* GETTING FUNDED: A Q&A with Brendan Ross

DAILY FUNDER

SEPTEMBER / OCTOBER 2014 | ISSUE 5

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FUSION

By Sean Murray

MURRAY

If the theme of July/August was Change on All Fronts, then this period is best defined by Fusion. Today's business lending environment is an exotic soup; Methodologies are being mixed, matched and reconfigured. But fusion is prevalent in many more ways than the obvious.

Alternative lending is not a man's domain. In this issue you'll meet six very influential women. We delve into their backgrounds in an attempt to get their perspectives on success in this business. Here we explore fusion, not just through ideas and backgrounds, but in the very gender dynamic of the industry itself.

There is indeed another level of fusion, that which exists between lender and merchant. As alternative lenders grow, they may discover their own need for financing. But where to start and what to do? It's a paradoxical circumstance. Brendan Ross, president of Direct Lending Investments, recognizes the challenge business lenders face when they play the role of merchant and offers them concrete guidance in our Q&A.

And finally, the two sides of the stacking debate could best be described as nuclear fusion. Nothing heats up the members of our trademark forum more than a good stacking thread. In Issue 3, we shared a legal threat that's being used to scare stackers and in Issue 4, we revealed that more than half of the participants in our poll were in favor of stacking.

Undoubtedly we felt it necessary to carry on this conversation in a controlled manner (a story!). In "Better Practices," we dive head first into ethics in an attempt to discover right from wrong.
Can the industry *fuse* the gaps?

Sincerely,
Sean Murray

BETTER

Alternative business lenders believe that developing

BY AUTUMN CAFIERO GIUSTI

Industry leaders say ethics and best practices have taken center stage in the alternative business lending industry now that hedge funds and Wall Street investors aim to take this booming funding source mainstream.

In just a few short years, alternative lending has evolved from an emerging small-business funding mechanism to a multi-billion dollar industry. With this form of lending thrust into the spotlight, thought leaders in the space say establishing these best practices will be a necessary self-policing step to keep customers happy and regulators at bay.

GREIST says that putting the client first will ultimately benefit everybody

"If we all adhere to good practices and really put the client first, it's not just going to benefit the company. In the long run, it's going to benefit the whole industry as well," said Scott Greist, CEO of American Finance Solutions based in Anaheim, California.

Lower fees, longer-term loans and greater transparency rank among the areas industry leaders cite as goals for alternative lending. The practice of stacking has also come under heavy scrutiny. Industry leaders say that having merchants overextend themselves and ultimately go out of business only hurts the funding companies in the long run.

Some warn that while the spotlight might be good for industry growth, it could also capture the attention of regulators who want to oversee it. Industry critic Ami Kassar says that if alternative lenders don't step up and start regulating themselves, someone else might start doing it for them.

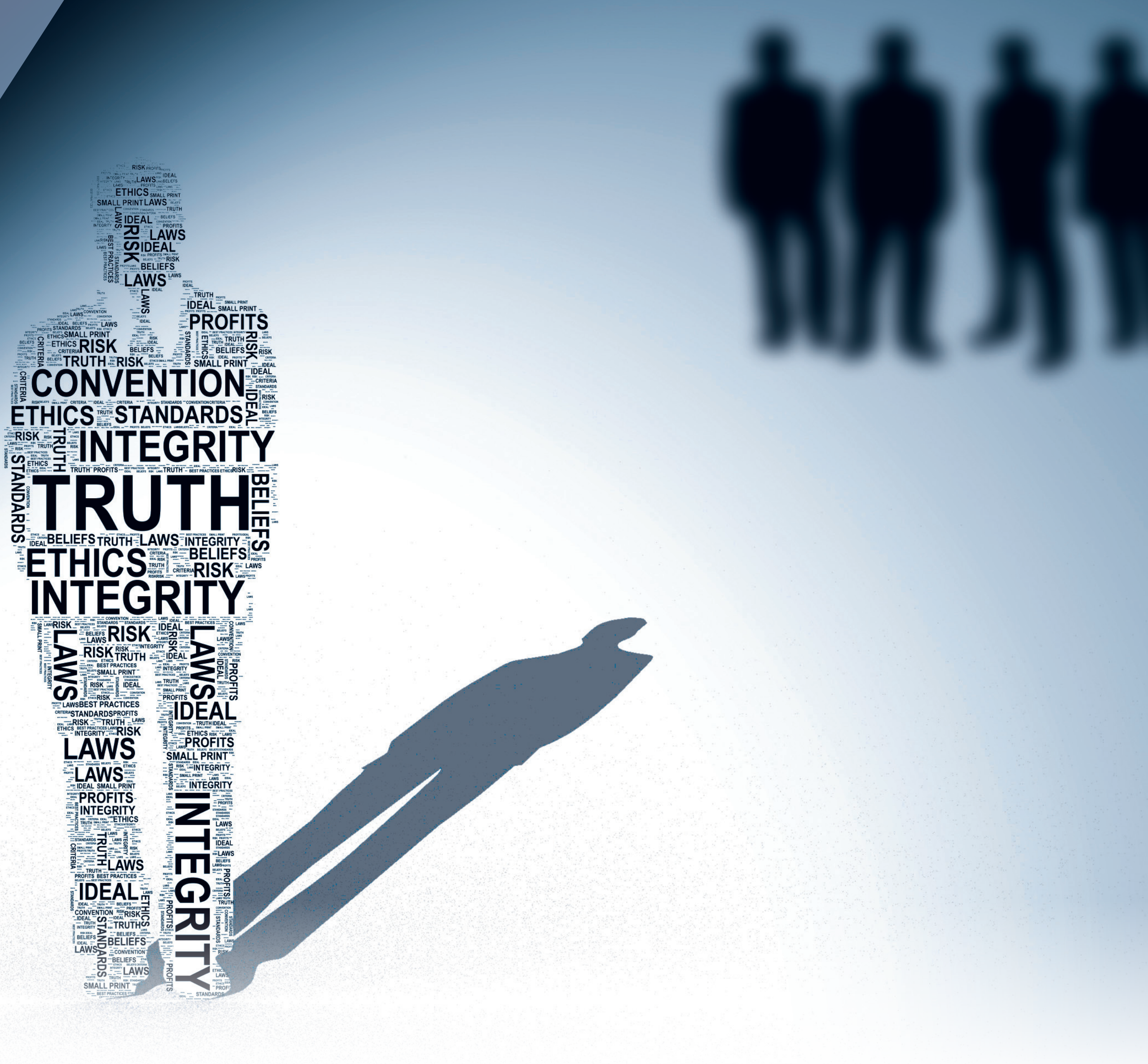
"I think that if the industry doesn't start to adopt many of these standards on their own, at some point in the future there will be regulation. And that will be much more difficult for the industry if it doesn't adopt standards now," said Kassar, founder and CEO of Philadelphia-based MultiFunding.com, which helps identify loan options for small businesses.

The challenge funders face is balancing ethics with profitability. Although industry members contend that implementing best practices will actually boost customer retention and profits.

"If you can take care of a client, they're going to become a good partner with you and also a very profitable client with you in the long term," Greist said.

PRACTICES

good ethics is the key to a prosperous future



Stacking under scrutiny

As far as ethics go, the practice of stacking stands out as one of the most controversial subjects in alternative lending. Many industry members look down on the practice of providing a merchant with a secondary cash advance on top of an existing advance from another funder that the merchant is still paying off.

Andy Reiser, CEO of Strategic Funding Source in New York, says he is starting to see some of the larger companies carry out questionable practices in regard to stacking.

"In the early days, we used to only see bad behavior from the newer, less professional companies. Now we're starting to see it from some of the larger companies," he said.

Although Reiser is not a proponent of stacking, he says that he's come to terms with the fact that stackers are going to carry out the practice no matter what. He says lending companies might as well figure out ways to give out those loans themselves, rather than become consumed with trying to weed out stacking. Strategic Funding Source tells its clients that if they need more money, they're better off sticking with them than going out and obtaining capital from another company, which is going to give it to them at an extraordinarily high rate and for a short term, Reiser said.

