WRITTEN STATEMENT OF

DAVE CARPENTER
PRESIDENT, J.D. CARPENTER COMPANIES, INC./SHORTSTOP CONVENIENCE STORES
MEMBER OF THE BOARD OF DIRECTORS, LIBERTY BANSHARES

ON BEHALF OF
THE NATIONAL ASSOCIATION OF CONVENIENCE STORES

BEFORE THE UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON THE JUDICIARY

HEARING ON THE "CREDIT CARD FAIR FEE ACT OF 2009, H.R. 2695

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Chairman Conyers, Ranking Member Smith and Members of the Committee, thank you for inviting me to share my views regarding payment card "swipe" fees. My observations are based on my experience both as the owner of a chain of convenience stores and part owner of a large community bank. From either of my vantage points, these fees have long been out of control, and they are nearly suffocating my retail stores while yielding no profit at all for my community bank. Therefore, I fully support the Credit Card Fair Fee Act of 2009 and other efforts to help rein in swipe fees.

Overview

I am owner and President of ShortStop, a chain of six convenience stores. The stores are located in Des Moines and other locations in eastern Iowa. This is a family business, and I started working in the business as a young teen, continuing through college, until my father died in 1996 and I took over running the business. Fuel sales make up a large part of our sales, but we also sell a wide array of beverages, prepared and packaged food, and other convenience items.

I am testifying today on behalf of the National Association of Convenience Stores ("NACS"), of which I am a member. NACS is an international trade association representing the convenience store industry. The industry as a whole includes about 145,000 stores in the United States, sells nearly 80 percent of the gasoline in the nation, and employs about 1.7 million workers. It is truly an industry for small businesses, and more than 60 percent of convenience stores are owned by one-store operators. Because of the tremendous, detrimental impact that swipe fees are having on convenience stores, NACS has long advocated for a more competitive and transparent system of payment card interchange fees, and I support these efforts.

Indeed, I want to make sure Committee Members are aware that yesterday, NACS delivered a petition with more than 2 million signatures from our customers asking Congress to create transparency and competition for swipe fees. This is on top of the 1.7 million signatures 7-Eleven delivered last year, bringing the total to 3.7 million Americans who have taken time from their busy day to sign a petition asking Congress to act. We and our customers hope Congress is listening.

In 2002, I became an owner and board member of Liberty Bank Iowa. Liberty Bank Iowa has more than $1 billion in assets and 30 locations throughout central and eastern Iowa. I am now a member of the board of directors of Liberty Banshares, the holding company for Liberty Bank Iowa. Unlike many community banks, Liberty Bank Iowa issues its own Visa credit and debit cards, rather than outsourcing our card operations.

Because of my roles as a retailer as well as co-owner of a community bank, I am in the unique position of understanding the effect that runaway card fees have on convenience stores, as well as the negligible impact of payment card operations on community banks' profitability.

