deBanked

September/October 2017

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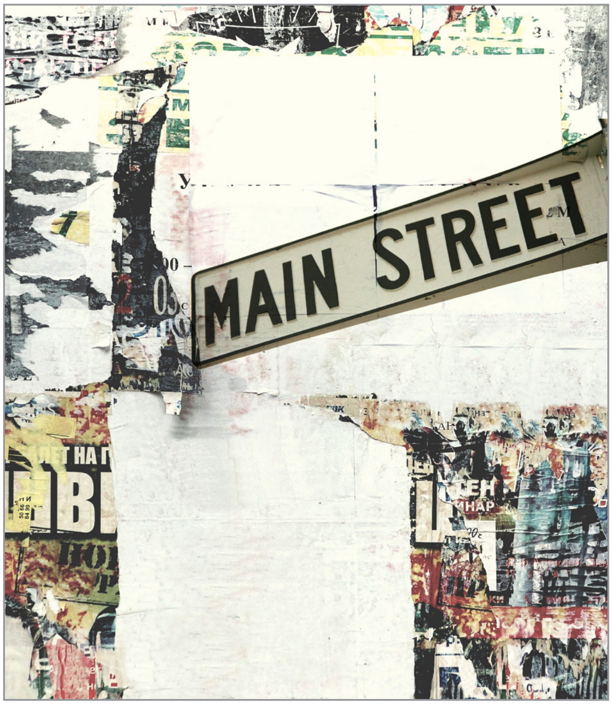

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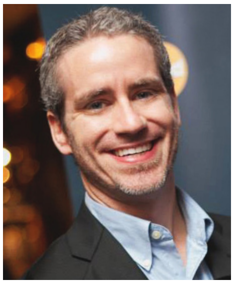
Letter From the Editor



BY
SEAN MURRAY

The lead generators say the market is more challenging than ever. The biggest small business funders are reporting more revenue than ever. Well, not all of them. This Summer and early Fall, the industry said goodbye to a few companies that were funding hundreds of millions of dollars to small businesses each year combined and their competitors are benefitting from the void. Brokers are recalibrating while merchants are continuing to say 'yes' to non-bank alternatives. In this issue, we spoke to sources across the spectrum including small business owners that openly shared their alternative finance experiences.

And it might get easier for small businesses to qualify for credit now that the three major credit bureaus are no longer including liens and judgments in their reporting. That change has put the industry on red alert to bridge the information gap, while others had no idea that had gone into effect. Who better to benefit from this demand for lien and judgment data than fintech companies that have built their businesses on alternative credit information? It's almost as if the old guard of traditional finance are pushing their customers towards their newer, hipper, more technologically equipped competitors.

Despite all the tech, small businesses continue to rely on individuals to guide them through the financing process, whether they be a sales representative at a commercial finance brokerage or a direct capital provider. Broker Fair 2018 will be the largest gathering to-date of those salespeople. Scheduled for May 14, 2018 at The William Vale in Brooklyn, NY, Broker Fair is the one event you simply don't want to miss. You can register at **https://brokerfair.org.** Expect to hear a lot about this between now and May since it's being hosted by yours truly.

Be well, fund many.

–*Sean Murray*

GOODBYE LIENS AND JUDGMENTS

CREDIT BUREAUS HAVE STOPPED REPORTING THIS DATA, SO NOW WHAT?

by ED MCKINLEY

Justice can require sacrifice. Take the example of a decision by the three major credit bureaus – Equifax, Experian and TransUnion – to stop including some liens and most judgments in their credit reports.

The change makes life a little less unfair for consumers who fell victim to reporting errors. Many invested precious time and large amounts of money trying unsuccessfully to correct their credit histories and restore their reputations.

But for the alternative small-business finance industry, omitting data on liens and judgments increases costs, creates extra work and can even give rise to an unsettled feeling in the pit of the stomach. "You're not looking at a full credit report anymore, which is kind of scary," one alt funder admits.

Yellowstone Capital CEO Isaac Stern provides an example to illustrate what's at issue. "Imagine I'm the Ford Motor Co. and I want to do a lease with you," he says. "But I don't have the information that you happen to have judgments from Chrysler, Chevy and BMW, so I approve your lease. Imagine that! Without full information, how do you make accurate decisions?"

Operating without the data could prove dangerous, agrees David Goldin, who sold his U.S. Capify operations to Strategic Funding Source in January but still runs Capify UK and Capify Australia and remains open to U.S. opportunities. "The IRS could come in and seize credit card processing accounts and prevent the lender from getting paid," he says. "Once you have a judgment a creditor could come in and freeze bank accounts."

Fears aside, the change in reporting probably won't dry up alternative small-business credit – even in the short run, Goldin predicts. Alt funders will adjust quickly, he says, noting that they can compare the old and new credit scores of long-time customers to spot patterns and apply those patterns to their calculations. The industry can also tap alternative sources of information.

Even with those reassurances, the transition would have been easier if the industry had more advance notice, alt funders say. "We found out July 31 when a Reuters rep emailed us and said this is going into effect tomorrow," recalls Stern. "That was really weird – I've got to tell you." Experian didn't provide a heads-up even though Yellowstone is one of its largest New Jersey customers, he notes. "We were a little bit annoyed, but what are going to do?" Meanwhile, Goldin says he didn't begin researching the situation until deBanked asked him about it. "I don't think anyone really knew about it" much in advance, he says.

But the industry is finding out and taking action. Yellowstone, for example, is performing a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workaround by integrating the judgments and liens section of the Clear investigative platform into the information underwriters see when they open a file, Stern says. The integration required a couple of weeks of hard work by the Yellowstone tech team, he notes.

Clear, which is provided by Thomson Reuters, amasses public records that can date back 20 years and can fill more than a hundred pages, he says, adding that you have to know where to look for the relevant information. "You have to dig through it," he says.

In the past, Yellowstone performed a Clear report on most files just before funding them, Stern explains. Now, the Clear report is scrutinized more extensively and earlier in the process – before the file is approved. As a result, Yellowstone underwriters will have all the information they need, but it will take them a little longer to get it, he says.

Yellowstone incurred the expense of obtaining additional user licenses from Clear, which cost it $800 to $900 monthly Stern says. Experian now charges the same price for less information, he notes.

Accommodating the changes didn't require more underwriters but it became necessary to hire four additional data entry clerks to input information until the integration with Clear was completed, Stern says. Now that Clear and the Yellowstone systems are working together, the four extra clerical workers will shift their attention to inputting data from the increasing number of applications coming into the company, he says.

Most Alt funders won't need to employ more people in their underwriting departments because changes to their models will be automated, Goldin says. "I don't think this is as much of a game changer as people think it is," he says of the credit bureaus' new approach to reporting." It's just one extra step. It's more of a nuisance issue than a manpower issue."

> **COMBINING ALTERNATIVE DATA WITH TRADITIONAL DATA HAS BECOME MORE IMPORTANT WITH THE BUREAUS' DECISION TO STOP SUPPLYING DATA ON LIENS AND JUDGMENTS...**

However, a challenge arises for underwriters because leaving out the liens and judgments will result in higher credit scores for some loan or advance applicants, Goldin says. That means some alt lenders may need to go to the trouble and expense of tweaking their risk models to compensate for the change in the scores reported by the credit bureaus, he maintains.

The impact may be greatest among alt funders who rely on quick online decision-making, Goldin says. Adding extra steps to the process increases the difficulty of maintaining the speed that provides a selling point and a source of pride for those companies.

