

# Reach

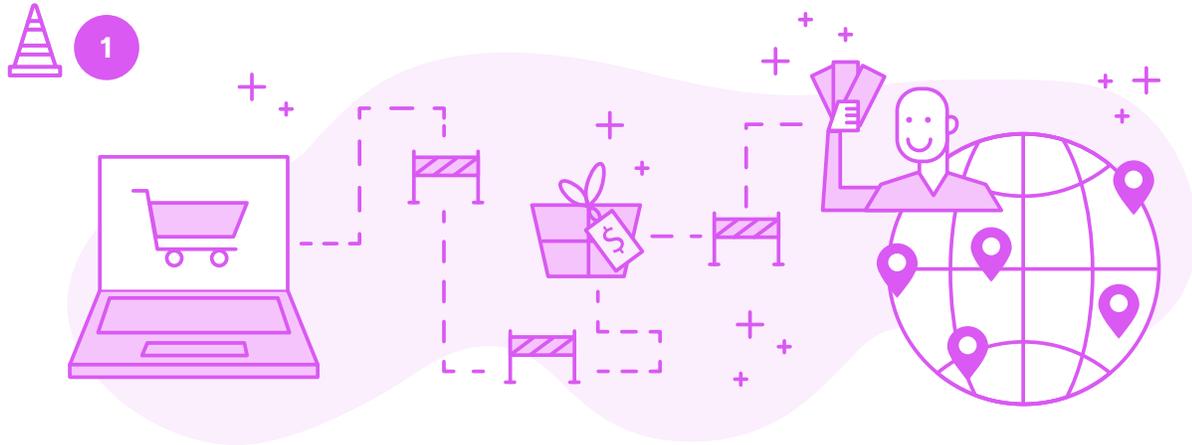
## The Merchant of Record Model

Why a Customer-First Payments  
Strategy Works Better for Everyone

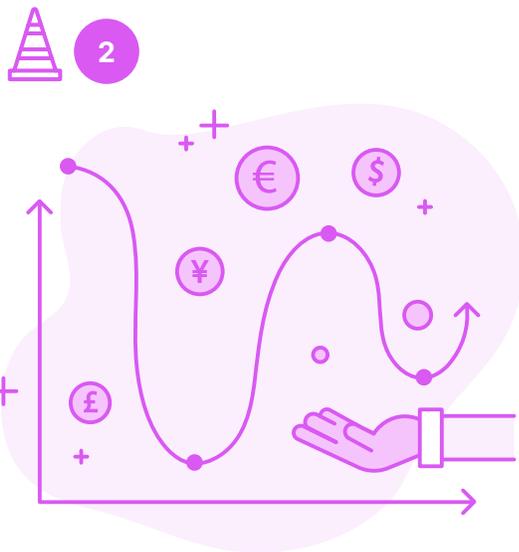
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# 01 Executive Summary



Online retailers already have the ability to reach into international markets, but even if a consumer wants to make a purchase and a retailer wants to make a sale, a series of barriers can create friction that prevents a transaction from being completed.



Retailers must understand how the volatility of currency can affect their profits.



Retailers must navigate a series of compliance, taxes and regulations that can stop them from optimizing their payments or offering best practices.



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Online retailers must also be sensitive to specific needs of local consumers...



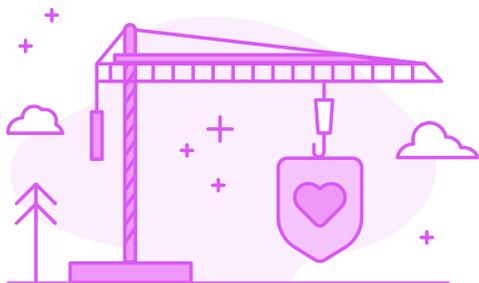
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...including alternative payment methods that vary from country to country...



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...and must build trust...

