Introduction

Accepting payments is a simple process when the only form of payment you accept is cash. It gets more complex as you add additional forms of payments like checks or credit cards. While some businesses can survive, and even thrive on a cash-only basis, the reality is most businesses cannot hope to survive much less thrive without accepting credit cards. A credit card payment comprises the majority of payments after cash and is the default method of payment online. This makes accepting credit cards imperative for most businesses.

Unfortunately it seems that handling cash is taught far more frequently and in detail then accepting credit cards. Merchant accounts are far more complex than most merchants know. The merchant services industry generates billions of dollars in revenues each year and there are a lot of players on multiple levels all trying to capture a piece of the pie. Each player adds a layer to the process of accepting credit cards and increases the complexity of not only the process of accepting credit cards but adds to the cost structure as well. To make it worse, getting good information is difficult to accomplish. Half of this is a result of the majority of information available about merchant accounts are made available by merchant account providers. This means what you are reading is at the very least tailored to bathe their company in a positive light or can be a blatant sales ad disguised as "an informative article". In many cases the merchant account providers do not want you to know how it all works as an educated merchant will be more difficult to sell an average rate plan to. After all, knowledge is power.

> The see an example of how difficult it can be to get reliable information read our blog post An Example of Why Merchants Find It Hard to Get Good Information.

The following article has been written to explain the many mysteries surrounding merchant accounts. It tackles several aspects some of which are usually transparent to the merchant. The goal is to educate you about merchant accounts so you can make better decisions about the merchant account you currently have or the merchant account you are seeking. While it doesn't go so far as to explain how you should shop for a merchant account (that article is in the works) it will give you enough information to make informed decisions. Areas we will cover are:

- **Who's who in credit card processing**
  Find out who the players in the merchant account industry are and what their role in the process is. We start at the top with the credit card companies themselves (Visa, MasterCard) and work our way down to the sales agent who establishes your account.
- **The basic elements of merchant accounts**
  To better understand how rates and fees are determined and charged it is important to understand how a merchant account works. The type of merchant account and fees charged are affected by the environment the credit card is processed and even the kind of credit card is being used to make the purchase. We will look at the elements of a merchant and transaction to get a better understanding of how these factors affect a merchant account.
- **Rates & fees**
  The most important, and yet the most confusing, aspect to accepting credit cards are the rates and fees associated with having a merchant account. Some fees are "standard" while others are not. Some companies use different names for essentially the same fee. Some rates look better than others but are they really? We will look at the most common fees and explain when and how they are charged.
- **Establishing a merchant account**
  Just understanding how the rates and fees of a merchant account are charged does not make a merchant educated about merchant accounts. You need to understand the fine print of the contract you are signing as well as how the processing bank will view your account with them. Their outlook on your merchant account can mean the difference between smooth sailing and money being held for months or years. We will take a look at what factors they are most concerned with and how you can ensure your merchant is not a burden to your business.

The Players

One of the main goals of companies that establish merchant accounts is to simply a complicated process. By simplifying it not only do they make their jobs in selling the service easier, but it also makes it easier for the merchant to understand as well. As with any other business, there are also many layers of participants who make a service happen. Knowing whom all of the players in establishing merchant accounts really isn't necessary to accept credit cards. But knowing who affects your rates and how your account operates allows you to make better informed decisions when establishing an account or working with an existing account.

The Card Companies

Without the credit card companies there would be no credit card to accept. These companies not only issue the credit cards and govern how consumers may use them, but they also govern how the merchants may accept them.

Visa and MasterCard

Visa and MasterCard are separate worldwide payment service organizations composed of member institutions. They set and enforce rules and regulations governing their bankcards, such as operational and Interchange procedures. They create advertising and promotion programs to support their brands and develop new products to serve banks and consumers and are also responsible for conducting clearing and settlement processing of credit card transactions through Interchange. They supervise the bankcard processing function within their members' banks.
Combined Visa and MasterCard account for 83% of all credit card transactions in the United States.

American Express

American Express started off as a travel card and is often classified as a "Travel & Entertainment" card. However, it is a true credit card like Visa and MasterCard and is accepted at most types of business. American Express is the preferred credit card of many businesses and, although American express usage is far less than that of Visa and MasterCard, businesses that deal primarily with other businesses (b2b) or is frequented by business professionals may see American Express as their primary credit card being accepted. Unlike Visa and MasterCard American Express is not comprised of member banks but is its own entity. This means you need to apply directly with American Express or your merchant account provider needs to be an authorized representative to establish the account for you.
American Express accounts for 13% of all credit card transactions in the United States.

Discover Card

Discover Card was started by Sears and is the newest of the four major credit cards. Although Discover Card has more cardholders then American Express, in terms of processing it is by far the smallest of all of the major credit card providers. Like American Express, Discover Card is not comprised of member banks but is its own entity and a merchant account must be established directly through them. Unlike American Express, however, Discover Card is now partnering with processing banks to have merchant accounts established just like Visa and MasterCard.
Discover Card accounts for 4% of all credit card transactions in the United States.

Others

While Visa, MasterCard, American Express, and Discover Card comprise the overwhelming vast majority of credit card transactions in the United States, they aren't the only credit cards some merchant may see in the normal day-to-day of operating their business. Foreign credit cards like the Japanese issued JCB credit card are fairly popular on the west coast in Hawaii. Some restaurants may accept the Diners Club card. Truck stops may accept fleet cards. Since these special cards are so limited in their use and acceptance this article will not cover them.