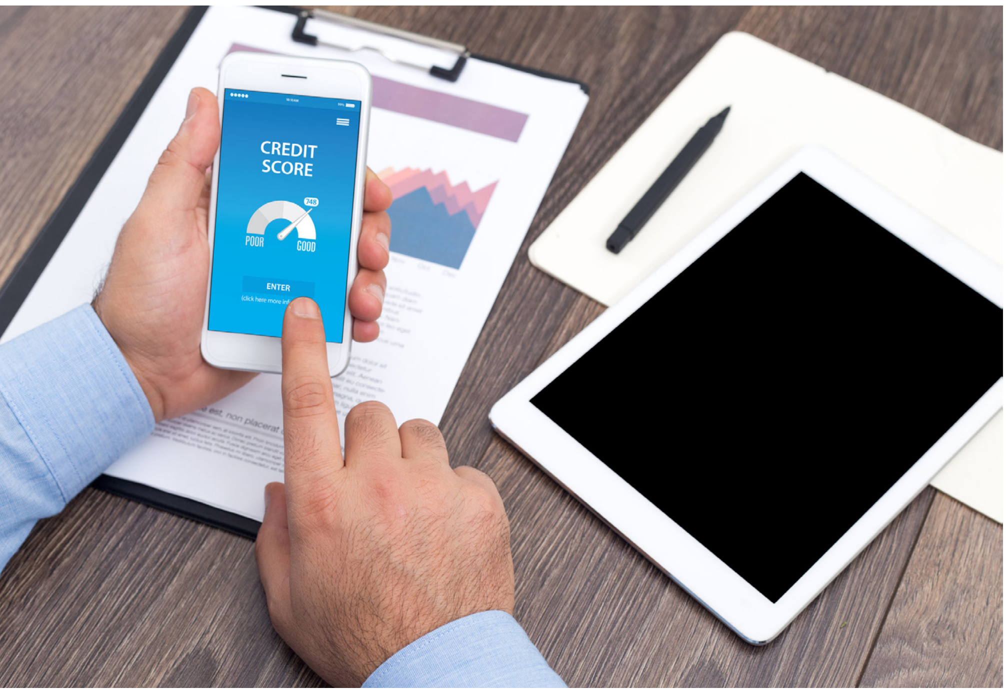
While Clear is helping to fill the gap at Yellowstone, it's not the only company providing much-needed data. LexisNexis Risk Solutions isn't a credit bureau and will thus continue to disseminate information it gathers from courtrooms on liens and judgments, Goldin notes. Alt lenders who weren't already using the vendor's service or were using it only when an application reached a predetermined threshold will face added expense because of the credit bureaus' decision, he says.

Indeed, LexisNexis Risk Solutions views the credit bureaus' hiatus on some liens and judgments reporting as a business opportunity to increase its sales by supplying the missing data, according to Ankush Tewari, senior director of marketing planning in the company's business services section. The company was already selling data on liens and judgments and anticipates selling much more of it, he observes.

For 15 years LexisNexis Risk Solutions has been selling RiskView Solutions, a product that contains liens, judgments and other information not generally found on credit reports, such as the assessed value of a consumer's home or a list of a consumer's professional licenses. It offers no data on loan repayment but its other information helps

define a consumer's creditworthiness and character, Tewari says. Lenders can combine that peripheral information with credit scores for a more complete customer profile that outperforms the credit score alone, he suggests.

And there's more. LexisNexis Risk Solutions has reacted to the credit bureaus' decision by creating RiskView Liens & Judgments Report, which lists only those two types of records. "The credit bureaus announced these changes a year ago, and we knew there would continue to have a need for that data," Tewari says. The company prices the RiskView information based upon the transaction volume, he notes, so a lender pays less per transaction as volume increases.



With this emphasis on liens and judgments, one might well wonder who tracks down the information. Companies like LexisNexis Risk Solutions gather and disseminate public records on liens and judgments from courthouses throughout the United States, says Tewari. Over the years the company acquired some of its competitors and eventually was spun off from its sister company, LexisNexis, which built its name partly as an aid for lawyers researching cases, he notes.

For decades, LexisNexis Risk Solutions has been providing the credit bureaus with raw data not only on liens and judgments but also on bankruptcies, Tewari says. The bureaus have then parsed those files electronically and appended the data to credit reports, he continues.

Problems arose because the credit bureaus' tech systems could not always link the court documents to the right person when the courts provided only a name and address, Tewari maintains. Courts often limit information in their records to those two identifiers because they're reluctant to divulge additional identification that criminals could intercept and use to commit fraud, he says.

Tewari traces the bureaus' inaccuracies in matching court records to the right people to what he calls the bureaus' "DNA." The bureaus are accustomed to receiving "clean" information from lenders on a regularly scheduled basis. Conversely, some of the LexisNexis Risk Solutions data, gathered from obscure places like county deed offices, may arrive in a form that's far from clean, he notes.

However, that lack of court information or inconsistencies in the presentation of that information doesn't pose problems for LexisNexis Risk Solutions because the company cleans the data before analyzing it. Tests indicate its linking methodology works accurately with just a name and address more than 99.9 percent of the time, Tewari contends. Thus, the company can establish that John Smith at 1234 Maple Street is the same person as John A. Smith at 1234 Maple Street, he says. He considers that linking technology the core of the company's operations.

The information LexisNexis Risk Solutions can supply becomes vital to lenders because studies indicate that people who have a lien or judgment on file are twice as likely as people without them to default on a consumer loan and five times as likely to default on a mortgage, Tewari says. "The data didn't become less important because the credit bureaus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decided not to include it anymore," he maintains. "It's still just as predictive as it was."

Meanwhile, other types of information can also help lenders make decisions, notes Eric Lindeen, vice president of marketing for ID Analytics, a credit risk and fraud risk management company that offers a credit score called Credit Optics, which it bases on a combination of traditional and alternative credit data.

Alternative credit data is defined as anything the credit bureaus don't include in their reports, Lindeen says. Examples include the bills consumers pay for cell phones, utilities and cable television, he notes, adding that rent is also sometimes considered alternative credit data. The category also encompasses records from marketplace lenders.

A consumer's tendency to pay those bills on time, late or not at all can reflect on creditworthiness, Lindeen maintains. That history becomes relevant for alt funders because the small businesses they serve constitute a hybrid of consumer and commercial credit, he says.

Using that data, ID Analytics can spot people who are good credit risks when the credit bureaus still consign them to "thin file" status — the limbo where applicants don't have enough credit history to evaluate their creditworthiness, Lindeen maintains. About 60 percent of near-prime applicants qualify for credit when lenders factor in alternative data, according to an ID Analytics study he says. At the same time, alternative data can also expose weaknesses among individuals with excellent traditional credit scores, he observes.

Combining alternative data with traditional data has become more important with the bureaus' decision to stop supplying data on liens and judgments, Lindeen says. Leaving out that data will raise some credit scores, and the effect will be strongest among near-prime individuals with good but not great traditional scores, he notes. With those consumers, a 10-point shift could make a big difference in qualifying for credit, he says.

"Even though it's a small population, it's a critical population," Lindeen says of those newly minted prime applicants. They may number only one in a hundred of a particular funder's portfolio, but they may advance to another risk pool and consequently invalidate a risk model, he suggests. Over time, risk managers will adapt to the change and oversee a "risk migration," he predicts.

Overall, between 6 percent and 9 percent of consumers will see their credit scores rise because of the bureaus' new policy, Lindeen estimates. The change usually won't exceed 20 points, he says. Still, about 700,000 will see an improvement of 40 points or more, he continues. "That's a significant increase for a nontrivial population," he says. "It's likely their performance will stay the same as their score goes up."

A study by VantageScore Solutions, the company that provides the VantageScore credit scoring model to the credit reporting bureaus, projected scores would increase an average of 10 points for slightly more than 8 percent of the scorable U.S. population.

Those changes are characterized as "minimal" by Francis Creighton, President & CEO of the Consumer Data Industry Association, a trade group

that represents the three major credit bureaus as well as about a hundred other companies – mostly smaller credit bureaus around the country, resellers of credit bureau information and background screening companies.

The credit bureaus decided to curtail reporting of judgments and liens as part of the National Consumer Assistance Plan, or NCAP, Creighton says. NCAP is an agreement reached in March 2015 among the three major credit bureaus and the attorneys general of 31 states, who were pressing for fairness in credit reports. Many observers call NCAP a "settlement" but the agreement did not result from a lawsuit, he notes.

