MERCHANT CASH ADVANCES ARE NOT SALES

by

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Introduction

We learn early in legal education that a party cannot sell property it does not own. Yet merchant cash advance (MCA) agreements frequently characterize transactions as sales of receivables that do not yet exist and are not identified as specific accounts. In resolving challenges to these agreements, courts have often focused on contractual language addressing reconciliation, repayment structure, and risk allocation, sometimes at the expense of more fundamental questions about whether a present transfer of such a property interest can occur at all. This article argues that MCA agreements, as commonly structured, cannot constitute true sales where, at the time of execution, the merchant lacks rights in the receivables purportedly transferred, and where the agreement *purports* to convey not *specific accounts* receivable but a fixed dollar amount sourced from an undefined stream of future receivables. Courts should not reach the familiar risk-allocation factors unless the transaction is first capable of effecting a present transfer of property. Where a merchant lacks present rights in identifiable receivables, an MCA agreement should not constitute a sale as a matter of law, regardless of how risk is allocated.

I. Background

Recent economic disruptions have intensified liquidity pressures on small businesses, particularly those with limited access to traditional credit. When confronted with sudden and unanticipated cash demands, merchants increasingly turn to MCAs marketed as purchases of future receivables, often structured with daily or weekly automated withdrawals and repayment costs that, depending on structure and fees, often substantially exceed the costs of conventional commercial financing. These arrangements frequently function as short-term liquidity bridges during moments of acute distress, precisely when merchants have the least bargaining power. As the following analysis shows, however, the legal characterization of these transactions turns not on the

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urgency that precipitates them, but on whether the agreements can give rise to a present transfer of identifiable property as a matter of law.[1]

MCAs are alternative funding available to businesses with limited or poor credit history,[2] and they have been compared to other forms of high-cost short-term financing: businesses get money now in exchange for withdrawals from future income. In a typical arrangement, a funder provides an upfront advance in exchange for the right to collect a specified dollar amount from the merchant's future receipts, often through automated debits. As characterized by the MCA industry, these transactions are purportedly sales of receivables: the entity offering the merchant cash advance "buys" future receivables from a merchant at a discount. Rather than lend $100,000 at a stated interest rate that could exceed statutory caps in some jurisdictions if characterized as interest, the MCA offers a "cash advance" of $100,000 with a factor rate of (for example) 1.3 for a period of twelve months. The entity "buys" $130,000 worth of receivables for $100,000. Add in, say, an origination fee of $1,000 and a processing fee of $250. The MCA funder takes payments five days a week via automated withdrawals, and the transaction—depending on repayment cadence and fees—can be expressed as an effective rate exceeding that of traditional commercial lending. Importantly, the withdrawals continue *until the purchase price is satisfied.* Crucially, these transactions do not identify any particular receivables to be transferred but instead grant the funder a right to collect a fixed amount from an undifferentiated stream of future receipts until that advance is satisfied, and sometimes beyond. In other words, MCA providers purport to purchase not a specific piece of property, but a *specific amount* to be collected from a *source* of the debtor's property.

This article proceeds in three parts. First, I review the existing case law and demonstrate that, even under existing case law, most MCAs are loans, not sales. Second, I suggest that courts conduct a threshold inquiry when determining whether MCAs can constitute a sale: (1) whether the seller has a cognizable right in property purportedly being sold, and (2) whether the property purportedly being sold constitutes specific property. Third, I briefly explore some bankruptcy implications.

[1] *See* Alina Selyukh & Scott Horsley, *A Shadowy Industry Is Helping Small Businesses Pay Tariffs—at a High Cost*, NPR (Feb. 9, 2026), https://www.npr.org/2026/02/09/nx-s1-5628425/shark-tank-tariffs-loans-cash-advance.

[2] *See* Kara J. Bruce, *Desperation Finance: Merchant Cash Advances in Bankruptcy and Beyond*, 42 EMORY BANKR. DEV. J. 1, 3 (2026) (describing MCAs as high-cost financing and analyzing their characterization as sales or loans).

II. Existing Case Law

Courts consider (or at the very least purport to consider) the *substance* of MCAs rather than form when determining whether to classify the agreement as a sale or loan.[3] Substantively, there are two big overarching and related considerations: first, is the right to payment absolute?[4] Second, is there actually a transfer of risk?[5] To answer these big questions, courts typically consider three factors: (1) "whether there is a reconciliation provision in the agreement;"[6] (2) "whether the agreement has a finite term;"[7] and (3) "whether there is any recourse should the merchant declare bankruptcy."[8] Courts "need not find the presence of all three factors in concluding that a transaction is a loan."[9]

The factor-based framework described above presupposes that the agreement is capable of transferring receivables as property in the first place. This article therefore proposes to split the inquiry into two analytically distinct questions. The first is a threshold property question: whether, at execution, the merchant has present rights in the receivables purportedly "sold," and whether the agreement identifies specific receivables rather than granting the funder a right to collect a fixed dollar amount from an undifferentiated stream of future receipts.

