

So You Want to Get Paid?

A Payment Processing Primer

Payment processing is one of those aspects of your business that you shouldn't have to worry about. It's not your expertise and it's not one of the things you love about your business. However, since payment processing *discount rates* can range from 3% to 15% of revenues, it is very important to your bottom line that you choose a payment processor that fits your needs and reduces your overall processing costs as much as possible.

Types of Payments

There are 5 major ways you can collect online payments. (Not including my Uncle Sol who will not be available for 3 to 5 years, with time off for good behavior.) They are:

- ◆ Credit cards (Domestic and International)
- ◆ ACH or Direct Debit from a checking account
- ◆ Charge to Mobile Phone
- ◆ Cash (It surprises most people that your company can easily accept cash for online payments. More on this later.)
- ◆ Other Alternatives (Charge to Home Phone or 900#)

Later, we'll explain each of these in a little more detail. First, let's look at how payment processing works.

How Payment Processing Works

Because of regulation, the process is actually extraordinarily complex. The good news is, you don't need to understand most of it. Here are the simple parts of payment processing you should understand.

Issuing Bank

Your customer has a credit card. It has been issued by a bank such as Chase, Wells Fargo, Citibank, etc. That *Issuing Bank* guarantees that wherever the credit card is used, that the merchant will get paid. The issuing bank then collects from the user.

VISA and Other Associations

A credit card might say VISA, Mastercard, Discover or another name on it. VISA, Mastercard and the others are just *associations* that banks belong to. The association ensures that its member banks, and the merchants accepting their card, are in compliance with their standards and that payment flows smoothly when charges are made on a credit card.

How Payment Processing Works (cont.)

Merchant Bank

The *Merchant Bank* is the bank that you the merchant deal with. Similar to the way the issuing bank ensures the customer's credit worthiness, the Merchant Bank ensures your credit worthiness. Obviously, the ability to charge people's credit cards is a very powerful position and they must guarantee that you are a legitimate business who will deliver the purchased goods. If you don't, they are on the hook to return the money. If the bank grants you the right to charge people's credit cards, they give you a *merchant account*.

Merchant Bank's Processing Arm

Sometimes the Merchant bank may also have a payment processing arm, where you can apply for a merchant account. However, these banks typically only deal directly with large, low-risk entities. Dating sites don't generally fall into this category. If they will take you, you still may find them too confusing and may find it is easier to deal with a *Payment Processor*.

Payment Processor

This is a company that is designed solely to help you get a merchant account from the *Merchant Bank* and then process your payments and give you your money, (after taking their fee off the top.) They will help you get a merchant account from the association like VISA and you will be known as the *Merchant of Record*.

Third Party Processor

Sometimes you are too high risk for any bank to make you the *Merchant of Record*. You may be too small, too new or in a very high risk business like any site with nudity. When this occurs you may have to go to a *Third Party Processor*. In this case, they are the merchant of record. That bad news here is that they are much more expensive than if you were the merchant of record. The good news is that they are full-service and handle everything including collections, *chargebacks*, refunds and payment customer service calls, so if you are a small operation, they take a lot of problems off your hands.