Under NCAP, the bureaus will continue to include bankruptcies in their reports because the records meet the standard of providing a name, address, Social Security number and date of birth and because visits to the courthouse to update records occur at least every 90 days. About half of liens don't meet those standards and will be removed from credit reports, and nearly all judgments fail to adhere to the standard and will no longer appear on the reports.

Although Creighton declines to say how many consumers were victims of credit reporting errors, he emphasizes the severity of the problem for each victim. "If you were one of the people who had a name similar to somebody else or a similar Social Security number, it would impact you a lot," he maintains. "I don't know how widespread it was, but it was disruptive enough for individual people that it's better just not to have it."

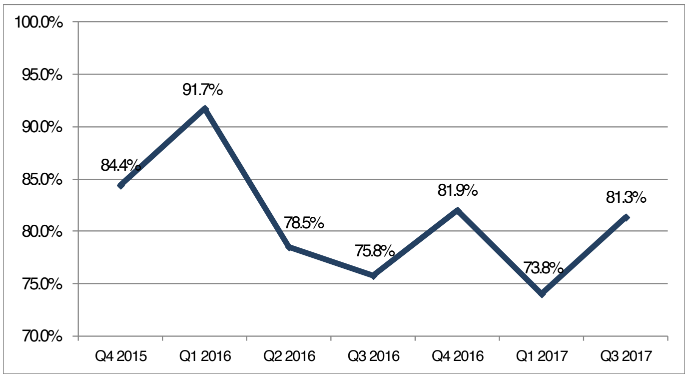
A Federal Trade Commission study released in 2013 reported that a sample of 1,000 credit reports indicated that 25 percent had at least one error that could reduce scores, according to published reports. Such findings prompted state attorneys general to seek remedies that resulted in NCAP.

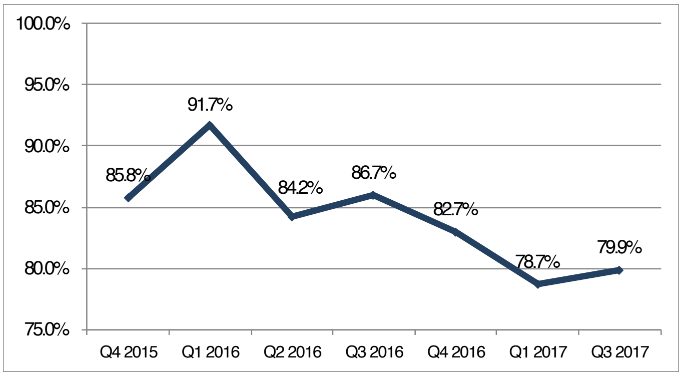
The bureaus planned to implement another major portion of NCAP in September when they were to begin waiting 180 days before reporting medical debts, Creighton notes. At the same time, debts for medical expenses covered by insurance policies were to be omitted from credit reports, he says.

Changes brought by NCAP represent part of ongoing efforts to improve the system, according to Creighton. "We want accurate information in the reports," he says. "That's good for everybody."

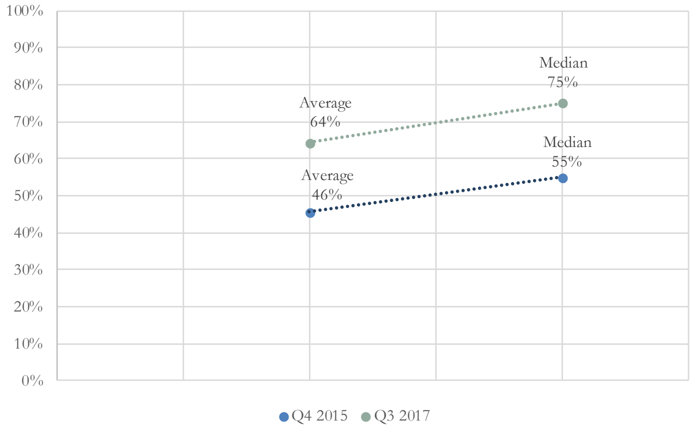
Bryant Park Capital and deBanked surveyed industry CEOs in the 3rd Quarter of 2017

CEO Confidence Index
What is your overall confidence level in the continued success of the small business lending / MCA industry over the next 12 months?



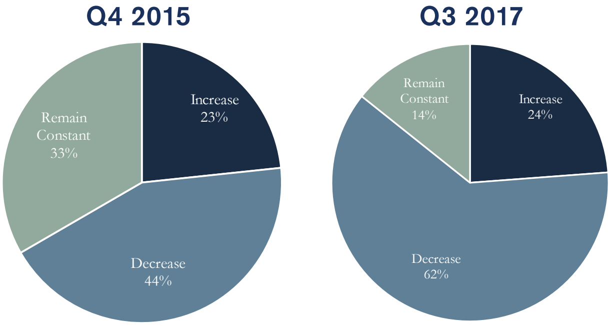


CEO Confidence Index
What is your confidence level that you can access the capital needed at reasonable costs to continue to grow over the next 12-24 months?



Where is Business Sourced?
CEOs: What percentage of your originations come from external/ISOs versus internal marketing?

Where is Business Sourced?
CEOs: Do you expect the percentage of external/ISO originations to increase or decrease?



THE VOICE OF MAIN STREET – SMALL BUSINESSES SHARE THEIR EXPERIENCES WITH NON-BANK FINANCE

By *PAUL SWEENEY*

If she hadn't scored the $250,000 loan through Breakout Capital in 2015, Jackie Luo says, the commercial-software firm she heads in Baltimore could not have made the "strategic hires" and purchased the new server to support additional customers and maintain the company's 30% growth rate.

"Without that infusion of capital" from the McLean (Va.)-based lender, says Luo, chief executive at E-ISG Asset Intelligence, the software solutions provider would have been hard-pressed to deploy the "bandwidth and capacity" necessary to meet burgeoning demand.

And demand there is. Luo says billing for her company's services helping more than 100 businesses and government agencies improve operational efficiency by keeping tabs on multiple assets — human, financial and equipment — topped $1.5 million last year, up from $1 million in 2015. This year, moreover, E-ISG is on track to collect nearly $2 million.

Meantime, she says, the $250,000, 10-year note at 6% interest she obtained with the help of Breakout was both a good deal and convenient: she reports securing the financing in three weeks, compared with the six months that a commercial bank would likely have taken. In addition, she's been able to forge a better relationship with Breakout than with a faceless financial institution.

"We are a small business," she says, "and we'd be just one in a million at a big bank like Wells Fargo. They wouldn't give us much attention." With Breakout, Luo adds: "I have the freedom to make decisions about infrastructure investments without worrying about the short-term. And I don't have to deal with people second-guessing me."

Had she not gotten the financing, moreover, "I would not be able to pay myself," she says. "I'd have to use my salary as working capital."

Luo is not alone. Her company's story of finding much-needed capital from a nonbank financial company is increasingly common. It has always been challenging for small businesses to obtain credit from a big bank — roughly a financial institution larger than $10 billion in assets. But the small and community banks that have been the lifeblood for small businesses have also been winding down their small-business lending as well, according to a March, 2016, working paper published by the Federal Reserve Bank of Philadelphia.

"As recently as 1997, small banks, with less than $10 billion in assets, accounted for 77% of the small business lending market share issued by commercial banks," co-authors Julapa Jagtiani and Catharine Lemieux write in "Small Business Lending: Challenges and Opportunities for Community Banks." However, the market share dropped to 43% in 2015 for small business loans with origination amounts less than $1 million held by depository institutions.

"The decline is even more severe for small business loans of less than $100,000," they add, "where the market share for small banks under $10 billion declined from 82% in 1997 to only 29% in 2015."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The Philadelphia Fed study notes that alternative nonbank lenders are filling a widening gap. "By using technology and unconventional underwriting techniques, many alternative lenders are competing for borrowers with offers of faster processing times, automatic applications, minimal demands for financial documents, and funding as soon as the same day." And the Fed study finds that it's likely that nonbank lenders, which are growing rapidly, are having a positive effect by "increasing the availability of credit, particularly to newer businesses that do not have the credit history required by traditional lenders."

