DRN-4604920

The complaint

A company, which I will refer to as S, complains that Elavon Financial Services Designated Activity Company treated it unfairly by imposing a cash reserve and restricting access to its funds.

What happened

Elavon told us:

- In early 2023, S had an existing merchant services account with Elavon. The terms of that account allowed Elavon to undertake regular credit reviews, and establish a cash reserve on S's account (that is, to delay the payment of funds that would otherwise have been immediately payable to S, and hold those funds in reserve until all of S's obligations to Elavon had been met).

- It has strict guidelines in place for assessing new and existing customers while remaining compliant with its credit policy and internal audit requirements.

- On 27 February 2023 it notified S that a credit review was scheduled on S's account for March 2023. It went on to request further information to help it complete that review.

- On 11 April 2023 it wrote to S to explain that it had decided to place a cash reserve on S's account. It took that decision because of concerns about S's financial situation and processing.

- One of S's directors contacted it on 11 April 2023, and it replied on the same day to explain that S's chargebacks and refunds were very high as a percentage of its total transactions. Chargebacks represented 3.61% of transactions over the last 12 months, and refunds were 20.15%. It said that these facts caused it concern, and it would like to know if S had any explanation for the high levels.

- Elavon also told S that as S's acquirer it held some responsibility for these transactions. It later explained that that is because it carries a substantial risk of incurring liabilities in the event of a merchant's insolvency and/or inability to meet its contractual obligations. The principal risk for Elavon is potential chargeback liabilities and/or credits for refund transactions in the event that a merchant becomes insolvent or otherwise fails to deliver the goods or services that a customer purchased from the merchant.

- On 14 April 2023, one of S's directors complained about the actions Elavon had taken up to that point.

- On 24 April 2023 it told S that following the credit review, all negative batches (batches containing refund transactions) would be stopped, meaning that Elavon would not pay money to the cardholders unless S provided funds to allow it to do so.

Elavon also said that any further refunds to cardholders would need to be pre-paid. It did not at any point refuse to process refunds for S's customers

- On 25 April it issued a termination notice to close S's merchant account after a 60-day notice period. That closure date was later expedited at the request of one of S's directors.

S's directors told us:

- They were told on 10 April 2023 that their Elavon terminal had been restricted and a reserve imposed because they had not provided the information Elavon had requested. But they co-operated with all the information requests they received, and made clear that they were willing to provide further information if Elavon needed it.

- Elavon unfairly and unreasonably placed a restriction on S's account. That meant funds paid by S's customers were unavailable to S, causing financial distress to the company.

- They told Elavon that Elavon's actions meant S could no longer fulfil its own customers' orders and so Elavon would need to refund S's customers for any orders placed during the time the account was restricted. Elavon did not refund the customers, so S had to inform its customers that they would have to open a chargeback to recover their funds.

- They opened an account for S with an alternative merchant services provider, but a couple of months later Elavon made contact with the new provider to say that S had a high level of chargebacks. Elavon did not disclose that the reason for those chargebacks was Elavon's own failure to refund S's customers directly.

- The underlying problem here was Elavon's failure to communicate effectively. That caused a domino effect resulting in further chargebacks, significantly affecting the reputation of S and creating mental, financial and emotional distress.

One of our investigators looked at this complaint, but did not uphold it. He sympathised with the difficult position S's directors were in, but he thought Elavon had treated S fairly. S's directors did not agree, so the matter was referred to me.

My provisional decision

I issued a provisional decision on this complaint in March 2024. I said:

> "I understand that the outcome of this complaint is very important to S's future, and that its ability to take card payments is key to its success as a business. But in light of the evidence I have seen so far, I don't think it would be fair for me to order Elavon to pay compensation. I explain why below.
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> I'm aware that there is a dispute between the parties as to whether Elavon should have asked for further information about S at the time that it did and in the way that it did. But I think the primary dispute here is about the outcome of the credit review rather than the way in which Elavon went about obtaining information from S. S's directors think that Elavon was wrong to introduce a cash reserve, and Elavon maintains that it was entitled to do so. But I don't think the dispute about when and how Elavon should have asked for information makes a material difference to the

outcome here. By 11 April 2023 Elavon was satisfied that it had the information it needed to carry out its credit review, and it had decided to place the cash reserve.

