

Fees! Fees! Fees!

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Companies can't raise prices, so they're socking consumers with hundreds of hidden charges--and that's creating stealth inflation and fueling a popular backlash

America used to be the land of the free. Now, it's the land of the fee. Companies, hard-pressed for money, are taking every possible opportunity to nickel-and-dime people to death. Need a monthly brokerage account statement mailed to you? Ameritrade (AMTD) may charge you \$2 per statement. Want your hotel room cleaned? The Alexander Hotel in Miami Beach, Fla., will bill you an extra \$2.50 daily for housekeeping. Have to return a new camcorder? Best Buy (BBY) Co. will dock you 15% as a "restocking fee." Want to buy a season ticket for pro football? The New York Jets will make you pay \$50 for the privilege of getting on their waiting list.

The U.S. economy has become sneaky. Inflation is officially low, but Americans face an ever-growing mountain of extra charges that are pushing up the true cost of purchases. No area is safe, from retail to finance to travel to sports. "You have companies charging fees for things that were free on an unprecedented scale," says Claes G. Fornell, marketing professor at the University of Michigan Business School.

The extra hits -- each one typically small by itself -- add up to big money. AT&T (T) could bring in as much as \$475 million by charging its long-distance customers a new 99 cents monthly "regulatory assessment fee." Fresh fees for services such as housekeeping will generate \$100 million for hotels this year, according to PriceWaterhouseCoopers. Fees on consumers who pay bills online bring banks an estimated \$2 billion. And credit-card late-payment fees -- up by 11% over the past year, on average -- could reach an astonishing \$11 billion this year, estimates investment bank R.K. Hammer.

The fee frenzy is mainly an attempt by Corporate America to escape the brutal price wars of the past few years. Companies can't raise list prices without losing business, so they are burying higher charges in the fine print instead. "It's much easier to raise a price through obscure fees and surcharges than it is to raise a sales price," says Stephen Brobeck, executive director of the Consumer Federation of America.

The plethora of stealth charges makes it much harder for consumers to use the Internet to do comparison shopping, as they started to do in the late 1990s. The result is that apparently simple buying decisions are turning into a hopeless and discouraging labyrinth. In response, frustrated consumers are fueling a backlash, including the creation of new vigilante organizations to pressure companies to roll back fees.

The growing significance of extra fees means that inflation is understated. Surprisingly, many add-on charges are not reflected in the Bureau of Labor Statistics consumer price index. One reason is that many companies, especially in airlines and telecom, haven't provided the BLS with a full breakdown of their charges. In addition, fees for such things as credit-card late payments and airline-ticket changes -- both rising -- are not included in the government's figures. The implication: Fears of deflation may be overblown. Instead, the true rate of inflation, so important for setting monetary policy, is probably higher than the 2% or so that the BLS is reporting.

State and local governments are also willing participants in the fee game. Rather than hike taxes, politicians are hitting up Americans with a bewildering array of fees, fines, and penalties. Cash-strapped states will pull in \$2.6 billion in new revenues this year by raising more than 200 different fees on everything from fishing licenses to fingerprint processing to driving with new tires. On Aug. 15, the fine for driving without possession of a driver's license in New Jersey jumped to \$173, up from \$44. Some of the charges are ridiculous: With some exceptions, blind

Massachusetts residents will now have to shell out \$10 once, and \$15 every five years, for certification that proves they are legally blind.

Already, the new wave of consumer outrage is having serious consequences for politicians. One reason California Governor Gray Davis lost so much support was the popular outrage after he hiked car-registration fees that he had cut several years ago. They will triple this year, to an average of \$234 annually, up from \$76.

Corporations are feeling the heat as well. A string of suits involving fee abuses filed by class-action lawyers, state attorneys general, and private groups like the AARP are under way. New York State Attorney General Eliot Spitzer made Sears, Roebuck & Co. and EchoStar Communications (DISH) Corp. pay millions of dollars to settle claims of excessive surcharges on recycling car batteries and undisclosed satellite-service termination fees. "We were not aware New York had a law capping the fee, and once we knew we changed it almost immediately," says Sears spokesman Bill Masterson. Echostar points out that there was no finding of wrongdoing and that it settled to avoid costly litigation. And a California Superior Court judge has ordered MasterCard and Visa to refund \$800 million to customers for charging hidden fees on purchases made in foreign currencies. Visa denies the charges and is fighting the ruling. MasterCard plans to appeal the suggested restitution procedures.

There are other signs that popular dissatisfaction with fees may finally be having an impact. Fees for using ATMs have been a bane of consumers for years. On Sept. 3, Washington Mutual (WM), one of the most aggressive retail banks in the country, stopped levying such charges on users of its ATMs in the New York area, even ones with accounts at other banks. Meanwhile, Congress is weighing tougher disclosure requirements for mutual-fund fees and for mortgage closing costs, which can be hundreds of dollars. "There are incredible abuses out there," says Housing & Urban Development Dept. Secretary Mel Martinez.

Fees have long been a fact of life in some industries, such as financial services and travel. Car renters, for example, are used to having their bills inflated by extra charges, such as gas-tank refill penalties.

But the urge to raise fees has gotten out of hand. One of the worst offenders is the telecom industry, which advertises cheap wireless and long-distance calling plans and then lards on extra charges that add 20% to consumers' cell-phone bills, on average. Many wireless-service providers are charging extra to help pay for new technology to enable customers to switch companies without giving up their phone numbers. Sprint PCS, for example, is charging 18 million customers \$1.10 a month, which would amount to \$238 million annually. Sprint refuses to confirm or deny the total. AT&T's regulatory assessment fee, charged to its long-distance customers, covers such items as property taxes and expenses associated with regulatory proceedings.

