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Who's on First?

The Curious Effects of Mergers and Acquisitions

For those of us who are old enough to remember, you may recall the comedy team of Abbott & Costello and their trademark play on words routine entitled, "Who's on First?" The premise is that Abbott & Costello are watching a baseball game. Costello is trying to determine the names of the infield players. So, they engage in a humorous exchange in which Costello asks Abbott, "Who's on first?"

Unbeknownst to Costello, "Who" is the actual name of the player on first base; "What" is the actual name of the player on second base; and "I don't know" is the actual name of the player on third base.

What follows is a laughable misunderstanding in which Costello becomes frustrated as he repeatedly tries to discover the name of the player on first base.

All too often, players in the bankcard acquiring industry feel like Costello in the "Who's on First?" routine. Frequent mergers and acquisitions ("M&A") involving banks, ISOs, processors/third party service providers, and merchant account portfolios keep us begging the proverbial question.

Put another way, we ask, "Who owns the accounts? Where did the residuals go? Who's in charge? Who's responsible?" Using Abbott & Costello's baseball team as a construct, we can unwind the essentials of M&As and achieve a basic understanding.

I. Who's on First: The Original Players

This is the easy part. When a merchant account is formed, you generally have the original merchant, ISO, acquiring bank and processor/third party service provider. You have a series of agreements, which define the relationships between these players. The merchant agreement specifies the terms by which the merchant will relate to the ISO, acquiring bank, cardholders, and sometimes the third party service provider.

Then there are the agreements which govern the Bank-ISO relationship and the Bank-Processor relationship. At this stage, the players know each other, know their positions and what roles they play on the team. Life is good and the merchant account operates smoothly. Then it happens—someone "lets the dogs out" and everything changes—a merger or an acquisition occurs.

II. What's on Second: The New Players

To better discuss the new players resulting from mergers and acquisitions, let us consider the definitions of these terms. Black's Law Dictionary defines a "merger" as "The absorption of one company by another, [the] latter [company] retaining its own name and identity and acquiring the assets, liabilities, franchises, and powers of the former [company], and [the] absorbed company ceasing to exist as an independent business entity."

Black's Law Dictionary further defines "acquisition" as "the act of becoming the owner of certain property."

So, what happens in the bankcard industry when a merger or acquisition occurs? With a merger, one of the original players is absorbed by another company (a new player). It can be any of the following combinations, which join ranks to become one company (see chart below):

In an acquisition, one of the original players themselves (either the acquiring bank, the ISO, or the third party processor) is purchased by another company (a new player), or part of the original player's company or merchant account portfolio is purchased by another company.

To recap, we now know the legal definitions of mergers and acquisitions. We also know that the original players are either joined or replaced by new players in a merger or acquisition.

However, it is the resulting consequences of mergers and acquisitions, which can be simultaneously intriguing and confounding.

III. I Don't Know is on Third: The Consequences

Now that the merger or acquisition has taken place, the real fun begins. Either things operate wonderfully well or border on absolute chaos. I certainly support the practice of well executed M&As—those undertaken with good business judgment.

Such mergers and acquisitions allow for more efficient functioning of the bankcard industry through realization of better economies of scale and other beneficial mechanisms. However, based on the inquiries received by Bank Card Law, I know that most everyone would like to discuss the chaotic consequences of M&As.

Some of the most common bad side effects of M&As are:

- merchant accounts which get somehow "lost in the shuffle" from one company to the next,
- different or new procedures employed by the new company cause transactional difficulties such as increased charge-backs,
- ISOs and agents stop getting their originally agreed upon residuals,
- valuable merchant accounts are lost unnecessarily by the new acquirer, and
- no one is sure who is responsible for problem resolution and/or those responsible are overwhelmed or incapable of problem resolution.

For clarification, there are some general legal principles that apply to M&As and form a good foundation for understanding. First, the legal result of a merger in most jurisdictions, is that the absorbing company (the new player) stands in the shoes of the company it absorbed.

This means that whatever rights and responsibilities the original company had (i.e., residuals payment, debts, receivables,

fiduciary duties, etc.), now become the rights and responsibilities of the absorbing company (new player).

Likewise, in an acquisition, the company (new player) who acquires another company (original player) or some or all of its assets (i.e., merchant portfolio), stands in the shoes of the company it acquired or from whom it made an acquisition.

Therefore, you should look to the new player to contractually assume the role of the original player. But, remember that the legal principles above are general in nature, and there may be exceptions for a variety of reasons. Because of the numerous exceptions, it is strongly recommended that you consult a competent attorney to examine the contractual relationships of the players.

So, when faced with the post M&A question, "Who's on First?", you can at least draw upon some basic legal principles for understanding and hopefully fare better than the terribly confused Costello. Who knows, in your quest to determine who's on first, you may even discover, "Who let the dogs out!"

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