Only if the transaction can plausibly effect a present transfer of a property interest does it make sense to proceed to the three familiar risk-allocation factors (reconciliation, term, and recourse), which function as secondary indicators of whether the funder bears meaningful collection risk or instead has an essentially absolute right to payment.[10]

In engaging in this three-factor inquiry, courts increasingly focus on substantive risk allocation, specifically, whether the funder actually assumes

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[3] Fleetwood Servs., LLC v. Ram Cap. Funding, LLC, No. 20-CV-5120 (LJL), 2022 WL 1997207, at *9 (S.D.N.Y. June 6, 2022); LG Funding, LLC v. United Senior Properties of Olathe, LLC, 181 A.D.3d 664, 665–66 (N.Y. App. Div. 2020).

[4] *LG Funding*, 181 A.D.3d at 665.

[5] Lateral Recovery, LLC v. Cap. Merch. Servs., LLC, 632 F. Supp. 3d 402, 452–54 (S.D.N.Y. 2022) (citing *LG Funding*, 181 A.D.3d at 666).

[6] *LG Funding,* 181 A.D.3d at 666.

[7] *Id*.

[8] *Id*.

[9] Fleetwood Servs. LLC v. Ram Cap. Funding, LLC, No. 20-CV-5120 (LJL) 2022 WL 1997207, at *9 (S.D.N.Y. June 6, 2022).

[10] *See* Kara J. Bruce, *The Murky Process of Characterizing Merchant Cash Advance Agreements,* 42 BANKR. L. LTR. NL 4, Apr. 2022, at 1, 6–7.

the "risks, benefits, obligations, and other attributes we typically associate with ownership."[11] As Professor Kara Bruce beautifully puts it: "The ultimate question, again, is whether the buyer has acquired the risks and rewards of the purchased receivables (in line with a true sale) or has instead contracted for a repayment that does not vary based on the performance of the assets (in line with a secured loan)."[12]

In addition to the three-factor inquiry, some courts consider eight factors that center the risk allocation question, drawn from an article by Robert Aicher and William Fellerhoff:

1) Whether the buyer has a right of recourse against the seller,
2) whether the seller continues to service the accounts and comingles receipts with its operating funds,
3) whether there was an independent investigation by the buyer of the account debtor,
4) whether the seller has a right to excess collections,
5) whether the seller retains an option to repurchase accounts,
6) whether the buyer can unilaterally alter the pricing terms,
7) whether the seller has the absolute power to alter or compromise the terms of the underlying asset, and
8) the language of the agreement and the conduct of the parties.[13]

A. Reconciliation Provisions

Even where a court does not resolve the threshold property-transfer question, reconciliation provisions typically operate as the doctrinal proxy for whether the funder bears meaningful collection risk. MCA agreements must have legitimate reconciliation provisions to be treated as true sales. Most

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[11] Kara J. Bruce, *Revenue Based Finance in Bankruptcy and Beyond*, 45 No. 4 BANKR. L. LR. NL, Apr. 2025, at 1, 6 [hereinafter Bruce, *Revenue Based Finance*]; *see also* Williams Land Clearing, Grading, and Timber Logger, LLC v. Apex Funding Source LLC (*In re* Williams Land Clearing, Grading, and Timber Logger, LLC), Case No. 22-02094-5-PWM, Adv. Pro. No. 23-0024-5-PWM, slip op. at 5, 8 (Bankr. E.D.N.C. May, 16 2025) (citing Bruce, *Revenue Based Finance*, *supra* note 11, at 6, 7).

[12] Bruce, *Revenue Based Finance*, *supra* note 11, at 6.

[13] *See, e.g.*, Cap Call, LLC v. Foster (*In re* Shoot the Moon LLC), 635 B.R. 797, 813 (Bankr. D. Mont. 2021); *Williams Land Clearing*, slip op. at 5–6; *In re* Watchmen Security LLC, No. 24-0087-JMC-11, 2024 WL 4903363, at *8 (Bankr. S.D. Indiana, Nov. 20, 2024) (citing Robert D. Aicher & William J. Fellerhoff, *Characterization of a Transfer of Receivables as a Sale or a Secured Loan Upon Bankruptcy of the Transferor*, 65 AM. BANKR. L.J. 181, 186–94 (1991)) (disallowing the claim to be considered secured).

litigation around merchant cash advances centers around the existence and nature of a reconciliation provision. Because the buyer has purchased the future receipts, the amount they can take from the merchant should be linked to the actual receipts, if it is really a sale. If the receipts are less than expected, the amount the MCA funder withdraws from the merchant's account should be downwardly adjusted accordingly.

