

HB 826

COMMITTEE REPORT

2/17/76

HOUSE

Mr. Speaker:

Date 4/21/76

The Committee on COMMERCE has had HB 826

under consideration. A Majority of the members of the Committee

( ) recommends it DO PASS

( ) recommends it DO NOT PASS

( ) recommends it DO PASS WITH ATTACHED AMENDMENT(S)

( ) recommends it BE REPLACED WITH CS FOR \_\_\_\_\_ AND THAT

CS FOR \_\_\_\_\_ DO PASS

( ) "and" recommends it BE REFERRED TO THE \_\_\_\_\_

COMMITTEE

( ) reports it back WITHOUT RECOMMENDATION

"other"

Members signing the Majority report:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Members NOT concurring in the Majority report:

\_\_\_\_\_ recommends:

\_\_\_\_\_ recommends: Do not pass

\_\_\_\_\_ recommends: Do not pass

\_\_\_\_\_ recommends: Do not pass

\_\_\_\_\_ recommends:

\_\_\_\_\_ Chairman

## DIRECTORY OF MERCHANTS OFFERING DISCOUNTS FOR CASH

### 1. ISSUES INVOLVED IN TWO-TIER PRICING

#### What Are Third-Party Credit Cards?

Third-party credit cards are issued to consumers by companies that guarantee payment of the selling price--minus a service fee--to the merchant who accepts a credit card for purchase of goods or services.

There are two major kinds of third-party credit cards: "travel and entertainment cards" (T and E) and "bank cards." T and E cards (such as American Express, Diners Club, Carte Blanche) are used mainly in restaurants and hotels. In contrast, bank cards (such as BankAmericard and Master Charge) are largely administered by local banks and are accepted by a wider range of merchants. In both cases, a third party performs certain administrative functions for the consumers who want to use the card and the merchants who want to accept it.

#### How Do Third-Party Credit Cards Increase the Selling Price?

Merchants who accept either type of third-party credit card agree to pay a service fee to the credit-card issuer or administering bank--a fee usually ranging from 2 percent to 5 percent (and sometimes higher) of the selling price. This fee, like other business costs, is reflected in the price that merchants charge their customers. Since the selling price is the same for all customers, shoppers pay for the costs of credit whether or not they use a credit card.

*File with  
Paper bill*

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### What Is the Difference Between Third-Party Credit Cards and Charge Cards Issued by the Merchants Themselves?

Some retail stores maintain their own charge-account systems, which customers may use to charge purchases bought from these retailers. Unlike third-party credit cards (such as American Express or Master Charge), these in-house charge systems involve no one else in the credit transaction beyond the retailers and their charge customers.

In-house charge systems can generate profits for the retailers, since it is the retailers themselves--and not a third party--who collect any interest that may accrue on credit sales. Many merchants, however, either do not have or do not rely exclusively on their own charge plans. It is primarily these merchants who might be persuaded to give discounts for cash purchases.

### Why Haven't Most Merchants Offered Discounts for Cash Purchases in the Past?

Before passage of the FCBA (see page 8), contracts between participating merchants and the credit-card company (for T and E cards) or the administering bank (for bank cards) often included provisions that prohibited merchants from charging a higher price to credit-card customers than to cash customers. Under such contracts, merchants could not offer discounts for cash payment, even if they wanted to.

### Why Were Such Contract Restrictions Unfair to Cash Customers?

A credit-card customer receives the special privilege and convenience of paying for a purchase weeks or months later. But

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because the same selling price is used for all customers, cash customers subsidize the credit-card customers' privilege of postponing payment. Moreover, a cash customer saves merchants money because merchants keep the full amount of a cash sale. With a cash sale, they don't have to deduct the service fee they pay to a credit-card company or bank for a credit-card transaction--and they don't have all the paperwork that goes with it.

In short, cash customers get less and cost a merchant less. It is only fair that cash customers should pay less.