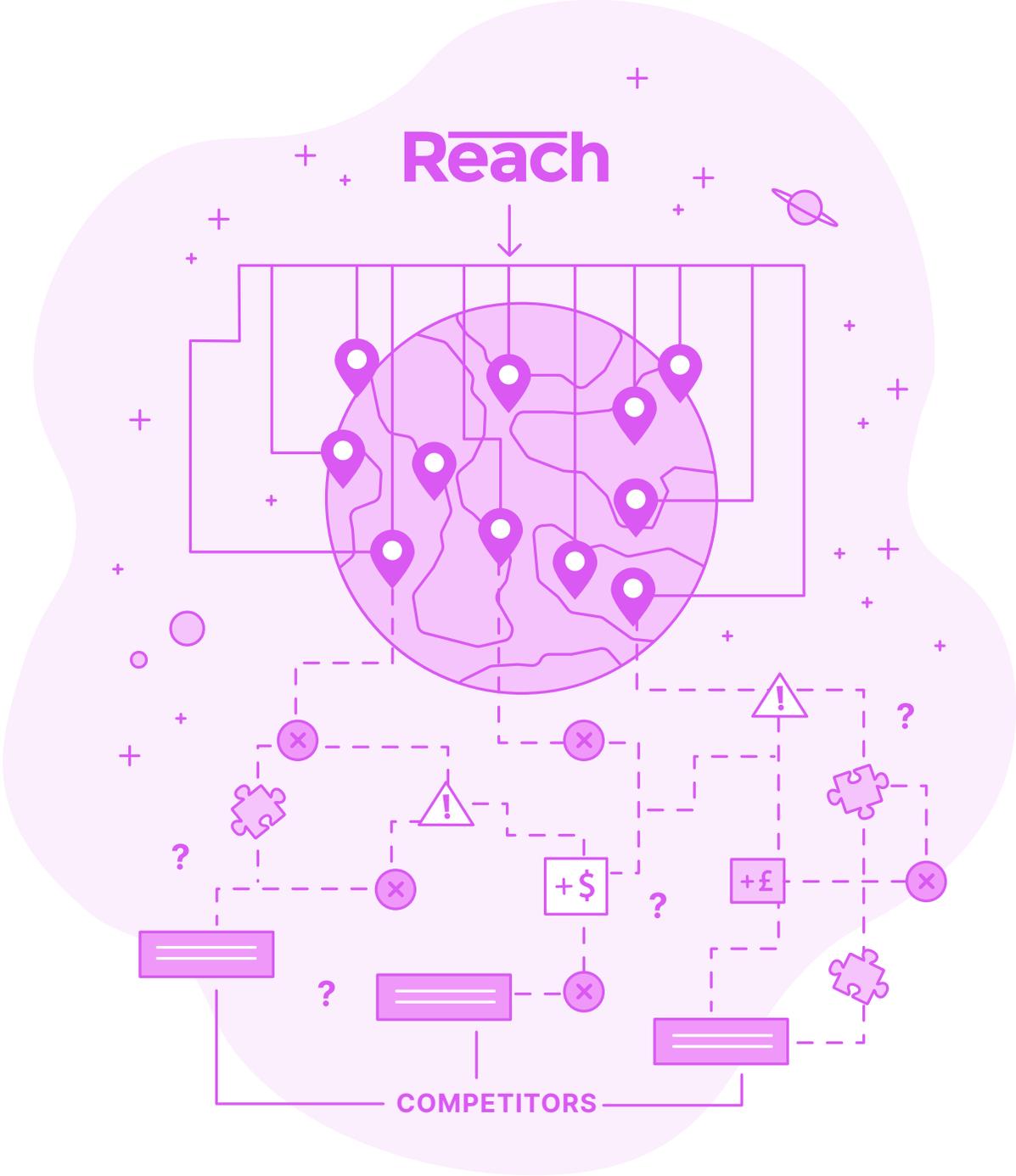


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...while being cautious of fraud.



A third-party **Merchant of Record** model, such as that used by **Reach**, offers online retailers a way to navigate and overcome barriers, including compliance and regulatory hurdles, in order to offer best practices, scale quickly in global markets, and compete with both retail giants and local players.



## 02 Introduction

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No matter where a retailer is based today, its customer base is global. Yet most merchants have yet to capture the full international market opportunity available to them, even as demand rises for cross-border transactions.

Too many merchants with expertise in their home countries are not properly sensitized to the wants and needs of international consumers, which can vary widely from country to country.

With too narrow of a view toward global customers, a retailer can easily fail to provoke the interest of consumers overseas. Even if it manages to engage with a customer and both sides want to complete a transaction, friction can arise that ultimately dooms a sale.