Meantime, the Small Business Administration reports that small businesses remain essential to the health of the U.S. economy. Businesses with fewer than 500 employees account for 55% of overall employment in the U.S., according to the agency, and are responsible for *creating two out of every three net new jobs*. Which means that alternative funding sources — which do not, it is worth noting, depend on depositors' money, as banks do — are playing an increasingly important and largely unrecognized role in the country's economic fortunes, notes Cornelius Hurley, a law professor at Boston University and executive director of the Online Lending Policy Institute. "They're still a small percentage of the overall lending picture," he says of nonbank financial companies, "but they're an emerging force and a lot of small businesspeople certainly depend on them. If they disappeared tomorrow," he adds, "a lot of businesses would be wiped out too."

To find out what is happening in the real world, deBanked interviewed small business owners around the country: among others, a Houston sports medicine provider, a Connecticut restaurateur, a Midwestern truck hauler, and a Maryland hardware-store owner. Some recounted being shunned by banks because of poor credit while others registered unhappiness with traditional financial institutions as inconvenient and impersonal. While some who turned to alternative lenders admitted they would have preferred not to be paying dearly for borrowing or for cash advances, most said the tradeoff was worth it.

The existence of alternative lenders has made it possible for these businesspeople to meet payrolls, pay contractors and suppliers even when business was slow or billings stalled. Customers with alternative funders – in addition to Breakout's customers, deBanked spoke to clients of Pearl Capital Business Funding and Merchants Advance Network– also reported that they were able to purchase or replace equipment and maintain inventory, hire additional employees and accept new customers, pay for upkeep and upgrades of their business's physical plant, and make other expenditures necessary to keep operations up-and-running.

Jason, for example, who heads a family business in Louisiana manufacturing and selling pesticides (and who asked to be identified only by his first name), reports that his suppliers began demanding that he pay in advance for chemical feedstock after he took a "financial hit following a nasty divorce."

The roughly $1 million (annual sales) business — which was started by his parents back in 1960 — furnishes chemicals mainly to cotton farmers and homeowners in Louisiana and Texas, most of whom purchase the company's products through feed and hardware stores. Jason says he spends a substantial

The smart choice for deals of all shapes and sizes

amount of time on the road handling sales and distribution.

His suppliers not only require him to pay for the chemicals upfront but, following his divorce, they now insist upon larger purchases as well. Following the departure of a previous lender, he says, Breakout stepped in with an $80,000, 12-month loan in March, 2016, which he was able to repay within six months. This was followed by a $60,000 borrowing in March, 2017, which he again paid down early – in 90 days, Jason says – and the account manager at Breakout "went to bat for me and gave me an additional discount for early payment."

Had Breakout not provided external funding, Jason says, he would have been "wiped out." He adds with feeling: "It would have meant the end of me." And sinking the fortunes of the company would also have spelled job losses for five employees, including both his son, who works part-time, and his sister, the business's co-manager. "Now I'm out of the hole," he says.

In Houston, Anna, co-owner of a physical therapy and sports medicine concern, was interviewed in August just before Hurricane Harvey loomed on the horizon. "We'd been around for four years and growing rapidly," she says, asking to be identified only by her first name, and "we couldn't keep up with the growth."

Anna recalls that a few years ago (she is vague about the exact dates) the company needed $50,000 to $60,000 to add equipment and staff to meet the growing demand. Because of some "ups and downs" in her business and credit history, however, a bank loan was out of the question. "My credit wasn't the best," Anna says, "and we had not been in business the five-to-seven years that most banks want." She began casting about for financing and quickly saw that factoring would not be a suitable choice for a business like hers, which depends heavily on third-party payments from health insurance providers. "Companies using factoring are taking money based on credit card payments," she says, "and we're not a restaurant or a bar. So we can't pay a percentage of every transaction." Typically, she notes, getting paid by an insurance company involves a "90-day turnaround."

Anna went online, did some research, and talked to three or four nonbank lenders searching for the "right kind of company." That led her to Breakout. "What I really liked about them is that they did a lot of due diligence on our field," she says. "They did their homework, asking us: 'What are your collections and payroll? How much outstanding debt do you have?' They also asked to see our actual bank statements."

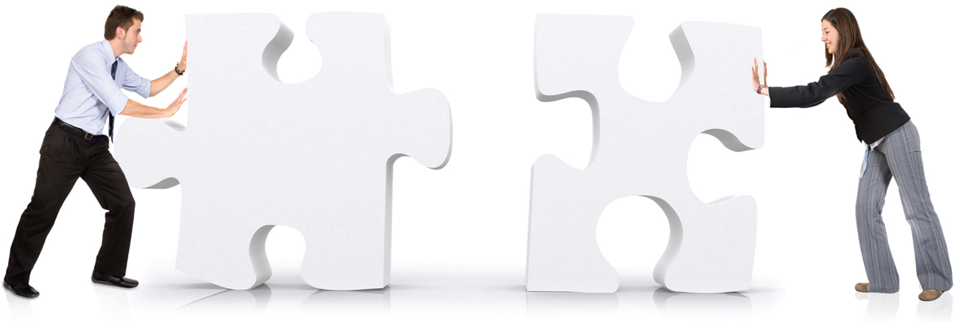
Despite the high level of due diligence that Breakout performed, Anna says, it only took "maybe three or four days" for the loan to be approved and for the money to land in her bank account. Before long, she was off to the races. With the added capital, she hired three more employees – bringing the employee headcount to 18 -- purchased more gym equipment, made payroll, and paid off miscellaneous expenses.

The added capacity and fortified staff, meanwhile, enabled the company to "almost triple its volume," the entrepreneur says. And not only did the financing "put me in a good financial place," Anna adds, but after repayment, Breakout made it possible for her to effect a merger with a competitor by approving a second loan for about $30,000. "The best thing about Breakout," she says, "has been the communication. One time I did need to make a payment two or three days late. But I just called (the account manager). I was very surprised because these kinds of companies are seen as a last resort. But it was like they were investing in us."

John Speelman, who owns Poolesville Hardware in Poolesville, Md., can boast a raft of five-star Yelp reviews online. "Extremely helpful and friendly service, surprisingly good selection (and) the complete opposite of a big box hardware chain," raves one customer. "It is so rare to find a well-stocked store that has helpful personnel—makes this store a real gem!" says another fan.

For his part, Speelman attributes much of his hardware store's popularity to the financing arrangement that he's been able to work out over the past eight years with Merchants Advance Network, a Fort Lauderdale (Fla.)-based alternative funder. "It takes money to make money," is one of his pet aphorisms.

Located roughly 35 miles west of the White House, the hardware store boasts a clientele who tend to arrive in BMW's rather than the pickup trucks that predominated a decade or so ago in this exurban community of some 5,000 denizens. Whatever their class background, though, they're looking for items that are not a good match for an online purchase. "People don't buy a toilet plunger,



a can of paint or picture-hanging stuff online," Speelman says. "Because they want to do that today," he says, "they won't order with Amazon. "

"One industry that has not been impacted" by online merchandisers, he adds, "is the garden center. They'll buy a garden hose, weed killer and seeding," he explains of his regular customers. "And light bulbs" while they're there, he adds. "We're like the 7-Eleven -- a convenience store."

To guarantee that convenience, Speelman pays cash-in-advance for most of his inventory, and banks have not been helpful. He contrasts the relationship he has with Michael Scalise, the chief executive at Merchants Advance, with loan officers at commercial banks. "It's hard to get a loan for anything in retail," he says. Never mind that he maintains "a high credit rating and I never bounce a check," he went on. "There are no more local banks. At M&T Bank, all the managers I knew are gone and there's always a new teller. The banking industry is a revolving door."