"We let the wolf into the hen house. Now the onus is on us to educate our clients," he said.

David Goldin, CEO of New York-based AmeriMerchant, believes stacking is unfair not only to the merchant, but also to the primary funder whose money is being put at risk.

He uses the example of a merchant who asks for $100,000, but the funding company advances the merchant only $75,000.

"It's not because they can't give more money; it's because they think the merchant can't handle it," Goldin said.

REISER believes that stackers are going to carry out the practice no matter what

If a second funder comes in to give that merchant an additional $25,000, that funder not only endangers the merchant's cash flow, but also puts the primary funding company's $75,000 in jeopardy.

Some funders contend there are some exceptions that make stacking acceptable. Heather Francis, vice president of Merchant Cash Group in Gainesville, Florida, says her company does not practice stacking.

"Most of the customers who come to us have a risky credit profile and cash flow issues to begin with. We don't want to put them out of business," she said.

However, Francis says she doesn't have a problem with second placements since merchants might run into a cash flow shortage before they've finished paying off their current advance, and might need a second advance to fund an emergency, such as a broken refrigerator or some other piece of equipment.

"As an industry, we have created longer-term programs, which obviously drove the need for stacking. But when it goes to a third, fourth and fifth (advance), that is creating an issue," she said.

Marco Lucioni, vice president of the small business program for Opportunity Fund in San Jose, California, believes the practice of stacking in and of itself isn't necessarily a bad thing. Ultimately, the issue comes down to leverage.

Stacking multiple loans is acceptable as long as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the combined payments of those loans don't exceed a certain percentage of a business' revenues. If that threshold is 10 percent, for instance, a single advance taking 12 percent of a business' revenues would actually be much more damaging than two advances that, when combined, take 8 percent of revenues.

"Really, our concern is making sure the loans are helping small business sustainability, and not the other way around," Lucioni said.

Critics scrutinize industry

Alternative lending has amassed its share of critics who question the industry's ethics, and Lucioni is among those who says he would like to see some changes take place. He has been trying to promote transparency in the industry and says his own company, a nonprofit, does this by reporting its APRs to its clients.

LUCIONI wants more transparency in the industry

"Our message in transparency of cost is everyone should disclose their pricing through an APR," Lucioni said. "It really allows the small business owner to choose wisely."

He points out that giving a one-month loan of $10,000 that costs $13,000 to pay back could end up being more expensive than a one-year $10,000 loan that costs $14,000 to pay back. Even though the one-year loan costs $1,000 more than the one-month loan, it's easier for the merchant to pay back that extra amount over the course of 12 months than in just one.

Ami Kassar has also questioned some of the industry's practices. Kassar, who blogs for the Wall Street Journal, argues that the industry should work toward helping business owners become bankable, as opposed to putting them out of business.

"The ultimate goal of the industry should be to help the business owners get to the point where they're bankable. No business should live in alternative lending forever," Kassar said.

Kassar believes that there will and always should be an alternative lending industry to help business owners that are unable to receive help from banks. But that industry should be transparent and clear and act as a crutch that businesses can lean on until they can secure a bank loan.

"If the industry recognizes and embraces that and works toward building products that help business owners get there, the companies that take that position will eventually be the leaders," Kassar said.

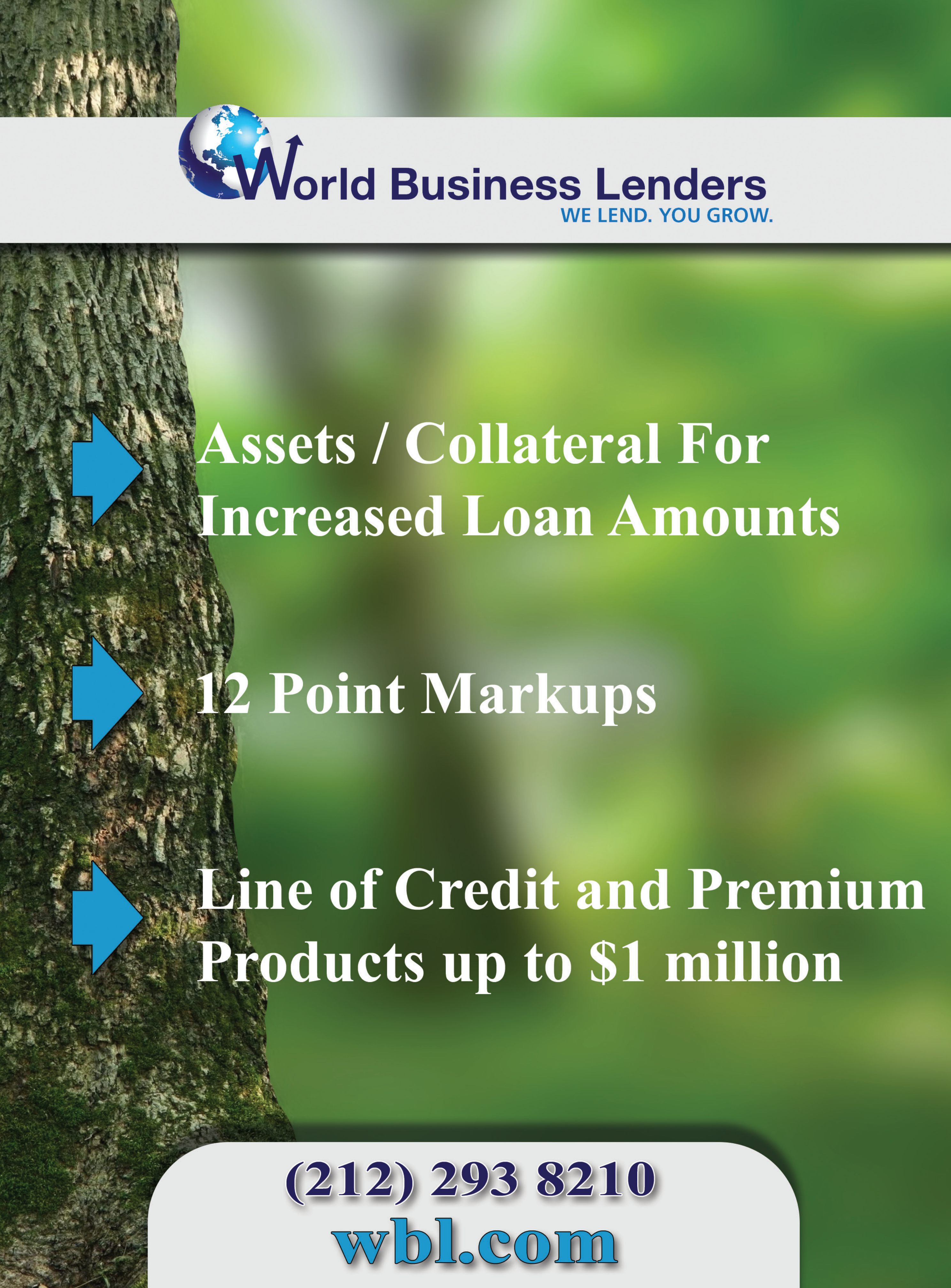
Critics from the mainstream finance realm take a more severe view of the ethics of merchant cash advance. Management consultant Mitchell D. Weiss, whose 30 years of banking experience is steeped in lending, opposes the overall practices of the industry and calls this type of lending "the financial equivalent of crack."

WEISS believes this type of lending is the financial equivalent of crack

He believes that merchant cash advances raise the likelihood that merchants will continue to borrow that money again and again, rather than get to the bottom of what's causing their business to fall short and solve that problem.

"It will eat up their profitability, and they'll have nothing left for themselves," Weiss said.

The more serious concern,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Weiss says, is that gaining access to cash at an accelerated rate sets merchants up for failure. "When you're accelerating the rate of cash, what do you do for an encore?" he asks. Weiss says merchants need to assess the rationale behind why they're borrowing money in the first place, and determine whether they're engaging in a financial activity that masks a fundamental problem.