I can see that the cash reserve was for around 10% of S's annual turnover, and it is obvious that a reserve of that magnitude would have a very significant impact on S.

The conditions S agreed to when its Elavon account was opened do give Elavon the right to establish a cash reserve in certain circumstances (including, but not limited to, circumstances in which Elavon "become[s] aware, or reasonably suspect[s] that [the merchant is] an Excessive Chargeback Merchant"). But whether Elavon had the right to establish a cash reserve is not the end of the matter, and I must also consider whether Elavon acted fairly.

The chargebacks on S's Elavon account were objectively high. For context, Mastercard defines a "Chargeback-Monitored Merchant" as a merchant with a chargeback ratio of more than 1% and at least 100 chargebacks in a calendar month, and an "Excessive Chargeback Merchant" as a merchant with a chargeback ratio of at least 1.5% and at least 100 chargebacks in two consecutive calendar months. Elavon says S's chargeback ratio was 3.61%, and in the circumstances, I think it was reasonable for Elavon to have concerns.

Elavon is also right to say that a merchant's high chargeback ratio can have significant consequences for itself. Merchant acquirers like Elavon have their own obligations to the card schemes, and must comply with the schemes' chargeback monitoring programs.

I am satisfied that Elavon did review the financial information S's directors provided, and that it made its decision to impose the cash reserve after considering all the information available to it. S's directors later provided further information, particularly as to the reasons for S's return and refund levels, but Elavon was not prepared to change its decision.

Given that the account's terms and conditions say Elavon was entitled to decide to impose a cash reserve, that I think Elavon had legitimate concerns about the conduct of S's account, and that Elavon was itself exposed to financial risk if S did not meet its obligations, I don't think it would be fair for me to say that Elavon was wrong to make the decision it did. I do have some concerns about whether Elavon could have handled the matter in a way that would have been less disruptive to S's business – for example, whether it could have first given warnings about S's high chargeback rate, or imposed a smaller reserve – but I haven't asked Elavon for any further information about those concerns. Ultimately, I think that even if I were to find that Elavon could or should have handled this matter better, it still wouldn't be fair for me to award compensation to S.

S's directors' response to Elavon's decision to impose the cash reserve was to make their own decision to stop trading through Elavon. That meant Elavon never did reach a cash reserve of anywhere near the amount it had said it wanted, and so I don't think it would have made a difference if Elavon had initially imposed a smaller cash reserve. Given S's directors' explanations about S's business, I don't think that they would have been able to significantly change their chargeback or refund ratios even if Elavon had given them warnings, so again I don't think a warning would have made a practical difference.

I am aware that Elavon continued to take payments from S's customers after putting the cash reserve in place, but that is because S continued to send those payments to

Elavon for processing. I know S's directors wanted Elavon to stop processing the payments, but Elavon wouldn't even have known about the payments unless S (or S's agents) had passed the relevant details on to Elavon. If S's directors wanted Elavon to stop processing payments, it was their responsibility to ensure that the details of those payments were not sent to Elavon.

I am not persuaded that Elavon ever refused to process refunds for S's customers. However, I do accept that Elavon told S's directors that it would only process refunds to extent those refunds were pre-paid by S. I think that was reasonable, particularly as by that point S had stopped sending new payments to Elavon for processing. If Elavon had paid the refunds without first asking for funds from S, that could have left Elavon out-of-pocket.

S's directors say that the fact the refunds weren't processed caused a domino effect, because S had to advise its customers to request chargebacks instead. I appreciate that the additional chargebacks will have further impacted an already very high chargeback ratio. But as I've said, I don't think Elavon did anything wrong in refusing to refund transactions without pre-funding – and so I don't think it would be fair for me to uphold this complaint because the chargebacks increased.

