

3 Factors in Educating Merchants about ATM Interchange Fee Reductions

To retain the loyalty of ATM affiliates and merchants, education is key.

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The last few years have seen significant declines in interchange fees paid to U.S. ATM deployers by financial institutions, leading to a lot of dissatisfied merchants. To retain the loyalty of their ATM affiliates and merchant clients, ISOs need to do a better job of explaining to them why they are seeing less revenue from interchange. They also should suggest ways in which ATM deployers and merchants that host other companies' ATMs in their stores can replace lost income from interchange.

"Most interchange fees paid to ATM operators range from 20 cents to 30 cents, which is around half of what they were five years ago," said David Tente, executive director of the U.S. chapter of the ATM Industry Association.

According to Irvine, Calif.-based ATM solutions provider National Cash Systems, the weighted average interchange rates for all ATM transactions including withdrawals and non-cash transactions such as balance inquiries have declined from approximately 50 cents per transaction 15 years ago to 23 cents currently, and that is before paying processor and sponsor bank fees.

In November and December 2012, the ATMIA and Kahuna ATM Solutions partnered for their third annual survey of independent ATM deployers. Respondents said their top concern is further reductions in interchange, followed by migration to EMV chip card technology and Americans with Disabilities Act lawsuits. Nearly one-third (31.4 percent) of the 108 respondents named proper accounting of interchange fees among their top three nonlegislative/compliance/network-related concerns.

According to the ATMIA, IADs account for around 50 percent of the ATMs in the U.S.

Networks

The card networks have been cutting their ATM interchange rates to win more market share among debit card issuers. In April 2010, MasterCard cut the interchange its card issuers paid for ATM cash withdrawals over the Cirrus network.





Visa tier structure for U.S. domestic approved ATM cash withdrawals, effective April 14, 2012

Fee program name	Minimum quarterly transactions	Interchange rates
ATM Level 1	24 million	\$0.35
ATM Level 2	3 million	\$0.42
ATM Level 3	less than 3 million	\$0.50

Prior to April 2010, MasterCard charged all MasterCard issuers a flat interchange fee of 50 cents per Cirrus withdrawal. Then the network introduced a tiered system, under which issuers are charged different rates based on their transaction volume. Issuers with small transaction volumes continue to be charged 50 cents, but larger issuers with higher transaction volumes are charged either 35 cents or 45 cents.

Visa and the regional debit networks such as STAR, Pulse and NYCE followed MasterCard’s example in cutting interchange rates. In April 2012, Visa replaced its two-tier structure with a three-tiered system. Under the new system, U.S. domestic Visa and Plus ATM withdrawals for the highest-volume tier fell from 50 cents to 35 cents — a 30 percent drop. For tier-two transactions, the interchange rate is now 42 cents; for tier three, the interchange rate remains 50 cents.

In addition to reducing interchange fees, the networks have significantly increased the acquiring fees they charge ISOs for providing access to their networks.

Visa raised its ATM acquiring fee in April 2012 from five cents to 15 cents, while MasterCard increased fees from five cents to 17 cents in April 2010. To cover their costs, ISOs are forced to pass on these acquiring fees to their clients by deducting them from the interchange the clients receive.

Lack of understanding

“A lot of retailers don’t understand that, because ISOs receive less interchange revenue, they have to increase their fees or restructure the profit sharing to merchants to compensate for their reduced income and cover their costs,” said Judi Suzuki, president of National Cash Systems. “The problem is that merchants don’t understand the financial dynamics of the ATM industry, so it’s difficult for them to grasp why their ISO’s fees are increasing.”

As most ISOs have had to restructure their interchange-sharing agreements with their merchants and affiliates, the result has been that mer-

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— Donna Embry, senior vice president, strategic development, at Payments Alliance International.



Fees paid by consumers, FIs and ATM owners to process ATM transactions

	Who pays	Who receives	Description
Surcharge fee	Consumer	ATM owner	Paid to the ATM owner by the consumer when using an ATM not owned by his or her financial institution
Foreign fee	Consumer	Consumer's financial institution	Paid to the consumer's financial institution by the consumer when using an ATM not owned by the card-issuing financial institution
Interchange fee	Consumer's financial institution	ATM owner	Paid to the ATM owner for the costs of operating and maintaining the ATM
Switch fee	Consumer's financial institution	EFT networks	Paid to the EFT networks for routing transaction information over the network
Acquiring fee	ATM owner	EFT networks	Paid to the EFT networks for the use of the network by the ATM owner

Source: U.S. Government Accountability Office analysis of Federal Reserve and industry documents. From the GAO report "Automated Teller Machines: Some Consumer Fees Have Increased."

chants have become dissatisfied and started to look for better deals from other ISOs. But Tente warned that it's fruitless for ATM deployers to shop ISOs for better rates on interchange.

"Once an ATM deployer gets used to receiving a certain level of interchange, and that revenue stream decreases, the deployer will be upset," says Donna Embry, senior vice president, strategic development, at Payments Alliance International. "But no-one should expect to receive the same revenue in perpetuity, as the ATM industry keeps changing. The good news is that there are a number of innovative ways to replace lost revenue from interchange, for example by offering third-party ATM advertising or co-branding with financial institutions."

National Cash Systems suggests that one way that IADs may be able to recoup lost interchange revenues is by increasing their cash withdrawal surcharges by 25 cents or less. Other options include selling additional products and services such as merchant services or offering check deposits or bill payments for a fee. It is important that ISOs explore these extra revenue-generating options with their clients.

Communications

To prevent loss of customers, ISOs need to do a better job of explaining that declining interchange revenue is an industry-wide problem that isn't





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— Judi Suzuki, president, National Cash Systems

confined to specific ISOs. It is also important for an ISO to educate customers about how interchange and network fees are structured and about the ISO's own cost base.

“Some ISOs are struggling to make money in the current environment, and some are getting out of the business,” Suzuki said.

Merchants might not realize that their ISO is charged a fee for all ATM transactions, including balance inquiries, account transfers and even ATM withdrawals that are denied because of incorrect PIN entry. In addition, ISOs pay around \$50,000 a year to register with Visa, MasterCard, STAR, Pulse, NYCE and the other EFT networks, plus fees to sponsoring banks and processors.

“ISOs should do a better job of explaining the changes in interchange to their affiliates and merchants,” Suzuki said. “They need to be knowledgeable about what they are actually receiving in net interchange and be as transparent to their merchants and affiliates about fee structures as possible, because, the greater the transparency, the more trust they will get from their merchants and affiliates.”

About the sponsor:

Since 1997, National Cash Systems has established many successful relationships with thousands of merchants nationwide. The company's successful track record in providing clients with turnkey ATM and comprehensive payment solutions has earned it a reputation for delivering quality products while exhibiting financial stability and expertise. Visit www.nationalcash.com for more information.