Weiss says that merchant cash advance is an alternative that borrowers should consider only when things happen that are outside of the control of their business, such as when something has caught them by surprise.

"It is not a good product to rely on month after month," he said.

GOLDIN would like to see the sales force get more skin in the game

Leading by example

Alternative lending companies have been responding to industry scrutiny by maintaining in-house best practices and setting an example as an industry "good citizen."

Long-standing industry player CAN Capital Inc. of New York operates on the belief that tying its success to its clients' success will drive ethics.

"In terms of our corporate values, we exist to help our small businesses succeed," said Parris Sanz, chief compliance officer for CAN Capital.

Sanz says that his company works to uphold the original intent of the merchant cash advance, which is to help small businesses thrive by providing working capital. CAN credits itself as an industry pioneer and lays claim to inventing the merchant cash advance product in 1998. The company was founded by a small business owner, who saw her business face its own cash-flow issues.

Sanz says because of CAN Capital's roots, the company puts its small business customers at the forefront.

"We view our inspiration for the company as reflective of our role in the industry," he said.

The design of CAN Capital's merchant cash advance product drives its ethical behavior because the company succeeds only if its merchant clients succeed, and CAN Capital has no recourse against merchant clients that simply go out of business.

Sanz says the merchant cash advance that CAN Capital provides is a purchase of future receivables, not a loan, so it doesn't have a fixed term or minimum payment amount. Because CAN Capital is entitled only to a set percentage of a small business' card transactions, the amount remitted to CAN Capital ebbs and flows with the merchant's card sales.

That means that if a merchant's card sales volume declines, the amount of receivables delivered to CAN Capital goes down too. In that same month of low sales, there are few if any other financial relationships the merchant has that will be as fluid, Sanz said.

"They probably won't get a break on their rent," he said.

And provided the merchant doesn't breach certain covenants of its contract, such as by switching its card processor, CAN Capital takes the hit.

"We take the risk that their business may decline or fail," he said.

Other industry leaders have chosen to tackle fees in their quest for ethical responsibility.

Francis of Merchant Cash Group says the practice of charging high fees is something her company doesn't partake in. Some companies charge north of $1,000 in fees on a $20,000 advance.

Industry organizations such as the North American Merchant Advance Association, (see sidebar) are setting the stage for alternative lenders to achieve certain standards, but some leaders say regulation might be a foregone conclusion.

Merchant Cash Group charges between $80 and $250 for all advances, with $250 being the cap.

"They're already paying money on the advance. So we don't want to charge them exorbitant fees just to get their funding," Francis said.

Kassar of MultiFunding.com says he would like to see cash advance companies give brokers commission-based incentives to minimize or eliminate prepayment penalties for borrowers.

"Brokers today demand what, in my opinion, is a ridiculous price to get loans passed on to the small business owner. That makes it very difficult for the lender to not take the risk of a prepayment option," he said.

Kassar suggests that short-term lending companies could start offering brokers a percentage of what the loan earns on a monthly basis. The commission would be paid over the life of the loan, instead of up front.

"As the lender earns money, the broker earns money," he said.

Adopting a commission model could help short-term lenders avoid having to charge small business owners the kinds of huge up-front fees that could potentially put them out of business, he said.

Standards and the future

As the industry looks ahead to what's next in its growth cycle, leaders say that funding companies ultimately will need to get their houses in order, whether that's through self policing or outside regulation. Now that big-name investors are injecting billions of dollars in investments into alternative lending, the industry is in a position in which future success might hinge on how companies conduct business.

As CEO of one of the oldest players in the space, David Goldin has witnessed a lot of trends since founding AmeriMerchant in 2002. He says that as the industry matures, it's becoming more institutionalized, with private equity firms and other investors coming in. That means that cash advance companies that have been doing business with less-than-ethical brokers and ISOs are going to have to raise the bar, he says.

"If a company's making a $100 million investment into a merchant cash advance funder, they're probably going to require them to standardize and increase their policies and vetting procedures of who they're doing business with," Goldin said.

Goldin says AmeriMerchant's policy dictates that it won't work with firms with questionable business practices. For that reason, Goldin says he would like to see the sales force get more skin in the game because they're not respecting the capital of a funding company. Often, agents will push through a subpar contract just to get more deals approved.

"We like the model of allowing ISOs and agents to put money into a deal so that we know all of our interests are aligned," Goldin said.

Industry organizations such as the North American Merchant Advance Association, (see sidebar) are setting the stage for alternative lenders to achieve certain standards, but some leaders say regulation might be a foregone conclusion.

Reiser of Strategic Funding Source believes it's important for the industry to be ahead of the curve in terms of standards and says his company has been working to adapt to what the standards of the future might be.

"Ultimately there will be regulation in this industry. It's just a matter of time. And I think that's going to force standards on everyone," he said.

ETHICS SIDEBAR

NAMAA takes lead on best practices

For the past eight years, the North American Merchant Advance Association has existed with the purpose of streamlining the industry on a number of fronts, one of which has been the development of ethical standards and best practices guidelines. Industry leaders have credited the association with raising the profile of the merchant cash advance.

David Goldin, CEO of New York-based AmeriMerchant, is one of the founders and current president of the association. He says the group is reaching out and looking at different ways to promote merchant cash advance and to make the product more mainstream.

Goldin touts the association as an example of how competitors have come together to set standards. NAMAA started out as a group of funding companies that set out to defend what, back then, was an emerging industry. At the time, several industry members were facing patent litigation, and none of those members could afford to fight the litigation on their own.

"We all came together to fight it," Goldin said.

That effort evolved into what NAMAA is today. The association works to establish best practices and also build risk tools specific to the industry to prevent merchants from defrauding funding companies. NAMAA is updating its white paper on best practices, and also maintains a blind database of merchants who have defaulted.

Goldin believes that through these efforts, NAMAA has helped merchant cash advance earn legitimacy in the eyes of the mainstream media. He points out that five years ago, articles about alternative lending painted the practice in a negative light.

"NAMAA has done a great job educating the press, which has led to investors (coming in)," Goldin said. "The industry has really grown up."

CEO Scott Greist, whose company American Finance Solutions is a NAMAA member, applauds the association for helping fight fraud through its suspicious activity database, which allows members to check clients' information in a blind tagging system. Companies can enter in information that doesn't identify the client by name, such as a street address, and find out whether that merchant has an outstanding balance.

"Those things really help members lower bad debt and foster communication, and it helps in stopping the stacking between NAMAA members," he says.

CEO Andy Reiser of Strategic Funding Source, another NAMAA member, believes the association is headed in the right direction toward helping the industry achieve certain standards. But he points out that both the association and the industry are still young, and some of the biggest players in cash advance remain absent from the organization.

"I think the goal of NAMAA is important. And I don't think you'll be able to solve all the needs of a young and growing industry in the first few years of an organization," Reiser said. "That being said, it's a good start."

SIX WOMEN
OF ALTERNATIVE FINANCE

BY DALE LASZIG

If alternative lending had a wide enough lens for a selfie, what a richly layered portrait would appear. Every demographic group would be represented in the growing leadership ranks.

Imagine zooming in on that sea of faces to a select group of senior executives. Following are candid close-ups of six first ladies of finance.

HEATHER FRANCIS, Merchant Cash Group

Merchant Cash Group, established in 2008 and based in Gainesville, Florida provides credit accessibility to small to midsized business owners through the purchase and sale of future receivables. The company is focused on improving clients' risky credit profiles and building relationships with borrowers and affiliates.

Executive Vice President Heather Francis earned a degree in Health Promotion and Education from the University of Florida, a background that has served her well in alternative lending. Both health care and financial services rely on the skill of customer-facing professionals to foster customer longevity, she said.

"Success in any sales organization, health care or financial services, begins and ends with the customer," Francis said. "We don't have a sales force. We're strictly here to fund. One of our favorite sayings is that most people don't have to work with us. We want them to want to work with us."