It is unfortunate that S's relationship with a different merchant acquirer later appears to have broken down, but Elavon is not responsible for the actions of its competitors. Similarly, Elavon is not responsible for its competitors' decisions about what evidence those competitors wish to take into account before deciding whether to offer accounts to new merchants (or before deciding what terms to offer to new merchants). Unless S can show that Elavon reported information about it that was not true, I see no basis on which I could uphold this aspect of S's complaint."

Elavon did not provide any further evidence in response to my provisional decision. S's directors did, and I confirm that I have read their further evidence in full. Briefly, they said:

- Elavon failed in its duty of care, and gave them no warning that it intended to impose a reserve. It had many opportunities during the first three months of 2023 to explain that it had concerns about S's account, but it did not take any of those opportunities.

- They fully understand and accept that Elavon had the right to put a reserve in place, but they consider that the way Elavon went about doing so – with no communication – was unacceptable. They have only recently found out that their former Elavon account manager left the business in 2022 and their account was not given to anyone else. They believe that if somebody else had take over her responsibilities, they would have known that there was a possibility the reserve could be put in place, they could have planned for that eventuality, and S would not have suffered a loss.

- They noted my comment that S continued to send payments to Elavon for processing after the reserve was put in place, but they said they had no choice about that. Elavon had told them that it would look at additional information, giving them the impression that Elavon was buying them time. Elavon took a further 12 days to make its decision, but it should have explained from the start that it had made its final decision on 11 April 2023. Elavon misrepresented the position, and wrongly led S's directors to believe that it would reverse its decision if they provided more evidence.

- S's bank statements prove that at the time it had a healthy balance and was in a sound financial position.

- Elavon has still not complied with their Subject Access Request, but they are satisfied that it was Elavon that told their new merchant acquirer about the chargebacks.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

Having done so, whilst I am sorry to further disappoint S's directors I have come to the same conclusions as I did in my provisional decision. My reasons are given in my provisional decision, and expanded on below. I now confirm those provisional conclusions as final.

In my view, S's directors were always aware that Elavon might impose a reserve. As they accept, the contract they signed up to gave it that right. I don't think that Elavon was required to give a further specific warning.

In addition, S's directors knew that Elavon was conducting a review of S's account. Clearly they hoped that the outcome of that review would be that Elavon would not choose to make any changes (or even that any changes would be beneficial to S). But I consider that it is always a possibility that a review of this nature will produce changes which are not welcomed. Again, I don't think Elavon was required to give an explicit warning of the possible outcomes of its review.

The evidence available to me suggests that Elavon did not make its final decision on 11 April 2023. It appears that Elavon was willing to consider S's further financial evidence – and in fact did consider that evidence – but did not change its mind. It is obvious that Elavon and S's directors disagree about S's financial strength, but it is not for me as an ombudsman to tell Elavon what its risk tolerance should be. I thought carefully about all the evidence that has been provided to me, but I have not seen anything to suggest that Elavon was wrong to make the decision it did.

As I said in my provisional decision, it is unfortunate that S's relationship with a different merchant acquirer later broke down. S's contract with Elavon allowed Elavon to share information about S with Mastercard and VISA. The contract also explained that the card schemes in turn may choose to enter information about S into MATCH (Member Alert to Control High Risk Customer, maintained by Mastercard) or VMAS (Visa Merchant Alert Service, maintained by VISA). I don't know why the new merchant acquirer chose to take the actions it did, but Elavon is not responsible for the other merchant acquirer's actions. I haven't seen anything to suggest that Elavon has reported anything about S that was not true.

My final decision

My final decision is that I do not uphold this complaint about Elavon Financial Services Designated Activity Company.

Under the rules of the Financial Ombudsman Service, I'm required to ask S to accept or reject my decision before 6 May 2024.

Laura Colman
Ombudsman