NATIONAL RESTAURANT ASSOCIATION

State Legislation Prohibiting Interchange Fees on Sales Taxes & Tips

The Issue: Restaurants are the cornerstones of our communities and an engine of our economy. In 2024, the industry exceeded $1.1 trillion in sales and collected $216.7 billion for the business owner in taxes for all levels of government. However, this service for the state comes at a significant cost for the business owner, because credit card networks require restaurant operators to pay interchange fees (also known as "swipe fees") on the taxes they collect. The same is true for tips left by credit card for servers and bartenders. In both cases, the operator collects the money, but 100% of the amount is passed on to either the state or restaurant employees. But the swipe fees (averaging 2-4% per transaction) must still be paid on the total check amount, so those fees are coming out of restaurants' margins.

This is the only business relationship that a restaurant operator has where the service provider takes a non-negotiable cut of the business's profits on every transaction. The networks have complete control over the fees and the terms of the transactions. In fact, they don't just take a cut – they take a percentage of gross revenue while business owners only get their cut on the net margin after paying all their expenses. This is true for the largest, multi-state restaurant chains with hundreds of locations, the smallest independent local operators, and every size operator in-between.

The Bottom Line: Merchants are paying over $8 billion in swipe fees annually just to carry out their role in collecting taxes on behalf of states and localities. This figure is likely much higher for gratuities given that a conservative estimate for the typical restaurant tip is 15% across the nation. Get an estimate of the amount of interchange fees paid on sales tax in each state here.

The Solution: State legislatures across the country are introducing legislation to relieve business owners from overpaying swipe fees by excluding them on state and local sales tax and tips, at absolutely no cost to the state or local government. In 2024, Illinois was the first state to pass this type of legislation through the Interchange Fee Prohibition Act *(IFPA)* (Article 150, beginning on page 1098). It allows restaurant operators to recoup these interchange fees on both sales taxes and tips in two ways:

1. Deducting the amount of any tax or tip imposed from the calculation of interchange fees specific to each form or type of electronic payment transaction at the time of settlement; or
2. Retroactively rebating an amount of interchange fee proportionate to the amount attributable to the tax or tip on a recurring basis.

The law is currently being litigated in Illinois (discussed further in *Appendix A*).

January 2025

Summary: The legislation serves as an effective but optional tool for merchants—restaurant operators and other businesses are not required to engage in the process—to recover these fees either at the point-of-sale or through a retroactive reimbursement. If a retailer cannot separate this information at the time of settlement, they can receive reimbursement after the fact – just like the other after-the-fact settlement processes that the card industry has already put in place, like chargebacks. This type of legislation benefits all business owners by keeping dollars in the state and stimulating local economic activity (as opposed to sending these dollars to global card networks and banks in other states and even other countries). It will allow restaurant operators to hire more employees, invest in their business, and continue to contribute towards the communities they serve.

Restaurant Impact

Swipe fees are a top 3 cost for restaurant owners and operators. Accepting debit and credit cards is necessary to best serve restaurant customers, and ultimately, to stay in business. However, accepting card payments is one of the highest costs for an operator – often right behind labor and food. This is because two card networks control over 80% of the credit card market and dictate the amount in swipe fees that banks charge merchants for accepting their credit cards. Worse yet, swipe fees act as an inflation multiplier by adding 2-4% to an operator's cost for every single credit card transaction.

Swipe fees are non-negotiable. Restaurants and other merchants have no ability to negotiate the credit card rates that the two dominant card companies impose, nor in practicality are they able to seek out alternative payment processing options. This duopoly has so much power that it essentially forces business owners into a "take it or leave it" position if they want to accept credit cards with their logos on them. But the restaurant business is so competitive, they need to accept credit cards, or their customers will go to the restaurant next door or across the street.