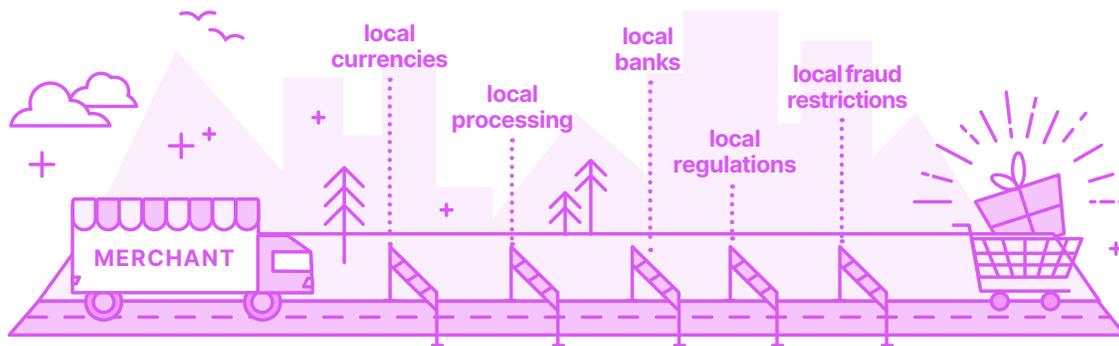
Within a retailer's home country, many customer-service decisions seem obvious: Conduct transactions in native currency, allow consumers to use the payment methods they prefer, and process the payment through a local provider. That's plain common sense, as well as best practice. But when merchants expect to sell into other countries, they must take into account that consumers in other countries want the same things — and often fail to do so.

A vast majority of global customers show a **preference for using the currency of their home countries** when buying online, but as of 2018, fewer than **10%** of the 1,000 largest online retailers actually offer transactions in multiple currencies.

Where do these pitfalls arise, and how can retailers reduce friction between themselves and international consumers?

At numerous points along the way to a sale, retailers must serve a diverse customer base in the way the consumer demands.

### Traditional Cross-Border Processing



They must offer local currencies, local processing of transactions, and drawing on local banks. They must allow the use of consumers' preferred credit cards or other payment methods. They must comply with local regulations and fraud restrictions.

For a consumer who clicks the 'buy' button and completes the checkout process, only to see the transaction fail, the results can be exasperating.



And for a merchant, not only is the transaction lost — so is the customer, for future purchases.

Overcoming these barriers can lead to numerous benefits for a merchant.

With solutions in place, outcomes improve, and a retailer can unlock a potentially huge market opportunity — if only it can give customers what they want. And satisfied customers become repeat consumers who sing the praises of the merchant. These brand evangelists then draw in even more cross-border customers.



To reach international consumers, a merchant has a choice. A retailer can set up a host of international subsidiaries that are capable of local transaction processing, but that can be an expensive chore that becomes a legal and regulatory management nightmare. Most retailers don't even go this far. Most simply process transactions cross-border, which may seem like an easy fix at first glance, but in fact, results in higher processing fees, higher decline rates, hidden fees to their global customers, and false positives in their fraud systems. So then, what is the best choice for a merchant who wants to sell overseas but wants to avoid both the hassle of managing hundreds of international offices and the poor customer experience of processing cross-border? If it fails to address the opportunity and take steps to overcome those barriers, it will simply leave money on the table.

Is it worth it for a merchant to set up shop in multiple countries? A retailer may opt to do it piecemeal, country by country, based on market size. It may be worthwhile for a retailer to do so in its largest international market, but the process of adding more countries does not scale very well. As its ambitions widen further, the retailer is likely to find managing relationships in multiple countries to be a cumbersome task. The more complicated the process becomes, the worse the ROI for a globally expanding retailer.

Instead of taking on this daunting task of localizing country by country, retailers can partner with a **Merchant of Record (MOR)** such as Reach to reach into numerous markets simultaneously. Merchants who have mapped out a clear plan for global success can outsource to a third party, a comprehensive international payments solution that is already attuned to the needs of global consumers in multiple countries. This is the **Merchant of Record** model.

## 03 The Merchant of Record Model .....

The Merchant of Record, or “MOR” model uses a **third party service provider to process transactions in multiple countries via local entities** that have established relationships with in-country banks.

The MOR is fully compliant with up-to-date local regulations, and gives retailers a one-stop shop for international payment processing, eliminating the need to establish and maintain connections in diverse geographies with disparate needs.

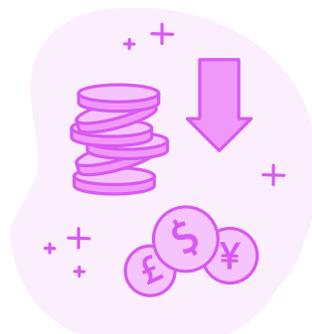
In this Merchant of Record model, the MOR takes flash title of the goods that are being sold to the end consumer. This means that merchants with no international offices can still be international. The advantage of this MOR model is that merchants can access local acquiring and payment methods while avoiding the difficulty of maintaining regulatory compliance, which requires a local entity in these markets. Instead, the MOR does this for the merchant.

Using the MOR model means that merchants can be as global as the MOR. **In Reach's case**, that means **a merchant can be local all over the world**, even without the added complexity of maintaining these foreign offices - they simply offload this administrative and organizational complexity to Reach.

