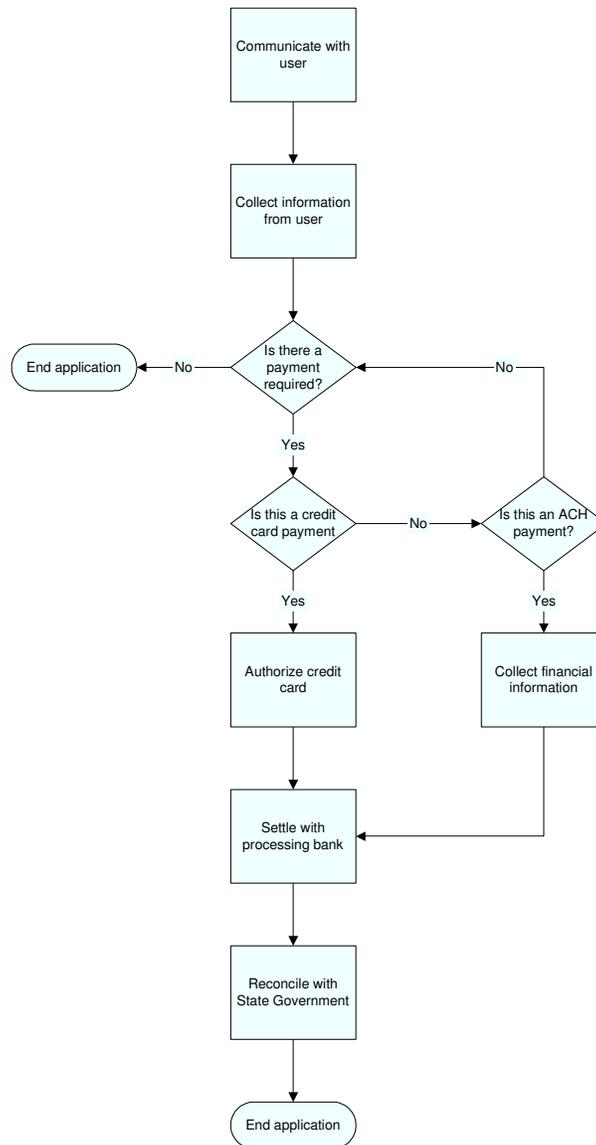
2. Scope

Facilitate credit card and Automated Clearing House (ACH) transactions received by the State of Ohio.

3. Mission

Develop a payment application that will facilitate both credit card and ACH debit transactions initiated via the Internet or IVR system, and can be utilized by a variety of state agencies, boards, or commissions.

4. Payment Process Flow



4.1. Communicate with user

Each state agency is responsible for the communications with their customers. The initial focus of agency web sites was to provide information to customers that would be available in a 24/7 environment. As the content of web sites became more mature, agencies began to further develop the sites to become more transaction based. The goal of this project is not to replace, or to play a roll in the communications between an agency and its customers. Rather it is the goal of this project to make the payment processing associated with web based or IVR

transactions more efficient, therefore allowing the agency to concentrate on their core applications and their communications channels with their customers.

An application level help desk is another area of communication with the customers that will be addressed by the agency that is hosting the application. All help requests of the centralized e-payments engine should be initiated by the hosting agency on behalf of their customer.

4.2. Collect information from user

As the user enters the web application they will be queried for information that is needed to complete the transaction. Examples of needed data may include:

- Name.
- Address.
- Customer identification number.

After the required agency specific data is collected there must be a determination of whether payment needs to be made. Most applications currently only have the option to accept credit card payments, however there is a movement toward offering the ACH debit option to the customers.

4.3. Identify payment type

Once the payment type is determined the customer is migrated toward the appropriate payment processing section to complete the transaction. This functionality is where the e-payments engine would come into play. The customer would be connected to the central e-payments engine via a common application programming interface (API) and the e-payment engine would complete the transaction.