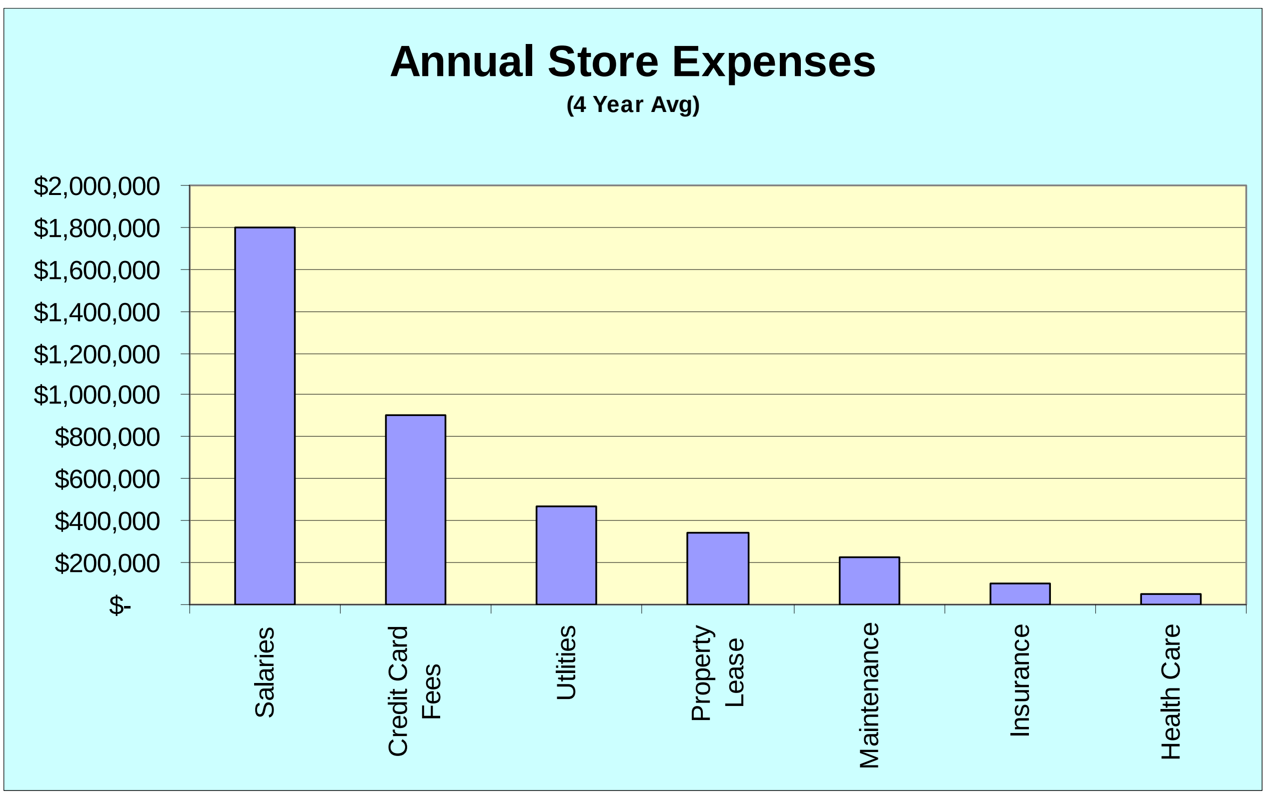
The first part of my statement will discuss the effect that swipe fees are having on my retail business. Thereafter, I will describe Liberty Bank Iowa's payment card business.

The Impact of Runaway Credit Card Fees on My Convenience Store Business

I know that this is not the first hearing this Committee has held on card fees, so you no doubt are aware that for the last four years, our industry as a whole has paid more to credit card companies to simply process our card payment transactions than we earned in pre-tax profits. My aim today is to describe what all of this means at the store-owner level.

The following data demonstrate how dramatically runaway interchange fees have affected my business. First, as shown in Figure 1, when various major expenses are compared for our six stores, it can clearly be seen that card fees are our second largest expense.