Phone companies justify their extra fees as the only way to cover expenses without losing customers. "Sprint's recovery of these costs via the surcharges will end when these costs are recovered as permitted by law," says spokesman Dan Wilinsky. Adds AT&T spokesman Bob Nersesian: "If you're advertising a higher rate based on your expenses, and your competitors are advertising a lower rate but adding various fees at the bottom of the line, what are you supposed to do?"

Other companies use charges to weed out unprofitable customers or to change their behavior. Some airlines have recently started charging passengers \$50 for paper tickets and \$25 for every bag over 50 pounds. Ameritrade's \$2 fee for monthly statements encourages people to wait for free quarterly statements or to get updates on their accounts online. And most online brokerages impose an extra fee on small-time investors who do not make a minimum number of trades. E*Trade Group Inc. and TD Waterhouse introduced in 2001 "maintenance" fees on brokerage accounts. "Our customers have access to streaming quotes, a rich set of research tools," says

Connie Dotson, E*Trade's chief communications officer. "If the account itself doesn't generate the revenues to offset the cost, then for that value we charge a maintenance fee."

Package-delivery companies such as United Parcel Service (UPS) Inc. and FedEx (FDX) Corp. have offset increased expenses by adding on fee after fee over the past few years. Starting in 1999, package-delivery companies charged \$1 per package for deliveries to remote areas. Now, they tack on "fuel surcharges" for the gas in the planes, trains, and trucks used to deliver packages. These fees are broken out on bills for regular customers, though not always for infrequent ones. Indeed, Airborne (ABF) Inc. has listed a 25 cents charge for handwritten airbills on its Web site even though the company says it doesn't charge it. "It covers us in case we do decide to charge the fee in the future," says spokesman Robert Mintz.

In the retail sector, fees take a different form. Target (TGT) Corp. and Best Buy Co. make customers pay a "restocking fee" of 15% for the privilege of returning electronics items such as camcorders, laptops, and radar detectors. Although neither Target nor Best Buy will disclose how much they earn from such fees, it's not small change for consumers. Best Buy justifies the penalty as a way to discourage people who would take the camcorder, say, and return it after using it once. Target did not return repeated calls.

So many people have asked about these restocking fees that Massachusetts' consumer-affairs department posted an alert about the practices on the Web in August. It warned that some retailers made people pay such fees even when they bought a defective product. "That's illegal," says Tatum Zuckerman, at the state's consumer hotline.

Not to be outdone, the original leader in fees, financial services, is finding new ways to raise revenue from customers. The growing dependence of banks on fee income has spawned a new breed of consulting, such as at Houston-based Strunk & Associates LP, which helps banks find new sources of revenue. One example: offering protection against bouncing checks, for a fee. Strunk justifies such fees as a way to improve customer service.

No one can beat the credit-card industry for its fee inventiveness. Deadlines for paying bills have been shortened to as little as two weeks, and they're strictly enforced, producing more late fees. Not coincidentally, the number of credit-card issuers with \$35 late fees doubled last year, says Consumer Action. People can avoid late fees by paying their bills over the phone or online. But some banks and credit-card companies charge for that, too. Washington Mutual charges virtually all of its customers a total of \$60 a year to pay their bills online. And it costs \$15 to pay bills at the last minute over the phone at MBNA Corp. and Provident Financial (PVN) Corp. MBNA and Provident say it takes staff time to process these payments by phone and that customers can pay online for free.

It does make sense to charge a premium for added services that cost more to provide, rather than force all customers to pay the same amount, whether or not they use the extra services. Splitting out such fees helps keep basic costs low. One example: charging extra for airline food. United Airlines Inc. has been trying out making passengers on certain flights pay \$10 for chicken sandwiches supplied by TGI Friday's and meals from Eli's Cheesecake. Northwest Airlines and US Airways Group Inc. have also started to charge for food. "It's proven to be extremely popular," says US Airways spokesman David Castelveter. "Customers have a choice."

But many fees have no such justification, and ultimately, the niggling could cost companies their customers. Consider Natalie Armstrong in Gorham, Me. She and her husband have been back to Sears only once since her husband Lester was ambushed in January by \$29 in late-payment fees along with a \$1 "service" charge from a Sears credit card for a \$14 part for his saw. After he convinced one clerk that his payment was actually on time, the company hit him with \$30 more in fees. In the end, he handed over \$60 in cash to a salesperson. After being contacted by BusinessWeek, Sears pledged to refund the late-fee charges.

Some banks are backing down after a barrage of criticism. Bank of America stopped charging customers to pay bills online last May when it discovered it could get more of their business if it offered the service for free. Last December, Bank One (ONE) Corp. ditched a \$3 charge for no-frills checking-account customers to use a branch teller when it discovered that irate customers were bolting to rivals. "Imagine if you are a retail store and your goal is to sell sweaters, and you're charging admission," says Charles W. Scharf, president and CEO of retail banking, who changed the policy after he got his job in May, 2002. "It's counterproductive."

Still, many businesses are holding firm. The New York Jets responded to fans outraged over the waiting-list fee by announcing that people lucky enough to get season tickets could deduct the \$50 they paid for waiting for them. The goal of the fee, says the Jets, is to prune the list to fans who are genuinely interested in buying tickets. "Some people aren't even alive who are on the list," says spokesman Ron Colangelo.

Nobody figures fees will be eliminated entirely. But as the country recovers from an era of corporate scandal, it's not too much to ask that companies keep prices easy to understand. That way people will know they're getting what they pay for.

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