The Card Issuing Banks

The card issuing bank is the bank that issues the credit card. They are a licensed member of Visa and MasterCard and can also be an Acquirer (see below). The Issuing Bank solicits, screens, and approves the cardholder for a credit limit. Once the cardholder has the card, the Issuing Bank approves or declines sales the cardholder wants to make with the card, bills the cardholder for charges to the card, and collects funds from the cardholder to pay the merchant for purchases.

Acquirers and Processing Banks

The Acquirer provides credit card processing services to the merchant by acting as the communications link between the merchant and the card issuing bank. The Acquirer is a member of Visa and/or MasterCard.

Member Service Provider / Independent Sales Organization

A Member Service Provider (MSP) is a licensed broker of credit card services or banks through which business is processed. A MSP is usually an independent salesperson or company who contracts with a bank or a processor to sell credit card processing, equipment, and services to the merchant. The MSP sometimes provides back office functions such as settlement and chargeback/retrieval management, equipment-related customer service, paper storage and retrieval, and supplies. MasterCard originated the term MSP, while Visa uses the term ISO (Independent Sales Organization).

Sales Agents

Sales agents are individuals who represent a MSP/ISO. They are not members of Visa or MasterCard and are not contracted directly with a bank or processor. As a result they are not allowed to sell merchant accounts under their own business name. They must use the business name of the MSP/ISO with whom they are affiliated.

> See our blog post Small Providers Are As Good As Large Providers to see why small providers are just as good as large providers.

The Cardholder

The cardholder uses the credit card given by the card issuing bank to purchase goods and services or to obtain a cash advance and receives a monthly bill from the card issuing bank for every purchase or use of the card. The cardholder is expected to sign the back of the card and limit its use to only authorized users, stay within the assigned credit limit, and pay the card issuing bank all or a minimum amount of the balance when the monthly bill is received.

The Merchant

The merchant provides goods and/or services to the cardholder. Visa and MasterCard require that the merchant be financially responsible and of good repute and adhere to all rules and regulations set forth by them. The acquirer requires that the merchant adhere to the merchant processing agreement they signed that details the prices the merchant will pay for equipment, discount rates and fees. It also spells out the terms and conditions under which the merchant will conduct credit card business, such as the card types the merchant will accept, chargeback rights, and access to the merchant's bank accounts.

Platforms and Networks

Processing Platforms, also known as Processing Networks, are the computer networks that electronic transactions occur over each day. There are multiple networks available for electronic transactions to occur over but the merchant does not choose which platform(s) they use. Each acquiring bank establishes

relationships with the processing platforms they feel would be best for their business model (usually basing the decision on cost and availability).
Not all platforms are created equally. Each platform establishes a unique API for which software and equipment can communicate with it. Thus, software and equipment cannot use a platform to process electronic transactions until it has verified that it can support that platform's API successfully. As a result some software and equipment will only work on some platforms and not others.
When choosing a merchant account provider, some merchants will base their decision on the platforms that provider has available to them. This will typically be because the merchant has a specific piece of software or equipment that only works on a specific platform. An example would be restaurants that use proprietary POS software.

Account Types

In the world of credit card processing one size does not fit all. Businesses operate in different manners and this affects the kind of merchant account they will have. It is important for a merchant account provider to establish a merchant with the proper account during the application process as to prevent the many problems that can arise if the merchant is improperly classified. Having the proper merchant account not only helps to keep a merchant's rates to a minimum, thus saving them money, but also helps to protect against fraud and chargebacks.

Retail (Card Present)

A retail business is face-to-face with their customers and can swipe their customers' credit cards through a credit card terminal and process them in real time. Brink â€˜n Mortar retail stores are typical examples of a retail business but they are not the only ones. Merchants who have stands at flea markets and have access to a telephone line and electricity can also be retail if they use a credit card terminal at their stand. A merchant with a wireless credit card terminal is also considered to be retail. Why? Even though they may be standing on a street corner while processing their transaction they can swipe their customers' credit cards through their credit card terminal and process the sale in real time. As a result they get all of the perks and benefits typically offered to a traditional retail store.

Card Not Present

Businesses that are not face-to-face with their customers at the time of sale are classified as Card Not Present (CNP) accounts. These businesses typically take payment in any of the following manners:

- Telephone
- Fax
- Email
- Mail

The one thing they all have in common is that the merchant is not face-to-face with the customer at the point of sale. These transactions are usually keyed into a credit card terminal or POS software.
Another form of CNP business is merchants who perform recurring billing. Although the very first transaction may occur in a retail environment (face-to-face with the merchant and swiping the credit card through a credit card terminal) every recurring transaction afterwards will not be swiped. Because these recurring transactions comprise the majority of the transaction for this merchant they would be considered a CNP merchant.

Internet

An Internet business is very similar to a CNP business. The distinguishing characteristic between the two is how the customer's credit card information is acquired. An Internet merchant acquires their customers' credit card information through their website. The customer's information is physically captured and transmitted through the merchant's website.

A business is *not* considered to be an Internet business for the following reasons:

- A company has .com in their business name
- The website that advertises their products but does not take payment
- Customers place an order over the phone by reading the contents off of the website
- The merchant uses a payment gateway to process their transactions

Although some of the situations listed above are characteristics of an Internet business, unless payment is accepted through the merchant's website, the merchant is considered to be a CNP business.

See our blog post Three Websites, One Merchant Account? to see how you should handle operating multiple websites and merchant accounts.

Mobile

A mobile business is very similar to a retail business. They are face-to-face with their customers at the time of sale. The main difference is that a mobile business does not have the means to process the transaction in real time. Typically this is the result of a telephone line or electricity being available at the point of sale.

To compensate for the lack of resources to process a transaction in real time, a mobile merchant typically uses a manual imprinter to capture an imprint of their customers' credit cards and obtain a signature. This allows them to manually process the transaction at a later point in time. It also offers the mobile merchant additional chargeback protection typically reserved for retail merchants.