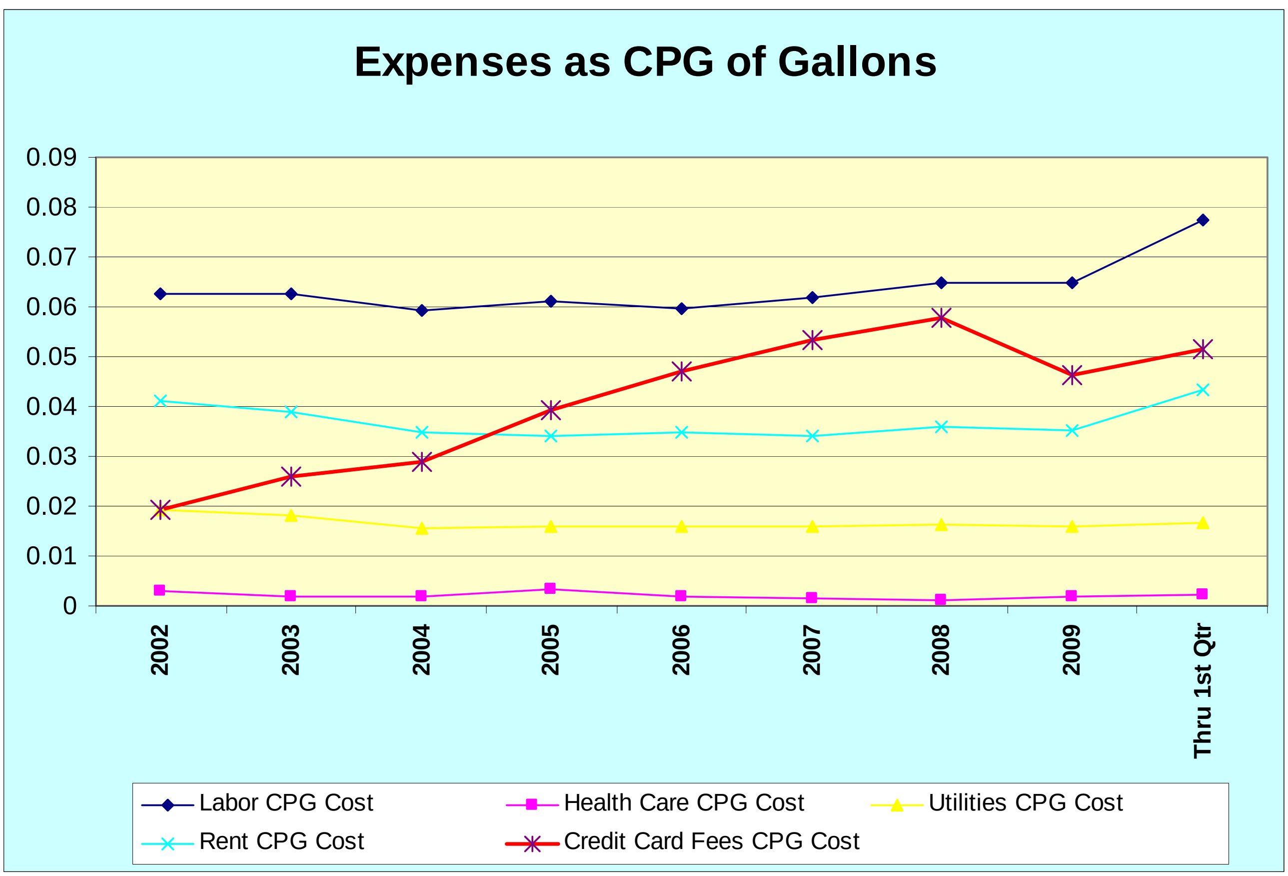
Figure 1



Only labor costs us more. ShortStop pays higher than average wages for the convenience store industry, so interchange fees likely represent an even larger chunk of expenses for the typical convenience store. I note, however, that Figure 1 reflects average figures for the entire chain. For some of my stores, card fees exceed even labor costs. For one of my stores, the amount we pay in card fees is twice what we pay for rent, four times more than utilities, and thirty times more than health insurance. I'm even paying card processing fees on the amount of each sale that we collect as taxes. Last year we paid more than $130,000 in swipe fees just on state and federal gasoline tax. We also pay swipe fees on any local or state sales tax. That is money that I don't even get, but I am paying interchange on it.

Figure 2 calculates certain store expenses by the number of gallons to determine a cost-per-gallon basis for two representative stores.