Because courts say there must be a reconciliation provision in order for these transactions to be considered sales, they *all* have so-called reconciliation provisions—the question becomes whether these provisions are illusory.[14] In practice, merchants often face procedural and informational barriers to obtaining reconciliation, and funders may rely on strategic drafting and procedural barriers to prevent reconciliation, thereby rendering the reconciliation provision illusory—and thus rendering the transaction a loan rather than a sale.

A reconciliation provision is illusory if: (1) it is discretionary rather than mandatory, or (2) the originator retains alternative paths to recovery (e.g., a security interest in other assets or withdrawal rights broader than receivables).[15]

1. Discretionary Reconciliation Provisions as Illusory Reconciliation

The easiest way for MCA originators to get into trouble is to make their reconciliation provisions discretionary. Consider the reconciliation provision in *Lateral Recovery*, *LLC v. Capital Merchant Services, LLC.*, for example: "At the Merchant's option, within five (5) business days following the end of a calendar month, the Merchant may request a reconciliation to take place, whereby [the funder] *may* ensure that the cumulative amount remitted for the

[14] *See* Lateral Recovery, LLC v. Cap. Merch. Servs., LLC, 632 F. Supp. 3d 402, 452 (S.D.N.Y. 2022) (holding that a reconciliation provision is insufficient where it is discretionary and does not meaningfully limit repayment); Lateral Recovery, LLC v. Queen Funding, LLC, No. 21 Civ. 9607 (LGS), 2022 WL 2829913, at *5–6 (S.D.N.Y. July 20, 2022) (holding that a reconciliation provision that is difficult to invoke and leaves the funder with discretion renders the agreement a loan); Haymount Urgent Care P.C. v. GoFund Advance, LLC, 609 F. Supp. 3d 237, 248 (S.D.N.Y. 2022) (holding that a reconciliation provision lacking practical availability supports characterization as a loan); *Fleetwood*, 2022 WL 1997207, at *13 (holding that a nominal reconciliation provision that does not affect repayment obligations is illusory); Davis v. Richmond Cap. Grp., LLC, 194 A.D.3d 516, 517 (N.Y. App. Div. 2021) (holding that discretionary reconciliation provisions and recourse upon business failure support treating the agreement as a loan).

[15] *See supra* note 14 and accompanying text.

subject month via the Daily Payment is equal to the amount of the Specified Percentage."[16]

The court said this reconciliation provision with its use of *may* was "wholly discretionary," and it didn't help that the provision added that the "potential reconciliation" was a courtesy and that it was "under no obligation" to provide reconciliation.[17]

2. Alternative Paths to Recovery

Even if the MCA makes reconciliation mandatory, that doesn't necessarily mean the provision is not illusory—if the MCA originator has another path to recovery then reconciliation does not resolve the question. For example, in *Fleetwood Services, LLC v. Ram Capital Funding, LLC* the MCA originator gave itself a right not just to future receivables but to "the payment of monies from Merchant's customers' and/or other third party payors . . . for the payments due to Merchant as a result of Merchant's sale of goods or services" until the entire purchase amount was repaid.[18] On top of that, it took a "security interest in and lien upon": (a) "all accounts, chattel paper, documents, equipment, general intangibles, instruments, and inventory"; (b) all proceeds thereof; and (c) "all funds at time in the Merchant's Account, regardless of the source of the funds."[19]

It likely also influenced the court's analysis that the MCA originator engaged in aggressive enforcement conduct, as reflected in the New York Attorney General's allegations:

> The NYAG has obtained affidavits from merchants testifying that Richmond never performed any reconciliations and failed and refused to reduce their daily payments when the merchant's receivable collections slowed down; instead of reducing the daily payments, Richmond threatened to destroy the merchant's business and, in some instances, implied that they would harm the merchant's owner if the

[16] *Lateral Recovery*, 632 F. Supp. 3d at 428 (emphasis added).
[17] *Id.* at 456–57.
[18] *Fleetwood*, 2022 WL 1997207, at *2.
[19] *Id*. at *4.