See our blog post How to Process Credit Cards at a Fair or Market to see how a mobile business may operate.

Seasonal Businesses

A seasonal business is only open for a specified period each year. This period is consistent and does not change from year to year. For example, a Xmas decoration store will be open every year from October through December. They won't need their account from January through September. Seasonal businesses can have their accounts closed for the off-months each year during which they will incur no fees including their monthly service charge.

Typical seasonal businesses include:

- Landscapers
- Fireworks sales
- Xmas/Holiday-based
- Some tradeshow merchants

Seasonal merchants cannot open and close their account at random times. The months they wish to be closed must be determined during the application period. They may vary slightly based on the needs of the merchant but this is on a case-by-case basis. Merchants who were not declared seasonal during the application process typically cannot close their account on a temporary basis. [1]

Types of Credit Cards

There are several different kinds of credit cards issued by Visa and MasterCard. There are differences between them may affect the rates charged for those cards and how a merchant is responsible for processing them.

Consumer Card

A consumer credit card is a plain old credit card carried by an average person. It is not tied to a checking account, offer any rewards, or associated with any business. It is not special in any way. These cards are becoming less and less popular as check cards and rewards cards gain in popularity.

Check Cards

A check card is very similar to PIN-based debit cards. Unlike a typical credit card where you wait until you receive your next bill to make payment, and maybe even make a partial payment, the funds for check card transactions are immediately withdrawn from your checking account.
Unlike PIN-based debit cards, however, you do not have to key a PIN number to complete the transaction. You simply sign your name as if you had used a credit card. Also, unlike PIN-based debit, no special equipment is required to accept check cards. The same equipment used to accept credit cards can also accept check cards.

Rewards Cards

A rewards card offers its cardholder special bonuses for using that card to make purchases. The bonuses will vary by card issuing bank. Typical rewards include airline miles and vacation packages.
All rewards cards are placed into a special Interchange table and typically cost more to accept then a traditional consumer credit card. They typically fall into a mid-qualified rate for retail businesses. Mobile, MOTO, and Internet businesses typically pay their qualified rate for these cards.

Business/Corporate Cards

Business cards, also called corporate cards, are carried by business owners. These are typically used to make purchases for the cardholder's business. They are popular amongst businesses as they offer extra features not traditionally found in consumer credit cards. The more detailed statements are their primary benefit.
Business cards are placed into a special Interchange table and typically cost more to accept then a traditional consumer credit card. They typically fall into a mid-qualified rate for retail businesses. Mobile, MOTO, and Internet businesses typically pay their qualified rate for these cards.

Purchasing Cards

Purchasing cards are virtually identical to business cards with one exception: they can only be used in predetermined businesses. All transactions outside of the predetermined businesses will be declined automatically.
The predetermined businesses are determined by SIC code. If a corporation has allowed a purchasing card to make purchases from a merchant listed in that SIC code the transaction will proceed normally. The company that the purchasing card has been issued to has the ability to determine what SIC codes a card may be used with. If a merchant has a customer that cannot make a purchase due to the SIC code restriction the customer will need to contact the card issuing bank to have the merchants SIC code added to their acceptable SIC code list.
Purchasing cards behave like business cards in terms of rates and fees as well as required fields.

Types of Transactions

Although processing a sale is the mostly completed and discussed transaction type it is certainly not the only one. Different transactions will affect your account, and thus your fees, differently.

Authorize & Capture (Sale)

This transaction is just a basic, common everyday sale. Whenever a purchase is made it really is a two step process, although the two steps are seamless. The merchant's POS system, in whatever form that may be, contacts the processing bank and acquires an authorization for that credit card transaction. It also requests for that sale to be captured, that is, to have the sale be completed and funds delivered to the merchant.

Refund

A refund is very similar to a sale except the flow of funds is reversed. A refund gives the money back to a customer's credit card. There are no penalties charged if a merchant issues a refund. A merchant may issue as many refunds as necessary.

Authorize Only

Auth Only transactions are very similar to Authorize & Capture transactions except the transaction is not captured. The merchant is issued a six digit authorization number indicating that the funds are available and the transaction is approved. However, the merchant will not receive those funds until they capture the transaction.
Authorizations are only valid for up to 30 days from when they are issued and for up to the amount they were authorized for. For example, if an authorization was obtained for $100, the merchant may use this authorization for any transaction up to $100 for that customer. However, they cannot go over $100 with that authorization number.
An Important thing to note is that the funds from authorizations are frozen on a customer's credit card and cannot be access by that customer. From the customer's point of view, that money is essential spent. Authorizations should not be used without a customer's consent and with care.
Authorizations are captured when a Force transaction is processed.

Force (Capture)

A Force transaction takes an existing authorization number obtained from an Auth Only transaction and forces the sale through so the merchant may receive those funds. Unused funds from an authorization are immediately freed for the customer to use.

Void

A void transaction erases another transaction of any type. It essentially makes that transaction act and appears as if it never existed.
Voids can only be performed before a POS device has successfully batched its transactions. Once a transaction has been batched a void cannot be performed.