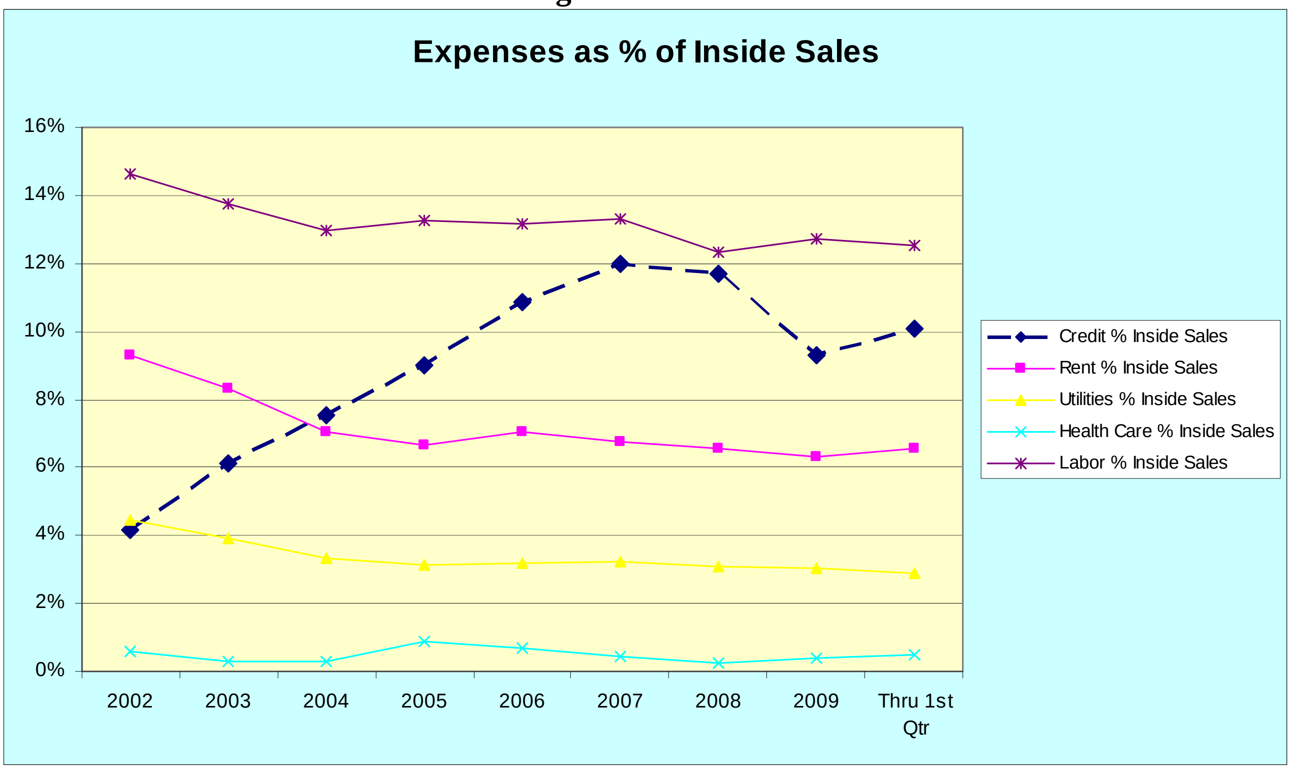
Figure 2



This analysis confirms that over the last five years, card fees have been the second largest expense we incur on each gallon of fuel we sell. It also shows the runaway pace of increases in our card fee expense, particularly when compared to our other major expenses. [1]

To eliminate any influence that fluctuations in fuel sales price might have on our calculations, in Figure 3 we performed the same analysis using convenience store sales.