> merchant failed to make the daily payments required by the Agreements. [20]

If this were really a sale, the court said, the MCA originator would not be able to go after the merchant, but only the account debtors.[21] The court concluded that the agreement's formal language did not reflect a meaningful transfer of risk or reward.[22] Indeed, the originator could not identify any revenue the merchant could receive that would not be potentially swept into the funder's control to satisfy the purchase amount.[23]

Fintegra LLC v. DNA Telecom Inc. provides another example of an illusory reconciliation provision. There, although the reconciliation indicated the MCA originator Fintegra "shall comply" with merchant's requests for reconciliation, it really only offered to ensure its accounting was accurate, not that it would account for downturn in receivables.[24] In addition, the agreement stated Fintegra would not complete a reconciliation in the event of default.[25] The agreement gave Fintegra the "irrevocable power of attorney" to "take any action or execute any instrument or document to settle all obligations due to Fintegra," and Fintegra also took a security interest in all of the merchant's equipment.[26] Thus, the court said there was "no discernible avenue by which defendants can reconcile their account so as to reduce payments in the event of declining revenue," and Fintegra did not assume the risk of "less-than-expected or no revenues."[27]

Similarly, in *Hi Bar Capital LLC v. Parkway Dental Services, LLC*, although the reconciliation provision included mandatory obligations, the agreement made insufficient funds an event of default, and also provided the funder with a security interest "in 'all of Merchant's assets of any kind whatsoever."[28] As in *Fleetwood*, the court found "there are virtually no circumstances where, if the accounts receivable would not be sufficient to pay the Purchased Amounts, [funder] would not be absolutely entitled to

[20] *Id*. at *5.
[21] *Id*. at *11.
[22] *Id*.
[23] *Id*.
[24] Fintegra LLC v. DNA Telecom Inc., No. 525923/2023, 2024 N.Y. Misc. LEXIS 41149, at *3 (Sup. Ct. Kings Cnty. June 27, 2024).
[25] *Id.* at *4.
[26] *Id*. at *10.
[27] *Id*.
[28] HI Bar Capital LLC v. Parkway Dental Servs., LLC, No. 533245/2021, 2022 WL 3757589, at *4 (N.Y. Sup. Ct. Aug. 25, 2022).

repayment."[29] Despite the mandatory language, the court applied "thorough and exacting scrutiny," in a "holistic and comprehensive manner" to determine the "real character" of the reconciliation provision.[30] In essence, because there was no transfer of risk and the funder could recover in any event, the transaction was a loan rather than a sale of receivables.

3. Drafting Responses and Judicial Treatment

MCA originators have responded to this series of rulings by crafting language that professes to bear the risk of loss without actually taking on such risk. For example, in *In re GMI Group Inc v. Reliable Fast Cash, LLC*, a bankruptcy case in the Northern District of Georgia, the MCA agreement included the following language:

> If Future Receipts are remitted more slowly than [Defendant] may have anticipated or projected because [Debtor's] business has slowed down, or if the full Purchased Amount is never remitted because [Debtor's] business went bankrupt or otherwise ceased operations in the ordinary course of business, and [Debtor] has not breached this Agreement, [Debtor] would not owe anything to [Defendant] and would not be in breach of or default under this Agreement. [Defendant] is buying the Purchased Amount of Future Receipts knowing the risks that [Debtor's] business may slow down or fail, and [Defendant] assumes these risks based on [Debtor's] representations, warranties and covenants in this Agreement that are designed to give [Defendant] a reasonable and fair opportunity to receive the benefit of its bargain.[31]

At first glance, this language appears to describe a genuine allocation of risk. The bankruptcy court thought so, too. The paragraph, however, does not impose any affirmative obligation on the originator to reconcile. The reconciliation language provides only that the debtor "*may request*" an adjustment to "more closely reflect the [Debtor's] actual future receipts" and that the originator

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[29] *Id*.

[30] *Id*. at 3.

[31] *In re* GMI Grp., Inc. v. Reliable Fast Cash, LLC, Ch. 11 Case No. 19-52577-PMB, 2019 WL 3774117, at *2 (Bankr. N.D. Ga. Aug. 9, 2019) (alterations in original).

"may adjust" the daily amount to "more closely reflect the [Debtor's] actual Future Receipts." The reconciliation mechanism is therefore entirely discretionary. This renders the reconciliation provision illusory. The court, however, considered the transaction to be a valid sale because nonpayment was not a default and bankruptcy was excluded as an event of default, and thus the funder could not be assured of repayment in any event and bore some risk of non-repayment.[32] In essence, despite a lack of clear method by which the merchant could seek reconciliation, the funder's more limited remedies were sufficient to convince the court that it bore enough risk to render the transfer a true sale. [33]

If funders are too greedy, by contrast, language insisting they bear the risk of loss may not be sufficient to persuade the court. Indeed, that exact same language ("if future receipts are remitted more slowly") was not enough to convince the court in another MCA agreement case heard on the same day. In *GMI Group v. Unique Funding Solutions*, the court found the agreement to be a usurious loan. There, the funder required the merchant to have, at all times, twice the "daily amount" (the amount to be daily debited according to the agreement).[34] If the merchant failed to have twice the daily amount in its account, it would default under the agreement and trigger unconditional liability.[35] Thus, although the merchant purported to understand it bore the risk of failure, the agreement was structured such that a reduction in receipts would trigger default and entitle the funder to a right to full repayment, so the funder did not in fact bear the risk of a downturn in receipts.[36]

Another way MCA originators attempt sneaky maneuvers is by just being vague and hoping courts will read their reconciliation provisions generously. This is what happened in *Landmark Funding*. The reconciliation provision provided "any Merchant may give written notice to LFG requesting that LFG conduct a reconciliation in order to ensure that the amount that LFG has collected equals the Specified Percentage of Merchant(s)'s Receivables under this Agreement."[37] Merchants said this was a sham because the provision

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[32] GMI Group, Inc. v. Reliable Fast Cash, LLC (*In re* GMI Grp., Inc.), No. 19-52577-PMB, 2019 WL 3774117, at *10 (Bankr. N.D. Ga. Aug. 9, 2019).

