Merchant Accounts - What You Should Know

June 2022

IntelliPay™

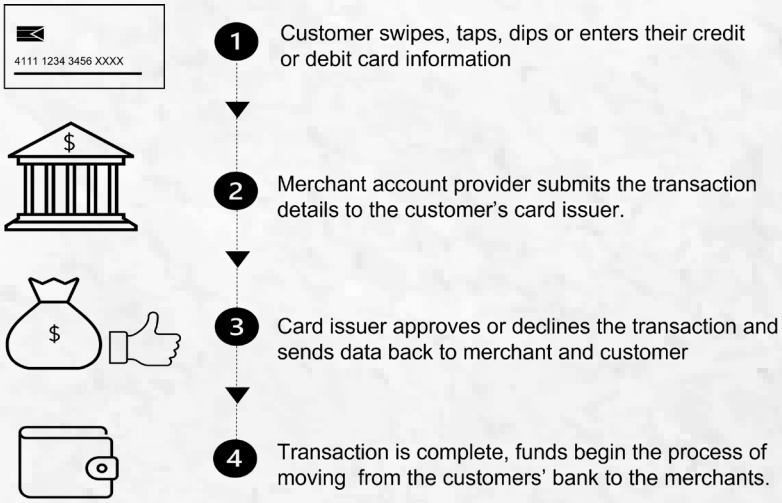
What is a Merchant Account?

A Merchant Account is a contractual relationship a business has with a bank to allow acceptance of card payments.

The bank that approves you for a merchant account is called an Acquiring bank (Acquirer) - they acquire your money for you. Acquirers must be member banks of a card association or network. The two largest networks are Visa and Mastercard.

A Merchant Account is NOT a business checking account. However, you must have a business checking account for the merchant account to deposit money from your credit and debit card sales.

Merchant Account Basics - Card Payment Processing



Your merchant account must come from a network member bank and can be originated by the bank directly, or more likely, through one of their sales agents, sometimes called Independent Sales Organizations (ISOs) or Merchant Service Providers (MSPs).

A merchant account is a contractual relationship a business has with a bank to accept card payments

Types of Merchant Accounts

There are five types of merchant accounts:

- Retail Merchant Accounts
- Internet/ E commerce
- Mobile Merchant Accounts
- Telephone Merchant Accounts
- Mail Order Merchants Accounts

Retail Merchant Accounts
A retail merchant account is a merchant account approved for use in a physical store where the cardholder and the card are present. Typically, the customer swipes, dips, or taps the card through a card reader to get the card information; this type of account is also referred to as a "swipe" account or "card present" account.

Merchant accounts typically have lower fees since the card owner is present and are considered less risky than other card-not-present types of merchant accounts.

Internet/E commerce
Internet/E commerce accounts are used for merchants who do not have a physical location and conduct business online.

Since the payment information is entered through a digital interface, the merchant can't physically see the card and the cardholder.

So, the merchant can't verify the cardholder's identity. As a result, there is an increased risk of chargebacks and fraud, and the merchant fees are also higher.

Mobile Merchant Accounts
Mobile accounts are ideal for businesses who travel to other locations to do business, such as food trucks, tool trucks, or industry show vendors.

Mobile accounts allow merchants to receive payments on their mobile device, typically a small reader that integrates with a smartphone.

Mobile accounts are easy to set up; however, the transaction fees can be higher.

Telephone Accounts
If your business is online, retail, or mobile, and you need to accept card payments over the phone, then a telephone account is the right choice.

Some of the other merchant account options mentioned earlier may include this feature or may offer it for a small additional fee.

Card payment information is entered through a virtual terminal hosted on a Payment Processors network.

Banks view merchant accounts like a line of credit

Types of Merchant Accounts cont.

Mail Order Merchant Accounts
This type of account allows merchants to accept payment cards on mail orders. As with a telephone merchant account, card data is entered through a virtual terminal.