4.3.1. Credit Card Payments

In order to complete a credit card transaction the customer must provide:

- Name
- Amount of transaction
- Card number
- Card expiration date

While it is not required to complete the transaction the following information can also be gathered to further verify the identity of the customer:

- Street address
- City, State and Zip code
- CVV2



Agencies that gather additional information to verify the identity of their customers and therefore reduce the potential for fraud will be granted a more favorable rate by card issuing companies.

Once customer information is gathered, the application will connect to a card authorization network to verify the named user, the card account, the expiration date, and that the user account has a sufficient balance to complete the transaction. The card authorization network will respond with either an authorization of the transaction or a non-authorization of the transaction. For non-authorizations the network also provides a code that identifies the reason for the rejection. All authorized transactions are held in a batch within the application that will be submitted for processing at the end of the business day.

4.3.2. ACH Payments

Similarly to credit card transactions, ACH payments require the customer to provide some basic financial information which includes:

- Name
- Amount of transaction
- American Bankers Association (ABA) routing and transit number
- Bank account number

Unlike credit card transactions there is no pre-authorization process with an outside entity for ACH transactions. The application will need to have an edit that will compare the ABA routing and transit number submitted against a nationwide database of routing and transit numbers for validation. After the financial information is collected it will be batched and submitted to a processing bank at the end of the business day.

4.4. Process payment with bank

The processing of payments at the bank occurs after the application completes the end of day batch processing, and the batches are submitted to the bank. There is a minimum of two batches that are processed by the application on a daily basis. One batch for the credit card transactions and one batch for ACH transactions.

The credit card batch is first sent to the credit card authorization network where it will be processed and then submitted to the merchant bank. Credit card batches traditionally settle at the merchant bank within 48 hours of submission.

ACH batches are built using the financial data gathered at the time the transaction was completed. The financial information is put into a National Automated Clearing House Association (NACHA) standard format prior to submission to the bank. The standard transaction set for Internet transactions will be either the Internet initiated transaction (WEB) or the consolidated collection or disbursement (CCD) transaction sets. Once the transactions are put into the proper batch format the batch is

submitted to the bank for processing. The traditional processing time for an ACH batch is one business day.

After the batches have been submitted to the bank for processing the state treasury monitors the bank accounts to verify the settlement of the transactions. The treasury has worked with the Office of Budget and Management to develop a system of recording the revenue for state accounts as they see it being credited to the states bank account. This process is semi-automated and does not require an agency to produce any paper documents to complete the recording of revenue.

4.5. Reconcile with state

The final step in the process is the reconciliation of the transactions. Following the recording of the revenue, state agencies will reconcile the recorded transactions against the transactions that were captured by the initiating application. The e-payments engine will have the ability to produce reporting both online and paper based that will assist with this endeavor.

5. Benefits

The benefits that could be achieved by implementing a central e-payments engine are both tangible and intangible in nature. The following items describe some of the potential benefits that a central e-payments environment presents.

5.1. Reduction in redundant data

The current state electronic payments environment allows for redundant data to exist because there are several individual applications that perform the same or similar function. Unfortunately, the redundant data that is captured is financial data of those doing business with the state of Ohio. Therefore not only is there redundant data but the data is of a sensitive nature. The e-payments engine consolidates the financial data into a single controlled and secure environment.

5.2. Reduction in redundant applications

As we progress toward a central e-payments environment there is no need to maintain individual agency applications that process electronic payments. The agency can concentrate on developing the functional aspects of their application that are unique to the agency. As a result of the agency not needing to develop a payments function in their application the agency can realize benefits such as:

- Decreased application development time
- Decreased application development costs
- Ability to utilize standard application programming interfaces

In general, the centralized e-payments engine will allow agencies to leverage a processing environment that ultimately will allow the agency the freedom to concentrate on their core programs and reduce development time and development costs at the same time.

5.3. Reduced maintenance costs

The maintenance of a transaction based system that includes payments can be quite burdensome. The main reason for this is the sensitive nature of the financial data that is resident in the system. The inclusion of financial data in a system requires robust security and clearly defined business continuity and disaster recovery plans. The e-payments engine reduces the cost of maintaining these systems because the sensitive parts of the system are no longer the responsibility of the individual agency. Also, the duplication of staff that have knowledge in the financial system is reduced.