Processing Fees

Naturally accepting credit cards is not a free service. In fact, this may be the one service that has the most middlemen! Every time you accept a credit card the following people all receive a fee from the transaction:

- Card Issuing Bank (they get the biggest cut)
- Card Association
- Acquirer
- Processing Bank
- Member Service Provider / Independent Sales Organization
- Sales Agent

It's this fee that makes establishing merchant accounts so lucrative. Although the fee each entity above receives is minute, when you have millions of cardholders making purchases at millions of business the numbers add up very quickly. So who gets to pay these fees? The merchant. Why? Because they are the ones in least in the position to ignore credit cards. Consumers can use another form of payment quite easily. But merchants need to accept credit cards if they wish to stay in business.
How fees are charged can get very complex and we won't try to explain it all here. But as a general rule you can get charged fees under these circumstances:

- Each transaction
  These fees are charged every time you accept and process a credit card transaction of some kind. Examples include the qualified rate and authorization fee.
- On a recurring basis
  These fees occur on a set schedule and usually are not dependent on your credit card processing usage. Examples include a statement fee and annual fees.
- One time based on a special situation
  These occur only when certain criteria are met and otherwise are not charged normally. Examples voice authorization fees and monthly minimums.

This article focuses on Visa and MasterCard's rates as they are the most complex as well as the most common fees most merchants will experience. They are based on Interchange which is explained below.

Interchange

Interchange is the clearing and settlement system where data is exchanged between the credit card processor and the card issuing bank. It is a part of Visa and MasterCard. Most communication that occurs between the cardholder, the merchant, the card issuing bank and the Acquirer or Member Service Provider (MSP) must go through Interchange (such as transactions, deposits, chargebacks, etc).
Interchange sends transactions that occur at the merchant level to the appropriate bank for posting, sends funds to the appropriate Acquirer for payment, and assigns a qualification level for each transaction. The qualification level determines what rate the merchant will pay for the transaction and is based on whether the merchant met the Visa/MasterCard standards set for the level. Different rates, or costs, are associated with the different Interchange programs. Visa and MasterCard, periodically redefine these standards, or qualifications.

Qualified Rate

The qualified rate is the lowest rate a merchant can pay for any transaction. To "qualify" for this rate the merchant must meet a set of criteria. The criteria will vary by style of account and type of business. For retail businesses, typically the merchant must swipe the credit card through their credit card terminal or POS system and answer all terminal prompts. For an Internet merchant this may mean capturing and verifying AVS and CVV. If a merchant fails to qualify their transaction they may pay a higher rate (see the section titled "Surcharges" below for more information).
The qualified rate is the fee most likely to be charged to the merchant and thus is the rate advertised by merchant account providers. Once again, this isn't the only rate you may pay. It is just the most common.
Here's an example of a qualified rate being applied to a transaction:

```
Transaction dollar amount: $35.00 Qualified rate: 1.69% + 25¢
(First calculate the percentage) 35 x 1.69% = 59¢
(Then add the transaction fee) 59¢ + 25¢ = 84¢
```

In the above example a merchant with a ticket of $35 would and qualified rate of 1.69% + 25¢ would pay 84¢ for that transaction. But what if their sale was for $65? Let's see:

```
Transaction dollar amount: $65.00 Qualified rate: 1.69% + 25¢
(First calculate the percentage) 35 x 1.69% = $1.10
(Then add the transaction fee) $1.10 + 25¢ = $1.35
```

As you can see the cost for that transaction is larger than the transaction for only $35. This is due to the percentage rate (1.69%). As the transaction grows larger so does the amount of that transaction dedicated to their qualified rate. If their transaction was smaller than $35 their overall costs would be smaller as well.

To see how rates and fees are calculated for any average ticket price be sure to check out our Basic Fee Calulator or Advanced Fee Calulator. They allow you to determine your costs based on your rates and average ticket price.

To compare the offers of multiple merchant account providers be sure to use our Basic Rate Comparison Calculator or Advanced Rate Comparison Calculator. These tools will tell you how much each account will cost you over the course of an entire year.

Transaction Fee

A transaction fee is a flat fee charged each time a successful transaction is processed. This mean the transaction fee is *not* charged if a transaction is declined. Only an approved transaction will incur this fee. In the above examples the transaction fee was 25¢

Authorization Fee

An authorization fee is very similar to a transaction fee except this fee is charged with every transaction regardless of the results of the transaction. This includes declined transactions. Essentially each time your credit card terminal, POS software, or payment gateway communicates with your processing bank this fee is charged.

Transaction Fee vs. Authorization Fee
So which fee am I being quoted? Good question. This will vary by merchant account provider so you need to ask which fee you are being quoted before you begin the application process.

Blended Rates

A blended rate is nothing more than a fee, either percentage based or a flat rate, which combines the qualified rate and transaction fee. So instead of having a traditional structured rate such as 1.79% + 25¢ per transaction that merchant might pay a flat percentage of 2.50% or a flat fee of $1 per transaction. Blended rates are calculated by taking a merchant's average ticket and determining what their fees would be for that sale. That cost then becomes the blended rate for that merchant. Here's an example of a flat blended rate:

```
Average Ticket Price: $40 Qualified Rate: 1.79% + 25¢
(First calculate the percentage) 40 x 1.79% = 72¢
(Then add the transaction fee) 72¢ + 25¢ = 99¢
```

In the above example a merchant with an average ticket price of $40 and a qualified rate of 1.79% + 25¢ could have a flat blended rate of 99¢. What if that merchant wanted a flat percentage rate? Well, we would continue using the above example and take it a step further:

```
(Take the flat rate and determine what percentage of the $40 it is) .99 / 40 = 2.48%
```

All we needed to do is find out what percentage of $40 99¢ is and we have our flat percentage rate. Blended rates may seem like a good idea but in reality they're not. When you stop and think about it the fees will be exactly the same as if the rate wasn't blended. After all, the blended rate is based on your average sale. So you won't be saving any money which is naturally your goal. To make it worse, you may lose out with a blended rate. Let's say your average ticket were to suddenly rise to $50 per transaction. Here's a comparison of your old rate (1.79% + 25¢) versus your new blended rate (2.48%):

```
(Find out what our blended rate will cost on a $50 transaction) 50 x 2.48% = $1.24
(Next, find out what our old rate will cost) 50 x 1.79% = .90 + .25 = $1.15
```

The difference is 9¢ per transaction. That doesn't seem like a lot but when you multiply that by the number of transactions you do per month, which may be hundreds or thousands, suddenly it doesn't seem so small. Imagine if your average ticket becomes $60 or more!