### Local processing through an MOR...



Leads to higher approval rates



results in lower overall fees



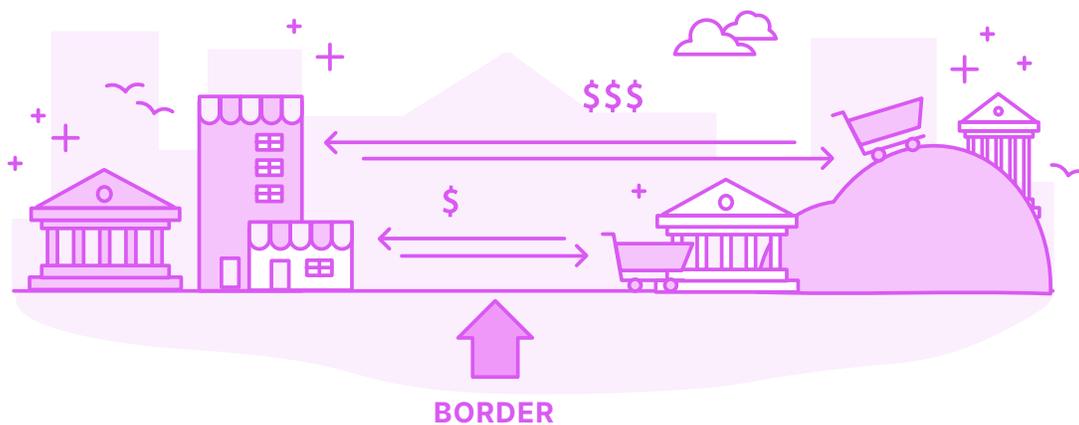
and eliminates foreign transaction fees for the cardholder

## 04 Credit Card Acquiring .....

Retailers doing business in multiple markets need to understand how credit card transactions work across borders, and the intermediaries that can help complete transactions — or block them.

A credit card acquirer is a bank that processes transactions on behalf of a retailer or other merchant. These can be local banks, or major international banks — for example, Royal Bank of Scotland, Allied Irish Banks, or Bank of America. Each transaction flows through a credit card acquirer, among several steps.

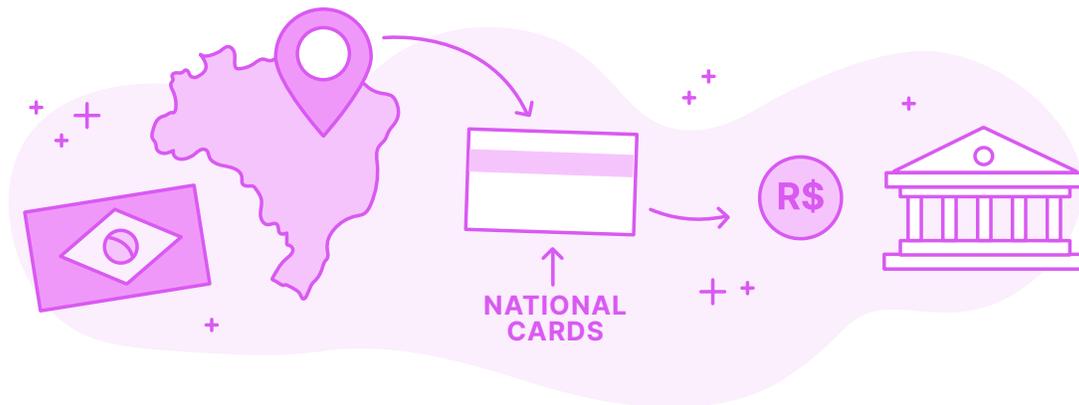
Cross-border transactions require relationships among multiple banks, and as the distance between the issuer and the processor gets larger, so, too, does the interchange rate charged for that transaction. Think of the process as being similar to data roaming on a mobile phone: The farther one gets from the original source, the more likely one is to incur charges.



Cross-border transactions are also seen by many processors as carrying higher risk. If a person travels into another country without telling one's bank at home, the traveler might find his or her credit cards useless, since any transaction can be declined. The same thing happens for online transactions. A failure of trust can doom a transaction as well. Suppose a customer in Japan is trying to make a purchase from a U.S.-based retailer's website. An issuing bank may see the transaction as posing a heightened risk, perhaps because it comes from an unknown acquiring bank, and therefore reject the customer's credit card outright. Customers rejected once are likely never to return.

In some geographies, a majority of consumers are restricted to using local banks.

