Federal Financial Analytics, Inc.

MEMORANDUM

TO: Federal Financial Analytics Clients

FROM: Karen Petrou

DATE: April 22, 2024

One could go on – indeed many do – about whether inflation is showing enough signs of a slow-down to warrant lower interest rates. I've said before that lower rates won't have the housing-affordability benefits advocates expect, but this doesn't address the underlying issue of just how hot inflation may be running. I'm not sure if anyone – including the Fed – really knows, but battles on my neighborhood listserv validated by growing data make clear that federal data overlook one hidden price hike driving more and more Americans flat-out crazy: credit-card surcharges that are nothing but shadow price hikes of as much as four percent.

In fact, card surcharges are the epitome of the "junk" fees the CFPB has vowed to quash. The credit-card late fees the Bureau lambasts are due to consumer sins of omission or commission – i.e., consumers have the ability – I would say obligation – to keep their card debt within amounts they can honor as well as the choice to pay on time. How much should be charged for paying late is obviously a point of discussion, but that consumers have a duty to pay on time is indisputable.

In sharp contrast, card surcharges are often unavoidable and ill-disclosed. The neighborhood listserv is something of a group rant, but it does include interesting illustrations of hidden credit-card surcharges that are often – think car-repair shops – meaningful and material add-on prices discovered only after the fix, quite literally, is in.

D.C. is an area where card surcharges are hitting a particularly raw nerve because a local ordinance requires restaurants to pay minimum wages, leading many to add a card surcharge – again, often hidden – in hopes of making up some of this added cost of doing business. This is a local issue, but restaurants around the country increasingly include a card surcharge and very often only after a diner has finished and thus has little choice but to pay. Diners may then stiff servers to make up the difference. This is bad for tip income; the surcharge itself is still a price hike because it's an unavoidable cost of getting what the consumer purchased.

Merchants will quickly protest this analysis on grounds that consumers can in fact avoid card surcharges. This is, though, only true if the merchant posts the surcharge prominently enough at the front-end of a transaction that the consumer can achieve elsewhere without a surcharge. The more merchants charging surcharges, the harder this is, especially when it comes to purchases in markets with scant competition such as those for contractual car-service agreements.

But don't consumers facing a credit-card surcharge have payment options that allow for alternatives to the surcharge if the consumer is fortunate enough to receive a front-end disclosure or if the consumer reads a bill closely enough to spot a back-end surcharge? Theoretically, but not really.

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Yes, one can pay the bill with wads of cash, but then one would have had to know to bring them along, taking the risk of irrevocable loss and paying the cost of going out of the way to an ATM. Could one use a debit card? Sure, but then the consumer takes on added risk of transaction error, a risk that grows ever higher as more and more merchants lack effective security and card numbers go more and more astray. With a credit card, the risk of fraud loss is on the issuer and I for one like it that way. Importantly, the fact that issuers absorb fraud losses doesn't mean card fraud is free to the cardholder. But I pay for this risk through the interchange fees baked into current prices along with the card fees known in advance when selecting among credit-card offerings.

What about Venmo? See above for lots of payer risk. Zelle? Maybe, but this is only a debit card on steroids – convenient, but still risky. Bring a check? To do so, most consumers will also need to bring grandma.

Are merchants right to blame banks for these surcharges because card interchange fees are too high? This is a longstanding debate in which merchants would be on far firmer ground if they could show that debit-card interchange fee reductions forced by the Durbin Amendment led to lower prices. Most research says they didn't, nor is there evidence that credit-card surcharges are proportionate to the costs merchants absorb when they take the card. Further, most merchants packed interchange fees into the pricing long before surcharges were added on. As a result, consumers in fact pay the merchant twice for accepting the card, once through the interchange fee incorporated in the underlying price and then again and in more than full via a surcharge.

Further, would it really lower merchant costs if borrowers skipped to payment alternatives? I wonder how many cashiers are left and if any of them now know how to make change.

If the CFPB really wanted to do something for consumers on the junk-fee front, it would take a hard look at credit-card surcharges. With a stroke of its ever-ready pen, it would strike a blow not just for payment-system security and consumer rights, but also materially lower goods-and-service prices. That's something most consumers desperately need that would also do the broader economy a world of good.