Figure 3

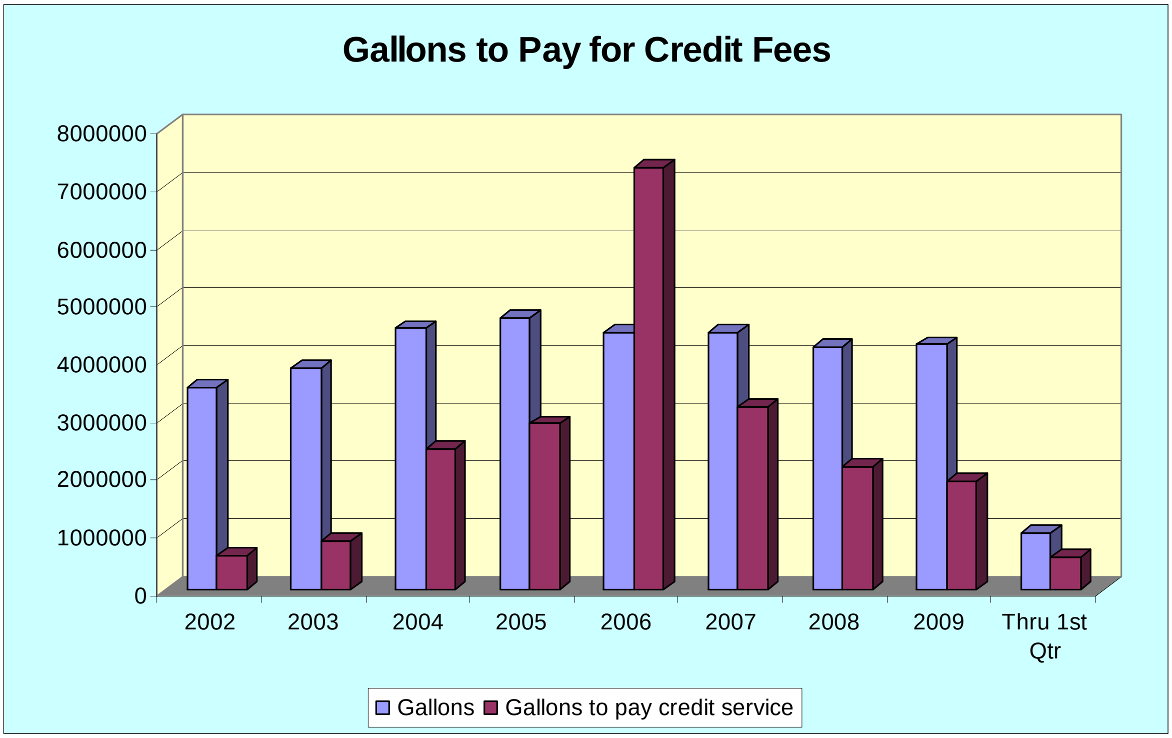


Dividing convenience store sales by certain store expenses, the result was the same – card fees are the second largest expense we incur, and the runaway nature of our swipe fees is plainly evident.

[1] The decline in credit card fee expense reflected in Figure 2 for 2009 is the result of the precipitous drop in gas prices that year after the price spiked the year before. As can be seen from the data for first quarter 2010, our card fee expense is on its way up once more. While the trends for other expenses also appear to be rising for the first quarter 2010, this is due only to the fact that gasoline sales volume in the first three months of the year is historically low in Iowa. When our expense data are viewed over an entire year, the slope of the lines for all expenses other than card fees remains relatively flat.

Figure 4 shows just how much it takes in card fees for us to sell fuel.

Figure 4



Taking sales and card fee data from one representative store, and separating out card fees paid on fuel sales only, it can be seen that on average, it takes **more than half** the gallons we sell and the associated profit just to pay the card fees. And in 2006, we were unable to sell enough fuel even to pay for the swipe fees on those sales. For some of our stores, this situation was not limited to 2006 and is a recurring issue because our margins on fuel sales are very low. In any event, these figures help demonstrate just how competitive our industry is, with retailers unable to earn enough to cover one of their significant expenses.

Importantly, none of these graphs account for fee hikes that Visa has announced for this month and July. I know of a company that has estimated that these hikes will result in a 5.9% increase in card fees paid on fuel sales alone. And these increases are not for interchange – they relate to the myriad of other fees the card companies charge merchants, such as the Assessment Transaction Fee, Partial Authorization Fee, Zero Floor Limit Fee, and various debit card fees. If you thought the fees on telephone bills were confusing, you should take a look at the tangle of fees charged for card processing.

And somehow, Visa's and MasterCard's supposed efforts to mitigate some of the fee burden for fuel sales ends up costing us more. Last year, they instituted a "small ticket fee" program to charge a lower fee for fuel sales transactions of less than $75. To provide some background, the Committee may recall that in 2008 when fuel prices spiked, card fees rose to unprecedented levels. When those were combined with the card companies' draconian rules that allowed them to refuse to pay retailers for sales over $75, the result was lost sales for retailers and upset customers because gas pumps automatically shut off at $75, before some customers' tanks were full. Customers who re-set the pumps to get more gas caused the retailer to pay a second, full swipe fee.

It should come as no surprise that the small ticket program, which was supposed to address these difficulties, comes with strings. First, when the increases in other components of card fees are taken into account, this change to the fee structure does not help my business, and will probably cost us more. This is the case because the small ticket program involves a decrease in the percentage-based portion of the swipe fee and an increase in the flat fee portion of the swipe fee. When gas prices went back down, the overall proportion of the swipe fee as a percentage of the sale actually went up, and is higher than it was under the old program.

Moreover, even if a fuel customer goes one penny over $75 in a transaction, the merchant goes from paying the "best rate" for fees on the total sale to the "worst rate," which is nearly double the "best rate." The card companies also refuse to give merchants any assurances regarding charge-backs on transactions greater than $75. So if a fuel transaction is more than $75, the merchant takes the risk on any amount above $75. And there currently is no authorization system that will allow merchants to avoid these types of risks, although we hear that Visa is working on one that might be made available a few years from now. The best a retailer can do is set a pump limit at $75, which is inconvenient for customers re-fueling trucks and other large vehicles because the pump shuts off and they must initiate an entire new transaction. And as mentioned, the retailer is charged a full, second swipe card fee for that second transaction even though it's the same customer simply trying to fill his or her tank.