Swipe fees are higher for card-not-present (CNP) transactions. Restaurant operators are not just paying fees when a physical card is swiped. Card not present – or CNP – transactions have always been important for restaurant delivery, but they exploded in the pandemic. One day, around 60% of all restaurant traffic was off-premises, the next, more than 95% was. In a very short period, restaurants were taking orders online, through mobile applications, third-party delivery services, and via contactless payments during curbside pickup. Each of these payments comes with significantly higher CNP fees. And with the rise in CNP payments came more consumer fraud that merchants are penalized for by credit card companies. Merchants are forced to pay 100% of the fraud costs and the chargebacks associated with CNP transactions, even if the operator has proof that they are not at fault.

Restaurant operators are already equipped to comply with this law today. Any restaurant that accepts payment cards – which is the vast majority of them – already has equipment that separates the sales tax portion of the ticket from the original purchase price. In fact, this has been done since the inception of the sales and use tax acts in 1955. Credit card companies typically

must add those figures together to determine the fees to charge in the first place. This would let them skip that step. Plus, restaurants already separately enter sales and tip amounts into their PIN pads. So, there are easy ways to apply the rule in real time, but it can also be done after the fact – both of which credit card companies are already doing today.

This legislation would provide much-needed relief from exorbitant swipe fees for restaurant operators. In the end, the collection of interchange fees on the tax and tip portions of the receipt actually creates an environment where credit card companies can make more money on a retail transaction than the restaurant or retailer. A breakdown of the estimated annual savings for an average restaurant in every state is provided in *Appendix B*.

Consumer Impact & Outlook

The Visa/Mastercard duopoly collected more than $172 billion dollars in swipe fees from U.S. businesses in 2023. The average family paid more than $1,100 in swipe fees, and they are feeling the pressure.

A recent survey conducted by Morning Consult and the National Restaurant Association revealed that **65%** of U.S. voters are concerned about credit card swipe fees for restaurant owners. The survey also showed that 80% of voters are concerned about the impacts of swipe fees on the prices they pay at restaurants, and **75%** are concerned about the price they pay at small businesses. When it comes to this issue in particular, **64%** of voters are opposed to swipe fees being calculated on sales tax and gratuities, and **72%** of voters would support prohibiting swipe fees on sales tax and tips.

Additional survey results pertaining to Illinois consumers and their outlook on IFPA is attached separately in *Appendix C* and *Appendix D*.

Just the facts: Setting the record straight

Credit card companies argue that the "sky is falling" any time Congress or state legislatures seek to make common-sense changes to swipe fees, and they often offer disingenuous explanations for why things can't change.

Fact: Customers will see no change in the payment process – still only having to swipe their card once.

The card companies only need to know the total transaction amount including the tax and the tip amounts. From that, they simply subtract the tax and tips and calculate the proper interchange fee. The current processing systems already have the ability to do this. Nothing in the legislation changes the customer experience.

Fact: Credit card companies and the business owners already have the technology to handle the change in this legislation.

Most states have laws that require state and local sales taxes be separately stated on a customer's invoice, receipt, or charge slip. Therefore, nearly every POS system currently used by restaurant operators contains the software to separately calculate the sales taxes, and of course tips. Additionally, if a merchant cannot update its software to transmit the tax and tip amounts at the time of sale, the legislation provides a second option for the merchant to submit the documentation to the card company and receive a refund or credit of the associated interchange fees.

Fact: This legislation will help small business owners by letting them keep a little more of their hard-earned profits.

There will not be significant cost for merchants to implement this legislation, and in the long-run it will increase the amount of their own profit they are able to keep. Restaurant point of sales systems already allow servers to enter a sales amount followed by a separate tip amount for transmission to the card company and most states have laws that require the sales taxes be separately stated on the receipt. If needed, the legislation provides businesses of all sizes the option to receive a portion of the interchange fees back through a rebate or credit process. In the end, the choice to pursue these savings lies with the business owner, not the credit card company.

Fact: The legislation will not be a burden for credit card companies and other financial sector entities.