To make it worse, merchant account providers understand that if your average ticket were to suddenly change they could lose money. So they pad the blended rate to account for such a contingency. Thus, you may lose out even if your average ticket stays steady. Blended rates seem attractive at first but when you look closer they offer no real advantage.

Surcharges

One of the complexities in accepting credit cards is when a transaction does not qualify for the Qualified Rate. The rates and fees you pay can vary depending on not only the situation under which the transaction occurred, but the type of credit card plays a role as well. Some transactions, possibly through no fault of your own, may incur higher fees for various reasons. Why this happens can vary from provider-to-provider so we cannot provide you with a complete explanation. But you should learn enough below to ask the right questions and intelligently review and acquire a merchant account.

Non-Qualified

So what happens if your transactions do not qualify for the qualified rate? Most commonly they are charged a Non-Qualified surcharge. This is the highest rate you can pay for a Visa and MasterCard transaction. Basically, by not performing the actions required to make the transaction "qualify" you are increasing the potential risk and exposure for loss the processing bank and Visa and MasterCard may experience. By increasing their potential for loss and increasing their costs they essentially charge you extra to pay for it.

Some possible reasons a sale may be charged at a Non-Qualified rate include:

- A credit card was not swiped through a magnetic stripe reader and AVS was not performed properly. Not supplying a zip code or street address will cause AVS to fail.
- Not supplying all required fields for a corporate/business credit card. This may include the tax amount for the sale or an invoice number.
- Delaying your batches until after 48 hours after a transaction is processed.
- Acquiring an authorization and then performing a Force transaction to capture the sale.

If you see a lot of non-qualified transactions on your processing statements this usually is an indication that you are making errors while processing your transactions. You should call the customer service department of your merchant account provider to find out why your transactions are being charged this fee and find how to correct it.

Partially Qualified (Mid-Qualified)

Unfortunately not all credit card sales qualify for the lowest rate possible. At the same time, they do not deserve to have the highest surcharges applied to them as it really is not the merchant's fault they did not qualify. For these exceptions a "middle ground" surcharge is applied. The cost of this surcharge is usually around half of the Non-Qualified surcharge.

Some possible reasons a sale may be charged at a Partially Qualified rate include:

- A credit card was not swiped through a magnetic stripe reader but AVS was performed properly.
- A special credit card was processed that cannot qualify for a qualified rate. (See the section "Special Credit Cards" below).

In general this surcharge is only available to card present/retail merchants as all other business types are essentially being charged this fee as their Qualified Rate already.

Special Credit Cards

As we saw earlier in this article there are many different kinds of credit cards available to consumers to make purchases with. Some of these credit cards are considered special by Visa and MasterCard and incur higher, and even sometimes, lower fees. Typically the reason for this is the credit card offers extra benefits to its users and thus carry a higher cost to operate. Someone has to pay for these extra costs and it is the merchants through higher fees.
How these credit card affect a merchant's fees will vary from provider to provider but it can happen in one of two ways:

1. A surcharge is applied to the purchase
   The most common, and oldest, way to handle special credit cards is to apply a mid-qualified or non-qualified surcharge to special credit cards. Even if a merchant does everything that normally would allow a transaction to be charged a qualified rate, the special credit card automatically is charged a surcharge anyway to cover its extra costs.
2. The credit card has its own special rates
   A newer way of handling special credit cards is to create special rates just for them. So instead of the merchant having a regular qualified rate only, they will know have a qualified rate *and* a rewards card rate. The rewards card rate will be different from their surcharges and only apply when they actually accept a rewards card.

Monthly and Annual Fees

Besides the fees incurred directly for processing credit cards there are other fees associated with establishing and running a merchant account. These fees occur on a regularly scheduled basis and may be indirectly related to the merchant's processing levels.

Statement Fee

The statement fee covers the cost for creating a statement for the merchant each month that details the processing history for the previous month as well as a breakdown of the fees incurred from that month's processing. It also typically includes the costs for customer service and technical support as well. However, some merchant account providers will separate their monthly fees for statements and customer service and tech support.
Most providers will not waive this fee even if you decline a paper statement being mailed to your business. This is because they still aggregate that data even if you don't elect to receive it. Plus it also includes your customer service and tech support costs for the month.

Monthly Minimum Fee

The monthly minimum fee is a fee which guarantees the merchant will be paying a minimum amount each month in processing fees. If a merchant's discount fees do not equal their monthly minimum fee they will be charged the difference between the two in addition to their discount fees.
Example:
A merchant has a discount rate of 2.50%, a monthly minimum of $25, and a monthly volume of $600.
The discount fees for the month will be $15.00 (.025 x $600). Because their discount fees are less than their minimum fee ($15.00 < $25.00) they will be charged an additional $10.00 as a monthly minimum fee ($25.00 - $15.00).
So, what is the purpose of this fee? Merchant account providers and their sales agents make their money by taking a very small percentage of every sale a merchant processes. Naturally this can be very lucrative. But, if a merchant is very small, they won't make very much money from them. So, to make up for this, they charge this monthly minimum fee. Then, when the merchant has a slow month, this fee is incurred and the merchant account provider still makes their profit from this merchant.