Merchant Cash Group trains and mentors its agents. Stephen Covey's Seven Habits of Highly Effective People is embedded in the corporate charter.

"Most people will tell you that I'm approachable," Francis said. "Being responsive is part of our culture. We care about each other and we want to win. Playing softball from the time I was 8 to 20 years old taught me the value of teamwork. I'm also fortunate to have worked with a boss in financial services who has mentored me and helped me grow under his leadership."

CANDACE KLEIN, Dealstruck

Dealstruck, established in 2012, is a crowdlending company based in San Diego that offers a mix

of peer-to-peer and traditional financing offerings to the market of borrowers between those that are bankable to those that are forced into sub-prime. The company's mission is to help business owners improve creditworthiness over time and ultimately become eligible for less expensive, more conventional forms of financing.

Candace Klein, chief strategy officer, is a practicing attorney who received a B.A. from Northern Kentucky University, and J.D. from the Salmon P. Chase College of Law.

Prior to joining Dealstruck, Klein co-authored the JOBS Act which legalized crowd funding for securities in the United States, and was founder and CEO of Bad Girl Ventures and SoMoLend. Klein, an advocate for female entrepreneurship, serves as General Counsel for Women Investing in Women, a global NGO focused on increasing access to capital for women business owners and access to capital markets for women investors.

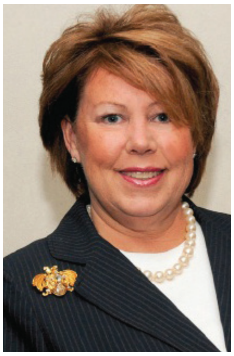
Klein considers her securities law background an ideal entrée to alternative lending, particularly due to both industries' reliance on data analytics.

"I'm a big believer in metrics," said Klein, "and I'm constantly thinking about how we can increase conversion rates. My goal is to find the right financial resource for every person who is seeking funding and to be increasingly able to measure that goal."

Klein manages conversion metrics at Dealstruck, where customer experience is a top priority.

"We're an online platform so our borrowers and investors often touch technology before they ever meet a human," Klein said. "We want people to get to us easily and seamlessly. We spend a ton of time educating our borrowers on cost differences between cash advance and loans. We strive to find the best possible products to fit customer risk profiles, and that drives us to continually innovate and expand product offerings."

Describing her management style as empowering, Klein admitted that some staffers may call it "over-delegating." She encourages employees to think of themselves as CEOs.



LISA MCGREEVY, Online Lenders Alliance

Online Lenders Alliance is a trade association based in Washington, D.C., dedicated to advancing best practices in online lending. Established in 2005 by a small group of Internet lenders seeking better standards and governance, the alliance works closely with local and federal government to shape policies that are favorable to its member companies.

President and CEO Lisa McGreevy is well-connected in Washington. As a high-profile lobbyist and one of the "Most Powerful Women in Washington," her experience working in the White House, Treasury Department, and Capitol Hill, has been an asset to the Online Lenders Alliance.

For almost a decade she has led the association's growth, advocating on behalf of its members, and actively participating in every initiative in the group's expanding ecosystem.

"We are innovators in online financial services," McGreevy said. "That means we're at the cutting edge of delivering credit. Unfortunately, state and federal laws have not kept pace with demands for credit and the technology available for them to obtain it. Consequently, regulators and lawmakers are trying to play catch-up and all too often consider laws and regulations that hinder, instead of promote, innovation in the financial services marketplace."

McGreevy added that changes in the online lending ecosystem have prompted the Online Lenders Alliance to broaden its focus from traditional short-term, small-dollar consumer loans to include all online financial services.

"OLA is innovative, entrepreneurial, and relentlessly focused on serving our members," McGreevy said. "The nimbleness of our members has given us the platform to adapt to changes in the marketplace, regulatory environment, and needs of our membership and their customers."

MARIA ESPINEL, Credit Cash LLC

Credit Cash LLC, a New York-based cash advance company, was founded in 2006 by Entrepreneur Growth Capital, an asset-based lender managed by three generations of financiers since 1937. Credit Cash, an innovator in the use of a lock box by a cash advance company, provides customized funding products to upscale clients with good to excellent credit.

Chief Operations Officer Maria Espinel's career in asset-based lending began at Abrams & Company, followed by senior management positions at United Credit Corporation, Finova Capital, and EGC, parent company of Credit Cash. Espinel graduated from Baruch College and is co-chair and past president of the Commercial Finance League.

> *Non-bank finance is frequently misunderstood. There are no local branches and mistrust can be prevalent among borrowers.*

Espinel was a pre-med student when she was initially approached by a finance company and offered a different career path.

"This was a great match," Espinel said, "since mathematics is my strong suit. I was also fortunate to have a strong mentor at this company. At the time, I didn't recognize that this mentorship would lead to a 30-year career in asset-based lending and merchant cash advance.

At Credit Cash, I've enjoyed working with three generations of owners. Back in 2004, when the asset-based loan market was getting competitive due to banks' relaxed lending standards; we started looking at alternative lending platforms. The MCA industry was relatively new and targeting small business. So we began offering advances to larger businesses, an area that we knew how to underwrite. Our goal from the onset was to attract larger clients with better credit."

Espinel described her management style as "permissive autocrat," mindful of individual employees and the company's best interests.

CARRIE DOLAN, Lending Club

Lending Club, established in 2006 and headquartered in San Francisco, is an online credit marketplace that matches creditworthy borrowers with investors looking for yield. Lending Club opened with one simple mission: create a more efficient, transparent and customer-friendly alternative to the traditional banking system.

Chief Financial Officer Carrie Dolan has seen loan volume double every year since the first loan was facilitated in 2007. More than $5 billion in personal loans have been originated through the Lending Club platform, $1 billion during the second quarter of 2014 alone, enabling more than 362,000 consumers to achieve their financial goals.

"In March 2014, Lending Club launched a small business loan platform," Dolan said, "with loans available up to $100,000, and in April we announced the acquisition of Springstone Financial, which offers financing to prime consumers looking for educational or patient financing. In May we announced our first alliance with a top-20 bank, Union Bank."

Dolan earned her B.S. and MBA in finance from the University of California, Berkeley, and worked at two publicly held companies before joining Lending Club. At Chevron she helped launch Chevron Credit Bank where she served on its board of directors and as chief financial officer. She served as treasurer at Charles Schwab and chief financial officer at Schwab Bank, a bank she helped launch in 2003.

"With a fast growing culture, my role is to help solve problems quickly," Dolan said, "bridge communications, and quickly adjust resources. I need to stay flexible and collaborative, but also know when to step in to provide more guidance.

"In early 2013, Lending Club announced that it wanted to be prepared to go public by the end of 2014, as markets permitted. As CFO, I'd manage the initiatives that would help us be ready for life as a public company: hiring, scaling, automation, procedure development, documentation and other activities intended to de-risk our business. My goal is to ensure we have the financial depth and breadth to support the company as we grow."

CHAOMEI CHEN, Lending Club

Lending Club's chief risk officer, Chaomei Chen, graduated from The Southwestern Jiao Tong University of China before moving to the U.S. where she earned an M.S. at Johns Hopkins University.

She has overseen business and credit risk within portfolios totaling more than $20 billion for companies including Providian Financial, the Washington Mutual Bank portfolio at JP Morgan Chase Card Services, and FleetBoston.

In her current role as chief risk officer at Lending Club, Chen is focused on establishing a risk management framework and infrastructure to support growth.

Risk management from Chen's point of view is never a single measurement – it's about mapping business objectives and aligning risk strategy appropriately.

"As chief risk officer I'd like to see this business continue to grow and provide great products and service to consumers, and continue to do so in a very responsible way that manages risk effectively," Chen said.

Because she used to teach at the college level, she said she thinks of herself more as a coach than as a boss.

"My management style reflects that," Chen said. "I give direction to the people on my team and trust them to implement collaboratively – and of course keep the lines of communication open to make sure we stay on track."