Individual transaction fees can be higher than with other merchant account types. Telephone and Mail Order merchant accounts are often combined into a single MOTO (Mail Order Telephone Order) account.

Merchant Account Application

To set up a merchant account, you must complete an application. The application will require specific information about your business, including:

- Company's legal name
- Bank account and routing number
- Tax ID (EIN)
- Processing volume - actual or estimated
- Business incorporation date
- Ownership information
- Authorized signer
- Voided check
- Bank letter

Getting Approved for a Merchant Account

Banks view merchant accounts much like they do a business credit line. The bank has some risk in approving you for a merchant account because if you receive some payments, go out of business, or can't cover refund payments; the bank must cover any of your customer chargebacks.

Your business has this chargeback risk typically.

When the bank reviews or underwrites your application and documentation, they decide how good a risk you and your business are based on their potential losses from your account.

One such risk consideration is chargebacks. Credit cards have a cardholder protection feature allowing the customer to dispute the charge for an undelivered or unfulfilled purchase.

Since the merchant must assume the chargeback risk, and the bank must guarantee this risk if you cannot, the bank evaluates your application for potential losses.

Other factors underwriters are looking at include, but are by no means limited to:

- credit ratings
- business maturity
- business financials
- quality of personal guarantees
- credit card volume requested
- average ticket size
- business type

Additionally, the bank or payment processor partner is underwriting the type of business you're in and the products you sell. Therefore, you technically violate your original merchant account agreement if you get approved to sell widgets and later switch to PVC fasteners or consulting.

While this may seldom be a fatal problem, you should still contact your payment processor and make arrangements to modify your original agreement to include these new products or services. This may cause card payment processors to re-evaluate your risk factors, rates, and fees.

As mentioned previously, Internet/eCommerce and MOTO accounts are intrinsically riskier than retail accounts primarily because you as the merchant cannot obtain information to assure you and the card network that the person giving you the card is the cardholder.

Because of this increased risk, banks' fees for Internet/eCommerce and MOTO accounts are higher than for retail merchant accounts.

Conditional Approvals

Acquirers or their agents will sometimes approve your application if certain additional conditions are met. Usually, these conditions have to do with helping offset the risk the payment processor thinks exists with your business.

One of these conditions might include a security deposit they can access if you can't cover account losses. This deposit can come in many forms; cash deposit, a "rolling reserve" where the bank accumulates a percentage of your credit card revenues until a deposit target is reached.

Or funding only a percentage of your credit card revenue for a specific period, holding back the balance, to "age" your account to assess chargeback volume, frequency, and behavior.

These deposits, holdbacks, or reserves can often be negotiated, but not always. For example, suppose the provider insists on some reserve, and you can't or don't want to tie up capital.

In that case, you might be able to negotiate a more palatable form of deposit, such as the holdback method, or change your application to a lower volume request. However, in most cases, you can ask them about your alternatives.

Bank Approvals vs. ISO Approvals

Banks, because of regulations and other needs, are historically very risk-averse. They must act with due regard to their depositors. Therefore, the risks they can take are minimal. We want our banks that way! We want them to not take risks with our money on deposit in their bank.

However, because of these requirements, they often decline a high percentage of merchant account applications except for certain low-risk accounts or applicants that are large depositors and have other significant business relations with the bank.

The banks' contracted agents, ISOs, and payment processors step into this gap and take some or all of the risk from the bank.

Filling the gap allows more merchants to be approved. For example, some ISOs approve up to 98% of all applicants. However, they may still apply various conditions to approvals and charge a higher rate than banks to help offset risk further.

But, for smaller merchants or newer, riskier businesses, ISOs or payment processors are usually more lenient and offer more options.

One important thing to remember is that you're being approved for a merchant account within the limits of your application.

For example, if you apply for a $50,000 monthly volume with $100 average tickets, you will only be approved for a $50,000 monthly volume.

If you exceed those parameters in the future, the merchant account provider may review your account for the additional risk, and your payment processor may impose follow-on conditions.