eWallet or eMoney Institutions

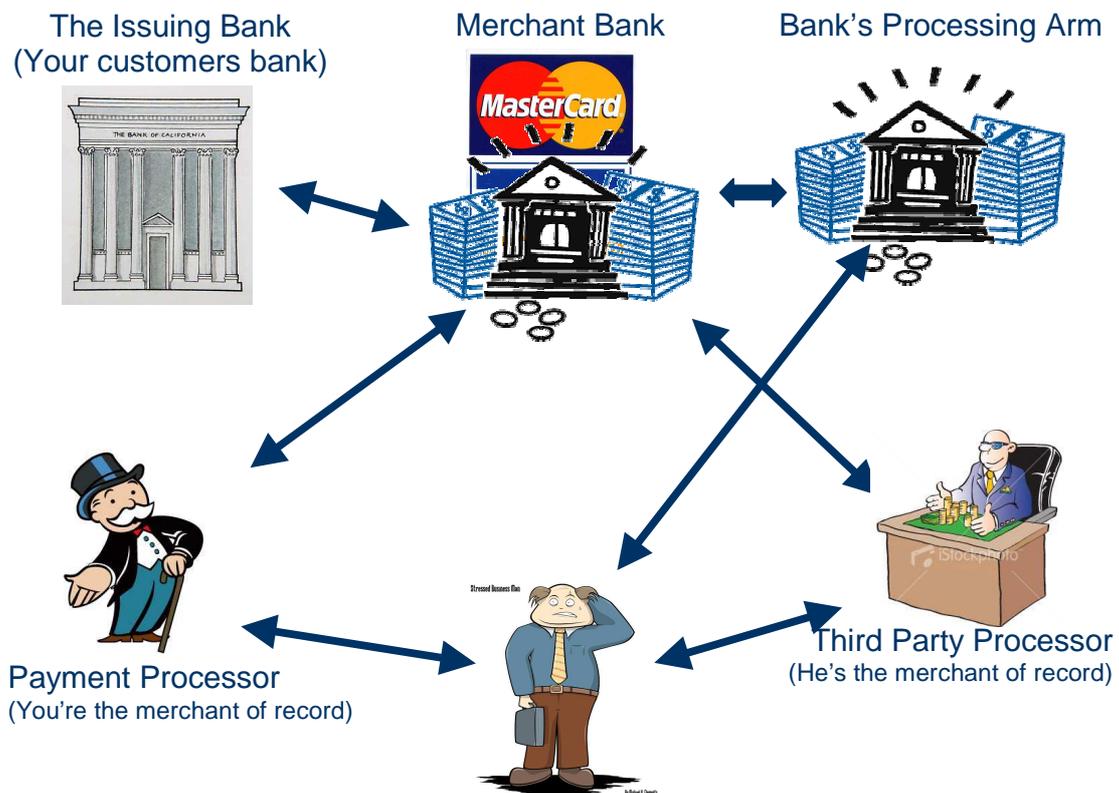
These are other ways to collect money that do not involve the traditional process. Examples are PayPal and ClicktoBuy. These do not typically offer a full array of services, so they are usually a supplement to your current payment processor. However, many consumers demand them. Because of this, many payment processors now include PayPal as part of their package.

How Payment Processing Works (cont.)

Alternative Payment Providers

Examples include PaybyCash and UKash. These are institutions that allow consumers to go to a retail location and pay cash for a prepaid debit card which can then be used on your site. Since estimates indicate that 40% of the population doesn't have a credit card with room on it, this is a great supplement to your normal payment processing. There are also alternative payment processors that just offer mobile payments or charge to 900 numbers. Some traditional payment processors have incorporated these alternative services or you can get them on your own.

Payment Processing Diagram

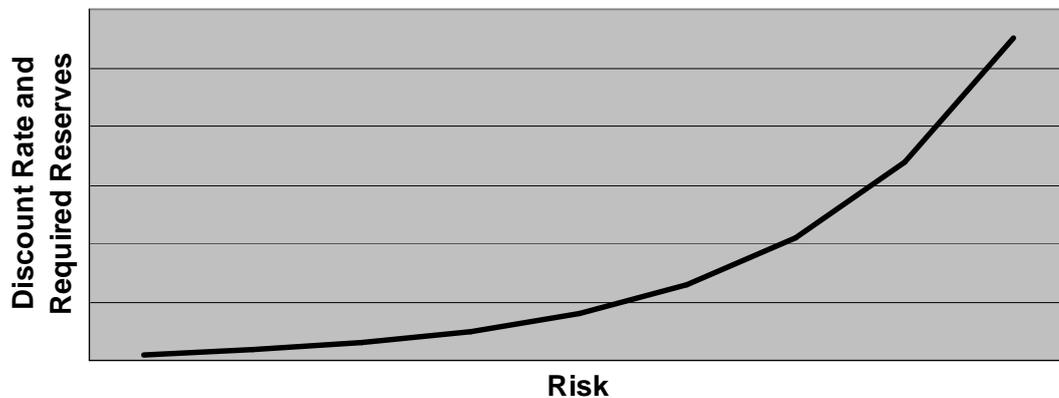


Understanding Risk

Risk is everything in payment processing. The higher your risk, the higher your *discount rate* and the greater the reserves you may have to allow the credit card processor to hold. Risk in this industry is simply the chances that the person who bought the product will call their issuing bank and ask for their money back. The issuing bank will demand this money from the merchant bank and the merchant bank will demand it from you, (if you are still in business.) This is called a *Chargeback*. If the merchant bank can't collect from you or if you can't show that it was a legitimate charge, they are on the hook and this is their risk. Factors that affect risk are

- Card Not Present (CNP) – All online transactions are CNP.
- Dating Industry – The dating industry is higher risk than some.
- Adult Industry – Considered one of the highest risk businesses.
- Age of Business – The older your business, the lower the risk.
- Annual Revenues – The greater your revenues, the lower your risk.
- Size of Transactions – The greater the transaction size, the higher your risk.
- Chargeback History – Once your merchant account has been granted, your chargeback history will be watched. If it is higher than they expected, they can increase you fees. If it is lower, you can negotiate to get your fees decreased.