So he opts for capital from Merchants Advance "when I need 30-40-50 grand in a day, I use Mike's money" even though the cost can be as steep as 25%, he says. If he doesn't have something in stock – specialty items like ammo boxes, a Sugarplum tent, as many as 32 packs of size D batteries, metric measuring tapes – he can put in a special order with suppliers. But he prides himself on the full panoply of wares on his shelves. "You can't sell from an empty cart," is another of his favorite sayings.

Lori Hitchcock, who also draws capital from Merchants Advance, is manifestly displeased with the banking industry. She's an owner with her husband of Hitchock Trucking, the couple's 60-year-old family business, which is located on a ten-acre tract in Webberville, Mich., situated between Detroit and Lansing, the state capital.

Of her experience with banks, Hitchcock says: "At the time we went with (Merchants Advance), banks weren't lending. And they're still not lending. We're considered high-maintenance and high-risk. Banks don't want a bunch of trucks" should they foreclose on a loan, she observes. "If you're a farmer, they can take all your land. Great! In this crazy world you live in, it's hard to get the banks interested."

The Hitchcock family's fleet of ten Peterbilt semis hitch up to more than 20 trailers and truck bodies – flatbeds, dump trucks, vans, and refrigerated trucks or "reefers" – and haul grain, sweet corn, onions, celery, fertilizer, and soft drinks across the Midwest. Most recently, she says, the family business took out $80,000 from Merchants Advance to expand its fleet and buy another reefer trailer and a backhoe. "Out here in the country, you always need a backhoe," she says.

To satisfy her lender, the company makes daily ACH payments. "I'm not going to lie and say that things aren't tight," she says. "It is a burden. You just have to have constant cash-flow – which we do have. And it's important to have good relationships...I can usually tell three weeks in advance if (making payments) is going to be challenging. So it all comes down to being loyal to people."

Whatever the struggle to keep up with debt payments, it beats using her own money. "My husband and I are raising a family," Hitchcock says, "and it's nice having the cash so you're not putting your personal earnings into the company."

In Manchester, Conn., a stone's throw east of Hartford, Corey Wry says that he wouldn't be able to operate his two, highly rated restaurants just off Interstate 84 – Corey's Catsup & Mustard and Pastrami on Wry – if he didn't have funding from

Pearl Capital, a New York (N.Y.)-based alternative funding company. A graduate of Johnson & Wales University in Providence, a restaurant-and-hotel school, Wry describes himself as "a culinary guy" whose first love is serving food that's both innovatively prepared and delicious. He candidly admits that his credit hit "rock bottom" after a confluence of untoward events.

Last year, a third restaurant in town, Chops & Catch, that he and some partners had "bootstrapped" had to shut down after six years of operation. Despite generally favorable reviews for such creative fare as the "lobsterburger," the surf-and-turf themed restaurant was a money-loser. He was also struggling to pay off credit cards. And he'd been late more than once on car payments.

At the same time, Wry was in the process of moving Pastrami & Wry — a deli whose moniker is wordplay on his last name – to a new location. Both the general contractor and electrician were "over-budget" on that project, he says. Meanwhile, Catsup and Mustard, a hamburger spot, needed to be spruced up. Says he: "It was getting busier and the original seats were worn. I had a hole in a booth big enough to swallow someone."

He approached a few banks for a loan and "it did not seem like it was going to happen," he says. "Then I got a cold call from one of these financiers. Some of them had super-high rates. When you have bad credit but need to make capital improvements you do what you have to do."

He's accessed more than $100,000 from several alternative funding sources, including Pearl – from which he reports getting merchant cash advances for $30,000. But hard as it is to meet the obligations, which typically require a daily ACH payment, the financing has made renovating the burger place possible. Moreover, he'd still be on the hook with plumbers and other contractors – all of whom are local tradesmen and would likely be paying him personal visits until they were repaid -- for the relocation of Pastrami & Wry.

"Business is good," says Wry, who at 40 is single, often works 15-hour days, and says that he doesn't have time for a girlfriend, much less a wife and family. "I've still got $3,200 on the books with the electrician," he adds, "which means that I won't be able to purchase a deli slicer. I have to plan these things out…"

James McGehee, a partner at the boutique accounting and tax-preparation firm McGehee, Davis & Associates, which is located in the Denver suburb of White Ridge, reports that the firm took a merchant cash advance from Pearl Capital, among other financiers, to bridge the gap between tax season and the rest of the year when billings invariably diminish.

"Our overhead is pretty high," he explains. "We've added two employees. We've been expanding on what we were doing, adding tax and accounting clients."

A very conservative, sober-sounding man, McGehee explained that his credit was nonetheless "trashed" after he suffered from health problems five years ago. "Major stuff," he says, "it was open-heart surgery." The medical ordeal meant that he could not work for a time and had trouble paying his bills. "Some family members helped me through the mortgage and utilities payments and I ended up in arrears and in credit card debt," he says.

All of which made an alternative source of financing his firm's only option. "I'm not sure how we heard about Pearl," he says. "I think they just happened to call. We took out [$11,000]. It was not a huge amount. We also borrowed $9,000 from another entity. We paid it all back during tax season. The terms were pretty steep," McGehee adds.

"But when you need the money for cash-flow," he explains, "you just absorb it. You grin and bear it. When you need the money, you need the money."

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THE SCOOP ON iPAYMENT'S MCA RENAISSANCE

By *GERELYN TERZO*

iPayment, a small business payment processing company, is placing a bet that it could be better the second time around in the MCA industry. iPayment Capital, which is scheduled to launch in the fall, is iPayment's second foray into the merchant cash advance market. In conjunction with this expansion iPayment tapped Tomo Matsuo as senior vice president to spearhead iPayment Capital.

iPayment's announcement comes on the heels of industry peers Square Capital's Q2 loan origination of $318 million and PayPal's acquisition of Swift Financial. Rather than remain on the sidelines, especially with access to data on some 137,000 small businesses, iPayment is making its move.

"Before Daily ACH loans and MCAs, we all started with the split payment MCA, and it's exciting to see the recent renaissance of that mechanism with companies like Square and PayPal making it a key product feature. Transaction-based underwriting and variable payback schedules have become much more mainstream thanks to companies like Square and Amazon," said Matsuo.

iPayment's timing for getting back into MCAs is apparent but also coincides with the industry being held under a microscope for some questionable practices, not the least of which involves stacking, which can get small businesses in over their heads. Matsuo said the industry has a shared responsibility to fix this.

"I think there's an opportunity for the industry to clean up some of the stacking and other practices. We all need to do more to better align ourselves with the needs and long-term health of the customers," said Matsuo.

Meanwhile David O'Connell, senior analyst at Aite Group, offered his thoughts on the future role of MCA in small business funding: "Although we will always have merchant card advances in large volumes and these will be important to SMBs seeking funding, some of this volume will be replaced as the practices of alternative lenders become more entrenched: the provision of capital to an SMB based on a variety of data sets that achieve a fuller view of an SMB's ability to repay only some of which is related to credit card volume."

BALANCE SHEET FUNDER

Similar to its predecessor product iFunds, iPayment Capital will be a balance sheet MCA origination business. The company has the benefit of hindsight with iFunds, which was before Matsuo's time there, as well as any missteps by the industry from which to pull.

"My job is to launch and build our own balance sheet MCA product, and we have a management team committed to the initiative," said Matsuo. "iPayment is in a unique position because of our long history with the product — as a funder, split payment technology provider, and referral partner — and have a lot of experiences to build upon. There's a great team at iPayment with a ton of institutional knowledge."

iPayment's access to customer data and insights certainly gives the company an edge. "It's a crowded market going after a finite universe of customers. From a customer acquisition standpoint, iPayment has the benefit of having 137,000 customers," said Matsuo.

iPayment also has solid industry partners including the likes of RapidAdvance with whom the company serves merchant customers. iPayment will continue to work with RapidAdvance and others on MCA. "We recently had the opportunity to strengthen our balance sheet, and we believe investing in iPayment Capital makes great business sense," said Matsuo.

