

Interchange Myths and Facts

Myth: Interchange fees are a “hidden tax” on consumers.

Fact: In fact, interchange fees are not a hidden tax – they are neither hidden, nor a tax. Interchange is not paid by consumers. It is a fee paid between the merchant’s bank and the cardholder’s bank that serves to balance costs in the payments system. Interchange is a component of the merchant discount fee, which merchants pay for the extraordinary benefits they receive when they choose to accept payment cards. These include increased sales, fraud protection and faster payment, among other benefits.

Merchant discount fees, which can include costs like processing transactions or terminal rental, are just one of many other costs a merchant incurs for running a business, such as electricity, rent or advertising costs. Consumers understand that merchants factor all of the costs of running their businesses into their prices. Attempts to classify such costs as a “hidden tax” on consumers would be similar to trying to misrepresent businesses’ rent or utility costs as a “hidden tax” on their customers.

Further, interchange fees are not hidden. MasterCard publicly discloses all of its interchange rates on its website, and merchants are free to disclose these fees (or the merchant discount fees they pay) to their customers. Merchants may choose not to disclose these fees to consumers just as they choose not to disclose any other cost of doing business or how they price their merchandise.

Myth: Reducing interchange would benefit consumers.

Fact: Interchange actually serves to reduce costs for consumers by balancing incentives for merchants to accept cards, issuers to issue cards, and cardholders to use their cards. There are costs that the parties in a payments network incur that need to be balanced among its participants. Simply slashing interchange fees for merchants will result in higher costs for card issuers and their customers, the cardholder. It’s that simple.

If issuers are not compensated, through interchange, for bearing the credit risk, fraud protection, and all the benefits they provide to merchants, they would likely issue fewer cards, limit consumer rewards and benefits and raise fees for consumers. In addition,

with fewer cards in circulation and fewer cardholders using them, merchants would ultimately lose the benefits they receive from electronic payments.

In Australia, where interchange was cut by government intervention, consumers are now saddled with fees and rising interest rates, and their rewards programs and benefits have dropped. Further, there is no evidence that merchants have lowered prices for consumers.

Myth: **Consumers receive no value from interchange.**

Fact: Consumers realize significant value from interchange, including greater choice and flexibility. By providing incentives for card issuers, interchange encourages banks to innovate and develop new payment options, broaden the range of card products available to consumers, and invest in cutting-edge security and fraud prevention measures. In jurisdictions like Australia where interchange has been regulated, consumer fees have increased and rewards and benefits have declined. Moreover, by incenting merchants to accept cards, interchange helps give consumers access to online and traditional merchants worldwide.

Myth: **More money is spent on interchange fees than cardholders' annual fees, cash advance fees, late fees and over-limit fees for credit cards.**

Fact: Interchange is not paid by consumers. It is a fee paid between banks to balance costs in the payments system, and is a component of the fee merchants pay, for the tremendous benefits merchants receive when they choose to accept payment cards. Moreover, retailers are free to offer discounts to cash and check users.

Myth: **Interchange is part of an illegal "price fixing" scheme.**

Fact: Although regulators in several jurisdictions have ruled against MasterCard interchange fees, ordinary "price fixing" is not the legal theory on which they have based their decisions. Instead, the issue has been framed in terms of who should set interchange fees and/or what is the appropriate level of interchange. No court has found interchange to be illegal, whether as part of a price fixing scheme or otherwise.

MasterCard establishes default interchange rates to provide incentives to merchants to accept cards and to card issuers to provide innovative card products that meet consumer demand. Importantly, while MasterCard sets default interchange fees to enable efficient interaction among thousands of financial institutions, it receives no revenue from those fees. On this basis, MasterCard maintains not only that interchange fees do not undermine competition but that, in fact, they enhance it by facilitating the offering of products and services that otherwise would not exist in the marketplace.

Myth: Interchange fees hurt merchants' business.

Fact: Interchange is set to accomplish one goal: maximize output – meaning more cards in consumers' hands, more merchants accepting cards, and more sales. It provides a mechanism for balancing the higher costs of issuing cards with the costs of card acceptance. The fact is that merchants accepting MasterCard receive extraordinary value for a relatively small fee. That's why in the last 40 years, MasterCard has gone from zero to more than 25 million merchant acceptance locations.

The benefits to merchants of choosing to accept MasterCard are significant, and include increased sales, management of lending losses, fraud, and the costs of complying with regulations. In exchange for a small merchant discount fee, merchants can participate in a payment system that is far more cost effective for them than issuing their own proprietary card or some other form of store credit.

Myth: MasterCard does not disclose its interchange rates and rules to merchants.

Fact: MasterCard publicly discloses its U.S. interchange rates and operating rules that apply to merchants by making them available without restriction on its Web site, www.mastercardmerchant.com, along with comprehensive information to help merchants understand the rates and how they apply. These steps are intended to help foster an ongoing dialogue with merchants, acquirers and others about interchange rates and disclosure.

Myth: **MasterCard rules prohibit or essentially make it impossible for merchants to disclose these fees to consumers.**

Fact: MasterCard has no rule prohibiting merchants from disclosing what they pay for acceptance. Merchants are free to disclose merchant discount fees, interchange fees, or any other cost they incur. They are also free to steer customers to another form of payment or to offer customers a discount for using cash or check. Merchants may choose not to disclose these costs to consumers just as they choose not to disclose any other cost of doing business or how much they “mark up” their merchandise.

Myth: **Card company rules prohibit merchants from offering discounts for cash and check.**

Fact: MasterCard has always allowed merchants to offer discounts for cash and check. Gas stations, for example, used to regularly offer cash discounts, but the majority independently ceased this practice. These types of businesses came to recognize that payment cards, such as MasterCard, offered them significant benefits over cash or check transactions.

Myth: **Merchants have no choice but to pay a set interchange fee.**

Fact: If a retailer is dissatisfied with the merchant discount rate it negotiated with its bank for MasterCard acceptance, that retailer has several options: it can provide discounts to those who pay with cash or check, negotiate a different merchant discount rate with its bank or switch to a bank that offers more competitive rates, or choose not to accept MasterCard cards. There is significant competition for merchant acceptance among financial institutions and payment card providers. Merchants, of course, are free to choose which payment options they accept and can choose to encourage their customers to use a particular payment choice.

Myth: **Interchange fees have risen “dramatically” in recent years and Americans pay the highest credit card interchange fees in the world.**

Fact: Interchange *rates* have risen very slowly (1.9% since 1990 – well below the rate of inflation). Total interchange *fees* paid among banks have increased because more and more merchants have chosen to accept payment cards to increase their revenues and

obtain the many other benefits that payment cards offer. The value of these benefits increases all the time as innovations like PayPass and a multiplicity of new card offerings incent more consumers to choose to pay with their MasterCard cards.

In addition, according to the Aite Report, U.S. merchants actually pay merchant discount fees that are below those charged in most other countries around the world.

Myth: **There is a lack of competition in the payment card arena.**

Fact: There is tremendous competition among payment card providers. In addition to MasterCard, Visa, American Express and Discover, there are many debit networks, including Electron, Interlink, PULSE, Star, NYCE and Tempo. Alternative payment providers such as PayPal and Google Checkout are further evidence of the strong competition in the payments marketplace. Merchants, of course, are free to choose which, if any, payment cards they accept and can choose to encourage their customers to use particular brands.

Myth: **MasterCard collected \$36 million in interchange fees last year alone.**

Fact: MasterCard does not receive any revenue from interchange.