5.4. Cash Management

One of the primary success factors for any business is the ability to manage the flow of cash in and out of the organization. Electronic payments accelerate the payment flow to the state and reduce the float associated with traditional payment channels such as the mail. Also, the central e-payments environment can assist in cash management because payments made to the state through the system are initiated prior to the state receiving the money. Therefore the state has a better idea of when funds will be received and the amount of funds to be received in contrast to waiting on the mail and not knowing when funds will be received.

6. Obstacles

As with most everything there are a few obstacles that will be encountered when developing the e-payments infrastructure. The most difficult obstacles relate to the cost of doing business in the electronic world. For many state agencies, entrance into the e-payments world will actually increase their costs because the new environment is not replacing an old process; rather it is an additional access channel for their users. As a result of the increased cost of maintaining an additional avenue of access for a user the agency must either absorb the additional cost as the cost of doing business, or choose to charge a convenience fee for access to the system. The following section will address convenience fees to customers and the discount fees that are associated with credit card transactions.

6.1. Convenience fees charged to customers

The rules governing the use of convenience fees for credit card transactions are set by the card issuing company and are written to ensure that credit card holders are not discriminated against due to the use of the card. The Visa position on convenience fees is as follows:

A “convenience fee” is a charge imposed upon the Visa cardholder at the point of sale for providing a bonafide *convenience* to the customer in connection with the payment transaction, not for the privilege of using the Visa payment card. For example, a convenience fee can be levied (under Visa rules and subject to full compliance with the Convenience Fee Criteria described in the Attachment B) for the use of an access device, such as a Voice Response Unit (VRU), that provides customers with the option to pay the amount-due through the device rather than going to the merchant

location to pay in person. In other words, the convenience must be related to a payment channel that is outside the merchant's customary acceptance methods.

As long as the card issuing company rules have been met regarding convenience fees, then a fee may be assessed.

In the Internet environment a convenience fee must be assessed to all payment methods available on a web site or IVR system. If a site has the ability to accept credit card and ACH debit payments, the convenience fee must be applied to both payment methods. This is a point of contention because the cost of an ACH transaction can be substantially less than a credit card transaction, and the agency could potentially absorb the cost of the ACH transaction.

6.2. Credit card discount fees

The fee associated with acceptance of credit cards is known as the discount fee. The discount fee has many parts but is referred to as an aggregate fee that represents the cost of doing business using credit cards. A common rate for the discount fee is 2%. An example of how the discount fee is calculated is:

Purchase amount x Discount rate = Discount fee

$\$100 \times 2\% (.02) = \2.00

The result of a discount fee is that the agency does not receive the full amount of the purchase which in some instances is a violation of revised code. To remedy this problem arrangements have been made with the merchant bank to forward the full proceeds of all transactions to the agency and then the merchant bank will invoice the fees to the agency on a monthly basis.

6.3. Multiple Banking Relationships / Custodial Accounts

Most of the state of Ohio agency financial transactions are processed as revenue through the state's central accounting system (CAS). Transactions that are posted through CAS are deposited in the state's primary bank. There are some agencies that do not process through CAS due to the nature of their account. Those agencies that do not process through CAS are said to have custodial accounts with the state Treasury. The Treasury maintains many custodial accounts for various state agencies, all of which could leverage the capabilities of the centralized e-payments environment. In order for a custodial agency to utilize the e-payments environment, the application must have the ability to segregate payments at the custodial level, and communicate with the appropriate bank. The application would also need to reconcile those transactions back to the initiating application and the Treasury's general ledger.

7. Next Steps

7.1. Develop software requirements specifications

In order to best evaluate the most appropriate solution for a central e-payments infrastructure we must first understand and document what is required of the system. The software requirements specifications (SRS) document is the tool that will be used to illustrate what is required of the system.

7.2. Develop RFP for software selection

Using the SRS document as a base we will develop an RFP for software selection or use the SRS document to evaluate vendor solutions as they apply to the requirements as they have been outlined in the document.