[33] *Id*.

[34] *GMI Grp., Inc. v. Unique Funding Sols., LLC (In re GMI Grp., Inc.)*, 606 B.R. 467, 482 (Bankr. N.D. Ga. 2019).

[35] *Id*. at 486.

[36] *Id*. at 486–87.

[37] Landmark Funding Grp. LLC v. Alt. Materials LLC, No. 534708/2022, 2024 N.Y. Misc. LEXIS 852, at *3–4 (Sup. Ct. N.Y. Cnty. Feb. 29, 2024).

related "only to collection of payments and not to any adjustment of the amount of the Daily Payment based on [Marchant's] actual Receivables."[38] The court took an optimistic view: "[I]f LFG collected more than it was entitled to, then LFG will credit to the Account all amounts to which LFG was not entitled . . . [a]lthough not explicitly stated, in that event LFG would surely lower the daily remittances going forward."[39]

Some courts have nevertheless inferred that such language implies an obligation to adjust future remittances. That conclusion is in tension with the pattern of conduct of the various MCA originators that appeared before that court. Interestingly, in an aside the court reveals that it really sees this transaction as a loan rather than sale:

> Further, there is no merit to the argument that plaintiff 'knew' the defendants had no receivables and offered them funds anyway . . . . If that were true then the defendants, may surely be responsible for seeking to obtain funds they had no way of ever returning.[40]

This reasoning reflects an implicit assumption that the transaction operates as a disguised credit arrangement rather than a true sale.

B. Finite Terms and Recourse

Courts don't spend much time on the "finite term" provision—all of the MCA contracts have unlimited repayment periods, which apparently courts like to think makes them less loan-like. As I'll discuss in the next part, however, this just shows what a beguiling product this is—it's not future receipts over a period of time, it's a certain dollar amount of future receipts, with repayment limited to a percentage of the merchant's receipts, and thus the duration of repayment dependent on the merchant's cash flow. The only situation in which the seller is not repaid is if the business stops generating accounts altogether. Otherwise, they can keep deducting, albeit less at a time, assuming the reconciliation provision is working as it's supposed to.

As for recourse in the event of bankruptcy, courts are fairly clear on the fact that if the guarantor is on the hook in the event of bankruptcy, then the right to repayment is considered absolute and there is not actually any transfer of

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[38] *Id*. at *4.
[39] *Id*.
[40] *Id*. at *6.

risk.[41] If the transaction is being evaluated in the context of a bankruptcy case, the very fact that the funder is *seeking* recourse in bankruptcy by filing a proof of claim *proves* that the MCA lender believes it has recourse in the event of bankruptcy.[42]

To the extent MCA originators are trying to say they have valid security interests in multiple of the merchant's assets, you can add that to this factor as well—though as discussed that often also gets folded into the reconciliation provision analysis. In essence, if the MCA funder has recourse in the event of bankruptcy—or any default really—then the reconciliation provision is meaningless because it's not actually linked to the value of those receivables. The presence or absence of recourse, though, should have no bearing on whether a transaction is a loan. Otherwise, the whole category of loans known as "non-recourse loans" would not exist. Some loans include recourse and others don't, as Stephen Sepinuck and John Hilson elegantly point out in their article *A "Sale" of Future Receivables: Criminal Usury In Another Form*.[43]

III. MCA Agreements *Cannot* Constitute Sales in Certain Circumstances

In this Section, I urge a return to property fundamentals when analyzing when and whether MCA Agreements can ever constitute sales. First, where the merchant lacks a present right in the receivables, the merchant cannot sell the receivables, and the transaction can thus not be a sale. Second, where the agreement does not sell any specific property, the transaction cannot be a sale.

A. MCAs Cannot Be True Sales Where the Merchant Lacks Present Rights in the Receivables

This inquiry is not intended to displace the prevailing factor-based analyses courts employ when distinguishing loans from sales. Rather, it addresses a logically antecedent question those analyses often presuppose but

[41] Lateral Recovery, LLC v. Cap. Merch. Servs., LLC, 632 F. Supp. 3d 402, 456 (S.D.N.Y. 2022).