Matsuo pointed to opportunities within the smaller merchant segment for MCAs. iPayment Capital's average funding size will be somewhere between Square Capital's range of $6,000 – $7,000 and that of ACH alternative lenders at about $40,000. "We'll be right in the middle," he said.

Matsuo, a Bizfi alum, officially started in his new role on July 1, and he has no interest in looking in the rearview mirror. "At the end of the day, it comes down to pricing risk appropriately and maintaining proper controls," said Matsuo, adding: "We all want to grow, but there are responsible ways of doing so."

LEAD GENERATORS FACING ROUGHER ROAD

By *CHERYL WINOKUR MUNK*

Lead generators for alternative funders are facing stronger headwinds these days.

The business has gotten tougher for a whole host of reasons. A pullback in alternative lending necessitates fewer leads. On top of that, funders, ISOs and brokers have gotten pickier about the types of leads they'll accept. What's more, stricter application of the Telephone Consumer Protection Act (TCPA) is hampering lead generators' ability to solicit business owners. As a result, some lead generators have faded away, while others have been developing additional business lines or are broadening their reach to other areas within financial services to buoy earnings.

"I don't see any growth in the space for the next six months, or maybe a year," says Michael O'Hare, chief executive of Blindbid, a lead generation company in Colorado Springs, Colorado. "It's really unclear right now what's going to happen, but we'll see."

The alternative funding industry has been in somewhat of a funk since spring 2016 when Lending Club grabbed headlines with a scandal that spooked the industry and also took out several senior managers, including the company's then-CEO.

It was the first time in the industry's relatively short history that people realized "it wasn't all puppy dogs and ice cream," says Justin Benton, a partner at Lenders Marketing in Santa Monica, Calif., a lead generator in the alternative funding space.

Since that time, there's been a lot of movement in the market, including companies that are consolidating or exiting the business, pumping the brakes or making shifts in product lines, Benton says. These developments have all had a big impact on the sheer number of clients that are looking for leads, he says.

Late last year, for instance, CAN Capital Inc.

stopped funding for several months, though it's back in business as of early July. This summer, Bizfi, one of the stalwarts of the alternative financing space, began giving pink slips to staff and in August the company sold the servicing rights to its $250 million loan portfolio to rival Credibly.

There aren't as many start-up ISOs or companies entering the alternative funding space—meaning more leads for existing funders—which, of course, is a boon for them. "There are still roughly 75,000 business owners every week who meet the criteria for an [MCA]. Now instead of there being 5,000 options in the space, there are 2,000, so those 2,000 are gobbling it all up," Benton says.

At the same time, however, TCPA regulations have gotten more stringent, making it dangerous to solicit businesses, says O'Hare of Blindbid. "Any phone call you make, you can get sued," he says.

Large funding companies generally take TCPA very seriously—especially if they've gotten hit with violations, O'Hare says. Smaller funders and brokers, however, aren't always as familiar with the restrictions; they think it's only an issue if you're calling consumers, as opposed to calling businesses, but that's not the case. "A lot of businesses today are using their cell phone as a main business line and also for personal use. If you call a cell phone that's on the DNC [Do Not Call Registry], you can potentially get sued."

Last year, he had a situation where a plaintiff pretended to be an interested business. When he passed along the referral, the plaintiff's attorney claimed TCPA violations and ultimately sued the funder. The funder balked, and it created numerous issues for his company.

His company now tries to educate funders about how to protect themselves from TCPA litigation. He sends out emails to funders with information about TCPA and provides contact information of attorneys who are well-versed in TCPA rules. He also provides funders with risk mitigation tactics and shares his list of known TCPA litigators so funders won't accidentally call them. He also provides direction to clients that receive a demand letter or complaint on how to respond and offers a list of TCPA defense attorneys, if they need.

"We've become almost extreme in how we try to avoid problems related to TCPA," O'Hare says.

To be sure, some of the changes lead generators are experiencing are indicative of a maturing industry.

A few years ago, lead generators could be less selective who they approached initially because the concept of alternative funding was so new to merchants, says Bob Squiers, chief executive of Meridian Leads, a lead generator in Deerfield Beach, Fla. Now, however, the cat is out of the bag, and, with business owners getting multiple calls a day, it's harder to get their attention, he says.

"They know, they've heard, they've been pitched. There's not too many unturned business owners. It's about getting them at the right time."

As a result, lead generation today requires more data to discern the good leads from the bad. Instead of going after half a million restaurants, lead generators are targeting the 20 percent that data suggests are the most viable funding candidates. "It's more of a sniper approach than a shotgun approach," Squiers says.

Rob Buchanan, senior sales executive at Infogroup in Papillion, Nebraska, who focuses on lead-generation for the fintech space, notes that within the past 18 months or so, clients have been going after "low-hanging fruit" when it comes to leads. They are looking for leads where business owners are actively looking for financing as opposed to relying primarily on UCC data. They are still using UCC data, but to a lesser extent than they were in the past, he says.

Not only do clients want very targeted and specific types of companies—but they are changing their minds more frequently about the types of businesses they're looking for, says Matthew Martin, managing director and principal at Silver Bullet Marketing, a lead-generating and marketing company in Danbury, Conn. They might ask for businesses of a particular size or credit quality—they are even seeking to exclude businesses within certain zip codes. They are also more amenable to leads from industries they deemed too risky a few years ago.

"I have clients that are constantly changing the parameters of what they want," Martin says.

The problem is that once you start narrowing the leads of possible merchants that can be funded, lead costs go up and many funders don't want to pay for that, says O'Hare of Blindbid. "The glory days when everything was wide open and you could generate leads really cheaply are pretty much gone."

Meanwhile, as some lead generators have faded into the sunset, others are forging ahead in search of new opportunities.

Benton of Lenders Marketing, for instance, says his company has started to focus its efforts in other areas of lending, including SBA, new business, mortgage, commercial, residential, auto and student loans.

Digital marketing is another area experiencing increased demand. Business owners that need money tend to use Google to find funding companies. Infogroup's digital marketing leads these businesses directly to funders, ISOs and brokers, Buchanan says.

"More and more funders, brokers and ISOs are leaning toward doing digital marketing," he says.

WORLD BUSINESS LENDERS ACQUIRED STRATEGIC ASSETS OF BIZFI

By *SEAN MURRAY*

The Bizfi marketplace is slated to live on, according to Stephen Sheinbaum who joined World Business Lenders (WBL) as a managing director in July. On September 20th, WBL purchased several assets from Bizfi including the brand, the marketplace, the Next Level Funding renewal book, and other related pieces of the company, he says. Sheinbaum founded Bizfi (then Merchant Cash and Capital) in 2005.

WBL, a Jersey City-headquartered small business lender will also be a lender on the platform.