The Cost of Risk



Choosing the Right Payment Processor

When looking for a payment processor you should be asking the following questions:

- ✓ **Do they accept dating and/or adult sites?**
Many do not.
- ✓ **Will you qualify for a merchant account?**
They should be able to give you some sense of this before you fill out the app.
- ✓ **Are They PCI Compliant?**
This is VISA's standard. If they are not PCI Compliant, don't deal with them.
- ✓ **Does the Bank Pay You Directly?**
If you are the merchant of record, you should be paid directly. The money should not go through the processor unless they are the merchant of record.
- ✓ **How many banks do they represent?**
A processor which represents multiple banks may be able to offer you more choices and get you a better deal.
- ✓ **Who owns the data?**
Typically, if you are the merchant of record, you own the customer data. If you use a third party processor, they own the data. This is important because if you decide to switch processors down the road you are going to want that data.
- ✓ **How much Customer Service assistance do you need?**
Some companies offer full customer service to your consumers on billing issues. They charge for this. Some processors do not offer this additional service, but are less expensive. If you are a small operation, you are going to want a processor that will handle this for you.
- ✓ **What method of payments do they accept?**
Almost everybody accepts the major credit cards. However, you are also likely going to want to accept direct debit from checking accounts as well as mobile phone charging and cash payments. If your processor doesn't accept these, there are *Alternative Providers* that offer these ala Carte.
- ✓ **What currencies do they accept and settle in?**
Most settle in US and Canadian Dollars plus some others. If you are based in another country, make sure they offer your currency as well.

Choosing the Right Payment Processor (cont.)

- ✓ **What kind of risk management do they offer?**
One of the best ways to prevent *Chargebacks* is not to accept payment from high risk individuals. A good payment processor should help you decide who not to accept payments from, thus lowering your risk. They can do this by assigning risk scores and keeping a database of “blackballed” customers. If they don’t offer risk management, go somewhere else.

- ✓ **Do they offer customized scrubbing?**
This simply means that when they are assigning risk scores and deciding who not to accept payments from, you get input into this process.

- ✓ **Can you set your own refund policies?**
The easier it is for a consumer to get a refund, the less likely they are to chargeback. Balancing how easily you give refunds with the number of chargebacks that occur, will maximize your revenue.

- ✓ **What is their discount rate?**
This is simply what the payment processor gets for his services expresses as a percentage. It is typically 3% to 15% of the charge depending on how much service the processor provides, who is the merchant of record, your risk score and your ability to negotiate.

- ✓ **What are their setup fees?**
Some payment processors have setup fees. Some do not.

- ✓ **When do you get paid?**
Depending on your size you can get paid up to once per day or as little as once every 2 weeks.

What's it Going to Cost Me?

Total costs vary widely so it's good to talk to a number of processors. Understand that rates are negotiable both at the time of signing the contract as well as down the road once your track record has been established.

- **Discount rate: 2% to 15% of sale**
Varies based on services provided, merchant of record and your risk score.
- **Transaction fee: \$0.25 to 0.50 per sale**
This is on top of the discount rate.
- **Set up fees: \$0 - \$1500**
What you pay when you sign up with the payment processor.
- **Reserves: 5-15% of monthly revenues**
How much the payment processor is going to hold back from you just in case you get too many chargebacks. After 6 months to a year of history, reserves are up for reevaluation.
- **High Risk Reg. Fee with Visa and MC (\$1500)**
If you have nudity on your site, this is a standard fee.

Finally, remember this. **Everything is Negotiable**, particularly in this industry. Negotiate the best deal you can up front. Then keep in mind you can renegotiate again after you have 6 months to a year of history.

A Few Final Thoughts

Talk to 3-4 different processors and choose the one that is right for you. The least expensive may not be the best. You may need services that the low-cost provider doesn't offer, that if you don't have, may end up costing you more in the long run.

For further information, Courtland Brooks keeps a spreadsheet which compares many payment processors. None of these companies are clients, so you know it is unbiased. Email mark@courtlandbrooks.com for the spreadsheet.