

WHAT MAKES MERCHANTS VALUABLE?

My clients often ask me what steps they can take when building their portfolio of merchants to make the portfolio as valuable as possible to a potential purchaser. Some items to consider when building your portfolio to make it attractive to purchasers are your rights to move the merchants, the processing platform, the merchant quality and the size of the portfolio.

The main focus of this article is concerned with the value of a portfolio of merchants developed by a sales agent or ISO that is originating in the range approximately of 100 to 300 merchants per month. In that size range, the sales agent or ISO is not usually contracted directly with a bank. Instead, it has a relationship with one of the larger ISOs or credit card processors. I will also discuss the sale of merchants and the merchant agreements. This discussion does not contemplate a mere sale of the right to be paid the residual stream associated with the merchants, which is usually a much less valuable transaction to a potential seller.

Right to Move Merchants

Probably the most important thing you can do to increase the value of your merchant portfolio is to obtain the right to move your merchants. There are usually two components that affect the right to move the merchants. First, you must have the right to assign the merchant agreements to a potential purchaser. Since the sponsoring bank must always be a party to the merchant agreement, you must get the bank's consent to assign the merchant agreement in addition to getting the consent of the ISO if you are not in a direct relationship with a bank.

Second, having portability means segregating your merchants in a separate BIN and ICA. By doing this, it makes it easier to move the merchants to another credit card processor without having to reprogram the merchants. This may be less of a concern to purchasers that already operate on the exact same processing platform as you do.

ISOs are not usually willing to give an agent or smaller ISO an unequivocal right to move merchants right away. You must usually wait until at least the end of the initial term of your agreement, usually three to five years, before most ISOs will allow you to move merchants.

The value to a potential purchaser in being able to move the merchants relates mainly to the money it can save from combining your merchants with its existing merchants. If an existing ISO buys a merchant portfolio, it usually does not have to hire too many more people to provide the main customer service and risk functions that the seller had been providing. Consequently, the purchaser can earn more money from the same merchants because its costs are lower.

In addition, the purchaser may be able to use its pricing for the merchants that may be more favorable than the seller's pricing. Again, we are assuming a smaller ISO or agent is selling to a larger ISO. As a rule, larger ISOs are able to obtain better pricing than smaller ISOs and sale agents. As a result, when the large ISO buys the seller's merchants, it can apply its better pricing to allow it to make more profit from the merchants than the seller was able to collect.

Processing Platform

What processing platform you select can also have a large impact on the value of your portfolio of merchants. For example, the First Data platform has traditionally been used by ISOs and banks that have the lion's share of processing relationships in the bankcard industry. By setting yourself up with a bank or ISO that is processing through First Data, you may make yourself more attractive to a larger group of potential purchasers since more ISOs and banks process through the First Data platform than any other platform. The logic is that if you pick one of the other smaller processing platforms, then the group of potential purchasers is much smaller. Of course, there are exceptions to this rule to the extent that some ISOs on smaller platforms are aggressively seeking agents and ISOs to purchase.

Merchant Quality

It seems obvious, but the higher the quality of the merchants, the better price you can expect to get for your portfolio. The market generally values retail merchants more highly than it does mail order/telephone order (MO/TO) and internet merchants. In addition, merchants that rarely if ever process credit card transactions, but just pay their monthly minimum and statement fees are generally less valuable. However, this it not to say these types of merchants should be avoided.

The non-processing, internet and MO/TO merchants can sometimes be easier for you acquire than retail merchants. This in turn will allow you to increase the overall number of merchants with less expense than if you only acquire retail merchants. As will be explained below, having a small percentage of these "less desirable" types of merchants in your portfolio may not have a big impact on your overall merchant value but may increase your merchant count leading to a more valuable portfolio overall.

Other important aspects of merchant quality relate to the "seasoning" of your portfolio and whether you have any large merchants. The "seasoning" refers to how long the merchants have been in your portfolio. The logic is, that the older the merchant, the more likely it is to continue to process with you, thus making the merchant more valuable. In addition, purchasers try to avoid portfolios that have too many large merchants. The reason is that if a portfolio is dependent on just a few merchants for a

large amount of its processing and profits, there is a large risk those merchants could leave and greatly impact the value of the portfolio.

Portfolio Size

Portfolio size is something that is also of great importance to building portfolio value. Simply put, many purchasers will not entertain purchasing a portfolio that is below a certain size. You must be able to build up a portfolio of substantial size (at least 2,000 to 3,000 merchants) before any of the larger purchasers will be willing to consider purchasing your portfolio. The commitment of time to purchase a portfolio of merchants and the costs associated with the purchase, do not warrant the effort unless the portfolio is of sufficient size.

These are not all the factors one needs to consider when mapping out a strategy to maximize the value of a portfolio of merchants. However, they are a good starting point and each should be carefully considered to allow you to get the biggest check possible on the sale of your portfolio.

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