Credit card companies already provide corporate accounts with the ability to separately report and track "level 2" data, including taxes. In fact, Visa offers a service known as "Visa Spend Clarity" (formerly known as "IntelliLink") that **sells** this level 2 data back to merchants. Visa makes clear to merchants that "no special hardware or software is required" for their existing service. You can access basic documentation on Visa's service here. Additionally, Mastercard's interchange guide below shows merchants qualify for LOWER interchange if the merchant sends in level 2 data (Program Name "Data Rate II" is the interchange rate when the merchant sends tax amount, whereas Program Name "Standard" is the interchange rate when the merchant does NOT send tax amount).

merchant-rates-2023-2024 Save

mastercard

U.S. Region Mastercard Commercial Rates - Small Business Credit

Program Name	Level 1 / Business Core (USD)	Level 2 / Business World (USD)	Level 3 / Business World Elite (USD)	Level 4 (USD)	Level 5 (USD)
Charities	2.00% + 0.10	2.00% + 0.10	2.00% + 0.10	2.00% + 0.10	2.00% + 0.10
Data Rate I	2.65% + 0.10	2.80% + 0.10	2.85% + 0.10	2.95% + 0.10	3.00% + 0.10
Data Rate II	1.90% + 0.10	2.05% + 0.10	2.10% + 0.10	2.20% + 0.10	2.25% + 0.10
Payment Transaction	0.19% + 0.53	0.19% + 0.53	0.19% + 0.53	0.19% + 0.53	0.19% + 0.53
Rebate	0.00% + 0.00	0.00% + 0.00	0.00% + 0.00	0.00% + 0.00	0.00% + 0.00
Standard	2.95% + 0.10	3.10% + 0.10	3.15% + 0.10	3.25% + 0.10	3.30% + 0.10
T&E Rate	2.35% + 0.10	2.50% + 0.10	2.55% + 0.10	2.65% + 0.10	2.70% + 0.10

Fact: This legislation will NOT impact card companies' and bank's ability to provide fraud protection.

Though merchants already pre-pay for fraud mitigation through interchange fees, credit card companies and banks generally pass fraud costs back to merchants in the form of chargebacks. When a fraud claim is made, the merchant returns the payment for the goods or service to the bank without the return of their product/service. The merchant pays an additional fee to facilitate the chargeback.

Fact: Other states have passed similar legislation and several are considering it.

Last year, Illinois became the first state to pass the *Interchange Fee Prohibition Act*. Additionally, this type of legislation has long been introduced and considered in a myriad of other states but have been quietly killed due to financial sector resources and scare tactics.

Fact: Passage of this legislation does not threaten credit card rewards programs.

This is merely another repeated scare tactic from the financial sector. Banks use rewards to attract customers to their products, and it's disingenuous for banks to say that rewards will go away because banks are no longer able to apply swipe fees to sales tax when they are still making money on the transaction amount, not to mention their egregious interest rates and other inflated fees they charge. Restaurant operators and other retailers offer rewards programs even though they operate on far thinner margins (the average restaurant pre-tax margin is 3-5%; money center banks average profits of 27% and Visa and Mastercard are at 50% or more).

Fact: Merchants cannot merely just write off interchange fees as tax deductions.

No one should be confused into thinking merchants just get this money back. They don't. It's just that they aren't penalized by having their profits look larger than they actually are and getting taxed on that higher, fictitious amount. Just about any business expense can be deducted in that it reduces the actual amount of your profit so that you aren't paying taxes on money you didn't actually make. But, making less money or making no money at all is not made better by the fact that you aren't overpaying on taxes. The banks are making it sound like this is a tax credit and you get all the money back for the fees you pay. You don't. Under their logic, businesses should pay all their workers millions of dollars every year and just recover all that money from the government. Of course, that's not how it works. Credit card companies taking away potential profits is not reimbursed by government tax authorities, nor should it be. Only a banker could come up with that type of argument.

Fact: This legislation represents a better solution for retailers than to be reimbursed through a state-funded "dealer discount" or "vendor compensation."

Some states offer a "dealer discount" or "vendor compensation," where the state reimburses a small amount to a small business for its losses on interchange fees collected on sales taxes. However, this amount is less than the amount that would be saved if this legislation were to pass

into law. Additionally, "reimbursing" this cost with taxpayer dollars isn't a fair solution because swipe fees are already a hidden cost that consumers end up paying and it creates bad incentives for the credit card companies to raise fees even higher because they are being subsidized by the state government.