Not All Merchant Accounts, Merchant Account Providers - or Merchants - Are Created Equal

Some larger credit card processing companies do not give their merchants (account holders) individual merchant ID numbers/accounts. Instead, you are designated a merchant within their platform, and your merchant account is associated with your email address.

Therefore, when you leave their platform, you will not be able to transfer your merchant account to another platform and will need to establish a new merchant account.

Other payment processing companies focus on a particular type of client and understand that marketplace very well. Therefore, their merchant account products, services, pricing, and risk management behavior differ from other payment processors that serve a different business market.

For instance, a payment processor focusing on the small office, home office, or small business market knows certain things about that market and arranges its products and pricing to suit their risk management and profit requirements.

Typically, this provider will charge a higher discount rate and somewhat higher fixed fees and generally have a formula for approving most accounts under certain volume restrictions.

However, these business clients generally don't generate high volume processing, have a disproportionate failure rate nationwide, and sometimes have cash flow problems making the chargeback risk higher

When this payment processor approves this merchant account, they will set specific alarms in their software to monitor the account's behavior.

For example, they'll know about all chargebacks, whether the average ticket is within the range, the merchant applied for, whether the account exceeds the monthly or annual processing dollar volume they were approved for, and more.

In some extreme cases, if the merchant's processing sets off an alarm, the merchant account will be automatically or manually disabled until the merchant and the payment processor discuss the situation and resolve it. These payment processors usually have so many merchant accounts to manage that manually reviewing all the daily problem traffic can become a huge task, so they automate many of these issues.

Don't worry. No payment processor wants to shut off accounts unless the risk is too unmanageable. However, being disabled like this can be fatal if your business depends on your ability to accept credit cards!

Therefore, having a merchant account from a payment processor appropriate to your needs is essential

Other payment processors target high-volume merchants as their target markets and understand that market better than any other. This payment processor typically doesn't want the small business customer.

Because they understand high-volume accounts can have behaviors that differ from the small business payment processor - approval criteria are different, risk management is different, and account management is considerably different.

For instance, the processor rarely shuts off a high-volume account for exceeding its volume requirements. Instead, the payment processor would call and rework the account requirements while continuing service to the account.

Payment processing companies can also work across all markets and may or may not service all account types equally well.

Therefore, having a merchant account from a payment processor appropriate to your needs is essential.

Managing Your Merchant Account Lifeline

Your merchant account is one of the most important business relationships you have. It is an income and cash stream, a vital sales tool, and above all, it's a bank relationship for your business.

It isn't a trivial relationship. For instance, if your business merchant account is ever terminated by a payment processor, getting another merchant account in the future will be very difficult, if not impossible.

This bank account requires attention and management. You want to stay on good terms with your payment processor for many reasons.

- You may want to increase your limits as your business grows

- Your chargebacks may surge because of a lack of inventory or supply
- You may be able to negotiate lower prices as your credit card business grows
- You need an additional merchant account
- Your credit rating can suffer if the relationship goes bad
- Your business enters some tough times, and your chargeback payments are slow and others.

You need a good working relationship with your payment processor to handle these situations. To build this relationship, you need to stay in touch with them. Therefore, it would be best to inform them of circumstances that may affect them or your account in advance.

Some of these circumstances might be:

- Your sales have picked up, and you're worried you may exceed your volume limits
- You've changed your sales tactics, and your average ticket is higher than noted
- Holiday shopping looks like it will push you over your limits
- You want to pick up a product line that will affect the volume and average ticket
- Do you want or need a permanent increase in volume or average ticket limits
- A chargeback from a customer is unjust, and you need them to reject the chargeback
- Your business products have substantially changed from the type you applied to sell, and you need those new ones to be allowed
- You want to negotiate better rates or fees.

Treat this account as you would any vital financial relationship.

Additional Merchant Accounts

If you have a retail store and a retail merchant account, you must get an additional merchant account to accept mail orders or Internet orders.