This fee is **not** required by Visa and MasterCard to have an account with them. Many processing companies offer merchant account with excellent rates without the monthly minimum fee. [2]

Annual Fee

Annual fees are exactly what their name implies. They are charged each year that the merchant has their merchant account through their current provider. Some merchant account providers charge this fee on the anniversary that the merchant account was established while others charge this fee on a set date each year. There are several different types of annual fee including membership fee and merchant club fees. Regardless of the name they all serve the same purpose.
This is not a standard or common fee for establishing a merchant account.

Other Fees

There are many *potential* fees that may be incurred while accepting credit cards as payment. There is no way for us to list all of them and that's okay. The odds are you won't incur most of them. The fees listed below are some of the few remaining fees worth mentioning. If you see another fee on your statement call your merchant account provider for an explanation as to what the fee is and why you incurred it.

Voice Authorization

Occasionally a merchant may be instructed by their credit card terminal to call for a voice authorization. All merchants are provided with a voice authorization phone number when their merchant account is established. If they call this number and receive an authorization or decline they will be billed a voice authorization fee.
With computerized systems being more advanced than they were twenty years ago voice authorizations are less common then they used to be. However, they are still common for some merchants. A merchant may call for a voice authorization for their own reasons and not because they were prompted to do so. Typically this is used by mobile merchants for large purchases to verify the order before they give away their merchandise. By receiving authorization for their transaction over the phone they can be sure they will be paid before they part with their merchandise.

Chargeback/Retrieval Fee

This fee is only charged when a transaction processed through your merchant account is disputed. This is always a fixed fee usually in the $15 - $35 range. It is charged for each chargeback and is incurred regardless of whether the chargeback is successful or not.

Batch Fee

This fee is incurred each time your credit card terminal or payment gateway settle the transactions stored since the last time a settlement occurs. This fee is charged for each batch that is settled. Typically a merchant settles their sales once per day but occasionally a merchant may have a reason to settle their sales more frequently (their credit card terminal's memory may be full). Each batch settled will incur this fee. The number of transactions do not affect this fee. The same amount is charged whether one transaction is settled or one thousand. This fee is not incurred if there are no transactions that need to be settled.
Most merchant account providers charge a higher fee for batches. Some merchant account providers simply consider a batch just another transaction and only charge a transaction fee which is no different than running a regular transaction (no percentage is charged, just a flat transaction fee).

> Read our blog post Save Money By Batching Your Terminal to see why you should settle your transaction every day.

Application Fee

Some merchant account providers charge a fee when a merchant submits an application for a merchant account. This fee is designed to cover the merchant account provider's costs for processing the application and submitting it to their processing bank for approval. Since merchant account providers do not make any money from a merchant account until after the account is established they may charge this fee to make sure if the application is declined they did not lose any money attempting to establish the merchant account.
This is not a standard or common fee for establishing a merchant account.

AVS Fee

Address Verification (AVS) is required on all non-swiped credit card transactions. Failure to do so will cause a transaction to incur a surcharge thus doing so is important whenever a transaction cannot be swiped through a credit card terminal (which is every transaction for all non retail merchants).
Most merchant account providers include AVS for free with all non-swiped transaction but not all do so. Some will list this as a separate fee in order to make their costs appear to be lower. Be sure to calculate the cost of AVS into all non-swiped transaction. Non-retail merchants should add their AVS fee to their transaction fee to get an accurate understanding of their real costs.

> Be sure to read our blog post The AVS Game and Always Decline Transactions That Fail AVS? to learn more about AVS.

Setup Fee

This fee is very similar to the Application Fee except it is not incurred unless a merchant account is established. Only at that point is this fee incurred. Merchants whose applications are declined do not incur any fees (unless an application fee is also charged).
This is not a standard or common fee for establishing a merchant account.

Reprogramming Fee

This fee is charged to cover the costs of labor when reprogramming an existing credit card terminal or computer software.
This is not a standard or common fee for establishing a merchant account.

Cancellation/Termination Fee

Just as the name implies this fee is charged when a merchant account is terminated. Since most merchant account providers do not charge an application fee or setup fee they incur a loss for every merchant account they establish until the merchant processes enough sales volume to make their account profitable. To ensure that each merchant is profitable most merchant account contracts contain a clause that imposes a penalty if the merchant leaves before the contract expires.
Some contracts are open ended and do not have a cancellation fee. This contracts allow the merchant to leave at any time. Some have a fixed term where if the merchant reaches the term without terminating the contract they will not incur a fee if they terminate the contract after that point. So if your contract is for two years you can leave anytime after two years has passed without incurring a cancellation fee. Some fees reduce in size as the contract progresses. For example, if a merchant leaves during the first year of their contract they may occur a $300 cancellation fee but if they leave during the second year they only incur a $200 fee.

Establishing a Merchant Account

Establishing a merchant account can be anywhere from a smooth and easy process to a nightmare. Where it falls is both the product of the merchant account provider and the merchant themselves. The better the communication between the two the smoother and faster the process is.

Applying for a Merchant Account

An account can be opened in as little as four hours or as long as a few days depending on when the application is submitted and the underwriting guidelines of the processing bank. The application process should never take longer than that without a clear and legitimate reason. If your application is taking two weeks to be approved and you've had little to no communication with your sales agent, something is wrong and you should consider canceling your application.
Establishing a third party account will vary from provider to provider as each has its own criteria and verification process. Your account can go live anywhere from immediately to several days or weeks. Also, the services made available to you may depend on verification of your business or personal information.
For planning's sake the process setting up of a merchant account should be started two or three weeks before you expect to go live. This will allow for unexpected delays and testing of the account and gateway.[3]

Contracts

All merchant account providers require that every business sign a contract when establishing their merchant account. At the very least this contract will specify what the merchant's responsibilities are as well as those of the merchant account provider. This ensures that the merchant account provider has as much protection as they can from loss due to risk and other factors. (See "Security and Risk" below to see why this is the case).
Another important factor specified in some contracts is the length of term of the contract. Some contracts require the merchant honor their contract for a set period of time. Failure to complete the contract will result in a penalty being assessed also known as a cancellation fee.
The entire contract should be available to the merchant *before* they sign it.