COLLECTIVE WISDOM

Some words of advice from industry leaders

Opportunities and threats

As a relatively young industry, non-bank finance faces increasing demand for its products and huge competition within its value chain. Additionally, its products and services are frequently misunderstood by borrowers. Despite their varying backgrounds and specializations, the executives expressed similar views about the industry's opportunities and threats.

Managing growth was considered the top challenge, followed by the need to improve public perception. There was broad consensus on the need for educational outreach and brand recognition to boost alternative lending's credibility.

The growth challenge

Managing growth is critical for any business and especially true for non-bank lenders striving to stay apace with an influx of new customers and seemingly limitless scalability.

"We just had our first billion dollar quarter (in the second quarter of 2014)," said Chen, "and topped $5 billion in loans originated through the platform. Making that milestone possible means we onboard five to 10 new employees every week. Growth is a challenge in itself but the bigger challenge is managing our risk levels and maintaining a solid return to our investors at the same time."

Klein said that, just as in any marketplace, at Dealstruck, they struggle with balancing supply with demand.

"As a start-up company in rapid growth mode, we're constantly looking at ways to streamline the borrower application process which may necessitate raising additional capital to build out the best lending base," Klein said.

Francis agreed, saying that "extreme growth" taxes the system.

"At Merchant Cash Group the volume of incoming requests, leads, and deals can sometimes make us feel more reactive than proactive," Francis said. "Getting back to being proactive sometimes requires bringing on new staff and developing faster software."

An underwriter's typical workday might include applications from a construction company, restaurant, janitorial service, and nail salon.

"A mental reset is required each time a new file is opened," said Francis.

McGreevy said that the challenges in non-bank finance are similar to those faced by financial services as a whole.

"The marketplace is changing swiftly. The demand for innovative financial products over the Internet is increasing and government is way behind," McGreevy said. "Consequently, non-bank professionals need to negotiate between the companies innovating quickly to meet a rapidly changing marketplace and working to bring regulators and lawmakers along."

The people-don't-get-us challenge

Non-bank finance is frequently misunderstood. There are no local branches and mistrust can be prevalent among borrowers.

"Online marketplaces like Lending Club don't have a branch at every street corner to build trust through physical presence," said Chen. "We need to build trust through different means."

Chen said that building trust was the greatest challenge for Lending Club.

"We've achieved that goal by adopting a disciplined approach to credit and risk management, and offering great transparency into data and performance," Chen said. "Our size is also now allowing us to attract large, demanding investors whose participation in our marketplace builds trust for other market participants. Newer or smaller marketplaces will continue to face the same challenge."

Francis said that when it comes to trust, it is important to think about brand recognition.

"When you say bank, people think Wells Fargo, Bank of America. When you say alternative lending, there's no immediate point of reference," Francis said.

The Online Lenders Alliance works hard to address misconceptions and drive legitimacy throughout the non-bank lending ecosystem. Its efforts include education, communication, collaboration and advocacy with government and institutional leaders.

McGreevy called consumer protection a global phenomenon, noting that many U.S. laws and regulations are emulated in other countries, particularly in the United Kingdom, where consumer groups are very active.

"U.S. citizens are fortunate to live in a participatory democracy," McGreevy said, "where they can express their views and petition the government for redress, as we recently did with Operation Choke Point."

Operation Choke Point, a multiagency initiative by the Department of Justice, was designed to "choke off" access to the payments system by industries considered high risk for fraud.

A recent report by the House Government Oversight Committee concluded that the effort unfairly targets the online lending industry by intimidating banks into not processing transactions between lenders and their customers.

Espinel noted a slow but steady improvement in public perception of non-bank finance.

"When we were laying the groundwork [for cash advance] in 2004/2005 there was skepticism in the financial community," Espinel said. "Back then, underwriting was not as sophisticated and there were higher default rates. Credit Cash was able to bring some old school credit work to our underwriting model."

Espinel said that she is encouraged by the increasing level of professionalism in the industry, and that is continuing to attract more capital.

"Five years ago, few banks would entertain lending to this industry. Now some major banks are competing to get deals," Espinel said.

Advice for a newbie

Non-bank finance is attracting new talent, many of whom seek advice from established professionals. McGreevy encouraged incoming professionals to develop their writing skills and learn the art of storytelling. Francis and Klein recommended researching prospective employers.

"Research, research, research," said Francis. "Don't go it alone. Call or email me if you're considering a career move for current information on the company."

Francis emphasized the importance of joining a reputable firm that supplements earnings during the inevitable learning curve when "you don't want to be depleting your own pocket."

"Just don't stack," Francis said. "Not only because I don't believe in the practice, but because you could be accelerating the decline of a business. And never stop learning. Funding without understanding the market and the fundamentals of underwriting is pointless. This is a collaborative business, where we help each other."

Espinel said she rarely sees stacking in her end of the market, but she believes that the practice is not in a client's best interest.

"My advice to any career seeker is to work in a field for which you have a passion," said Espinel. "Remember to always maintain the highest level of integrity. If you stay true to those virtues and are able to communicate to all stakeholders, you will succeed."

Take a hard look at the management team, recommended Klein. Make sure that you're comfortable with your prospective employer's experience, maturity, and industry knowledge. Recognize that the greatest risk always lies in default. A strong risk management team well-versed in workouts and collections will protect and defend an agent's hard-won portfolio.

Klein added that agents should take the time to explore ancillary revenue streams.

"There's saturation at the top with non-bank lenders compared to the banking industry," Klein said. "There's so much opportunity in the midmarket and down markets to find ways to work with borrowers throughout the borrower lifecycle."

Smile and say, Cheese!

Klein predicted better days ahead with democratized access to capital, increased transparency in lending, and funding professionals who are committed to growth.

Espinel sees a silver lining in the ongoing economic recovery.

"As difficult as the great recession was, the opportunities it helped create are vast," Espinel said. "If you're a self-starter seeking something a little different, then this can be a very rewarding path. There's more flexibility here than in traditional finance, and you can be more creative."

THERE IS NO MAGIC BULLET

Collecting from fraudulent merchants may take longer than you think

BY PAUL A. RIANDA, ESQ.

Clients call me fairly regularly saying a cash advance has gone into default just weeks after the advance was made to the merchant.

The client wants to take immediate action to collect from the merchant given the fraud the merchant has perpetrated on the cash advance company.

As will be explained below, regrettably it is not that easy to move forward against the merchant even if a merchant commits fraud.

The Set Up:

The call I get from the cash advance company usually starts with the same fact pattern: the cash advance was made, and only days or weeks after the advance, the merchant is no longer paying.

The merchants typically switch to a new point of sale terminal and processing company if the cash advance is being repaid in a split funding type of arrangement.

Or, the merchant blocks the cash advance company's access to the merchant's bank account if the funds are being collected by automated clearing house.

In either case, the merchant has repaid little if any of the advance. That the merchant had no intention to repay when it induced the cash advance company to provide the advance is fraud. The merchant misrepresented that it was going to repay the advance and also intentionally kept the cash advance company from collecting— a clear-cut case of fraud.

So it should be easy to seize the merchant's assets, cash and the like right?

Not so fast.

UCC Filings:

Some clients inform me that they have filed a UCC-1 statement and ask if that can be used to seize the defaulting merchant's assets.

Many cash advance companies file UCC-1 statements as part of providing a cash advance. The UCC-1 form is filed in the state where the merchant is located to let other people know that the cash advance company has a lien on certain assets of the merchant.

In the event that the merchant defaults on the cash advance by committing fraud, the cash advance

company theoretically can now go in and seize those assets under the authority granted under the UCC-1 filing.

Sounds like a great way to collect from the merchant. But, the problem is that in reality it does very little to help the cash advance company.

The Uniform Commercial Code allows for the self-help remedy of seizing the property that is subject to the UCC-1 lien in the event the merchant defaults. But the law also states that the cash advance company cannot commit a "breach of the peace" in doing so.

For the most part, any act of violence, such as breaking a lock to get into a business, is seen as a breach of the peace.