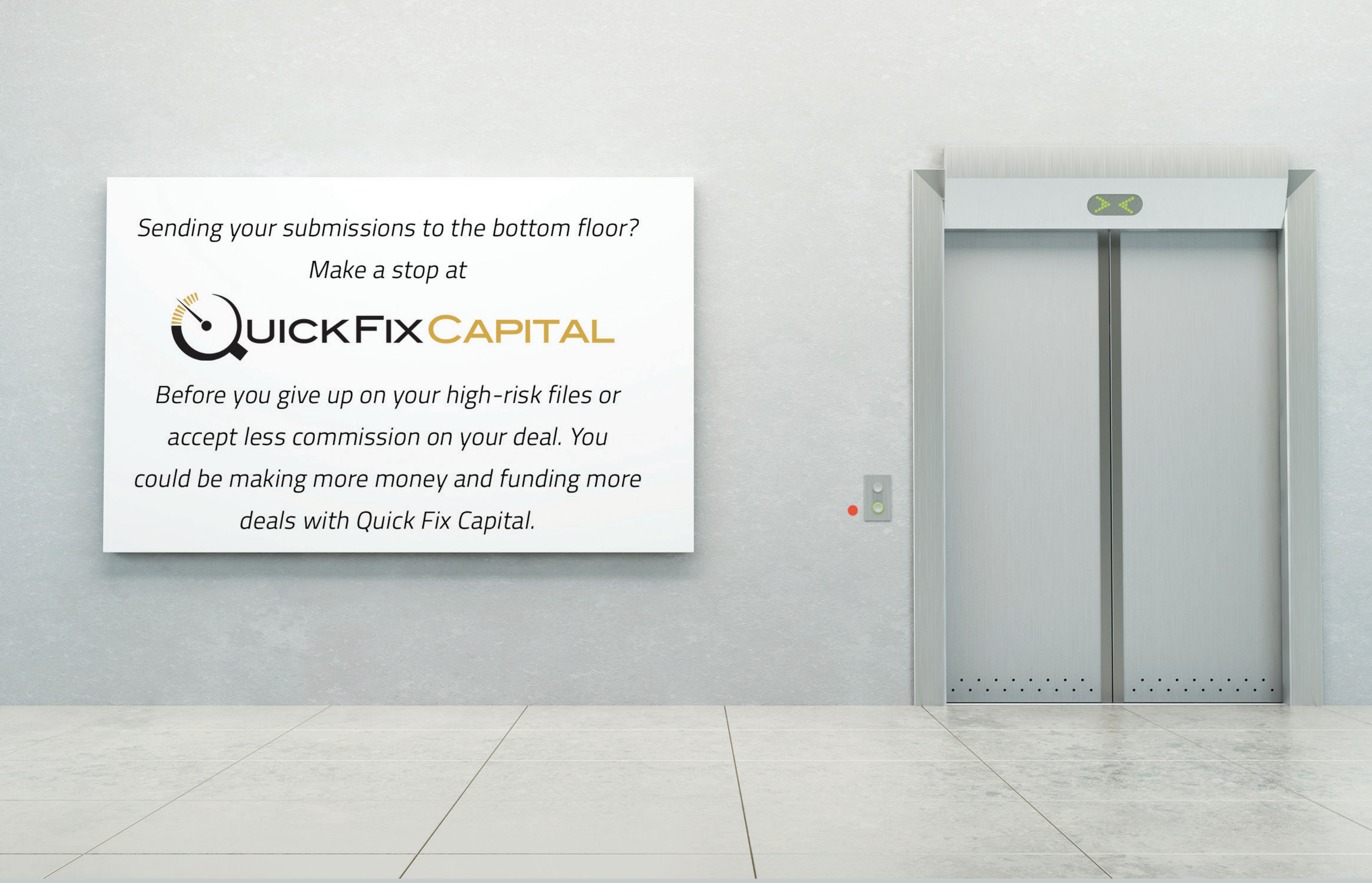
Other key Bizfi personnel have joined WBL including former Managing Director of Renewals John BellaVia, VP of Sales Michael Caronna, and Sales Manager Ryan Bressler.

The asset purchase does not affect the deal forged with Credibly to service the $250 million portfolio, Sheinbaum explains, which is separate.

While lesser known among the mainstream fintech media, WBL has been a stalwart player in the non-bank lending industry for years. Their ambitions and size became more apparent when deBanked attended their invite-only annual shareholder meeting at the Waldorf Astoria in NYC in 2015. The company went on to open a massive office in Jersey City in July 2016 that was attended by Jersey City Deputy Mayor Marcos Vigil, Councilwoman Candice Osborne, Archbishop David Billings and Mitchell Rudin, the CEO of Mack-Cali. At the ceremonial ribbon cutting, WBL CEO Doug Naidus said that he wanted to build a company that lasts, one that he can look back on and be proud of.

Now with the Bizfi brand and marketplace in tow, the company is uniquely positioned.

"[It's a] game changer here," Sheinbaum said. "2.0 here we come!"



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INDUSTRY *NEWS*

7/17 – Online lender Upgrade, launched by former Lending Club CEO Renaud Laplanche, revealed it had already hired about 100 people

Credit risk startup James Closed $2.7M funding round led by Gaël de Boissard

7/18 – Former Bizfi COO Tomo Matsuo joined iPayment as an SVP to oversee its new merchant cash advance division

7/21 – SoFi Chief Revenue Officer Michael Tannebaum departed the company

7/27 – Lendio surpassed $500M in lifetime originations

RealtyShares acquired marketplace platform Acquire Real Estate

7/28 – Former MB Financial Bank SVP Stan Scott became VP at Gibraltar Business Capital

Prosper Marketplace shut down its Prosper Daily (formerly BillGuard) app

7/31 – First Associates Loan Servicing announced the opening of their new 1000-seat capacity operations center in Baja California, Mexico

8/1 – Ron Suber joined Credible.com as executive vice-chairman and a member of the board of directors

PeerStreet integrated with Personal Capital

8/2 – Lending Loop Raised $2M, launched automated investment platform

PeerIQ Secured $12M in Series A round

OnDeck partnered with Payment Source in Canada

Bread raised $126M in equity and debt

8/3 – Kabbage secured $250M in Series F round from SoftBank Group, was valued at more than $1.25B

8/9 – Former Capital One VP Heather Tuason became Chief Product Officer of StreetShares

PayPal acquired Swift Capital

8/10 – Coinbase raised $100M at $1.6B valuation

8/11 – Former SoFi employee Brandon Charles filed a lawsuit against the company alleging among other things that he witnessed sexual harassment in the workplace

8/14 – Prosper closed $500M securitization, announced $775M in Q2 loan originations, $41.4M net loss

Bitcoin surged past $4,000

8/15 – iPayment announced the formation of its new merchant cash advance division, iPayment Capital

8/16 – Fifth Third Bank made another equity investment in ApplePie Capital, agreed to purchase loans through the company's marketplace

8/19 – Former CFO of Credibly became President of Western Funding

8/22 – Former SoFi employees filed a lawsuit against the company over wage issues

8/23 – Ellevest raised $32.5M

8/24 – AutoFi raised $10M in Series A

8/25 – Rep. Maxine Waters called for a Congressional hearing on SoFi's bank charter application and ILC charters in general

8/29 – Snap Finance secured $100M credit facility

8/30 – IOU Financial announced Q2 originations of $26.2M (US) and a net loss of $2.08M (CAD)

ShopKeep launched ShopKeep Capital, a merchant cash advance service

8/31 – Bizfi wound down operations, sold servicing rights to its $250M portfolio to Credibly

9/2 – Bitcoin price surpassed $5,000

9/5 – Former Chief Sales Officer of OnDeck, Paul Rosen, joined CoverWallet as COO

9/6 – Square revealed that they would apply for an ILC charter, following in the footsteps of SoFi

9/7 – Former Director of External Sales at OnDeck, Jared Kogan, joined Pearl Capital as Chief Revenue Officer

First Internet Bank Announces Strategic Partnership with Lendeavor, Inc.