Fact: This change can be made one state at a time, without disrupting the global payments system.

Visa and Mastercard already charge more than 600 different swipe fee rates to merchants and have intentionally made the system incredibly complex. Processing systems already handle varying taxes by states. If a retailer cannot separate this information at the time of settlement, they can receive reimbursement after the fact – just like the other after-the-fact settlement processes that the card industry has already put in place, like chargebacks.

Appendix A

Q&A: Illinois Interchange Fee Prohibition Act and Litigation Challenges

Q: What does the Illinois state interchange fee law do?

A: The Illinois law prohibits credit card networks, banks and processors from charging or receiving interchange fees on sales tax and tips. The Illinois *Interchange Fee Prohibition Act* (IFPA), which was signed in June 2024, prohibits participants in the electronic payments system, including "an issuer, a payment card network, an acquirer bank, or a processor," from "receiv[ing] or charg[ing] a merchant any interchange fee on the tax amount or gratuity of an electronic payment transaction," if the merchant submits data about the tax or gratuity amount to its acquirer bank either at the time of the transaction or within 180 days after the transaction (815 ILCS 151/150-10). . The IFPA is scheduled to take effect on July 1, 2025.

Q: Who is challenging the Illinois law and what are they claiming?

A: Financial industry trade associations are arguing that the Illinois law is preempted by federal law and are seeking to block the Illinois law from being applied to the entities it covers. In August 2024, national and Illinois trade associations representing banks and credit unions filed a lawsuit in the Northern District of Illinois (NDIL) federal court against Illinois Attorney General Kwame Raoul (in his official capacity as an enforcer of Illinois state law), claiming that the Illinois statute is preempted by federal law and thus should be deemed invalided.

Q: What has the court decided in this lawsuit challenging the Illinois law?

A: The court denied the preliminary injunction with respect to credit card networks but allowed it with respect to national banks. In December 2024, Judge Virginia Kendall issued an opinion denying the financial industry's motion for a preliminary injunction with respect to credit card networks like Visa and Mastercard but granted the injunction for national banks and federal savings associations.

FEBRUARY 2025 UPDATE: On Thursday (2/6), a federal judge issued a second opinion deciding the remaining issues in the Illinois preliminary injunction filing against the Interchange Fee Prohibition Act (IFPA). Judge Kendall ruled that **all players within the payment ecosystem (apart from national card-issuing banks and out-of-state state-chartered card-issuing banks) are required to comply with the law on July 1, 2025.** In other words, credit card companies/networks, federal and state credit unions, in-state banks, and payment processors will all have to comply with the law by its effective date later this year. This is important because the credit card companies are the ones who effectively run the entire payment ecosystem, including dictating how much merchants pay in interchange fees.

Q: Did the judge rule that state laws regulating interchange fees are preempted by federal law?

A: **No.** The December court order was not a final decision on the merits of the case, but a decision on whether to stop the implementation of the law while the court considers the state statute is preempted by various federal laws. In its opinion, the court said that there was a likelihood that Illinois' law would be found to be preempted as applied specifically to federally chartered national banks and federal savings associations, but did not say that the IFPA was likely to be found preempted as applied to card networks or to other entities involved in electronic payment transactions like payment card networks, processors, and non-federally chartered issuer and acquirer banks. It's particularly noteworthy that in its opinion the court disagreed with the financial industry associations' argument that federal preemption should extend to card networks like Visa and Mastercard, as those entities set the interchange fee rates that are charged to merchants and thus would be subject to civil penalties for Visa and Mastercard transactions in Illinois in which the fees charged fail to comply with the law's requirements.

Q: What happens next?

A: **The Illinois law is still scheduled to come into effect on July 1.** With this February 2025 development, we anticipate the plaintiffs (i.e., financial sector trade associations) will file for an expedited motion for summary judgement in an effort to win back what they lost in this round, but this effort would require Judge Kendall to overrule her own decisions.