[42] *See, e.g.*, JCS Hospitality LLC v. LG Funding LLC (*In re* JCS Hospitality), Adv. Pro. No. 24-0034-5-PWM (Bankr. E.D.N.C. Sept. 16, 2004) (Slip. Op. D.E. 18, at 8); Williams Land Clearing, Grading, and Timber Logger, LLC, v. Apex Funding Source LLC (*In re* Williams Land Clearing, Grading, & Timber Logger, LLC), Ch. 11 Case No. 22-02094-5-PWM, Adv. Pro. No. 23-0024-5-PWM, slip op. at 7 (Bankr. E.D.N.C. 2025).

[43] John F. Hilson & Stephen L. Sepinuck, *A "Sale" of Future Receivables: Criminal Usury in Another Form,* TRANSACTIONAL LAW., Aug. 2019, at 1, 1.

do not resolve: whether a transaction is capable of effecting a present transfer of property at all.

We all learned in property law the principle of *nemo dat qui non habet*, "one cannot give what one does not have." As Stephen Sepinuck and John Hilson explain, a sale of future receivables is:

> both a metaphysical and legal impossibility. It is metaphysically impossible because the essence of a sale is the transfer to the buyer of that which is being purchased. A transfer of future rights to payment—that is, rights that as yet do not exist—cannot occur unless and until the rights to payment arise. It is a legal impossibility for much the same reason. The law simply does not comprehend or countenance a present transfer of future property.[44]

One can promise to sell something one later acquires, but that is a contract, not a transfer of property. Another way to understand that the property transfer can't possibly have occurred is to remember that, when one drafts a security agreement with an after-acquired property clause, the security interest does not attach until the moment the debtor has rights in the collateral. Courts are increasingly emphasizing these fundamentals.[45]

The Consumer Financial Protection Bureau agrees.[46] Although businesses may not be subject to oversight by the Consumer Financial Protection Bureau (CFPB), it's worth noting that the CFPB came to the same conclusion: MCA transactions can't possibly be sales simply because the merchant cannot sell something in which it has no right.[47] In this context, the CFPB has reasoned that MCAs cannot function as sales and therefore constitute credit for purposes of the Equal Credit Opportunity Act (ECOA) (which prohibits unlawful discrimination in credit actions).[48] The ECOA defines credit as "the right granted by a creditor to an applicant to defer payment of a debt, incur debt and defer its payment, or purchase property or services and defer

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[44] John F. Hilson & Stephen L. Sepinuck, *A "Sale" of Future Receivables: Disguising a Secured Loan as a Purchase of Hope*, TRANSACTIONAL LAW., Apr. 2019, at 15.

[45] *See, e.g.*, *In re* Watchmen Sec. LLC, No. 24-00087-JMC-11, 2024 WL 4903363, at *4 (Bankr. S.D. Ind. Nov. 20, 2024) (quoting Hilson & Sepinuck, *Sisguising a Secured loan*, *supra* note 44, at 15 concluding a prepetition debtor has no power to transfer postpetition receivables).

[46] Small Business Lending Under the Equal Credit Opportunity Act (Regulation B), 88 Fed. Reg. 35, 150 (May 31, 2023).

[47] *Id.* at 35, 223.

[48] 15 U.S.C. § 1691a.

payment therefor."[49] MCA providers, says the CFPB, advance funds to merchants and grant them the right to defer payment by allowing repayment over time.[50] Further, the CFPB interprets ECOA's definition of credit without consideration of factors such as the absence of recourse or analysis of who bears the risk of loss.[51] This reasoning is difficult to reconcile with the defining features of a traditional factoring transaction.[52]

B. MCA Agreements Cannot Be Sales Because They Do Not SellSpecific Property

"I, Chrystin Ondersma, hereby sell you $50,000 from my future paychecks, for the price of $30,000. You shall be entitled to take 3% of my paychecks until that amount is satisfied."

It is difficult to characterize that transaction as a sale. There is no principled basis to treat the transaction differently merely because the $50,000 amount is sourced from future sales rather than from future paychecks.

"I, Chrystin Ondersma, hereby sell you $50,000 from the proceeds I receive from the sale of any of my personal property. You shall be entitled to take 3% of all my sales until that amount is satisfied."

Note that at this point I don't even have any specific contracts to sell any specific property, but, even if I did, it should be clear that what is purportedly being sold is *not* specific property but instead just a specified amount.

This comparison illustrates why the absence of a finite repayment period does not, standing alone, support characterization as a sale—of course there is not a finite period, because what is being remitted is *not* property but instead a specific amount over time. The percentage amount limits how much can be taken at any given time, but it does not reduce the total amount to be repaid. Note also that while the specified amount cannot decrease, it *can* increase substantially in the event of default—yet another indicator that what we have here is a loan and not a sale.