Personal Guarantee

When applying for a merchant account most small and medium-sized merchants will notice that a personal guarantee is required to establish the merchant account. A personal guarantee basically says that if the business cannot fulfill its obligations to the processing bank then the processing bank can legally pursue the guarantor to fulfill those obligations. This basically means if your business owes the processor money and it does not or cannot pay then the bank can come after the guarantor seeking those funds.
The reason why the processing bank does this is because of the high risk they are exposed to due to the nature of their business. If a new merchant commits fraud or just mismanagements their business and merchant account, the processing bank can be on the hook for a large sum of money.[4] Naturally they wish to protect them from this scenario as best they can. By having the owner put their personal assets behind the business they mitigate this risk.

Security and Risk

Risk is the single largest factor influencing the establishment and maintenance of a merchant account. As with anything financial, someone stands to lose a lot of money if something goes wrong, whether intentional or not. In the world of credit card processing the ones with the most to lose is the acquiring/processing bank. As a result, they make all of the decisions about whether or not a merchant account is established, under what conditions, and whether that account continues to process normally or have their account closed.

Chargebacks

The biggest buzz word in the world of merchant accounts is "chargeback". A chargeback is when a customer initiates a refund for a purchase they made on a credit card by contacting their card-issuing bank. The reasons for this can vary greatly but generally is a result of a customer being dissatisfied with their purchase. The customer may or may not have contacted the merchant about remedying this situation ahead of time. They may even be completely wrong. However, responsibility falls on to the merchant to ensure that the transaction goes smoothly and the customer is satisfied. A failure somewhere along the fulfillment process, including at the customer service level, can lead to a chargeback.
When a merchant receives too many chargebacks, approximately 1% of their sales, they risk having their merchant account shut down and losing the ability to accept credit cards again (see "The Match File" below).

> To learn more about chargebacks and how to both handle and prevent them be sure to read our article The Chargeback Challenge and our blog post Why Retailers Always Win Chargebacks.
>
> To see common misperceptions about chargebacks read our blog posts Merchant Account Providers Want Chargebacks? and A Contract Does Not Mean Chargeback Protection.

Reserve

One way a processing bank may protect themselves from the risk a merchant account exposes them to is to hold some of that merchants funds in a special account called a reserve. A reserve allows a processing bank to cover potential future costs they may have associated with the merchant including chargebacks and potential fraud. If the merchant is unable to cover the costs of future chargebacks, possibly because they already have gone out of business, the processing bank can access the funds held in reserve to cover those chargebacks. If they didn't have the funds held in reserve they would have to pay those chargebacks out of their own funds.
The amount of the reserve can vary from a small fixed amount to a large fixed amount or an entire month's worth of credit card processing. How the amount held in reserve is determined is based on the amount of exposure the processing bank faces from a particular account. This can only be determined at the time the merchant applies for the merchant account.
Reserves can be created and work in several ways. Sometimes a processing bank will hold all of the funds owed to a merchant until they reach the predetermined amount of the merchant's reserve. Sometimes the processing bank will hold one month's worth of processing and return it after the following month has passed. This is called a rolling reserve. With the exception of rolling reserves funds held in reserve are not available to be returned to the merchant until the potential for chargebacks for their account has passed. Since chargebacks can usually be filed for up to six months after a purchased is made a merchant won't see their funds held in reserve until up to six months after they close their account. In the case where a business offers a service that takes an extended period of time to complete (e.g. an annual subscription) the merchant may not see their funds for as long as eighteen months.

High Risk Businesses

Some businesses by their very nature have higher than normal chargeback rates. Sometimes this is due to the product or service offered by the merchant being in high demand but also being high priced (e.g. high end electronic, jewelry, etc.). Sometimes it is because the service causes customers to be misled whether intentionally or not (e.g. multi-level marketing schemes). Regardless of the root cause these businesses will usually find it difficult, if not impossible, to establish a merchant account.
The businesses considered to be high risk will vary from merchant account provider to provider. However, there are some businesses and industries that are consistently considered high risk. This list includes:

- Adult Book Stores
- Adult Entertainment
- Adult Novelties

- Adult Video Stores
- Advanced Sales
- Check Cashing Services
- Child Pornography
- Collection Agencies
- Credit Repair Services
- Dating/Escort
- Diet Marketers/Programs
- Exotic Dancing Establishments
- Multi-level Marketing
- Pharmacies (Card Not Present/Internet)
- Pornography
- Sexual Encounter Firms
- Telemarketing
- Time Share
- Travel Clubs/Tours/Guides
- Vacation Packages

For these businesses to accept credit cards they typically have to turn to high risk merchant account providers. These companies are typically off shore and always charge higher rates than traditional merchant account providers. Rates can go as high as 20% of sales and some may charge set up fees of $1,000 or higher. The reason why these rates and fees are so high is the high risk merchant account provider needs to make sure they make enough money to cover the costs of the high number of chargebacks they will receive.

> Be sure to also read our blog posts Changing or adding products after establishing a merchant account to see why you need to plan ahead when opening a merchant and What Exactly is Adult Content? to learn more about the most common type of high risk content.

The Match File (A.K.A. Terminated Merchant File)

The Match File is a database file used by MasterCard and Visa processing banks to identify specific merchants and owners who have had their merchant accounts terminated. Once a merchant is on this list it is highly unlikely that future merchant account applications will be approved. The Match File is essentially a BLACKLIST from which it is almost impossible to be removed.