Q: Should other state legislatures be concerned about the status of the Illinois litigation?

A: **No.** The state of Illinois is within the United States Court of Appeals for the Seventh Circuit. The other two states in the Seventh Circuit include Indiana and Wisconsin. Legal challenges of legislation in other states that are part of different Circuits may interpret the law differently.

Q: If the legislature or AG's office is concerned with the Illinois model legislation, what can we do?

A: **In response to the lawsuit results, the NRA has developed alternate model legislation that focuses more squarely on payment card networks.** This legislation provides numerous prohibitions on current payment card network practices, including prohibiting price-fixing between networks and card-issuing banks and eliminating the "Honor All Cards" rule, among others.

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Appendix B

Annual Savings for an Average Restaurant if Interchange Fees are Eliminated on Sales Tax and Gratuities

	Fullservice Restaurants				Limited-Service Restaurants	
State	Sales Tax Savings	Gratuities Savings	Total Savings	% of Sales*	Sales Tax Savings	% of Sales*
Alabama	$3,100	$5,000	$8,100	0.5%	$2,600	0.2%
Alaska	$600	$4,900	$5,500	0.4%	$500	0.0%
Arizona	$3,600	$6,400	$10,000	0.5%	$3,000	0.2%
Arkansas	$2,500	$4,000	$6,500	0.5%	$2,800	0.2%
California	$3,400	$5,700	$9,100	0.5%	$2,900	0.2%
Colorado	$3,000	$5,700	$8,700	0.5%	$2,500	0.2%
Connecticut	$2,200	$4,500	$6,700	0.5%	$1,700	0.1%
Delaware	$0	$5,800	$5,800	0.3%	$0	0.0%
District of Columbia	$5,800	$8,700	$14,500	0.5%	$2,700	0.2%
Florida	$3,300	$6,700	$10,000	0.5%	$2,200	0.1%
Georgia	$2,600	$5,400	$8,000	0.5%	$2,200	0.1%
Hawaii	$2,200	$7,400	$9,600	0.4%	$1,300	0.1%
Idaho	$1,700	$4,100	$5,800	0.5%	$1,600	0.1%
Illinois	$3,200	$5,000	$8,200	0.5%	$2,600	0.2%
Indiana	$2,400	$4,500	$6,900	0.5%	$2,200	0.2%
Iowa	$1,600	$3,500	$5,100	0.5%	$1,700	0.1%
Kansas	$1,800	$4,100	$5,900	0.5%	$1,900	0.1%
Kentucky	$2,000	$4,900	$6,900	0.5%	$1,800	0.1%
Louisiana	$3,300	$5,300	$8,600	0.5%	$2,500	0.2%
Maine	$2,300	$4,200	$6,500	0.5%	$1,700	0.2%
Maryland	$2,500	$6,200	$8,700	0.5%	$1,700	0.1%
Massachusetts	$2,400	$5,900	$8,300	0.5%	$1,600	0.1%
Michigan	$1,800	$4,400	$6,200	0.5%	$1,500	0.1%
Minnesota	$2,600	$4,900	$7,500	0.5%	$2,100	0.2%
Mississippi	$2,000	$4,300	$6,300	0.5%	$2,000	0.1%
Missouri	$2,500	$4,500	$7,000	0.5%	$2,300	0.2%
Montana	$0	$4,100	$4,100	0.3%	$0	0.0%
Nebraska	$1,800	$3,900	$5,700	0.5%	$2,000	0.1%
Nevada	$4,300	$7,900	$12,200	0.5%	$2,700	0.2%
New Hampshire	$2,900	$5,100	$8,000	0.5%	$2,100	0.2%
New Jersey	$2,200	$4,900	$7,100	0.5%	$1,500	0.1%
New Mexico	$2,400	$4,800	$7,200	0.5%	$2,600	0.1%
New York	$2,900	$5,100	$8,000	0.5%	$1,800	0.2%
North Carolina	$2,600	$4,800	$7,400	0.5%	$2,500	0.2%
North Dakota	$2,000	$4,200	$6,200	0.5%	$1,800	0.1%
Ohio	$2,400	$5,000	$7,400	0.5%	$1,900	0.1%
Oklahoma	$2,400	$4,200	$6,600	0.5%	$2,600	0.2%
Oregon	$0	$3,900	$3,900	0.3%	$0	0.0%
Pennsylvania	$1,800	$4,300	$6,100	0.5%	$1,300	0.1%
Rhode Island	$2,600	$5,000	$7,600	0.5%	$1,700	0.2%
South Carolina	$2,500	$5,000	$7,500	0.5%	$2,200	0.1%
South Dakota	$1,500	$3,800	$5,300	0.5%	$1,700	0.1%
Tennessee	$3,600	$5,700	$9,300	0.5%	$2,900	0.2%
Texas	$3,200	$5,900	$9,100	0.5%	$2,800	0.2%
Utah	$2,400	$5,100	$7,500	0.5%	$2,200	0.1%
Vermont	$2,100	$3,500	$5,600	0.5%	$1,800	0.2%
Virginia	$3,200	$4,700	$7,900	0.5%	$2,800	0.2%
Washington	$3,100	$4,500	$7,600	0.5%	$3,000	0.2%
West Virginia	$1,600	$3,700	$5,300	0.5%	$1,700	0.1%
Wisconsin	$1,900	$3,400	$5,300	0.5%	$2,200	0.2%
Wyoming	$1,500	$4,100	$5,600	0.4%	$1,600	0.1%