Consider the case of a U.S.-based merchant selling into Brazil. About **70%** of online credit card transactions by Brazilian consumers are conducted using so-called “national cards.” Those cards accept transactions using only local currency — the Brazilian real — and may be processed only through Brazilian banks. Therefore, a merchant would need to have a relationship with local credit card acquirers in order to complete a transaction with a consumer who has only a national card.



Moreover, in the roughly **30%** of online transactions in Brazil that involve international cards, the issuing banks charge **high foreign exchange transaction fees** that discourage purchasing. In addition, the Brazilian government levies the Imposto Sobre Operacoes Financeiras (IOF) tax, a **6.38% tax on cross-border transactions** that shows up as an unwelcome line item on the customer’s credit card statement.

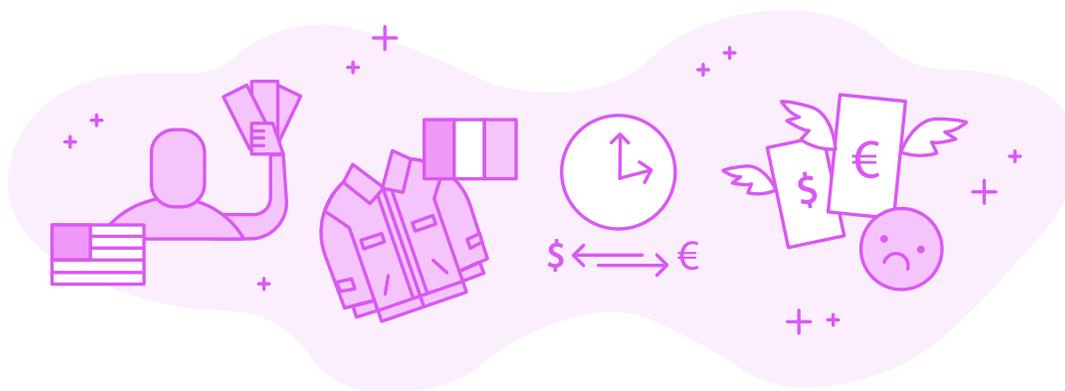
Processing transactions locally is obviously the best option for retailers, and can eliminate some steps that can hamstring a cross-border transaction. Yet some barriers can stop a retailer from doing so. One must be in compliance with local regulations, maintain local entities staffed with various levels of employees, ensure these offices have local operations and that money flows through the local offices, and manage local bank accounts and connections to local banks.

## 05 Currency Management .....

A retailer may see other currencies as foreign, but to a customer in another country, one's native currency is the most familiar one. Global consumers are always paying in their local currency, regardless of what retailers offer and accept.

Trouble is, intermediaries such as local banks or services such as PayPal can drive up prices by an average of 3% — and sometimes far more — by adding fees and other ancillary costs. Moreover, the number of steps in a cross-border transaction can impede checkout flow, raising another barrier that can thwart a purchase — and erode consumers' trust.

Attempting to manage multiple currencies, however, opens up a retailer to a basket of potential problems, mostly tied to risk management. Day-to-day fluctuations among currencies can change the value of a transaction, sometimes drastically. That can lead to unfortunate outcomes for either party in a transaction: A customer can be angered by the change in an item's cost, or a merchant can get stuck with lost value and slimming margins.



For example, suppose an online shopper in the U.S. sees a jacket on an Italy-based retailer's website, pushes the 'buy' button, and makes a purchase based on its price quoted in euros. The jacket ships, but by the time the transaction is processed and settled, the conversion rate between U.S. dollars and euros has shifted, leaving the retailer with less revenue than it expected when it quoted the price.

Or, consider the case of a Canadian consumer who returns a pair of shoes that didn't quite fit to a U.S. retailer. The retailer's price never changed in the U.S., but the conversion rate to Canadian dollars changed over the course of a week. The retailer received a certain purchase price, and refunded the same amount in U.S. dollars — but the Canadian consumer received a bigger refund than the price originally paid. That's great if you're the consumer, but it's bad news for the retailer.

Foreign exchange rates can change quickly. When the U.K. held its Brexit vote in June 2016, for example, the value of the British pound changed substantially overnight. An item that cost **\$1,000** in the U.S. would have cost a U.K. consumer **£681.30** on June 22, but **£733.04** on June 24. After the election, a customer returning an item purchased before the vote would receive **7.6% more money back** — more than £50 — than he or she originally spent, if the retailer processed the return and the original transaction in U.S. dollars.

A retailer with its sights on reaping the rewards of the global marketplace would have to manage a host of currencies — perhaps dozens — adding additional levels of complexity that can require research, additional staff and costs, and technology investments. In the Brexit example, managing the USD to GBP currency pair is clearly complex. As merchants add more currencies to service their local consumers, that complexity only increases. Managing the risk of 5, 10, or even 50 currency pairs is far more than a typical retailer can or should manage.