For a business or merchant to be added to the Match File they need to violate Visa and MasterCard rules in some way. The most common reasons include:

- Fraud
- Factoring (ringing sales for another business)
- An excessive number of chargebacks
- The processing bank concludes that serious violations of the merchant agreement could result in increased loss exposure to itself or the credit card community.

Once a merchant has been placed on The Match File only the processing bank that added them can remove them from it. The merchant must work with them directly to accomplish this.

You do not want to be on the Match File! [5]

Things You Can't Do

Just because you have a merchant account doesn’t mean you can do anything you want with it. Visa and MasterCard has guidelines governing their use. Here are some things you cannot do: [6]

- Personal Use

Visa and MasterCard do not allow their services to be used for personal reasons. All accounts must be established for one business and to be used only for that business' products and services. An account cannot be established for an individual nor can a merchant use their merchant account for personal reasons.

- Factoring
  Visa and MasterCard do not allow more than one business to use a merchant account. All accounts must be established for one business and to be used only for that business' products and services. When a business processes transactions for another business, even if they own that business, they are “factoring”.
- Charge More for Credit Card Transactions
  Visa and MasterCard does not allow a merchant to charge more for products/services paid for by their credit cards. They do not want paying by credit card to be seen in a negative light.
  If a merchant wishes to offset the additional costs of accepting credit cards, they should do one of the following:
  - Increase prices on their products/services for all purchases
  - Increase prices on their products/services and then offer a cash discount

  Charging a convenience fee for accepting credit cards is not considered acceptable.
- Set a Purchase Minimum
  Visa and MasterCard do not allow merchants to set a minimum purchase amount for which credit cards may be used. For example, a merchant may not declare that a purchase must be at least $50 in size in order to use a credit card for payment.

Payment

Naturally an important aspect of accepting credit cards is how fast you get your money from your credit card sales. Merchant account providers typically provide funds within two business days of when a batch is settled. This means if you process a sale on a Monday and settle your terminal that night, you will receive your funds that Wednesday. Weekends and Holidays do not count as business days so if a batch is settled on a Thursday night the funds from those transactions will not be available to the merchant until the following Monday.

It is possible to have your funds deposited into your business account with 24 hours of settling a batch. For this to occur the process bank must have a direct relationship with the bank you have your checking account through. An example of this is merchants who have a merchant account through Nova Information Systems and a checking account through Regions Bank will receive their funds in one business day due to the direct relationship that Regions Bank has with Nova.

An overlooked but important feature to note when selecting a merchant account provider is how your funds are deposited and your fees are subtracted. Ideally when you receive your funds you will receive the full amount of the deposit without any fees due being taken out. The advantage to this is it allows bookkeeping to be greatly simplified. If you have a batch of $500 settled on Monday, you can expect to see a deposit of $500 on Wednesday. No need to guess what fees were taken and if there are any problems you can spot them quickly. The fees for your transactions will be deducted at the beginning of the following month at one time. Shortly thereafter you will receive a statement that will detail your transactions and subsequent fees.

Getting Started

Once you have established your merchant account you still have responsibilities. Those responsibilities can be easily managed once you have an understanding of what they are and experience handling them. But for a new merchant they are probably at their most critical point and are outlined below:

1. Do a test transaction
   Run a transaction through your credit card terminal for $1.00. Ideally you can a test credit card number provided by your merchant account provider but using a real credit card is just as good. The goal is to verify that everything is programmed properly into your credit card terminal and that a transaction will run smoothly from start to finish.
2. Verify deposit of funds

After running a "live" transaction check the bank account you associated your merchant account with to make sure those funds have been deposited into that account. There are two things to keep in mind when verifying your deposits:

1. It takes two business days for Visa and MasterCard transactions to be deposited and up to three days for Discover Card and American Express

2. The amount deposited *should* be the same as your previous batch's total. However this may not be the case if you are having funds held for a reserve or have a merchant account where your fees are debited daily.

3. Check your statements
   As mentioned above there are many rates and fees you may be charged besides those quoted by your merchant account provider. In order to verify your quoted rates are corrected and see how often you are incurring surcharges and other fees you should review **each and every processing statement**. If you are making errors while processing this will be the fastest way to catch it and have it corrected. Also, if any errors were made by the processing bank or merchant account provider while establishing your account, it is better to catch it now then six months to a year later. Many processing banks have a policy of only refunding erroneous charges up until the next statement arrives. They then consider you satisfied with your statement and will not refund any fees you may have been entitled to.
4. Order supplies
   In general accepting credit cards does not require much in terms of physical equipment and supplies. Especially if you are an Internet or home based merchant. But if you are face-to-face with your customers, at the very least, you will want to provide them with a receipt of their purchase. There's nothing worse than finding out you've run out of receipt tape in the middle of a busy day. Ordering extra supplies is a good way to make sure you don't get caught off guard and can focus on processing your sales instead of figuring out how to get supplies in a hurry.
   The good thing about merchant accounts is once they are up and running for a couple of months you don't really need to pay much attention to them as they don't require much maintenance. Once you have reviewed a couple of statements and verified that everything is in order it pretty much will be the same thing month after month. All you really need to do on an ongoing basis is review your monthly statements to look for potential processing mistakes on your part by finding surcharges that you don't normally see. Also, your processor will occasionally put important notices on your statements which you need to look out for.

Conclusion

By now your head should be spinning from all of the new merchant account information it now possesses. And there's still more this website can do for you! Be sure to use your new knowledge along with our merchant account comparison worksheet and any of our four rate and comparison calculators to get the best merchant account for your business.