Source: National Restaurant Association estimates

*Represents interchange savings as a percent of annual sales for an average restaurant

MORNING CONSULT

TO: The National Restaurant Association
FR: Morning Consult
DT: January 2025
RE: Credit Card Swipe Fees

Prepared for the National Restaurant Association

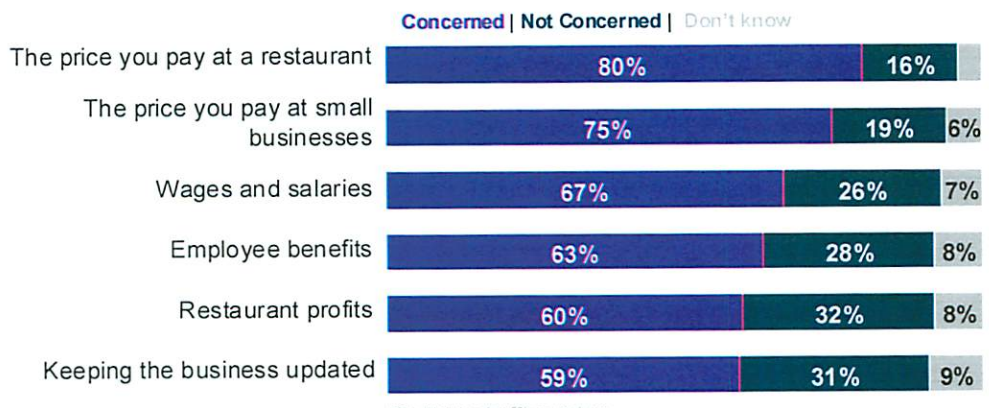
NATIONAL RESTAURANT ASSOCIATION

Morning Consult ran a survey, on behalf of the National Restaurant Association, about swipe fees and their financial impact on restaurants. The results show that a **large majority of voters are concerned about the financial impact credit card swipe fees have on restaurant owners** and that **many agree that swipe fees should not be calculated on sales tax and gratuities.** Voters also agree that prohibiting credit card swipe fees from being calculated on sales tax and gratuities would help keep tax dollars in their states' economy and **stimulate economic activity**.