Once again Stephen Sepinuck and John Hilson capture this concept well: in a sale of receivables, *specific receivables* are sold, and those receivables

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[49] 15 U.S.C. § 1691a(d).

[50] Small Business Lending Under the Equal Credit Opportunity Act (Regulation B), 88 FR 150, 35, 223.

[51] *Id.*

[52] *See* Nickey Gregory Co. v. AgriCap, LLC, 597 F.3d 591, 601–02 (4th Cir. 2010).

have a specific face value; in MCA contracts, by contrast, the buyers "receive[] an unlimited amount of receivables" until the specified amount is paid in full.[53] Further, they explain, "if these transactions were truly sales, there should be no concept of making the uncollected portion of the Purchased Amount becoming due and payable; it would simply be collected (or not) from the receivables."[54]

IV. Bankruptcy Issues

This discussion is not intended to be exhaustive. Bankruptcy cases involving MCAs can raise a range of issues including, among others, disputes over the automatic stay and the characterization of postpetition revenues as cash collateral. These questions are fact-dependent and vary across jurisdictions. The purpose here is instead to show how the threshold property inquiry—whether the merchant transferred a present interest in identifiable receivables—frames and often resolves the downstream bankruptcy analysis.

A. MCA Transactions as Claims and Debts for Bankruptcy Code Purposes

Regardless of what these transactions are, they are claims and therefore debts under the Bankruptcy Code. According to the Bankruptcy Code, as the court pointed out in *In re Hill*, debt is simply liability on a claim.[55] A "claim" within the meaning of the Bankruptcy Code is either a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured" or a "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment."[56] The court noted that the funder did not "argue that it had no right to payment, and, in fact, argues the opposite—that it had the right to debit Network Salon's account under the Agreements."[57] Thus, the court held, regardless of whether the MCA agreement

[53] Hilson & Sepinuck, *Disguising a Secured Loan as a Purchase of Hope*, *supra* note 44, at 17.

[54] *Id*.

[55] Gecker, LLC, v. LG Funding, LLC (*In re* Hill), 589 B.R. 614, 622 (Bankr. N.D. Ill. 2018).

[56] 11 U.S.C. § 101(5)(A)–(B).

[57] *In re* Hill, 589 B.R. at 622.

would be considered a loan under state law, the transactions "created a debt."[58] This makes MCA funders putative creditors for bankruptcy purposes.

Recent bankruptcy decisions further underscore the importance of resolving threshold property questions before determining whether postpetition revenues constitute property of the estate or cash collateral.[59] Not all bankruptcy courts agree, however. In *GMI Group v. Reliable Fast Cash* (discussed above), the court concluded that the debtor likely retained some interest in its receivables, making them property of the estate.[60] As discussed above, the court considered the transaction to be a valid sale because nonpayment was not a default and bankruptcy was excluded as an event of default; thus, the funder could not be assured of repayment in any event and bore some risk of nonrepayment.[61] But even if the transaction constituted a valid sale, how could the funder acquire a property interest in future receivables at the time of the agreement if the receivables did not yet exist? At the time of the bankruptcy filing, the most the funder can have is a contract for a future sale of future receivables, which as we know is a simple prepetition claim like any other.

B. Secured or Unsecured

When a merchant enters bankruptcy, MCA providers should be treated as unsecured lenders. A prepetition debtor typically cannot transfer an interest in accounts receivable that do not yet exist. Under 11 U.S.C. §§ 552(a), "property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case."[62] Postpetition transfers require court approval. Judge Carr, in *In re Watchman*, persuasively articulates this:

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[58] *Id*.

[59] *See, e.g.*, *In re* IVF Orlando, Inc., 2025 Bankr. LEXIS 2573, at *21–22 (Bankr. M.D. Fla. Oct. 3, 2025) (concluding that postpetition receivables were not transferred under merchant cash advance agreements and were not subject to any prepetition security interest where the debtor lacked rights in the receivables at the time of execution).

[60] *In re* GMI Grp., 2019 Bankr. LEXIS 2494, at *33 n.13.

[61] *Id* at *32–33.

[62] 11 U.S.C. § 552(a).

> It cannot be posited that a prepetition debtor somehow has the authority and power to sell or otherwise transfer any interest in accounts receivable which do not come into existence until postpetition and are, therefore, property of the bankruptcy estate . . . . any claim that such a security interest would attach to Debtor's postpetition receivables would be defeated by 11 U.S.C. § 552(a). [63]

Because any property right in future receivables cannot arise until the debtor owns the receivables, such property cannot be acquired before commencement of the case. Therefore, § 552 requires that MCA transactions governing any receivables the debtor acquires postpetition would necessarily be unsecured, not secured.