Overall for the ShortStop chain, interchange fees have grown more rapidly and significantly than **all** of our other expenses. And we cannot control interchange fees the way we can control other expenses. For example, we could change employee schedules if we needed to reduce labor costs; we can invest in new technology to reduce utility expenses; and we put our business and health insurance needs out for competitive bid yearly to help keep those expenses at a manageable (or at least predictable) level.

But our interchange fees are what they are, and we have absolutely no ability to negotiate those fees. As a result, we have had to cut costs even more in other areas to offset the increases in card fees. Our customers and employees are financially stressed. Yet, the customer must pay more for everything he or she purchases, and our employees may have their hours cut, their benefits cut, or get no raises. And stores may lose money, or fail to grow enough to adequately distribute overhead costs. My business has not expanded as it could because of runaway card fees. Thus, any particular cost that we cannot control actually has a far broader, negative impact on every aspect of our business, our employees, and our customers.

To propose that we simply use cash discounting reflects a lack of understanding of this retail business. Fuel sales are so competitive – every station has its prices on big signs outside for all to see – that if we advertised a lower price for using cash, some competitors would match our price for credit transactions at their stations. The competition would kill us. And because of the credit card companies' onerous labeling rules for cash discounting, attempting to discount the thousands of other items we sell inside the store would be an impractical, logistical nightmare. Unlike Visa and MasterCard, our industry isn't permitted to agree on pricing schemes for our stores. Instead, the incredibly competitive nature of our business gives our customers the best price possible in their respective market, and keeps us constantly looking for ways to improve our sales and cost structures.

An especially problematic aspect of the interchange fee hikes we have seen in recent years is that they are completely unpredictable. While we obviously cannot expect that prices will always be predictable, given the years of experience my staff and I have in this business, we are able, for the most part, to accurately project the cost of large expense items. With the exception of credit card fees. As a case in point, I went to a bank in 2002 to obtain capital financing to expand, and I submitted a budget with estimated expenses to the bank. My estimate was extremely accurate for every expense with the exception of credit card fees, which had risen so dramatically during a period of just a few years that they exceeded my estimate by $500,000. Those fees have become so oppressive it seems there is nothing we do can overcome it; payment card fees are literally choking the air out of our business, and it is becoming increasingly difficult to run a business when I have no ability to predict increases in our second largest expense.

Nor do we have the ability to choose one type of card over another, because the banks that issue the cards all demand that we accept all cards within their portfolio. Unlike all of our other suppliers of goods and services, banks are not competing for our business. This stands in stark contrast to suppliers like Coke and Pepsi, as just one example. If we do not like the price Coke seeks for its fountain syrup, all I have to do is call up the Pepsi distributor. With this type of competition, we get a decent price. Most companies fight very hard to do business with our industry, allowing us to negotiate the very best deal for us and our consumers.

The fact that we do not get a competitive price for card fees is not due to a lack of trying. From 2007 to 2009, I was president of the national advisory council for marketers of a major oil company. With the strength of this player and the voice for more than 7,000 stores behind me, I certainly hoped to achieve enact degree of change on behalf of all of us. But what I learned was even the biggest of the big have no ability to negotiate with these financial entities. The best we got were marginal concessions on some processing fees that make up only a tiny part of the total fees we pay; and those concessions came at the oil company's expense. On interchange, which is the bulk of what we pay, Visa and Master Card refused to budge. I felt that if a company representing more than 7,000 stores could not make any headway in attempting to negotiate on interchange, it is unlikely that anyone can.

Worst of all, there are no other realistic options: our customers expect us to accept these cards, and all of our competitors accept them, so we do not get more business by accepting cards – there simply is no business without accepting cards. Visa and MasterCard are another form of currency and we must take them like we must take cash. Indeed, approximately 80% of ShortStop's sales are paid by credit and debit cards, and we expect that percentage to increase as more young people patronize our stores. At this volume, we can pay reasonable fees for interchange and processing, and it is not my position, or that of NACS, that card processing should be free. What I and other convenience stores cannot continue to do, however, is pay exorbitant fees to subsidize card programs like travel rewards, and absorb the costs of the poor credit risks that issuers have been all too willing to take on.

