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## TITLE

From Exchange Rates to Actual Charges

## TOPIC

This article explains some of the differences between "interbank" ("official") exchange rates and the conditions which in practice are applied by banks and credit card companies when buying and selling small amounts of currency.

## DISCUSSION

The exchange rate information published daily by newspapers, central banks and other public sources is based on an average of interbank transactions, which occur electronically. These conditions, in which the difference (or spread) between the bid and the ask (or buy and sell) price is between 0.03% and 0.07%, are usually applied only to transactions of one million dollars or higher.

When exchanging small amounts of cash at a local bank branch, the rates are usually about 4%-5% less favorable than the interbank rates. This percentage, which is reduced as the volume increases, represents the bank's revenue on the transaction.

When a credit card is charged in a currency other than the cardholder's charge currency, the cost of the conversion is between 1% and 3%. This means that the exchange rate which is applied when the card is charged, and which gets printed on the card statement, is by about 1%-3% less favorable to the cardholder than the interbank rate.

For example, if Robert from Germany uses a credit card linked to his German bank account to buy \$100.00 worth of goods from the United States, his card is likely to be charged \$100.00, but his credit card statement will show the equivalent of about \$102.00 (which he settles in German mark). An exchange commission of 2% is of course quite good, compared to what banks charge for exchanging small sums of cash, but Robert might wonder why the charge is not exactly the same as one would obtain by applying the "official" exchange rates.

We have asked a major credit card company (which will be referred to as "CardCompany" in the following) to explain the process:

*"Currently CardCompany exchange rates are not make publicly available. However, to determine the exchange rate for CardCompany transactions, CardCompany uses a wholesale market rate or a government mandated rate in effect one day before our system's processing date. Added to this 'base' exchange rate, CardCompany assesses the Member financial institution a 1% conversion fee. The bank may or may not pass this cost along to the cardholder. This would be indicated in your credit card agreement or disclosure statement.*

*In addition, a Member may request that our system calculate an additional percentage to cover any costs they incur as a result of converting a foreign transaction. This fully loaded figure is the exchange rate sent to the Member bank that is ultimately charged to the cardholder. For specific information regarding how the exchange rate will be applied to your account, please contact the financial institution that issued your CardCompany card."*

In practice, by asking a few card issuing organizations we determined that the above tends to result in a 2% premium. The maximum exchange commission we could

verify with different cards was about 3%.

Exchange commissions do not apply between European Economic and Monetary Union currencies (e.g. to and from mark and euro, or franc and lira), although a "service charge" may be applicable when converting cash.

#### Related Links

- [Foreign Exchange Markets and Terminology](#)
- [Exchange Rate Information and Disclaimers](#)
- [Considerations on Exchange Rate Data Providers](#)
- [The Euro](#)

#### Article Information

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