Some cases have held that even verbal confrontations constitute a breach of the peace. So from a practical perspective, it is almost impossible to use a self-help remedy against a defiant merchant.

From a practical perspective, it is almost impossible to use a self-help remedy against a defiant merchant.

That is also true in the event the UCC-1 is only securing an interest in future credit card receivables as many do. Seizing those receivables would involve potentially going to the merchant's bank and asking it to divert the funds.

No bank is going to do so unless you have some sort of court order.

Another recent approach cash advance companies have been using to try to obtain assets is to send a letter to the merchant's new processor demanding that the processor divert the funds to pay off the defaulting cash advance company's debt.

Although creative, there is really no right for the cash advance company to receive any funds from the merchant's new processor. If the new processor acquiesced, this would actually be a breach of the terms of the merchant agreement between the merchant and the new processor.

How About Court Intervention?

So how about the courts? Can't they help out in a clear-cut case of fraud by allowing you to go in and seize assets right away?

I am afraid to say it is not that simple.

There is no easy way to speed up the legal system.

You have to file your lawsuit and let the case wind its way through the courts. In California for instance, it takes about 12-18 months to get to trial in most jurisdictions. Defendants can usually delay the outcome longer than that if they really want to.

In some states given court backlogs, it can take many more years before you get anywhere close to trial, resulting in defendants holding onto and potentially hiding their assets for a considerable amount of time.

There are some states that have ways to expedite the process but the term "quick" is relative.

For instance, in California there is something called a "prejudgment writ of attachment." You file a motion to get one and if you do, then you are able to go and seize the assets of the defendant just like if you have a judgment from a trial. So you can go in and seize bank accounts, take assets and even have a "keeper" go into the merchant's business and collect all merchant's customers' payments for your benefit.

The issue is that can take some time.

You still have to file a lawsuit, and then bring your motion. You have to show that you have a "probability of prevailing" in the lawsuit, which can be very fact-intensive, which of course makes bringing the motion expensive.

And then often the court will allow the defendant additional time for discovery to try to show why it will be able to win. In the end if you were able to win the motion in six to nine months you would be doing pretty well.

Some states also allow for what is known as a "confession of judgment." The merchant you are making the cash advance to signs a document that states if the merchant defaults on the cash advance, you can take the confession of judgment down to the courthouse and file it to get a judgment.

Again, sounds easy in theory but maybe not so much in practice.

The number of states that allow this practice is fairly limited. And, the courts tend to look at these filings fairly closely.

The court clerks generally review the confessions of judgments and they are very good at their jobs. They are very adept at finding the smallest failure to comply with the applicable procedural and substantive rules to reject a filing.

And the courts for the most part are underfunded. So if you are lucky enough to get through on the first try it will still take months.

And the fact is the judgment may be of little help right away. If the merchant resides in a state that is not the same one where you obtained the judgment, you are going to have to take the judgment to the state where the merchant resides to get what is called a "sister state" judgment. This again takes more time and money.

And there is also the possibility that the judgment will be rejected, as many states do not allow for confessions of judgments to be confirmed in their state.

So as you can see, even with a slam-dunk case against a merchant that has committed fraud, your options are limited and it is highly unlikely that you can immediately collect anything from the merchant.

The underlying conclusion then is that there is no magic bullet that is going to allow you to collect from a merchant quickly if there is a default, even a fraudulent one. So, you better do your due diligence on the front end to minimize the number of defaults.

Even with a slam-dunk case against a merchant that has committed fraud, your options are limited and it is highly unlikely that you can immediately collect anything from the merchant.

Paul A. Rianda, Esq. is an attorney who has specialized in providing legal advice to the cash advance and bankcard industries for over 15 years. For more information about this article or any other matters, please contact Mr. Rianda at (949) 261-7700 or via email at paul@riandalaw.com.

* The information contained herein is for informational purposes only and should not be relied upon in reaching a conclusion in a particular area. The legal principles discussed herein were accurate at the time this article was authored but are subject to change. Please consult an attorney before making a decision using only the information provided in this article.

Don't release your inner JERK onto the fantasy gridiron

BY THE ETIQUETTE INSIDER

Calling all armchair quarterbacks, the time is quickly approaching. The time for you to bask in your glory of football knowledge, forgo all your responsibilities and spend your weekends analyzing the ESPN Fantasy Football draft kit.

Who needs to mow the lawn, buy groceries, or take your grandma to her bingo game when you can be picking out your draft options and trash talking?

DailyFunder and Merchant Cash Group host a great fantasy football league that allows members of the Alternative Finance Industry to compete against each other outside of the funding numbers, all while contributing to charity. It is a great opportunity to network, build relationships, and enjoy some friendly competition.

In this month's etiquette insider I am going to lay out some great etiquette tips for draft day and some tips for the whole season. OK, well not really etiquette tips, since there really is no place for niceties in football. This issue is more of a "how not to come off as a jerk" handbook for this football season

DRAFT DAY ETIQUETTE

Auto drafters: Now most people can sympathize with busy schedules and that it's not easy to accommodate everyone's schedules so that all can attend draft day, especially with leagues at 12+. If you are one of those people who can not attend in person then please be respectful of others times and have a set draft ready so that when it is your turn in the draft pick the computer is not randomly picking for you and using the full 2:30 of draft time.

2:30 max: For those of you out there who think that using the max time of 2:30 to make a selection makes you look like you are being wise and precise with your pick… you are wrong. You are just being a time suck. Just like with the auto drafters, you should have your selection made ahead of time so that when it is your turn you can make your pick and we can move the draft along swiftly. I also advise that you have multiple options to choose from within your ranking of who you want so that if your guy is taken you can quickly move to your second choice. No one wants to be stuck in the draft processes until 10 at night.

Fan Boy Teams: We understand you think the New England Patriots are the best thing since quarter length sweatshirts came out. This does not mean you need to make your whole fantasy football team from their roster. The point of Fantasy Football is to build a roster of the best players throughout the NFL … if there could be an ultimate fantasy team, who would it be? FANTASY not FANBOY.

Pouting: there's no pouting in fantasy football: So you are upset that you are not in the league that you wanted, maybe the draft time wasn't convenient for you, or that someone took your running back in the first pick of the draft. Do not sign into the draft, pick six quarterbacks, and then leave to auto draft the rest of the time. That is just poor taste and then everyone is going to be put out the rest of the season. It is just best that if you are not happy with the team you are on then just back out or pull your big girl panties on and finish out the rest of the draft and season with some dignity. Who knows, that running back may be on IR after the first game and then you will be happy you didn't have to find a replacement.

SEASON ETIQUETTE

Switch it up: It really stinks having to go up against an opponent who has half his team sitting out on a bye week or IR. If you are going to participate in Fantasy Football then you need to participate. It takes very little time to update your roster and with phone apps you can do it anywhere.

Trash Talk/Smack Talk: So everyone loves a little quick wit and banter back and forth, it is one of the main draws of Fantasy Football. This part can also make you look like the boob you are so it is important to know when to and when not to Trash Talk.

DO Trash Talk during the draft: You have unlimited potential at the start of the season and you can play it off that you know what you are doing

DO when you are undefeated even at 1-0

DO when you are up by 20 points on a Sunday evening and your opponent only has the kicker left to play on Monday night

DO NOT Trash Talk when you are clearly down by 40 points or more

DO NOT if you are a fan boy

DO NOT if you auto drafted

Think you can handle it and want to participate in this year's League, contact Sean Murray at : sean@dailyfunder.com or Heather Francis at: heather@merchantcashgroup.com and we'll get you signed up.

INSTITUTIONAL INFUSIONS

Learning some fundamental truths may help your MCA business move from the Wild West to Wall Street


ROSS

BY MICHAEL GIUSTI

Three things are standing in the way of your merchant cash advance business and a potential infusion of cash from an institutional investor: volume, trust and defaults.

That was the message from Brendan Ross, president of Los Angeles-based investment firm Direct Lending Investments when he sat down with the DailyFunder to discuss how nontraditional business lenders might graduate into the big leagues and engage institutional investors like him in potentially funding deals.