8. Glossary and Acronyms

ABA Number – Also known as Routing Number, Transit/Routing number. A nine-digit number which identifies a specific financial institution. Routing numbers are administered by the Routing Number Administrative Board under the sponsorship of the American Bankers Association and officially maintained and published by Thomson Financial Publishing.

ACH Network – Funds transfer system governed by the Rules of the National Automated Clearing House Association, which provides for the inter-bank clearing of electronic entries for participating financial institutions.

Acquiring Bank/Merchant Bank – The bank that does business with merchants enabling them to 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.

Acquiring Processor - The processor provides credit card processing, billing, reporting, settlement, and operational services to acquiring banks.

Authentication – A data security technique used to ensure that the professed sender of information of a payment order is actually who he claims to be.

Authorization (Credit Card) – The act of insuring that the cardholder has adequate funds available against their line of credit. A positive authorization results in an authorization code being generated, and those funds being set aside. The cardholders available credit limit is reduced by the authorized amount.

Authorization (ACH) – An agreement by a receiver to allow for posting of debit or credit items to their account. Authorizations for debit transactions must be authorized in writing or similarly authenticated by other means (for example digital signatures or PIN)

Batch – The accumulation of captured (sale) transactions waiting to be settled. Multiple batches may be settled throughout the day.

CVV2 - This number is printed on your MasterCard & Visa cards in the signature area of the back of the card. (it is the last 3 digits AFTER the credit card number in the signature area of the card). American Express cards show the cvv2 printed above and to the right of the imprinted card number on the front of the card.

Discount Rate – The fee a merchant pays its acquiring bank/merchant for the privilege to deposit the value of each day's credit purchase. The fee is a small percentage of the purchase price.

Electronic Check – A generic term for an ACH debit to a consumer account that is originated on the Internet or IVR.

Interchange – The exchange of information, transaction data and money among banks. Interchange systems are managed by Visa and MasterCard association and are very standardized so banks and merchants worldwide can use them.

Interchange Fee – A fee paid by the acquiring bank/merchant bank to the issuing bank. The fee compensates the issuer for the time after settlement with the acquiring bank/merchant bank and before it recoups the settlement value for the cardholder.

NACHA – The national trade association for electronic payments associations, which establishes the rule, industry standards and procedures governing the exchange of commercial ACH payments by depository financial institutions.

9. Acknowledgements

The e-Payments Automation Project Team

David White	Office of Budget and Management
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MC Adams	State Treasury
Rick Shipley	Department of Administrative Services
Michelle Pickering	Department of Administrative Services
Patrick McAndrew	Department of Taxation
Gilbert Ashbridge	Department of Taxation
Yvette Brice	State Treasury
Richard Byers	Department of Public Safety
Walter Callahan	Department of Public Safety
Barbara Hamilton	Department of Public Safety
Tom Hart	Department of Commerce
Cheryl Lyman	Department of Commerce
John Hopper	Judicial Services Commission
Jerry Howard	Department of Insurance
Chrissy Irvin-Brown	Department of Insurance
Leora Knight	Department of Public Safety
Kathy Ludowese	Department of Public Safety
Katie Merrill	Judicial Services Commission
Jeanine Moore	Department of Public Safety
Rhonda Perri	Judicial Services Commission
Carl Phillips	Bureau of Workers' Compensation
Jeff Pierce	Department of Insurance
Daniel Stuetzer	State Auditor
Patricia Utt	Department of Public Safety
Carol Wander	Bureau of Workers' Compensation

10.Attachment A: Ohio Revised Code Section 113.40

§ 113.40 Payment of state expenses by financial transaction device.

Text of Statute

(A) As used in this section:

- (1) "Financial transaction device" includes a credit card, debit card, charge card, or prepaid or stored value card.
- (2) "State expenses" includes fees, costs, taxes, assessments, fines, penalties, payments, or any other expense a person owes to a state office under the authority of a state elected official or to a state entity.
- (3) "State elected official" means the governor, lieutenant governor, attorney general, secretary of state, treasurer of state, and auditor of state.
- (4) "State entity" includes any state department, agency, board, or commission that deposits funds into the state treasury.

