

You need to enable JavaScript to run this app. Your request is being processed. Please wait. FDIC-Insured - Backed by the full faith and credit of the U.S. Government Accept Mail Offer See If You Pre-Qualify For What's Ahead Customer Service Sign In Credit One Central Categories Credit Education Personal Finance Life Events Financial Planning Glossary Home Blank Personal Finance Credit Card Annual Fees and Why They're Charged Author: Sean P. Egen March 12, 2020 Topics: Credit Card Nobody likes fees. Check that. Nobody likes paying fees. Businesses that charge fees like them because they help offset the costs of doing business and hopefully contribute toward a business bottom line. Many of the fees we pay, we consider justifiable. For example, your health club charges you a fee for the cost of buying and maintaining workout equipment and keeping the building up and running. Your state's department of motor vehicles charges a fee to process and issue you a driver license. Your homeowners association charges fees to maintain common areas of your neighborhood and to prevent your next-door neighbor from painting his house a shade of lavender that could drive your home's value down. But when it comes to an annual fee for a credit card, some people feel this particular fee is not justifiable. Well, I'm prepared to make the case that there are actually valid reasons for charging a credit card annual fee. Two, to be precise. REASON #1: YOUR CREDIT CARD OFFERS VALUABLE BENEFITS The main benefit most all credit cards offer is that they provide you with instant credit for making purchases. But all credit cards are not created equal. Some offer perks and benefits that others don't. Rewards Credit Cards A rewards credit card is a prime example of a card that provides valuable benefits above and beyond that of a basic, no-frills credit card. With a rewards card, you earn rewards just for making purchases with that credit card. The rewards you earn can take multiple forms depending on the credit card, including cash back rewards, points, or even airline miles. Rewards are typically earned as a percentage of purchases made with the credit card or as X points or airline miles awarded for every dollar you spend. So, for example, if you have a rewards credit card that offers two percent cash back rewards, you would earn a \$2 rebate typically redeemable for a statement credit for every \$100 in purchases you make with that card. Or, if you have an airline mileage credit card that rewards one mile for every dollar you spend, spending \$100 with that particular card would earn you 100 airline miles redeemable for air travel or other rewards. If a credit card issuer is giving you cash back rewards or points or miles redeemable for trips, gift cards, or more, doling out those rewards costs them money. That's where a rewards credit card annual fee comes into play. By charging cardholders an annual fee for the opportunity to earn these rewards, credit card issuers are creating a revenue stream to help them pay for the rewards programs they sponsor. So, is the annual fee for one of these rewards cards actually worth it? Well, that all depends on you and your spending habits. Say your annual fee on a 2% cash back rewards credit card is \$100. In this case, you'd have to earn at least \$100 in cash back rewards over the course of the year just to break even on the annual fee. Which means you'd have to spend at least \$5,000 on eligible purchases (2% of \$5,000 equals \$100) annually. Spend any more than \$5,000 on eligible purchases with that same cash back rewards card, and that \$100 annual fee becomes a good investment because you will have earned more in cash back rewards than you spent for the opportunity to earn those rewards. Of course, the annual fee is only one fee that may be associated with a rewards credit card. To figure out if the rewards you're earning are ultimately worth the total cost of a rewards credit card, you also need to figure in any interest and other fees, such as late fees, you're paying in order to earn those rewards. But we'll save that discussion for another day. Suffice it to say that, in order to determine if an annual fee you're paying for a rewards credit card is worth it, it should, at the very least, be less than the minimum you expect to earn in rewards over the course of a year with that credit card. Other Credit Card Benefits Even credit cards that don't offer rewards offer perks and benefits that cash simply can't. For example, many credit cards offer zero fraud liability, which cash does not. They may also offer benefits such as no foreign transaction fees when traveling internationally, purchase protection, free credit score information, supplemental rental car insurance, and more. And the one benefit most all credit cards offer is that they report your payment history to the three major credit bureaus, which can help you to build credit and hopefully develop a healthy credit score. This is something neither cash nor debit cards can do for you. If you value these additional benefits, then the price of an annual fee for a credit card may well be worth it to you. REASON #2: YOUR CREDIT CARD ISSUER IS MITIGATING THEIR RISK If your credit is limited, or isn't good, and your credit score falls into the middle or lower end of the spectrum, you may discover that most of the credit cards for which you qualify charge an annual fee. Well, there's a reason for this, and it primarily has to do with the risk you represent to the credit card issuer. While there's also risk associated with granting credit to people with positive payment histories and higher credit scores, these folks have something that those with limited or mediocre-to-bad credit do not: a proven track record. A positive history of using and managing credit makes an applicant at least appear to be less risky to a credit card issuer and presents that applicant as a more attractive candidate to receive credit. But if you have little or no history with using credit, or your history demonstrates a lack of commitment to making consistent on-time payments, you may not qualify for a credit card with no annual fee. Annual fees charged by issuers that provide credit cards to people with little or less-than-ideal credit help these issuers lessen their risk. They are anticipating having more late or missed payments and higher default rates than they would serving people with higher credit scores. The annual fees help to offset the higher cost of serving

customers without proven track records of using and managing credit responsibly. When you think about it, its not dissimilar to a bank or finance company charging a borrower with so-so credit a higher rate of interest and less-favorable terms on an auto or home loan than they would another borrower with great credit. Only, in their case, there is an actual piece of collateral a car or home that can be repossessed should the borrower fall behind in payments or default on the loan. While credit card issuers may also charge higher interest rates to those with lower credit scores, they dont have the option of repossessing every item bought with their card from cardholders who miss payments or stop paying altogether. Annual fees help credit card issuers to mitigate risks and lower their cost of doing business with a riskier clientele. While Im sure I havent convinced you to love credit card annual fees (never my intention), hopefully you at least understand why they exist and that, yes, there are valid reasons for their existence. If you have good credit, chances are youll be able to find a credit card out there that meets your needs and doesnt charge an annual fee. Or at least one that offers benefits that outweigh the cost of the cards annual fee. If your credit isnt great, the good news is that, by using a credit card with an annual fee responsibly as in making consistent on-time payments every month and effectively managing your credit youll hopefully soon be in a position to qualify for a credit card with no annual fee. Or, again, one offering benefits you feel are well worth the cards annual fee. Looking for a credit card to help you build a positive credit history? See if you Pre-Qualify for a Credit One Bank card in less than a minute without harming your credit score! About the author: Sean P. Egen After realizing he couldnt pay back his outrageous film school student loans with rejection notices from Hollywood studios, Sean focused his screenwriting skills on scripting corporate videos. Videos led to marketing communications, which led to articles and, before he knew it, Sean was making a living as a writer. He continues to do so today by leveraging his expertise in credit, financial planning, wealth-building, and living your best life for Credit One Bank. This material is for informational purposes only and is not intended to replace the advice of a qualified tax advisor, attorney or financial advisor. Readers should consult with their own tax advisor, attorney or financial advisor with regard to their personal situations. Recommended Articles 7 Common Credit Card Fees: Why Banks Charge Them & How to Avoid Them How a Cash Advance Works & Its Pros and Cons What Happens When You Make a Late Credit Card Payment? Credit Cards Browse Credit Cards See If You Pre-Qualify Accept Mail Offer Application Status Support FAQs Contact Us Accessibility Credit One Central About Us Company Partnerships Community Careers Testimonials Credit One Bank Mobile App Privacy Terms of Use Security & Fraud Card Agreements 2025 Credit One Bank, N.A. All Rights Reserved. Member FDIC. This is a secure site.