

Merchants Are Now Consumers? FTC Settles Action Against Payment Processor After Alleging Its Merchants Are “Consumers”

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On July 29, the Federal Trade Commission (FTC) filed a complaint and executed a stipulated order with payment processor First American Payment Systems LP (First American) and companies that market its services — Eliot Management Group LLC (Eliot) and Think Point Financial LLC (Think Point) (collectively, the defendants). The FTC alleged that the defendants violated Section 5 of the Federal Trade Commission Act (FTC Act), 15 U.S.C. § 45, and Section 4 of the Restore Online Shoppers' Confidence Act (ROSCA), 15 U.S.C. § 8403, arising out of the marketing of First American's payment processing services to merchants and the alleged failure to provide clear and conspicuous contractual terms in the online application and agreement between First American and the merchants.

Section 5 of the FTC Act prohibits unfair and deceptive acts and practices by businesses against consumers. ROSCA is also a consumer protection statute that, among other things, prohibits businesses from charging consumers for goods or services sold in transactions effected on the internet through a negative option feature unless the business: (1) clearly and conspicuously discloses all material terms of the transaction before obtaining the consumer's billing information; (2) obtains the consumer's express informed consent before making the charge; and (3) provides simple mechanisms that allow consumers to stop recurring charges.

The defendants agreed to pay \$4.9 million to the FTC, which will be used for redress. This is an unprecedented case because the FTC is using consumer protection statutes to sue a processor for alleged acts against the merchants with whom the processors do business.

First American provides payment processing services to small businesses, and its sales agents are Eliot and Think Point. Although First American provides its payment processing services to small businesses, the complaint refers to the small businesses as “consumers” even though they are not consumers (some of the merchants, however, are sole proprietors). While it is not unprecedented for the FTC to sue a business for alleged violations of the FTC Act made against other businesses, this lawsuit represents the first time that the FTC has sued a payment processor for alleged violations of the FTC Act arising out of alleged false statements concerning payment processing services that are marketed and provided to other businesses. The alleged false statements, made through Eliot and Think Point, include the following:

- Although the written agreement between First American and the merchants stated that the merchants would have to pay an early termination fee, the defendants allegedly told the merchants (before the parties signed the

contract) that the merchants would be able to cancel the payment processing services at any time without an early termination fee. The merchants claimed that they were not aware of the early termination fee until they attempted to cancel the processor's services.

- Although the written agreement between First American and the merchants listed the fee schedule, the defendants allegedly told the merchants (before the parties signed the contract) that the processing fees would not exceed a certain dollar amount.
- The defendants also allegedly told the merchants that the merchants would save significant amounts of money on processing fees compared to their prior processing relationships. According to the complaint, that promise never materialized.

The complaint also alleges that the defendants violated the FTC Act by continuing to debit the merchants' accounts notwithstanding that the merchants expressly told First American to stop debiting their accounts. The defendants sometimes disguised the fact that they were attempting the debits by changing the company names associated with the debits. These debits occurred after the merchants terminated First American's processing services, and First American attempted to collect the early termination fee and other fees through the debits.

As stated above, ROSCA only applies to business-to-consumer transactions. Although automatic renewal clauses stating that the agreement will automatically renew unless terminated a certain number of days before the end of the current term are common in the payment processing industry, the FTC alleged that the automatic renewal (also known as a negative option) in First American's agreements violated ROSCA. The FTC alleged that First American violated ROSCA by failing to disclose all material terms of the transaction clearly and conspicuously, failing to obtain the merchants' express informed consent before charging them (after termination), and failing to provide simple mechanisms for the merchants to cancel the contract. The ROSCA violations also included: (1) allegations that the processor's sales agents did not discuss the automatic renewal with the merchants before the parties executed the agreements; and (2) allegations that the merchants could not review all of the terms and conditions of the agreement without clicking on several hyperlinks embedded throughout the online merchant agreement.

Our Take

Because the FTC sued a small business arising out of alleged acts in its business dealings with other small businesses, every payment processor that provides processing services to small businesses should be concerned about this case. In civil litigation, most breach of contract and fraudulent inducement cases with similar alleged facts would not survive a motion to dismiss where, as here, the written agreement that the parties signed is allegedly inconsistent with the oral representations made by the defendant. An integrated written agreement will most likely trump the contract and tort claims in civil litigation. While the FTC's complaint alleged that some of the merchants spoke English as a second language, nothing prevented the merchants from seeking redress through state laws that require an agreement to be in the same language in which it was negotiated. The FTC, however, stepped in and sent a signal that it will label small businesses as "consumers" in order to allow the FTC to state a

claim against payment processors irrespective of the state law remedies available to the businesses on an individual basis.

Another interesting point in this case is that the FTC alleged that the processor violated the FTC Act by debiting the merchants' accounts without consent. Engaging in such an act will likely violate Regulation E, which implements the Electronic Fund Transfer Act (EFTA). EFTA, like the FTC Act and ROSCA, only applies to consumers and it appears that the FTC did not allege an EFTA violation because the Consumer Financial Protection Bureau (CFPB) enforces the EFTA. In any event, this case may be a sign of things to come for payment processors under FTC Chair Lina Khan.

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