Ross said that one of the hardest things he faces when dealing with merchant cash advance companies is bridging the divide between how MCA players expect to get paid and how an institutional investor approaches compensation for a deal. One of the keys, he said, is to know that in an ideal world, you get paid when cash begins flowing in on a deal, not when the contract is first written.

He also said that like any lending relationship, there is an inherent trust factor that stands in the way of getting a deal in motion.

"The key to raising outside money is to find some way of getting me to trust your underwriting. Either you put a lot of your own money in, or we find somebody else who's underwriting I also trust and who is putting money in," he said.

But if all the details can be worked out, Ross said the potential up side of becoming a funding platform is huge, and it starts with engaging that first institutional investor.

DailyFunder: Which companies are in the best position to bring in an institutional investor to fund a merchant cash advance deal?

Ross: The first thing I look at is the organization that you have built. I'm not able to interact with a company until they emerge with some reasonable level of volume. A market leader, not a startup.

I also want to understand your story for how you are originating your deals.

If you are originating in a really boring way, like if you have spent the last 10 years rolling up credit card ISOs, then I like that a lot. If you are just another me-too player trying to originate from brokers, that is less interesting.

Different people have different concepts for how they are going to originate business. The best are the ones that have what I call "unique deal flow."

You tell me "I have a relationship with a huge ISO, and I'll be the only one in there, and my deal is unique and these guys can confirm that I am the only one in there," then I like that because it means you're getting good flow and it's not picked over, where I might be the dumb money taking the deals no one else will fund.

DailyFunder: Is that to say that only highly professionalized players should be looking at doing lending deals with you?

Ross: If they haven't created a highly professionalized operation, then that can still be fine, I just wouldn't trust them to service their own loans. We'd have to work with someone like Strategic to come in as the servicer.

If a servicer will not get in the deal, I am going to have far more concerns.

But, in an ideal world, they have a track record stretching back years and years. Maybe they even have audited financial data, but at the very least, they need some kind of track record.

DailyFunder: How important is it that they bring

audited financial records to the table?

Ross: I realize that having audited numbers is rare in the merchant cash advance world. Is it a nice thing to have? Yes, but I can't imagine I would get that almost ever. So, really, the first thing I want to look at is data on every single loan they have ever done. If they aren't keeping those numbers, and if they can't run a meaningful report, then it's probably not going to happen.

DailyFunder: Which businesses and which deals are most attractive to you?

Ross: I'm not really doing the underwriting on individual deals — I am looking for you to do the underwriting. That's why it is important for you to put money up.

If you have money in the deal, you won't want to lose it. And you are going to be better at underwriting these deals than I will, as will another syndicate partner that might be a servicer that we both trust.

If you bless it and somebody else blesses it, then I can come in for half or more of it, and I will know that it has been blessed by two people who would stand to lose money if the deal fell apart.

DailyFunder: It sounds like seeing your partners put skin in the game is important to you.

Ross: If you are sort of more mom and poppy, in order for me to work with you, what you need to do is relatively simple: we would need to find a third party servicer so you wouldn't be touching the money. And you would have to have enough capital in the deals that I would be confident that you would be hurt if a deal we did together lost money.

In a perfect world, you are taking 25 percent of the deal, Strategic, or somebody like them is taking 25 percent and I am taking 50.

Of course, this assumes you can afford 25 percent of the deal. If you can't, then what is the acceptable number? Maybe it is 10 percent. I don't know. But you have to be in the deal enough that I know you are going to personally suffer if a deal goes bad.

The more that you put in the deal, the less concerned I am.

DailyFunder: How might a typical deal between you and a merchant cash advance company be structured?

Ross: The first thing to make clear is that the investment is never in the merchant cash advance company — it is always in the loan, and that distinction is important.

Because, you may not be around long term, but I need those loans to finish being collected.

I need to be the owner of the loan. I need it sold to me in a way that is completely clean. The thing that I can't do is to give someone money to start a merchant cash advance company. What I can do is pay them as I go, based on some reasonable up-front markup plus profits earned on the loans.

When I write a deal, I am looking for bankruptcy remoteness. Bankruptcy remoteness means I own the loan. You have originated it. You have gotten the advance going, but I am the owner of it. You don't own it.

As for the specifics, well, the deal can be structured in a lot of ways. It really just depends. I just need to figure out and find structural ways to create trust that offset the natural lack of trust that comes from you getting paid up front while I get paid later.

That is everything. Everything is about trust and eliminating the need for it whenever possible.

DailyFunder: You mentioned bringing in an outside third party. Why do you see that as an important part of vetting a deal?

Ross: There are really two validation points. The first validation point is, are you in the deal. The second is, will a bigger servicer that would also like to participate as a syndicate also get in the deal. So, if the servicer will get in the deal, and you are in the deal, then obviously I am pretty comfortable with that deal.

Now if a partner comes to me who hasn't done many loans, then that is when we fall back on what I call these structural trust mechanisms. So, I should trust you because… why?

We get back to the big three, how much money do you have in, can we get a third party to come into the deals, and can we get a third party to manage the cash flow. If we can get these three things, and the better we are on these three things, then the less I need in terms of a track record.

DailyFunder: When is it just essential that you see that third party brought in?

Ross: If you are small, and you tell me, "I may be small, but I have great infrastructure in place and I can service these loans, and it is crazy to give some servicer 3 percent." I would have to say to you that it may sound crazy but that's how we are doing it because that way I don't need to trust you.

If there is one challenge in the merchant cash advance business, it is trust. That's really no particular disparagement to merchant cash advance – any lending business involves a lot of trust.

Lenders have had their trust violated for centuries. It is just actually hard to trust people with promises to repay money. That is a fundamentally hard thing, and it is doubly hard when people are getting an origination fee. Everything is about trying to work around that.

DailyFunder: You seem to keep coming back to the origination fee. Why does that part of the deal seem to give you pause?

Ross: See, the thing is, when a broker transitions to being a lender, they want to keep their origination fee and then also make fees as a lender. They are trying to add to their wallet. And that creates a tension between the person who is going to have to pay the origination fee and the lender.

The lender wants to see some of the money up front. And in a perfect world, I wouldn't have to pay anything upfront. In a perfect world, I would pay you based on a percent of what I earned on the portfolio.

But you don't want that. You as the broker becoming the lender, you still want to earn that origination fee.

And I understand that, but now the question is, how can I trust you? You want to get paid up front, and it is going to be hard to trust you because you could stick me with bad paper.

DailyFunder: Since trust is so important, how much of a role does the individual reputation and credit score of your potential partners weigh in?

Ross: I do run a background check on the members of the leadership team for lenders who I work with. It is a real criminal and credit background check.

I haven't had a situation come up yet where someone has failed a background check. And, obviously, I realize there is a difference between drunk driving and theft or embezzlement.

I also understand that people end up sometimes in the MCA space who have had colorful careers in the securities space. It doesn't make it impossible for me to work with them. But if they had been in the big house for white color crime, then that is probably a non-starter.

DailyFunder: When it comes to potential partners, how much of a role does their deal volume play in your decision to jump into a deal?

Ross: With an institutional investor, volume is very important. An institutional investor like me is not interested in working with a lender who can't keep a lot of money busy.

If you do four-month deals, and you have turnover each month of about 25 percent, and the maximum volume of loans you can do in a month is $1 million, then that means the most money you can keep busy is about $4 million a year.

As a fund manager, I don't make that much fees on $4 million. So, then the question is what are my costs going to be against managing you?

Now, if your volume is $10 million or more, then probably an institutional investor would have an interest in working with you. And if it is $20 million or more, definitely. The thing is, it is not that easy to keep $10 million busy. For most people that means writing between $2.5 million and $3 million in loans each month. That is a lot of loans.

DailyFunder: OK, so let's say an MCA business could keep that amount of money busy, how much could that kind of relationship be worth?

