

THE ARKANSAS TERMINATION FEE LAW

Below, I will discuss the potential impact to our industry of a recent law enacted in Arkansas that mandates disclosures to merchants and places a cap on termination fees in merchant agreements.

The Law:

Arkansas Code section 4-115-101 through 4-115-103 (the “Law”) places certain restriction on any person or entity offering “credit card processing” services in the state of Arkansas, subject to certain exceptions. The Law is effective as of July 31, 2007 for all merchant agreements entered into after that date. The first part of the law has some disclosure requirements. The Law requires the following items be disclosed to the merchant in at least eight point font: 1) the effective date of the contract; 2) the term of the contract; 3) the amount of any monthly minimum fee or charge for the credit card processing service; and 4) the amount of any fee or charge for terminating the contract or agreement.

The Law is silent on where these items must be disclosed. The Arkansas legislature was trying to ensure that these specific terms were able to be clearly seen by the merchant. Consequently, in my opinion, it is best to disclose all of these items on the first page of the merchant application where all the fees are typically set forth. In the alternative, one could place the required disclosures in the body of the merchant agreement. However, by burying the disclosures in the merchant agreement, it makes it less likely that the disclosures will comply with the spirit of the Law. Also, with these requirements, a specific merchant application and agreement must be used in Arkansas unless one wants to make the same disclosures to all merchants across the country.

The second part of the Law, the part limiting termination fees, is the most controversial part of the Law. That portion of the Law provides as follows:

“A person or entity that offers a credit card processing service in this state shall not charge: 1) A fee of more than fifty dollars (\$50.00) for terminating a contract for credit card processing service; or 2) a monthly minimum fee under a credit card processing service contract for more than one (1) month after the credit card processing service contract is terminated.”

Since the monthly minimum is usually in the \$15 to \$25 range, the Law effectively puts a \$50 cap on all termination fees. This necessitates another modification to the merchant agreement to state to Arkansas residents that only a \$50 termination fee can be charged. Since most all credit card processors charge a higher termination fee, it effectively reduces the income to them. In addition, the problem is compounded by the way many processors operate these days such as giving away free equipment and other

perks to merchants. Without higher termination fees, it is likely that many credit card processors will have a more difficult time getting a return on the investment they have made in free equipment or other enticements, since the merchant can leave without any significant monetary penalty.

The Exceptions and Penalties:

There are some significant exceptions to the Law that potentially render the Law unenforceable. The Law has an exception that states “[t]he foregoing provisions of this chapter do not apply to [a] national bank or a national savings association . . . that offers a credit card processing service.” Pursuant to the association rules, the sponsoring bank must be a party to every merchant agreement. The argument could be made then, that since the bank is a party to the merchant agreement, the exception applies to all merchant agreements.

As with all laws, the exception in this case is open to differing interpretations. One could also argue that the bank is not the primary beneficiary to the merchant agreement. In most instances, there is an ISO or some other organization that solicits the merchant, provides customer service and technical support and monitors the transactions for risk. As a result, that ISO, and not the bank, is making the bulk of the profits derived from the merchant and also arguably the one providing the “card processing service.” Under that line of reasoning, the exception to the law would not be applicable unless the bank was the only party to the relationship other than the merchant.

The problem with the Law like so many others is that the language used is subject to different interpretations and the lawmakers did not see fit to provide additional guidance by defining some of the more important terms in the Law. This leaves the industry in a situation where until there are some courts that actually apply the law and provide some written opinions on the Law, there will be uncertainty as to how the law will be applied. This state of affairs could last for many years, if not indefinitely, given the fact that it is likely this Law will not be litigated to the level necessary to have written opinions rendered that are binding on other courts.

The Law provides that any violation of the law constitutes an unfair and deceptive trade practice under Arkansas law. The main impact of that penalty is that anyone suing for a violation of the Law would be able to collect attorneys’ fees for having to pursue the case. This positions the Law such that a plaintiff’s attorney would have an incentive to file a class action lawsuit for violation of the law. An attorney filing such a lawsuit would all but be guaranteed the potential big payday with a bank, ISOs and other large financially strong companies as defendants in such a case.

The Future:

It appears that this is only the first of many laws that will be enacted regulating termination fees and disclosures to merchants in our industry. There are a number of other states that are considering similar legislation. My hope is that there is some consistency to these laws so that compliance with them is not too expensive and complicated. Another alternative is that the federal government passes a laws that preempts the state law on these issues. If we end out with a number inconsistent state laws, it will make compliance difficult and drive up the costs of operating in our industry.

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