C. Voidable Preference and Fraudulent Transfer Analysis

For courts that consider MCA agreements to be claims and funders to be creditors, voidable preference and fraudulent transfer analyses apply to any prepetition payments or transfers to MCA funders.[64]

Even those courts that consider MCA agreements to be valid sales of future receivables, however, may find certain transfers to nevertheless be subject to preference/fraudulent transfer analysis. In *GMI Group v. Reliable Fast Cash*, for example, although the court characterized the MCA agreement as a valid sale of future receivables, it concluded that a factual dispute remained as to whether certain garnished funds constituted property of the debtor and therefore denied summary judgment on the debtor's preference claim.[65]

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[63] *In re* Watchmen Sec. LLC, No. 24-00087-JMC-11, 2024 WL 4903363, at *4 (Bankr. S.D. Ind. Nov. 20, 2024).

[64] *In re* Hill, 589 B.R. at 620–22.

[65] GMI Grp., Inc. v. Reliable Fast Cash, LLC (*In re* GMI Grp., Inc.), No. 19-52577-PMB, 2019 Bankr. LEXIS 2494, at *41 (Bankr. N.D. Ga. Aug. 9, 2019) ("It is likely that the Debtor, notwithstanding the Agreement, still retained an interest in the garnished funds as, *inter alia*, Defendant has failed to provide any applicable legal basis under New York law for finding that the Debtor had no legal or equitable interest in the garnished funds. In the absence of any evidence to establish conclusively ownership of the $35,660.96 garnished funds—an essential element for the Debtor's preference claim in Count III, neither party is entitled to summary judgment as to Count III as to the garnished funds.").

D. MCA Agreements and Statutory Caps in Subchapter V and Chapter 13

In an anomalous twist, in *In re Heart Heating & Cooling, LLC* the debtor did *not* want the MCA agreement construed as an ordinary loan, in order to qualify for Subchapter V, which has a $7.5 million cap.[66] The debtor initially classified most of its debt as "merchant cash advance loans" but checked the box indicating they were nonliquidated and contingent.[67] At the eligibility hearing, the debtor argued these agreements were not debts because nothing was owed by the debtor, no proof of claim was filed, *or* the debts were contingent or unliquidated.[68] To the contrary, the parties had stipulated that the agreements were loans.[69] The court said the debts were not contingent because all events giving rise to liability happened before filing, and liquidated because the amount owing was readily ascertainable.[70] The court acknowledged that the debtor may have valid affirmative defenses against the debt, but that didn't render them unliquidated.[71] Because the debts were liquidated and not-contingent, they did count toward the $7.5 million cap, rendering the debtor ineligible for Subchapter V.

E. Enforceability

If the bankruptcy courts categorize the MCA agreement as a loan, then they may be usurious, unenforceable under nonbankruptcy law, and thus ineligible as claims in the bankruptcy case under 11 U.S.C. § 502(b). This is what happened in *Cap Call, LLC v. Foster* (*In re Shoot the Moon LLC*): the court categorized the agreement as a loan given the broad security interest in all assets, not just receivables, and that both parties referred to the merchant as the "debtor" rather than the seller.[72]

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[66] *In re* Heart Heating & Cooling, LLC, No. 23-13019 TBM, 2024 Bankr. LEXIS 689 (Bankr. D. Colo. Mar. 21, 2024).

[67] *Id*. at *9.

[68] *Id*. at *6.

[69] *Id*. at *55–56.

[70] *Id*. at *37.

[71] *Id*. at *52–89.

[72] Cap Call, LLC v. Foster (*In re* Shoot the Moon LLC), 635 B.R. 797, 813 (Bankr. D. Mont. 2021).

In many cases MCA funders are settling with trustees (to avoid unfavorable precedent) with some trustees achieving full recovery for creditors after filing preference and fraudulent transfer claims.[73]

Conclusion

The courts seem to be scrutinizing MCA agreements more carefully. Indeed, it appears increasingly unlikely that MCA funders can successfully maintain that their transaction is a sale if they don't bear the risk of a downturn in revenues—if, for example, nonpayment is a condition of default that triggers unconditional liability and/or the merchant also gives the funder a security interest in substantial collateral. Still, a threshold inquiry as to whether the merchant is selling *specific property* that they *actually own at the time of sale* would simplify the analysis and make clear that these transactions simply are not, and cannot be, sales. Debtors and trustees should not hesitate to challenge these transactions in order to facilitate operational restructurings or to recover voidable preferences and fraudulent transfers.

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[73] Hillary Russ, *Cash Advance Lenders in Small Biz Bankruptcy Crosshairs*, LAW360: BANKRUPTCY AUTHORITY (July 9, 2024), https://www.law360.com/bankruptcy-authority/articles/1856496/cash-advance-lenders-in-small-biz-bankruptcy-crosshairs.