### Don't Merchants "Absorb" the Cost of Credit Rather Than Pass It On to Their Customers?

Although the cost of credit is not shown on the price tag, it is an integral part of merchants' pricing decisions. It is taken into account in setting prices as part of the overhead--the general cost of operating a business. Merchants compute the selling price necessary, given competitive conditions, to assure an acceptable profit or rate of return on their investment. There can be no absorption of credit costs without passing them on to the customer, unless merchants reduce their profit margins, which is not likely.

### Won't Merchants Just Raise Their Prices and Then Discount to the Old Price?

Some may. But most will not, because conditions in competitive markets discourage them from increasing prices above the already prevailing market level. Merchants who raise their prices above that level risk losing business to their competitors.

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### What Will Happen to Prices If Two-Tier Pricing Becomes Widespread?

If the costs of third-party credit-card purchases are borne only by those who use third-party credit cards, the price of such a credit purchase may be somewhat higher than the prices under today's uniform price system. However, the price for a cash purchase would probably be somewhat lower.

### Won't Merchants Who Charge More for Credit Purchases Lose Business?

When some merchants grant discounts for cash payments and others do not, it is possible that those granting discounts for cash may lose some credit-card customers. Those merchants will also lose the extra income they formerly derived from cash customers under the old single-price system. However, those losses could be offset by a substantial increase in the number of cash-paying customers, particularly if the availability of cash discounts is well publicized.

### Why Would Merchants Want to Give Discounts for Cash Purchases?

Merchants who give discounts to cash customers may find that their sales volume increases significantly as a result of their discount policy. (For example, a 1974 survey sponsored by the Continental Illinois National Bank and Trust Company of Chicago found that 70 percent of consumers surveyed would pay cash instead of using credit if merchants offered discounts for cash purchases.) What's more, money from cash sales is immediately available to merchants without the time lag that results when merchants must forward their sales slips to credit-card issuers and await

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reimbursement. And with cash sales, merchants are relieved of the extra paperwork.

### 2. THE NEW LAW

In 1974, Consumers Union sued American Express and a Maryland bank administering BankAmericard. Consumers Union sought a ruling that provisions of the contracts between the third-party credit-card issuers and merchants that prohibited merchants from granting lower prices for cash were price-fixing arrangements in violation of antitrust laws. The lawsuits were settled, with American Express and the bank agreeing to notify their merchants that the challenged restrictions were no longer in effect. Similar agreements were arranged, in lieu of litigation, with Carte Blanche and with Central Charge Company and NAC Charge Plan (credit-card issuers in the Washington, D.C., area).

Although the Consumers Union lawsuits established the principle that merchants cannot be prohibited from adopting two-tier pricing, there remained two major legal obstacles to the widespread availability of cash discounts. First, other third-party credit-card issuers were not affected by the settlements. Second, merchants were hesitant to institute a two-tier pricing system because of concern that the granting of discounts to cash customers, while charging higher prices to those using third-party credit cards, might trigger the requirements of the Truth-in-Lending Act.

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The Fair Credit Billing Act (FCBA), which took effect on October 28, 1975, is intended to remove those two legal obstacles. Section 167 of the FCBA includes two important provisions:

First, the law declares unlawful all restraints, by contract or otherwise, of a merchant's freedom to use a two-tier pricing system for cash and credit customers. Thus the substance of the Consumers Union lawsuits has become law and now applies to all third-party credit-card issuers.

Second, the law states that the requirements of the Truth-in-Lending Act are not applicable to cash discounts of 5 percent or less. This exemption applies if the availability of discounts of 5 percent or less is conspicuously disclosed on the premises and is available to all prospective customers.

### After FCBA

Despite these victories, another obstacle still remains: Even with the passage of the FCBA, merchants are merely permitted to give discounts to cash customers; they are not required to do so. It is up to consumers to convince merchants that granting cash discounts is in the merchants' own interest.

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