Pulling Back the Curtain:

The Real Story Behind the Unregulated World of Credit Card Processing

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The credit card processing industry is one of smoke and mirrors. In order to explain what happens behind the scenes, you first need to understand the who the players are, who sets pricing and who makes the rules.

THE PLAYERS

Issuing banks–Issue credit cards to consumers (Ex. Bank of America, Chase, etc)

Card associations–A network that authorizes the debit or credit on accounts (Ex. Visa, Mastercard, Discover)

Processor–Entity that manages the equipment and transaction process as a middleman between the merchant and financial institutions

Merchant–The business that accepts credit cards as payment

THE RULES OF THE GAME

The credit card industry is designed to confuse and confound merchants with complex statements, long call hold times, and hundreds of rules and regulations. The players created the rules to make money, and constructed obstacles to keep making money. To start, the issuing banks work with the card associations to set the interchange cost, which is 80%-90% of what a merchant pays in fees. These interchange costs are different across business types and how each business processes the transactions. In some cases, the same transaction can have up to 4 different fees depending on how you process the sale. The same card being used may cost you 3%, but can be optimized to cost you as low as 1.45%. The answers on how to achieve the lower cost are disclosed, but are not easy to figure out as there are multiple things that must happen to qualify.

If an unregulated system has hundreds of rules and no oversight, how do you avoid being overcharged and taken advantage of?

The rules are also vary by business type. This means everything must be set up correctly when you sign up with the processor and they have to make sure your business category is correct. The problem here is that some business types have multiple codes that can be used and most processors don't analyze what is best for your business. These rules are set up in a large matrix which designates how much you pay and in turn how much the issuing banks earn. Until the merchants learn the rules and do everything they need to in order to get the optimal rate, then banks will continue to make more.

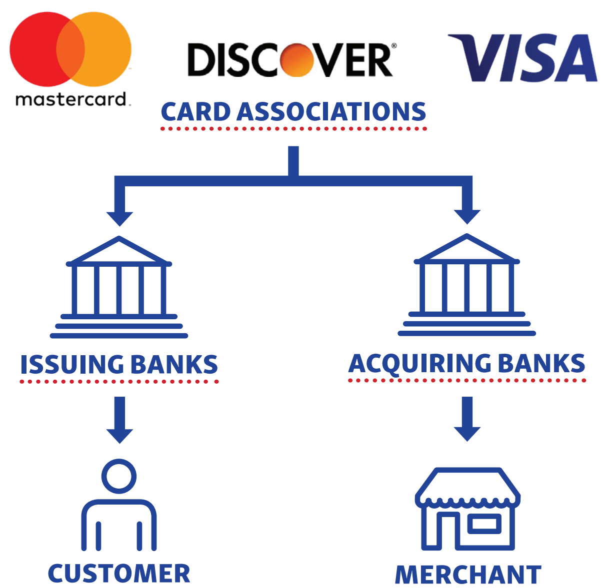
The reason behind all of this is "the battle of interchange and profit", which is controlled by the issuing banks and card associations. If profitability goes down as merchants get educated, then the only way to increase profits is to change the rules and categories. This occurred in 2020 and will also happen in 2021 when interchange rates are updated.

CHANGING THE RULES OF THE GAME IN 2020

The banks, specifically those that issue Visa, had begun to make significant changes and increases which were postponed due to Covid. Most of the increases and changes didn't happen and have been postponed until 2021. While rates didn't increase, the rules and card types changed in mid-2020- and those rules are dependent on the business types and card types being accepted. While the commitment to not increasing rates was held up, the changes and elimination of certain card categories in July 2020 did cause an increase in overall cost to some merchants.

MORE RULE MAKERS AND CHANGERS

The other side of the business, the processing side, can then take these rules and pass them on to the customer. However, they also can set the price, mark up fees, and create pricing schemes. Whereby after you follow one set of rules, you have to follow another set to get the best price. And these "rules", my friends, are what ultimately tell you how much you are paying off your gross sales amount. Even if you do everything correct from the Bank side, you can still pay more for those cards if the processor chooses to tell you that those card types are not qualified, and thus add large markups on top of the bank rules.



The acquiring/processing side is really the one that actually set the pricing that you ultimately pay, which means the sales rep filling out your paperwork will create a pricing scheme to save you money but also put a residual income in their pocket every month.

Here is an example of something that happened to a client processing about $10 million per year. The owner had a friend that worked as a sales agent for a processor. When the friend analyzed the statement he told the owner he can save him a few thousand a year. The owner signed up because, of course, he trusted his friend. However, there was another $14,000 a month that could have been saved if the friend actually cared to make sure the fees were at the absolute bottom. In this case, the friend and processor made an extra $14,000 per month. That means the rep was making $466 per day in profit, which really meant that the first $2,000 in gross sales each day went to pay the sales rep. ($2,000 in sales at a 23% net margin comes to $466).

PANDEMIC RESPONSE: HOW THE PROCESSORS ARE INCREASING THEIR BOTTOM LINE TO LOOK GOOD FOR THE FINANCIAL MARKETS

It would make sense to halt all changes and increases until 2021, due to the Global Pandemic and ensuing financial crisis. Or better yet, let's change the rules to support those that need relief now! Keep the other accounts status quo. The simple and ethical path would be to NOT make any changes unless they will help the business.

The worst part that we have now seen in Q4 is that the processing industry is actually increasing rates on the processor side. A few of the largest processor have added a "risk" fee in November of 2020. In my opinion this fee is completely made up, however the processor will probably come up with some reason why these transactions are risky. The fee basically surcharges each transaction between .25% to over 3%! Again, in my opinion this is a complete cash grab. We have seen some accounts that have absolutely no risk, such as a dentist, that now have this fee added.

The large majority of merchants won't even realize this happened since the monthly merchant statements are no longer mailed to the merchant. You have to go online to get them and to make matters worse, they are 10 times more complicated than your cell phone bill.

I am sure you realize by now that the nonsense that is happening in the credit card processing industry is completely unfair to business owners. Merchant Advocate has been helping business owners avoid these crazy rules and fees for over 15 years and this year, by far, has been the most disappointing. There is no reason for any company to profit from those that are hurting. In fact, you would think that some of these companies would create some sort of internal stimulus plan that can be passed to those business owners that need help.

Merchant Advocate helps business save money on credit card processing, WITHOUT SWITCHING PROCESSORS! For a free analysis of your account, reach out to **www.merchantadvocate.com/contact**