

IS AN ISO LIABLE FOR THE ACTIONS OF ITS INDEPENDENT SALES AGENTS?

By Paul A. Rianda, Esq.

Most ISOs and banks believe that by virtue of an independent contractor agreement between them and their sales agents, that they are not liable for the actions of their sales agents. However, this often is not the case. From a legal and practical perspective, if an agent engages in misconduct it is often the ISO that pays the bill.

Under most circumstances, when an ISO begins its relationship with a sales agent, the parties enter into an independent contractor agreement. This agreement sets forth the duties and responsibilities of the parties and usually includes a clause that states clearly that the sales agent is an independent contractor, not an employee, of the ISO. Ironically, although intended to be independent contractor agreements, many agreements between ISOs and sales agents are titled “Agent Agreements”.

Generally, this type of independent contractor relationship would serve to insulate the ISO from any liability it would have for the actions of the sales agents. However, general business practices in the bankcard business often times leads to situations where third parties sue ISOs in spite of this independent contractor relationship.

Legal Liability For Acts Of An Agent

Generally, anyone may appoint an agent to act for him or her in most any capacity. What that means is that the principal authorizes the agent to act on his or her behalf, often times in the context of entering into business relationships. This agency can take two forms – actual agency and ostensible agency. Actual agency is where the agent is directly employed by the principal. This is not the focus of our discussion because usually a sales agent is not employed by an ISO. Instead, we will focus on the legal theory of ostensible agency because it allows a principal to be liable for the actions of an agent when the principal intentionally, or through want of ordinary care, causes a third person to believe that another is the principal’s agent.

In order to be liable as a principal for the acts of an agent, the following factors generally must be present:

- The third party dealing with the agent must believe in the agent’s authority, and the belief must be reasonable;
- The belief must be generated by some act or neglect of the principal sought to be charged;
- The third person in relying on the agent’s authority must not be guilty of negligence.

From a legal perspective, the law of ostensible agency creates a situation where an ISO can be liable for the actions of its sales agent, even though the agent is not an employee of the ISO. Generally, especially for the smaller sales agents, they must sell and market their goods and services under the name of the ISO. Consequently, you have an independent sales agent with business cards, stationary, and advertising materials that bear the name of the ISO, not the agent. Consequently, a third

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party dealing with this sales agent can easily come to conclusion that it is dealing with the ISO and not the sales agent.

The documentation for a standard transaction between a merchant and a sales agent usually continues to build a case for ostensible agency. All the applications that are signed by the merchant generally have the name of the ISO and member bank on them, and make no mention of the fact that the person completing the sale is an independent contractor. Generally, all the contact phone numbers are for the ISO and not for the sales agent. When the transaction is completed the merchant often begins dealing with the ISO and not the sales agent. This again tends to strengthen the conclusion in the merchant's mind that the ISO and the sales agent are one in the same.

Practical Aspects of Agency Theory

Regardless of whether or not an ISO is able to eventually prove that the sales agent was not an ostensible agent, the ISO is likely to be one of the first parties sued in a lawsuit by a merchant or any other third party aggrieved by the sales agent. As a practical matter, since the merchant has only been dealing with the ISO for the most part, the merchant will attribute any acts of the sales agent, be they fraudulent or otherwise, to the ISO. I have had personal experiences on a number of occasions where sales agents have engaged in some questionable activities and the merchant has immediately sued the ISO for reimbursement of any damages that it has suffered. If the sales agent can no longer be found, the merchant will be looking to the ISO as a "deep pocket" for recovery.

In order to minimize the potential for such liability, it is imperative that ISOs notify merchants that its sales agents are indeed independent contractors. In the real estate industry, the larger national real estate broker franchises have sought to minimize their liability by setting forth in their advertisement, "that each office is independently owned and operated". ISOs and member banks need to get this message across to the merchants in order to minimize their potential liability. Clearly stating on the merchant application or other paperwork that the sales agent is not an authorized agent of the ISO, would serve to provide additional protection for the ISOs in the industry. It may not insulate an ISO from being sued, but at least it will give its lawyers additional ammunition in order to defeat any lawsuit brought by a merchant for the actions of a rogue sales agent.

This is not a situation where there is any easy answer for an ISO to avoid liability. But, understanding the potential for liability, and then working to minimize it is in the best interest of the ISO, sales agent and the merchant.

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