Even for a larger enterprise, the task can be very difficult, and that is considering the fact that larger companies have substantial teams devoted to the task. And if it's tough for a big company to handle, how can a smaller or medium-sized enterprise keep up?

For a smaller retailer who has yet to establish a worldwide presence, it may be easier to partner with a third-party service that handles international transactions, including currency management. Reach offers a turnkey solution that provides currency management by an experienced partner for merchants who don't want to shoulder the load themselves. Reach's Guaranteed FX brings consistency to the process by supplying a guaranteed rate to merchants, shielding them from the risks of abrupt fluctuations and exposure to unexpected shortfalls.

## 06 Alternative Payment Methods .....

Consumer expectations with regard to payment methods vary widely from country to country. While U.S. consumers might be accustomed to using credit cards or PayPal for online transactions, consumers in other countries might be more accustomed to using different methods in some instances.

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In some nations, credit cards themselves would be considered an alternative method of payment. Annual percentage rates (**APRs**) on U.S. credit cards average roughly **12.5%** – a manageable figure for most consumers. In Brazil, though, the average APR is about **450%**, making that payment method far less attractive for consumers looking to defer payments.



Instead, Brazilian consumers generally prefer other methods. Some people often buy merchandise online at a physical location — a kiosk, ATM or bank — using a voucher called a boleto which substitutes for cash, somewhat like a money order for a specific transaction. After the purchase is completed, the customer will then receive the item at home. Consumers who use boletos are often unbanked.

Brazilian consumers are also accustomed to buying items via installment plans, by agreeing on an interest rate and scheduling payments with a seller directly. A buyer might agree with a seller to buy a jacket via six installments, with a defined interest rate that removes uncertainty for everyone involved. Importantly, these agreements strengthen consumers' purchasing power, and consequently boost the average transaction value (ATV) per customer.

The **Merchant of Record provider is already aware of how retailers conduct business in multiple countries**, and knows consumer demographics and preferences.

By including alternative payment methods on a local basis in order to cater to a broad variety of in-country customers, it can implement customized payment methods, offering merchants superior return on investment. But failure to offer flexibility by providing a range of alternative payment methods is analogous to failing to offer the Visa or MasterCard methods in the U.S. — it discourages transactions and results in lost sales.

Knowing the importance of alternative payment methods, many payment solution providers sell clients on the fact that they can plug into hundreds of these alternative payments. While that may be persuasive for a merchant just starting out in the global marketplace, most seasoned retailers know that adding more payment methods simply cannibalizes existing sales.

Indeed, there are only a few key payment methods in each market that are **“must-haves.”** Knowing the difference between a must-have method and a method used by only a handful of consumers, or used by consumers of a different type of product entirely, means the difference between a smooth checkout and one littered with too many inappropriate options.

## 07 Fraud .....

Fraudsters are always on the heels of new developments in commerce and technology, and it is no surprise that in the world of ecommerce, there are many opportunities for bad faith actors. New technologies, and new ways of exploiting those technologies, have led to a rise in transaction fraud over the years.



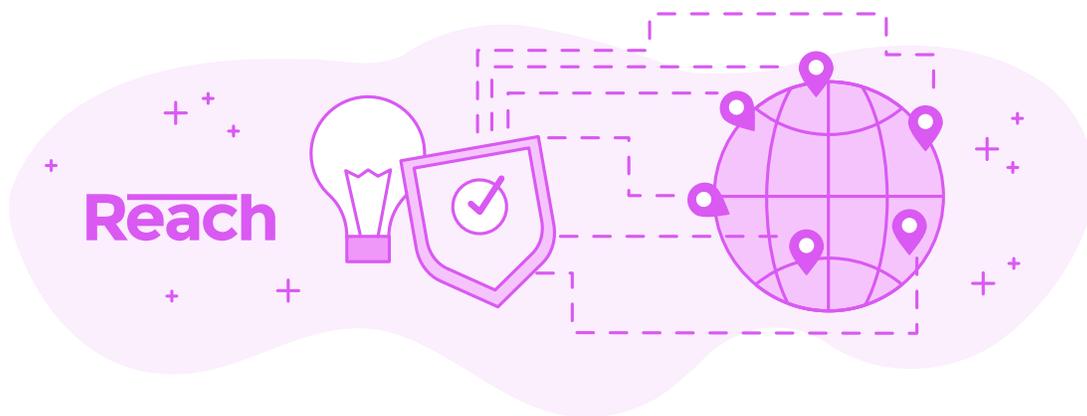
Visa estimates that the **number of compromised accounts rose 12% in 2016**, according to an August 2017 presentation.

