

PROTECT YOUR RESIDUALS IF YOUR ISO SELLS OUT

One common concern expressed to me by sale agents is what will happen to their residual payments in the event their ISO sell its portfolio of merchants or sells its entire company. Below, I will discuss the likelihood of a sales agent actually losing its residuals in such a situation and some ways for a sales agent to protect those residuals.

When a sales agent submits merchant accounts to an ISO, the sales agent expects to be paid for the revenue derived from those merchants for so long as those merchants continue to process with the ISO. However, it is very common in the bankcard industry for ISOs to sell their entire companies or to sell off specific portfolios of merchants. Such a sale may involve an ISO selling merchants to a purchaser, where the profits from those merchants is currently being split with its sales agents. The question then becomes that upon such a sale by the ISO, will the selling ISO's sales agents continue to receive their residual payments for the merchants that are sold by the ISO?

In the vast majority of cases, when an ISO is sold the sales agents are not impacted by the sale and continue to receive their residual payments. The company that purchases the ISO usually takes over all the contractual obligations of the ISO as part of the sale. Included in those obligations that are assumed by the purchaser of the ISO, is the contractual obligation to continue to pay all the sales agents of the ISO their monthly residual payments.

The purchaser of the ISO understands that it is only purchasing the right to the ISO's portion of the residuals derived from the merchants. For instance, where an ISO is splitting the profits derived from the merchants with 70% of the profit being paid to the sales agents and 30% to the ISO, the purchaser is in effect buying the right to receive only the 30% of the profits that are rightfully the property of the ISO. The remaining 70% of the profits derived from the merchants continue to be paid to the sales agents. Purchasers of large portfolios of merchants or ISOs do not want to be faced with multiple lawsuits filed by sales agents that had their residuals terminated due to a sale.

A problem can arise when the ISO sells off a portfolio of merchants and sells 100% of the profits derived from the merchants. Some purchasers do buy 100% of the profits and then make the selling ISO liable to the extent that any of the sales agents make a claim for their rights to the sales agents' portion of the residual that the purchaser is now receiving. I find that this usually only occurs with smaller ISOs that sell out while in the midst of some type of financial problems.

What generally happens in this situation is that the ISO sells the portfolio and then informs its sales agents that they are no longer entitled to their residual payments. Some ISOs just leave it at that and do not pay their sales agents any part of the purchase price. The ISOs know that often it can get away with this if most of its sales agents are small

and therefore cannot pay the legal bills in order to sue the ISO for the sales agent's unpaid residuals. Other ISOs will offer to pay the sales agent a one-time buy out which is usually a much lower multiple of the monthly revenue than the selling ISO received from the purchaser.

A sales agent has a few options to protect itself from losing its residuals if the ISO where it places its business sells a portfolio of merchants or its entire company. The easiest and best way for a sales agent to protect itself is to only submit merchants it originates to a large, reputable ISO. If you are dealing with a large ISO, it will have sales agents with large residuals that would be able to fund a lawsuit if the ISO just decided to sell the merchants out from under all its sales agents. The fact that the ISO has sales agents that have large residual streams makes it extremely unlikely that the ISO could successfully sell the merchants, quit paying its sales agents and not be sued in the process.

An additional safeguard is to make sure the proper protections are in place in the Agent Agreement. The first provision that needs to be reviewed is the assignment provision. The assignment provision dictates the circumstances under which the ISO may assign its duties under the Agent Agreement to another party. The assignment provision will often state that the Agent Agreement cannot be assigned by either party. Such a provision is a good start to protecting a sales agent.

Another issue the sales agent should address in its Agent Agreement is to make sure there is a provision that states that upon any change of control of the ISO (such as a sale of all of the stock of the ISO), the ISO still has to continue to fulfill all its obligations under the Agent Agreement. Although the sales agents may like to have the right to reject any change of control in its ISO, this type of restriction is very unlikely to be granted.

If the contract allows for the ISO to assign the Agent Agreement, at a minimum the provision should also provide for any assignee of the Agent Agreement to assume all the obligations of that ISO. The most advantageous provision for the sales agent however, should state that even if the ISO assigns the Agent Agreement to another party, the ISO still has a duty to fulfill its obligations under the Agent Agreement in the event the assignee fails to do so.

The other type of provision I like to add to the Agent Agreement provides that even if the ISO sells its residual stream and the residual stream of its sales agent associated with a portfolio of merchants, that the ISO must continue to pay its sales agents their portion of the residual stream. This ensures that at least if the ISO sells the entire portfolio residual, the ISO cannot use the excuse that since it is no longer getting paid that it has no duty to continue to pay its sales agents.

Under most circumstances, a sales agent has little chance of losing its residual payments in the event of the sale of its ISO. By picking the right ISO and adding some of the provisions mentioned above to the Agent Agreement, the sales agent can reduce that risk even further.

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