(B) Notwithstanding any other section of the Revised Code and subject to division (D) of this section, the board of deposit may adopt a resolution authorizing the acceptance of payments by financial transaction device to pay for state expenses. The resolution shall include all of the following:

- (1) A designation of those state elected officials and state entities authorized to accept payments by financial transaction device;
- (2) A list of state expenses that may be paid by the use of a financial transaction device;
- (3) Specific identification of financial transaction devices that a state elected official or state entity may authorize as acceptable means of payment for state expenses. Division (B)(3) of this section does not require that the same financial transaction devices be accepted for the payment of different types of state expenses.
- (4) The amount, if any, authorized as a surcharge or convenience fee under division (E) of this section for persons using a financial transaction device. Division (B)(4) of this section does not require that the same surcharges or convenience fees be applied to the payment of different types of state expenses.

(5) A specific requirement, as provided in division (G) of this section, for the payment of a penalty if a payment made by means of a financial transaction device is returned or dishonored for any reason.

The board of deposit's resolution also shall designate the treasurer of state as the administrative agent to solicit proposals, within guidelines established by the board of deposit in the resolution and in compliance with the procedures provided in division (C) of this section, from financial institutions, issuers of financial transaction devices, and processors of financial transaction devices; to make recommendations about those proposals to the state elected officials; and to assist state offices in implementing the state's financial transaction device program.

(C) The administrative agent shall follow the procedures provided in this division whenever it plans to contract with financial institutions, issuers of financial transaction devices, or processors of financial transaction devices for the purposes of this section. The administrative agent shall request proposals from at least three financial institutions, issuers of financial transaction devices, or processors of financial transaction devices, as appropriate in accordance with the resolution adopted under division (B) of this section. Prior to sending any financial institution, issuer, or processor a copy of any such request, the administrative agent shall advertise its intent to request proposals in a newspaper of general circulation in the state once a week for two consecutive weeks. The notice shall state that the administrative agent intends to request proposals; specify the purpose of the request; indicate the date, which shall be at least ten days after the second publication, on which the request for proposals will be mailed to financial institutions, issuers, or processors; and require that any financial institution, issuer, or processor, whichever is appropriate, interested in receiving the request for proposals submit written notice of this interest to the administrative agent not later than noon of the day on which the request for proposals will be mailed.

Upon receiving the proposals, the administrative agent shall review them and make a recommendation to the board of deposit regarding which proposals to accept. The board of deposit shall consider the agent's recommendation and review all proposals submitted, and then may choose to contract with any or all of the entities submitting proposals, as appropriate. The board of deposit shall provide any financial institution, issuer, or processor that submitted a proposal, but with which the board does not enter into a contract, notice that its proposal is rejected.

(D) The board of deposit shall send a copy of the resolution adopted under division (B) of this section to each state elected official and state entity authorized to accept payments for state expenses by financial transaction device. After receiving the resolution and before accepting such payments by financial transaction device, such a state elected official or state entity shall provide written notification to the administrative agent of the official's or entity's intent to implement the resolution within the official's or entity's office. Each state office or entity subject to the board's resolution adopted under division (B) of this section shall use only the financial institutions, issuers of financial transaction devices, and processors of financial transaction devices with which the board of deposit contracts, and each such office or entity is subject to the terms of those contracts.

If a state entity under the authority of a state elected official is directly responsible for collecting one or more state expenses and the state elected official determines not to accept payments by financial transaction device for one or more of those expenses, the office is not required to accept payments by financial transaction device for those expenses, notwithstanding the adoption of a resolution by the board of deposit under division (B) of this section.

Any state entity that prior to the effective date of this section accepted financial transaction devices may continue to accept such devices until June 30, 2000, without being subject to any resolution adopted by the board of deposit under division (B) of this section, or any other oversight by the board of the entity's financial transaction device program. Any such

entity may use surcharges or convenience fees in any manner the state elected official or other official in charge of the entity determines to be appropriate, and, if the administrative agent consents, may appoint the administrative agent to be the entity's administrative agent for purposes of accepting financial transaction devices. In order to be exempt from the resolution of the board of deposit under division (B) of this section, a state entity shall notify the board in writing within thirty days after the effective date of this section that it accepted financial transaction devices prior to the effective date of this section. Each such notification shall explain how processing costs associated with financial transaction devices are being paid and shall indicate whether surcharge or convenience fees are being passed on to consumers.