Retailers who have perfected their method of fraud detection in their home country are in for quite a surprise as they expand globally. Fraud is incredibly localized - the patterns, methods, and criminal rings are sophisticated and as differentiated as the markets they target. For many retailers, this means turning their fraud detection to stop a huge number of transactions. The trouble with this approach is that this means the retailer is stopping real customers abroad from finishing their transaction.

In these cases, where a retailer might terminate a transaction if it suspects fraud, even if the transaction would have turned out to be legitimate, it's important to realize just how much money is being left on the table. **International decline rates are roughly twice as high as domestic decline rates.** For example, with the U.S. and Germany, credit card rejections occur in roughly **5%** of transactions, but cross-border transactions between the two nations result in a **10%** decline rate — despite the fact that the actual rate of fraud is no higher in either country.

A recent Merchant Risk Council survey showed that while the global fraud loss rate was **0.5%** in 2016, individual countries' rates ranged up to **1.9%** (Mexico). In essence, this means that retailers are turning away good customers, which hurts their bottom line, hurts the customer experience, and results in bad word of mouth.

The **Merchant of Record model** allows retailers to **offload the burden of international fraud detection** by offering incredible **insight on local consumer preferences**, operational fraud rings, and patterns of fraud in each country.



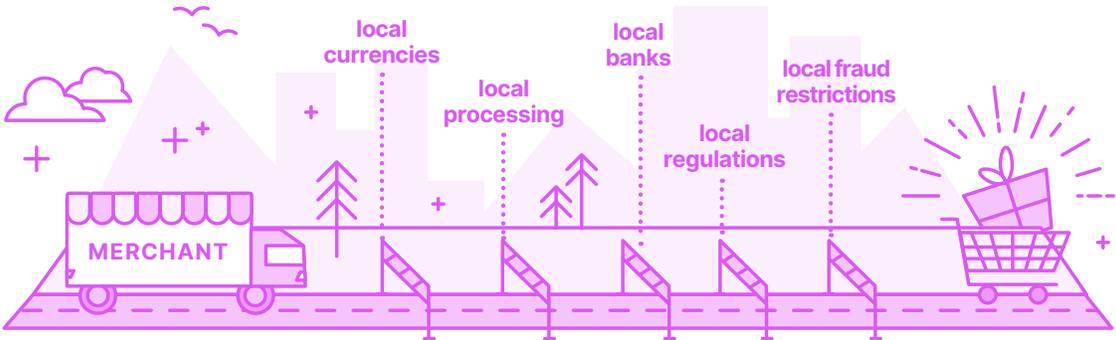
This insight into specific international markets means that retailers are only turning away bad customers - not legitimate ones. For retailers inundated with information about local market practices, the use of a partner who is familiar with local situations, such as Reach, leads to better identification of real fraud as opposed to false positives, and results in a higher conversion rate for legitimate sales.



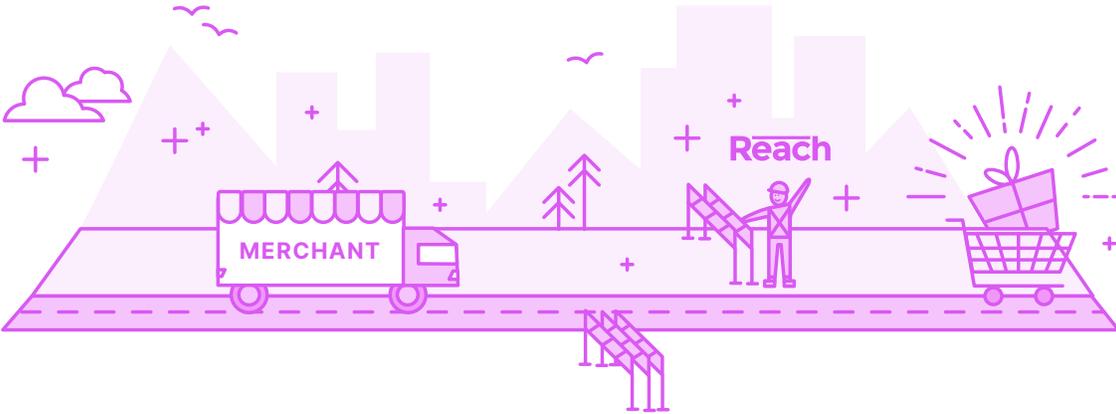
# 08 Conclusion

For a small to mid-sized enterprise, the Merchant of Record model helps navigate the world of global ecommerce by leveraging a deep knowledge base and existing international relationships in order to reduce barriers to entry among worldwide markets.