Key Findings – Swipe Fees

- Voters view expenses such as increased food and supply costs (89%), and labor shortages (79%) as the most concerning to restaurant owners, though two-thirds (65%) are also concerned about the impact of credit card swipe fees on restaurant owners.
- Most voters (56%) said they know a lot or some about credit card swipe fees. While a majority of voters know at least something about credit card swipe fees, they are unsure about who covers the cost of a swipe fee. A quarter (28%) of voters view these fees as being fully covered by business owners, while 16% said the fees are fully covered by consumers. Others view the cost as being mostly covered by the business owners and partially by consumers (19%) or vice versa, mostly covered by the consumer and partially by the business owners (15%). One-in-ten (9%) said the cost of swipe fees is split evenly by the business owner and consumer.
- A strong majority of voters are concerned swipe fees affect the price they pay at restaurants (80%) and small businesses (75%).

Please indicate how concerned you are about the impact of swipe fees on each of the following?



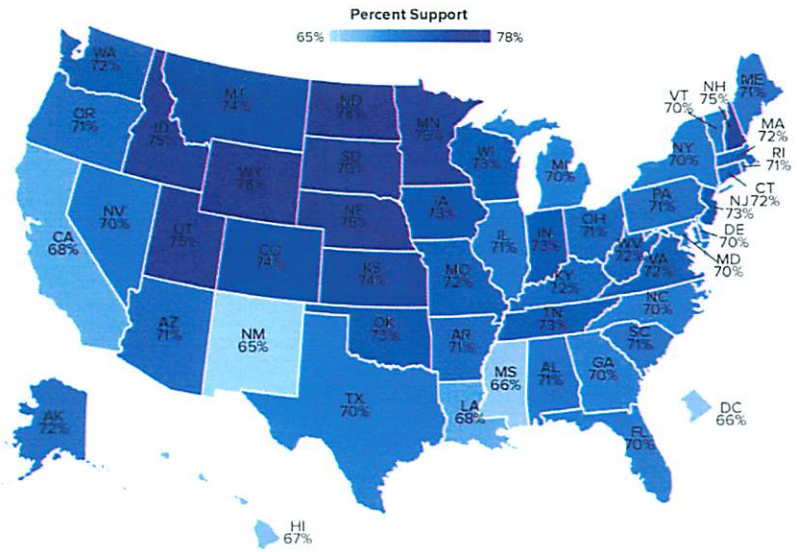
*Data labels less than 5% are not shown

- Three-in-five (60%) voters are concerned about the impact of swipe fees on restaurant revenue, and a strong majority of voters (79%) agreed swipe fees are a financial burden for restaurants. Both Democrats (79%) and Republicans (81%) agreed these fees are a financial burden.

Key Findings – Swipe Fees on Sales Tax and Gratuities

- A majority of voters (64%) oppose swipe fees being calculated on sales tax and gratuities for restaurant owners. Both Republicans (65%) and Democrats (62%) opposed the calculation of swipe fees on sales tax and gratuities.
- Three-in-four voters nationally (72%) support their state prohibiting swipe fees on sales tax and gratuities, and doing so is popular among both Democrats (73%) and Republicans (72%).

Some states prohibit charging swipe fees on taxes and gratuities. Would you support or oppose your state adopting a similar policy prohibiting swipe fees on sales taxes and gratuities?



- Voters agree (71%) prohibiting swipe fees on sales tax will keep dollars in their state and help stimulate economic activity. Three-quarters of Democrats (72%) and Republicans (72%) agree removing swipe fees from sales tax will promote economic activity in their state.
- While three-in-five voters (60%) are concerned about the financial impact of swipe fees on restaurant profits, after learning more, three-in-four voters (76%) find it concerning that restaurant owners pay more in swipe fees than their profit margin after accounting for all expenses.

National Methodology: This poll was conducted between December 20-24 2024 among a sample of 10,286 registered voters. The interviews were conducted online and the data was weighted to approximate a target sample of registered voters based on age, gender, race, educational attainment, marital status, region, home ownership, and 2020 presidential vote. Results from the full survey have a margin of error of plus or minus 1 percentage points.

State Methodology: State level findings are based on a model known as multi-level regression with post-stratification (MRP), where strata are based on census data, and results are adjusted to mirror demographics of each state.