Policymakers truly need to begin to see payment cards as a new form of currency, because at 80% of sales and growing, that is what payment cards have become and will be in the future. If the U.S. Treasury decided to offer a reward or a perk to everyone who obtained cash from a bank, there would be no question that taxpayers would not support such a system. And checks are cleared at par, not par plus a reward. So while I do not have a problem with paying a fee to process card transactions, I believe we have reached the point that the process of determining that fee cannot be left solely to the whims of the people sitting in the board rooms of the credit card companies.

In sum, the increases that I am seeing in credit and debit card fees are simply unsustainable. The amount I paid in card fees last year was considerably more than I pay on my entire debt service on my investment capital in the business. If interchange fees were half of what they currently are, I could support significant additional investment capital that I could use to open more stores and provide more jobs in my community. With lower interchange fees, I could also lower prices. And lower prices mean more sales. Accordingly, I support efforts to rein in interchange fees.

<u>The Significance of Interchange Fees for Community Banks</u>

With assets exceeding $1 billion and 30 locations, Liberty Bank Iowa is at the larger end of the spectrum of community banks size-wise. We issue our own Visa branded credit and debit cards rather than outsourcing the payment card operation, although the operation is very costly to run. In 2009, the amount of revenue the bank earned on interchange accounted for less than 1%

of the bank's total revenue. The amount of profit that interchange accounted for was zero. Last year was a typical year, meaning that our bank views this as a breakeven operation at best.

The reason we issue Visa payment cards is purely for the convenience for our business customers, who appreciate the ability to have "one-stop-shopping" when it comes to their financial needs. At one time we outsourced our card operations and the financial results were no better. We received a fee for each new account opened (we received no interchange or other fees), which was barely enough to offset the expense of outsourcing. In the meantime, our customers were unhappy with the service provided by the firm that handled the operation for us; this outsourced operation was not good for our brand. For these reasons, Liberty Bank Iowa took its card operation back in house.

My understanding is that ours is a typical experience for large community banks. Liberty Bank Iowa has several locations, a Marketing Department, a solid customer base, and the resources to make the credit card operation as successful as possible. If Liberty Bank Iowa does not make money on issuing cards, it is difficult to see how smaller community banks with fewer resources would have any different experience. It is my understanding that many smaller banks outsource card issuance, a model likely to yield little or no profit based on our experience.

In sum, Liberty Bank Iowa is in the card issuing business solely as an added service for customers. Interchange fees have little significance for us in terms of revenue or profit, and I understand the same to be the case for most other community banks. Therefore, I disagree with the contention that efforts to bring interchange fees under control will harm community banks. This is simply not an item that is significant to the business of community banks.

In fact, changes to the system might help. Right now, we compete with other banks for customers on the basis of price and service. But there is no price competition on interchange fees. If there were, we might have more ways to attract customers and increase this part of our business. But the way it is, the huge banks make big money on interchange and market heavily to our customers through direct mail and otherwise. Liberty Bank Iowa has not been able to effectively compete with that, given that part of the competitive playing field is closed.

It is important to note here that there is no other aspect of our bank's operation in which we charge the same set of default fees or prices as all of our competitors. We compete on savings account rates, checking account rates, lending rates, account fees, and everything else that we charge. I don't understand why we're allowed to agree to charge the same thing on interchange as every other bank. It just doesn't make sense. I am an entrepreneur and believe in free markets. And what I know is this: legal or not, the interchange market isn't free. It is rigged to guarantee big money for the largest banking institutions, leave banks like mine the leftovers from their feast (at best), and tighten the noose on businesses like ShortStop as much as they can without killing us (though sometimes it proves fatal).

Conclusion

I am fortunate to be able to serve my community in Iowa as a both a retailer and a community banker. I see the effects of card swipe fees from both of those perspectives. I believe these fees are out of control, that they must be addressed so that small businesses like convenience stores can thrive, and that this can be done without doing any harm to community banks' business model.