

Cracking the Code

Credit card processing bills are a jumble. Here's how to read yours.

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No one likes a bill, especially one filled with cryptic codes and indecipherable jargon. That's a pretty good description of a statement from a credit card processor. Such firms authorize credit and move funds through the banking system so that you get paid. For these services, you pay the processor a fee, known as the discount rate. Many processors tout low discount rates to lure new customers. Problem is, your bill can be so complicated that it's nearly impossible to figure out if you're paying that low rate--or a lot more, thanks to a host of surcharges and fees. We recently studied a dozen statements. While bills differ from processor to processor, here are some common fees you might see on yours.

1. That low rate? It may not be so low

Many monthly statements show your daily tally of credit card sales and the fees charged to process them. Translated into English, this line means that you paid your processor \$6.86 to process \$385.42 worth of MasterCard (NYSE:MA) sales on March 31. That's 1.78 percent, the discount rate you were likely quoted when you signed up. The processor uses those funds to pay the interchange, a fee set by MasterCard and Visa, and keeps the difference for itself. But not all credit card transactions are created equal; rewards cards and online transactions, for example, often come with higher interchange fees--and higher processing fees. There's a good chance your processor hasn't told you this.

2. Beware billbacks

To cover higher interchange rates, some credit card processors use billbacks. They'll charge a low discount rate on all of a merchant's transactions in a given month--in this case, 1.78 percent--then bill back surcharges on certain transactions the following month.

Billbacks are coded with a BB. This line shows that this merchant had 1,027 transactions in February that involved a MasterCard World card, which carries a higher interchange fee because it's a rewards card. The processor is passing on the additional cost of handling those transactions, \$565.35. Unfortunately, you can't see the actual rate you're paying because the processor doesn't provide the total dollar amount of these transactions.

3. Calculate the markup

It's not hard to estimate your actual rate. Take your average sales value (sometimes called "average ticket" on your statement) and multiply it by the number of transactions for a

given billback. Divide the surcharge by that amount and you'll find out how much you're actually paying on these sales. In this case, suppose the merchant's average ticket is \$20. Multiply that by 1,027 transactions and you get \$20,540. Divide the processor's billback surcharge--\$565.35--by that amount, and you end up with 0.0275, or 2.8 percent.

MasterCard, as it happens, charges about 1.84 percent for basic World card transactions, so the processor is clearing nearly a 1 percent profit. There's nothing wrong with making a profit, of course. But you have a right to know the rate you're being charged.

Case in Point

How to get relief

Andrew Ackerman, chief operating officer at Bunk1.com, a New York City firm that provides Web services to summer camps, prodded his credit card processor for more info on his company's billbacks and struck gold. It turned out that about 25 percent of his transactions did not qualify for the discount rate the company was quoted, about 2.3 percent. The rest were subject to steep billbacks. Ackerman shopped around and found another processor that offered better rates on many billbacks. Estimated savings: more than \$10,000 a year.

4. Qualified versus mid-qualified versus nonqualified

Because Visa's and MasterCard's interchange fees are so complex, processors sometimes categorize transactions as qualified, mid-qualified, and nonqualified. One rate covers all the transactions that fall into a category. Suppose this statement is that of a restaurant. When a customer pays with a generic Visa card, Visa charges an interchange fee of about 1.63 percent. The processor considers that a qualified transaction and charges a discount rate of 1.74 percent. If someone uses a Visa rewards card, however, the interchange jumps to nearly 2 percent. The processor labels it as mid-qualified and charges 2.85 percent. Every processor sets its own tiered pricing, so one type of credit card transaction may be considered mid-qualified by one and qualified by another. It's up to you to find out how your processor defines things.

5. No deal on debit

Visa and MasterCard charge lower interchange fees when a customer pays with a debit card instead of credit. The processors, though, aren't required to pass these savings on to you. The restaurateur on this bill, for example, is paying at least 1.74 percent on each transaction, including debit cards. But Visa and MasterCard charge about 1.3 percent on typical restaurant debit purchases. Make sure your processor gives you a break on debit.

6. Watch out for skimming

Some processors take a percentage of their fees when they reconcile your account at the end of each business day. As a result the figure called "total card fees" on your monthly statement is not a total at all. To estimate your true costs, look for a line on your bill that reads "less discount paid." It may be buried near the bottom and not be as obvious as shown here. That's how much your processor skimmed off your sales throughout the month. Add it to your "total card fees" to determine how high your fees actually are.

7. Hidden fee No. 1

AVS stands for address verification service. When you take a credit card order over the phone or online, that transaction qualifies for a better interchange rate if you key in your customer's address. That's because Visa and MasterCard consider AVS a way to combat fraud. Your processor may--or may not--pass these savings on to you. In fact, it might tack on an additional AVS fee to process these transactions. Not all processors do, so be sure to ask.

8. Hidden fee No. 2

This processor is charging 22 cents to process every credit card sale, refund, and authorization. Per-transaction fees typically range from 10 to 15 cents but can go higher, says Jeff Mandel, territory manager for Heartland Payment Systems, a credit card processor in Princeton, New Jersey. For companies with only a few, high-value transactions a month, this fee doesn't matter much. But if you have lots of smaller purchases, it can add up.

Case in Point

Find your real rate

The easiest way to determine what you're actually paying your processor is to divide your total fees by your total monthly credit card sales. John Dixon at Nekton Diving in Fort Lauderdale, Florida, crunched the numbers and was stunned to learn that he was paying an average of 6.5 percent, substantially more than the 2.5 percent discount rate quoted by his processor. He switched processors and has cut his fees in half, to just \$30,000 a year.