9/11 – SoFi CEO Mike Cagney announced he had resigned as board chairman and would be resigning as CEO later in the year

Lenda raised $5.25M Series A

9/12 – Groundfloor announced $100M loan purchase agreement with Direct Access Capital

Orchard unveiled its Deals platform

JPMorgan CEO Jamie Dimon called Bitcoin a fraud for stupid people

9/13 – dv01 closed $5.5M Series A

9/14 – SmartBiz Loans surpassed $500M in lifetime SBA loan originations

9/15 – Amid more negative press, SoFi CEO Mike Cagney announced he was resigning as CEO immediately

Enova announced $25M share repurchase program

9/20 – World Business Lenders acquired strategic assets of Bizfi including the company's brand and marketplace

9/22 – Prosper Marketplace raised $50M in a Series G round at a 70% lower valuation of $550M

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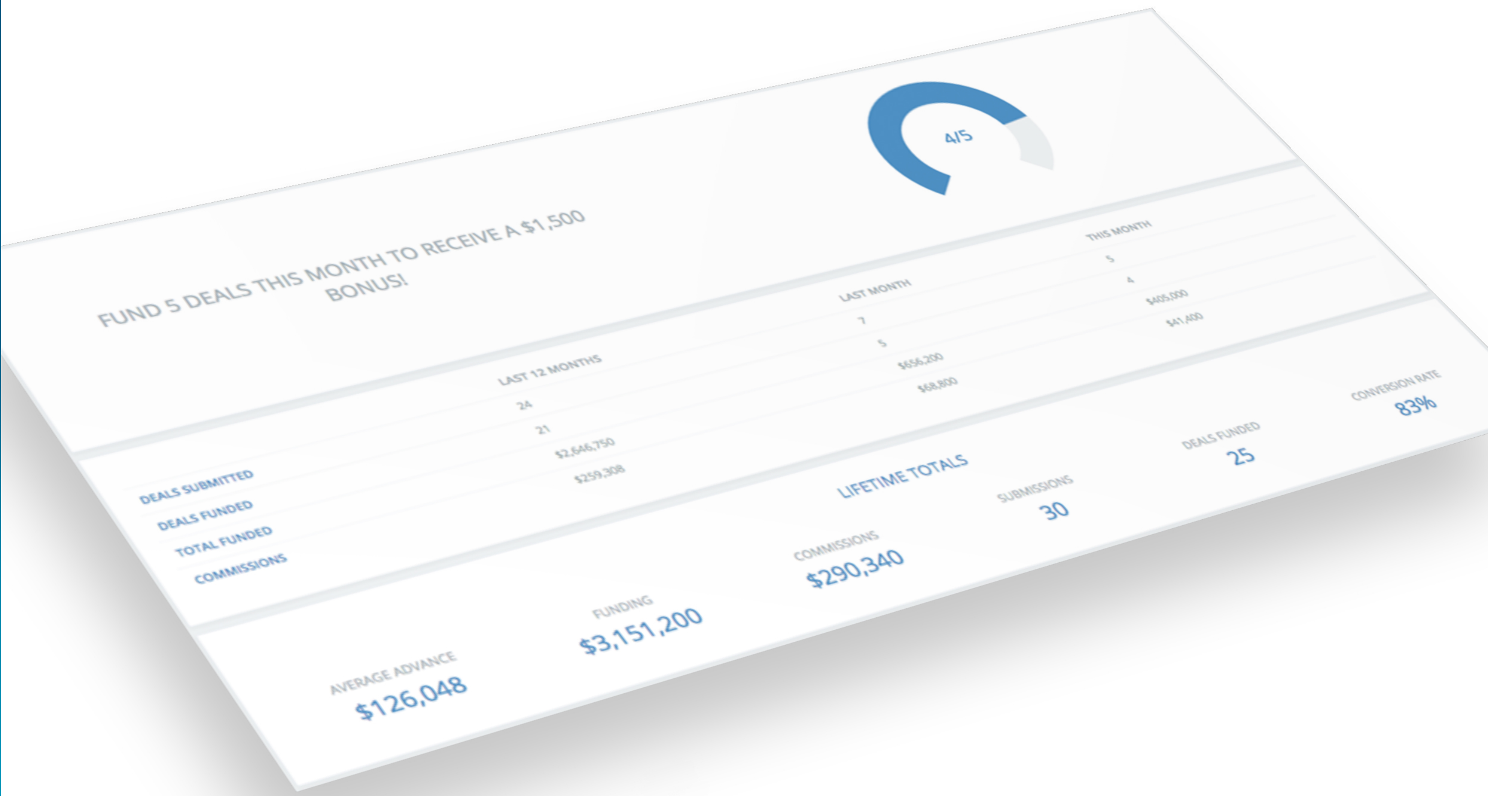

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5-YEAR WINDOW INTO **THE ALTERNATIVE SMALL BUSINESS FINANCE INDUSTRY**

ANNUAL REVENUE					
COMPANY	2016	2015	2014	2013	2012
Square[1]	$1,708,721,000	$1,267,118,000	$850,192,000	$552,433,000	$203,449,000
OnDeck[2]	$291,300,000	$254,700,000	$158,100,000	$65,200,000	$25,600,000
Kabbage[3]	$171,784,000	$97,461,712	$40,193,000		
Swift Capital[4]	$88,600,000	$51,400,000	$27,540,900	$11,703,500	
National Funding	$75,693,096	$59,075,878	$39,048,959	$26,707,000	$18,643,813
Reliant Funding[5]	$51,946,472	$11,294,044	$9,723,924	$5,968,009	$2,096,324
Fora Financial[6]	$41,590,720	$33,974,000	$26,932,581	$18,418,300	
Forward Financing	$28,305,078				
Gibraltar Business Capital	$15,984,688				
Tax Guard	$9,886,365	$8,197,755	$5,142,739	$4,354,787	
United Capital Source	$8,465,260		$3,917,193		
Blue Bridge Financial	$6,569,714	$5,470,564			
Lighter Capital	$6,364,417	$4,364,907			
Fast Capital 360	$6,264,924				
US Business Funding	$5,794,936				
Cashbloom	$5,404,123	$4,804,112	$3,941,819	$3,823,893	$2,555,140
Fund&Grow	$4,082,130				
Nav	$2,663,344				
Priority Funding Solutions	$2,599,931				
StreetShares	$647,119	$239,593			
CAN Capital[7]		$213,402,616	$269,852,762	$215,503,978	$151,606,959
Bizfi[8]		$79,886,000	$51,475,000	$38,715,312	
Quick Bridge Funding		$48,856,909	$44,603,626		
Funding Circle Holdings[9]		$39,411,279	$20,100,000	$8,100,000	
Capify[10]		$37,860,596	$41,119,291		
Credibly[11]		$26,265,198	$14,603,213	$7,013,359	
Envision Capital Group		$21,034,113	$19,432,205	$12,071,976	$11,173,853
Capital Advance Solutions		$4,856,377			
Channel Partners Capital		$2,207,927	$4,013,608	$3,673,990	$2,208,488
Bankers Healthcare Group			$93,825,129	$61,332,289	
Strada Capital				$8,765,600	
Direct Capital				$432,780,164	$329,350,716
Snap Advances					$21,946,000
American Finance Solutions[12]				$5,871,832	$6,359,078
The Business Backer[13]			$19,593,171	$11,205,755	$9,615,062

[1]Square (SQ) went public in 2015
[2]OnDeck (ONDK) went public in 2014
[3]Kabbage received a $1.25B+ private market valuation in August 2017
[4]Swift Capital was acquired by PayPal (PYPL) in August 2017
[5]Reliant Funding was acquired by a PE firm in 2015
[6]Fora Financial was acquired by a PE firm in 2015
[7]CAN Capital ceased funding operations in December 2016 but resumed in July 2017
[8]Bizfi wound down in 2017. Credibly secured the servicing rights of their portfolio
[9]Funding Circle's primary market is the UK
[10]Capify's US operations were wound down in early 2017 and their operations were integrated with Strategic Funding Source. Capify's international companies are still operating
[11]Credibly received a significant equity investment from a PE firm in 2015
[12]American Finance Solutions was acquired by Rapid Capital Funding in 2014, who was then immediately acquired by North American Bancard
[13]The Business Backer was acquired by Enova (ENVA) in 2015

5-YEAR **WINDOW INTO ONLINE CONSUMER LENDERS** (ABBREVIATED LIST)

ONLINE CONSUMER LENDER REVENUE					
COMPANY	2016	2015	2014	2013	2012
loanDepot	$1,296,453,643	$922,359,827	$538,087,552		
Elevate Credit (ELVT)	$580,441,000	$434,006,000	$274,000,000	$72,000,000	
Lending Club (LC)	$500,800,000	$430,000,000	$213,400,000	$98,002,000	$33,800,000
Avant	$437,929,000	$300,000,000*	$75,000,000		
SoFi	$350,000,000*	$114,700,000			
Prosper Marketplace	$136,005,000	$204,275,000	$81,317,000	$18,381,000	$6,807,527

* Indicates an estimate

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