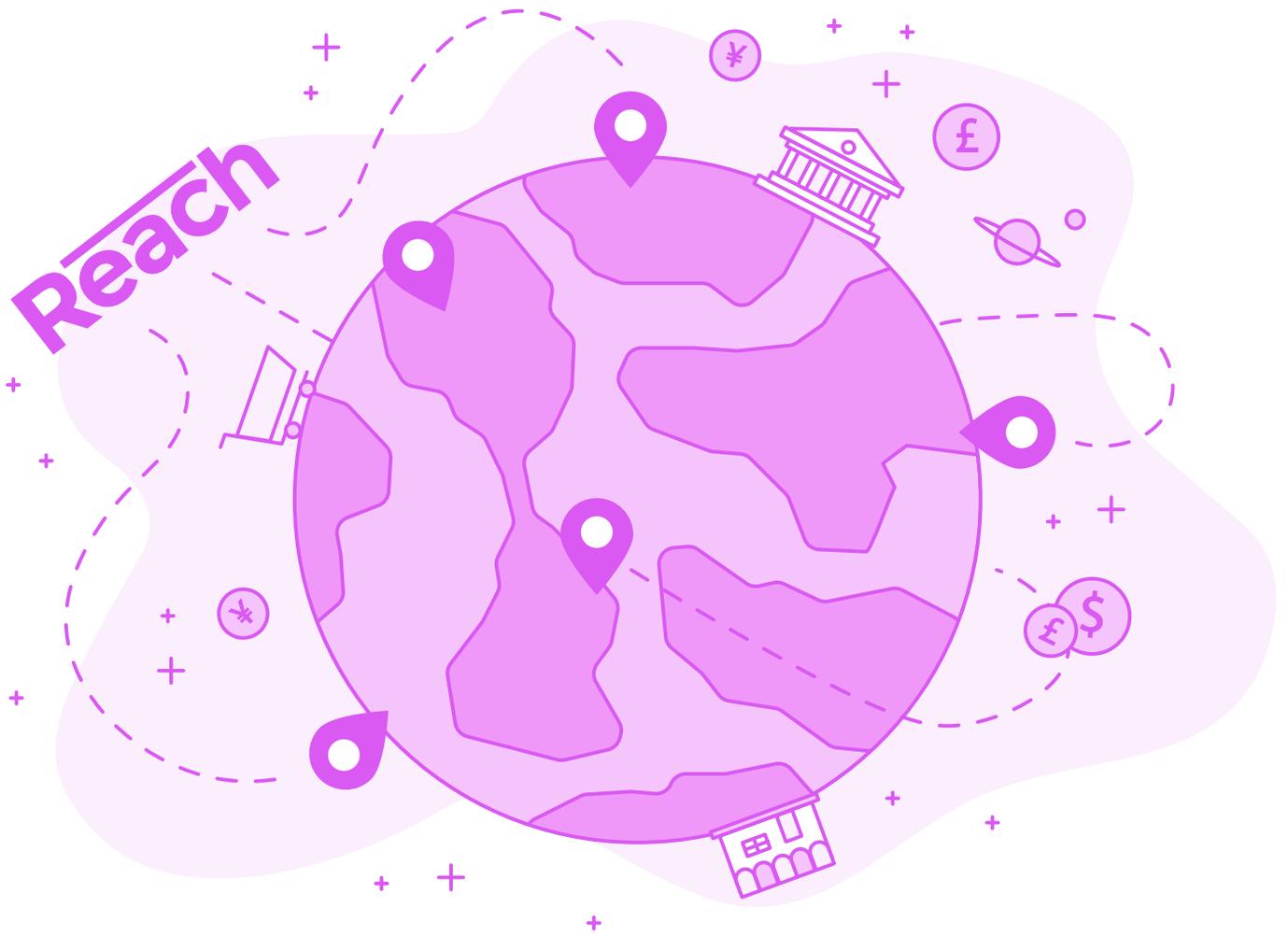
## Traditional Cross-Border Processing



## The Reach Way



The model provides a solution to managing the dynamics of multiple currencies as they fluctuate daily, and offers a cross-border service provider allowing in-country credit card processing in multiple markets. Retailers can gain a partner with specific expertise in diverse alternative payment methods which vary from country to country, and which can identify fraud more precisely and capture a higher rate of legitimate sales.



### QUESTIONS?

Contact Reach to find out how  
an MOR solution can work for you.

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