

SELLING YOUR MERCHANTS OR YOUR RESIDUAL STREAM

By Paul A. Rianda, Esq.

Whether or not you can move your merchants to another credit card processor or sell the revenue stream derived from your merchants to another party is usually one of the most important provisions to a merchant level sales person when entering into a contact with a credit card processor.¹ Below I will discuss the contractual provisions governing these issues, the practical aspects of moving merchants and also issues to be aware of if you sell your merchants or residual income.

Contact Terms:

The first important issue in analyzing any contract is to make a differentiation between contractual provisions governing the movement of merchants and those that address the sale of the residual stream derived from your merchants. Most contracts only deal with the issue of whether or not the sales agent is allowed to sell the revenue stream associated with the merchants. Such a provision allows the sales agent to assign its payments under the contract to another party. This is not the same as the right to move the merchants to another credit card processor. Most contracts only provide for, if anything, assignment of the residual stream and do not allow movement of the merchants to another credit card processor.

Many older contracts do not allow for the sales agent to move the merchants or to assign the revenue stream. This was the standard practice in the industry for many years but has fallen into disfavor in the last few years. Merchant level sales persons have become much more knowledgeable. They are, rightfully so, demanding that at a minimum they be allowed to assign the revenue stream associated with the merchants to another party. This allows the sales agent to have an exit strategy wherein it potentially can receive a large payout on its merchants without having to wait for continual monthly residual payments.

The most common provision that I have seen recently allows for the assignment of the revenue stream associated with the merchants by the sales agent, but with a right of first refusal on said sale in favor of the credit card processor. This is advantageous to the extent that it allows the sales agent to receive a bulk payment for its merchants and “cash out” without having to worry about the future collection and risk associated with the revenue stream. In addition, the right of first refusal by the credit card processor usually is of little importance to the sales agent, since the sales agent generally does not care if it is paid by the credit card processor or the entity that has made an offer for the revenue stream.

Less common is a right on behalf of the sales agent to actually move the merchants to another credit card processor. This right is rarely granted by ISOs or the processing networks because of the large values associated with an established portfolio of merchants. If indeed ISOs and other associated entities did allow for the movement of merchants, it could substantially reduce the value of their

¹ This article is written from the perspective of a “feet on the street” sales person and addresses contractual issues that would benefit them.

companies and endanger their business models. For these reasons, an actual right to move merchants in a contract is almost never granted.

Non-Compete Provisions:

It is important to make sure that any ability to assign the revenue stream or move the merchants does not run a foul of the non-compete provisions in the contract. The non-compete provisions, for the most part, do not allow the sales agent to engage in any conduct, direct or indirect, that moves a merchant to another processor. This prohibition usually is in force for so long as the agreement is in effect plus three to five years after the agreement is terminated. Consequently, once the merchants are placed with a credit card processor it is nearly impossible to move them to another processor without violating these provisions.

Any non-compete provision in the contract should make allowances for the ability to move the merchants or assign the revenue stream as set forth in the agreement. This cross-reference is necessary to make sure that there is no ambiguity in the contract as to the effect of the non-compete provision. In addition, it is prudent to add into the non-compete provision an exception allowing the sales agent to move merchants that are not happy with the credit card processor. For instance, as is often the case, after a credit card processor holds funds, the merchant wishes to move to another credit card processor. Under these circumstances, there should be an exception in the non-compete provision that allows the sales agent to move the merchant to another credit card processor. This type of situation occurs fairly regularly. Consequently, such a provision is essential to avoid any situation wherein the credit card processor could cease paying the residual of the sales agent, based upon a breach of the non-compete provision.

Sale of the Portfolio:

If indeed you do sell your revenue stream or the merchants in your portfolio, it is imperative that you structure the sales agreement to minimize your exposure for the continuing liabilities associated with merchants. When selling a portfolio, often the credit card processor will want you to continue to guarantee payment of any losses associated with the merchants, such as charge backs. Of course, it is in your best interest not to allow any such provisions. However, most credit card processors will insist upon such a continuing obligation. In order to alleviate the effect of any continuing obligation, the transaction should be structured so that you are provided indemnity from such obligations by the entity that is purchasing your portfolio. In addition, you should also obtain the consent of the credit card processor to pay for any such losses first out of the residual stream from the merchants in the portfolio. This will at least minimize the exposure to you, to the extent that as long as the merchants are still making money for the credit card processor, you will not be obligated to make good on any losses associated with the merchants.

Issues relating to the sale of a merchant portfolio and the revenue stream associated with the portfolio are key items to keep in mind both when entering into any agreements with a credit card processor and also upon any sale. The provisions related to these issues are critical to the extent that if

Portability of Merchants

you are not provided with the right to sell your merchants or residual stream, the value of your portfolio to you could be substantially diminished. Therefore, it is important to make sure that when you enter into an agreement with a credit card processor, the contract reflects your wishes as far as merchant portfolio portability so that you can derive maximum financial gain from your portfolio.

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