If you have an Internet store and are now opening a physical store, you'll want to get an additional retail merchant account with lower rates for those sales.

Typical Fee Structure

Depending on the Merchant Account Provider, the type of account you need, and the various risk evaluations, your merchant account fees may differ from items in this list. In addition, there may also be fees not listed here.

In any case, the payment processor must disclose all fees, and you should find them in your merchant agreement or other documentation from your sign-up process.

Generally, it's good to remember that payment processors don't make a large profit margin on each sale. They must be processing millions of dollars across all their merchants to make a reasonable income.

Many of the fees described come about because smaller, lower volume accounts are truly unprofitable for processors, and the fees are their attempt to break even or make a little on each merchant account.

However, you should pay attention to payment processor fees when shopping for a merchant account. It is important to note that all payment processors do not all use the same fee structure.

Some Merchant Account Terms

AVS Fee: A flat fee is charged for each Address Verification Request. AVS is for U.S. cards and is an attempt by card associations to manage fraud by comparing street address numerals and zip codes to those in the cardholder's file at his issuing bank.

The result is given to the merchant at the time of authorization. After that, the merchant can decide whether to honor the transaction or not.

Batch Fee: Some payment processors charge for each batch you settle. Authorizations accumulate in a file every day and are usually settled once daily. Therefore, you may accrue additional settlement or "batch" fees if you force mid-day settlements. $0.15 - $0.25 per batch.

Chargeback Fee: A flat fee for the administrative and transaction costs associated with handling a customer chargeback request. $20 - $100.

Customer Service Fee: A flat fee some payment processors charge to maintain their customer service facilities.

Discount Rate: The percentage collected by the bank from your transaction dollar volume. For MOTO accounts, typical Discount Rates run anywhere from 2.1% (relatively low) to over 3%. For instance, if your rate is 2.49%, you would be charged $2.49 on 100 dollars monthly. The discount rate is shared by your acquiring bank, the cardholder's issuing bank, the banking networks, Visa, Mastercard, or others.

Monthly Minimum: Many payment processors charge a flat minimum fee if other variable fees (discount rate and transaction fees, for instance) don't add up to the minimum fee requirement. If your other fees exceed the minimum, you shouldn't be billed the minimum. The minimum can vary widely among payment processors, ranging from $15 - $50. The average seems to be around $30.

Non-Qualified Rate: This is the additional discount rate charged by the bank and Visa/MC for transactions that violate ideal transaction profiles. Non-Qualified, Mid-Qualified, and Qualified Rates should be clearly defined in your Merchant Agreement with your payment processor.

Typically, you are charged extra (sometimes up to 1% more!) on transactions that are not run through the AVS system and aren't settled within 24 - 48 hours (time may vary per bank). Or are NOT a standard consumer credit card (meaning additional charges apply if the purchase is made with a corporate card, foreign cards, or others).

IntelliPay™ automatically settles your transactions within 24 hours and automatically runs AVS on all your transactions from U.S.-based cards, but you must understand your merchant accounts requirements on Non-Qual rates.

Retrieval Request Fee: If you request research on a past transaction, your payment processor may charge a fee to research their data stores and create documents for you. $10 - $25 per incident.

Sign-Up Fee: Also called an Application Fee. It can range anywhere from $50 - $300. Often refunded if the application is disapproved.

Statement Fee: Some payment processors charge a statement fee to itemize, print, and ship your monthly statement.

Transaction Fee: A merchant account flat fee assessed for each transaction you run. Typically, $0.15 to $0.35 per transaction.

An Alternative to All the Fees

For merchants struggling with high processing costs, IntelliPay, in addition to establishing all types of merchant accounts, offers several no-cost processing solutions that shift some or all of the processing costs to the cardholder.

These no-cost solutions are 100% card brand-compliant and are being used with our cloud-based platform to save time and improve margins nationwide to learn more, talk to one of our experts.