(E) The board of deposit may establish a surcharge or convenience fee that may be imposed upon a person making payment by a financial transaction device. The surcharge or convenience fee shall not be imposed unless authorized or otherwise permitted by the rules prescribed under a contract, between the financial institution, issuer, or processor and the administrative agent, governing the use and acceptance of the financial transaction device.

If a surcharge or convenience fee is imposed, every state entity accepting payment by a financial transaction device, regardless of whether that entity is subject to a resolution adopted by the board of deposit, shall clearly post a notice in the entity's office, and shall notify each person making a payment by such a device, about the surcharge or fee. Notice to each person making a payment shall be provided regardless of the medium used to make the payment and in a manner appropriate to that medium. Each notice shall include all of the following:

- (1) A statement that there is a surcharge or convenience fee for using a financial transaction device;
 - (2) The total amount of the charge or fee expressed in dollars and cents for each transaction, or the rate of the charge or fee expressed as a percentage of the total amount of the transaction, whichever is applicable;
 - (3) A clear statement that the surcharge or convenience fee is nonrefundable.
- (F) If a person elects to make a payment by a financial transaction device and a surcharge or convenience fee is imposed, the payment of the surcharge or convenience fee is not refundable.

(G) If a person makes payment by a financial transaction device and the payment is returned or dishonored for any reason, the person is liable to the state for the state expense and any reimbursable costs for collection, including banking charges, legal fees, or other expenses incurred by the state in collecting the returned or dishonored payment. The remedies and procedures provided in this section are in addition to any other available civil or criminal remedies provided by law.

(H) No person making any payment by a financial transaction device to a state office shall be relieved from liability for the underlying obligation, except to the extent that the state realizes final payment of the underlying obligation in cash or its equivalent. If final payment is not made by the financial transaction device issuer or other guarantor of payment in the

transaction, the underlying obligation survives and the state shall retain all remedies for enforcement that would have applied if the transaction had not occurred.

(I) A state entity or employee who accepts a financial transaction device payment in accordance with this section and any applicable state or local policies or rules is immune from personal liability for the final collection of such payments as specified in section 9.87 of the Revised Code.

(J) The administrative agent, in cooperation with the office of budget and management, may adopt, amend, and rescind rules in accordance with section 111.15 of the Revised Code to implement this section.

11.Attachment B: Visa Convenience Fee Guidelines

VISA U.S.A. Inc.
CONVENIENCE FEE GUIDELINES
JANUARY 2002

For a convenience fee to comply with Visa Operating Regulations, the following criteria must be met.

1. A merchant must provide a bona fide convenience in the form of an alternative payment channel outside the merchant's customary payment channels, and the fee must be disclosed by the merchant to the Visa cardholder as a charge for the alternative payment channel convenience that is provided. (A fee cannot be charged for the "convenience" of accepting Visa Cards.)
2. The alternative payment channel must be in a non-face-to-face environment. (Naturally, if the merchant has no physical (face-to-face) locations, its customary acceptance methods are all non-face-to-face, which means that existing mail/phone/Internet only merchants would likely not be able to provide an additional "convenience" and, therefore, may not levy a convenience fee.)
3. The convenience fee must be a flat or fixed amount regardless of the amount due to the merchant for the goods or services purchased. (A fee based on a percentage of the amount or the utilization of a tiered scale is not allowed).
4. The same convenience fee must apply to all forms of payment accepted in the alternative payment channel. (This means cash, check, ACH debit, vouchers, and all other payment cards.)
5. The fee must be disclosed to the customer prior to completion of the transaction, and the customer must be given the opportunity to cancel the transaction if the customer does not want to pay the convenience fee.

The transaction entered into interchange must reflect the amount that includes the convenience fee. The convenience fee may not be submitted as a separate transaction.