Ross: If you are originating $10 million a year, and you are able to keep 5 percent as an origination fee, you are making $500,000. As the lending platform for the deal, your goal is to make another $250,000 by bringing in institutional money to make the deal work — if you can keep your defaults under control. This whole business is about defaults.

DailyFunder: I'd love to talk about defaults. What is your perspective here?

Ross: First, you need to understand that I view a loan as late or dead much more quickly than most people do. If you run a merchant cash advance lending business and you don't have a payment from a borrower because they closed their bank account, and they aren't returning your phone calls, then the loan is dead then.

It is not dead in 45 or 60 days later. If you don't have access to the bank account, and they aren't returning your phone calls, then it is a dead loan.

DailyFunder: What do you consider to be acceptable when it comes to defaults?

Ross: If I have $1 million in loans, and $10,000 of them go dead in a month, that is 1 percent of the portfolio, and so that is a 12 percent annualized default rate.

If you have that same $1 million in loans, and you are writing three-month loans, and you had $30,000 die last month, then that is a 36 percent annualized default rate, and that is not going to work.

But, if we are talking an 18 percent default rate, could that work? Possibly.

Could 30 percent work? Well, now you are in a range where I am not thrilled. I am not thrilled about having three percent of the portfolio die at the end of each month.

If you can keep your defaults under control, you can make money because my investors don't need as much as your portfolio can generate.

DailyFunder: What is the bottom line?

Ross: The most important thing is the structural trust mechanisms and the volume. You can't get an institutional investor to work with you if you can't keep $10 million busy — you are just too small.

The best thing to do is to build up volume. Take your origination fee, build up volume, and focus, focus, focus on volume – get yourself a shop that has decent volume, and then give me a call and we can figure out how to get you transitioned to being a lender. You have got to have the volume.

But, the point is, if you are shopping for syndicate partners, and if your volume is big enough, you can shop for an institutional partner — someone like me.

If you are going to syndicate stuff out anyway, and your volume is good, then syndicate it to me because my yield requirements may be lower, and you can keep a piece of the profit.

HIDDEN DANGERS

Adding new products adds new legal concerns

BY ROBERT COOK, KATE FISHER AND CHRIS CHAMNESS OF HUDSON COOK, LLP

Traditional merchant cash advance companies are expanding their product portfolios to offer more choices to their customers.

As business models change, companies need to be aware that new legal requirements can arise. One particular federal law applies when a merchant cash advance company moves away from traditional merchant cash advances and begins to offer small business loans.

The federal Equal Credit Opportunity Act is familiar to any lender that offers consumer loans. But, both the ECOA and its implementing regulations (Regulation B) also apply to commercial purpose loans.

The rules are slightly different for commercial versus consumer credit, but penalties for violations are the same. These can include punitive damages of up to $10,000 in an individual action or up to $500,000 in a class action, plus attorneys' fees.

For commercial transactions, the ECOA can be enforced by the Federal Trade Commission as well as merchants that have been harmed by a lender's actions.

The primary purpose of the ECOA is to prohibit a lender from discriminating on a prohibited basis, including: race, color, religion, national origin, sex, marital status or age (provided the applicant has the capacity to enter into a legally binding contract); because part or all of an applicant's income derives from a public assistance program; or because the applicant previously exercised in good faith any right under the Consumer Credit Protection Act, which includes the ECOA.

We assume no funding provider that relies on daily repayments (a "daily funder") intentionally discriminates. (Whether you can get in hot water for unintentional discrimination is the subject for another article.) However, the ECOA also imposes paperwork requirements on lenders.

For a daily funder that is offering a new commercial loan product, it is easy to overlook these requirements.

The ECOA and Regulation B require a lender to tell an applicant when the lender approves or denies an application, or makes a counter offer. Notification requirements for consumer credit are very detailed, and when consumer credit is denied a lender must send a written "adverse action notice."

Fortunately, the less complex rules apply to business purpose credit. Regulation B allows a lender that takes adverse action on a business credit application to provide the notification orally.

Regulation B further provides different procedures of notification based on the revenues of the business applicant. One standard applies to businesses with revenues of $1 million a year or less. Another less formal standard applies to businesses with revenues of more than $1 million.

Applicants with revenues of $1 million or less: A lender must communicate a credit decision within 30 days of receiving a completed application. The lender can provide the notification of the action taken (approval, denial or counteroffer) orally.

However, the oral notification also must contain the information that appears in the second paragraph of the notice below. Business lenders have the option to provide this additional information in written form at the time of application. In this case, the lender must provide the additional information in a form that can be retained by the applicant. A notice such as the following complies with the ECOA:

> *If we take adverse action on your application for credit, you have the right to a statement of specific reasons as to why we took such adverse action within 30 days if you request the statement within 60 days of our notification. You may contact [the name, address, and telephone number of the lender] to obtain the statement of reasons.*
>
> *The federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The Federal Trade Commission, Equal Credit Opportunity, Washington, DC 20580 administers our compliance with the Equal Credit Opportunity Act.*

Of course, if an applicant asks for a statement of why the application was denied, be prepared to provide one that complies with the requirements of the ECOA and Regulation B.

Applicants with revenues of more than $1 million: A lender does not have a set timeframe in which to notify larger applicants of the action taken. The lender just has to inform the applicant of the lender's decision within a "reasonable time."

The lender does not have to provide a written notice with the application, but if the applicant requests, must provide a written statement of the reasons for any adverse action taken and a statement similar to the second paragraph of the notice above. Alternatively, a lender can follow the rules that apply to smaller applicants for all business loan applicants.

There is an argument that Regulation B permits a daily funder to follow these more lenient requirements for any applicant regardless of size, but the safe approach is to follow the rules for applicants with lower revenues.

TAKEAWAYS:

1 – Include a notice such as the one above on your application or on a separate form, and provide a copy to the applicant.

2 – Have procedures to ensure that applicants are promptly notified of your decision.

3 – Be ready to respond in writing if an applicant requests a statement of reasons for a denial.

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THE ART OF THE ADVANCE

Two champion sales leaders share formulas for success

BY DALE LASZIG

There are fortunes to be made in alternative lending. Getting there may require planning, persistence, and people skills in equal measure.

Roadblocks exist at every juncture of the lending process, from the introductory call, to the credit check, all the way through to the close. "Don't celebrate until the deal is funded," is the hue and cry of this business.

While self-help books abound on overcoming sales challenges, few address the nuances of dealing with the slings and arrows of non-bank finance.

So, what is the secret to success? DailyFunder is pleased to introduce two champion sales leaders who have fast-tracked their way to stunning success.

These are their stories.

CHAD OTAR, Excel Capital Management

Excel Capital Management, LLC, established in 2012 and based in New York City's financial center, is a one-stop-shop for business owners in need of capital.

The company originates many types of working capital loans, including merchant cash advance, factoring, and credit card processing. Excel attributes its growth to the skills and industry knowledge of its underwriters and relationship managers.

Managing Partner Chad Otar tried a number of different jobs in the restaurant and healthcare professions after earning a bachelors degree in Psychology in 2011 from CUNY Brooklyn College.

"I was out of college and couldn't find a career that I enjoyed," Otar said. "I tried the restaurant business where I worked as bus boy, waiter, and then manager. I tried medical school."

> "I tried the restaurant business where I worked as bus boy, waiter, and then manager. I tried medical school."

When Otar was a med student, his brother, a stockbroker, began to talk to him about an up-and-coming industry called alternative lending. After reluctantly agreeing to meet his brother's colleague who owned a funding company, Otar began working part-time at his brother's apartment, setting appointments and doing various pre-call activities.

"My brother had to drag me to this meeting [with the lender]," Otar said. "At the time, he was considering going into [alternative lending] and wanted to try it out. We had always worked well together. So I set the appointments, he closed the deals, and we split the commissions. I was simultaneously helping my brother and learning a trade."

Within a first week of working together the brothers closed their first deal, netting Otar $1,000. The rest, as they say, is history.

It didn't take long for Otar to want an expanded role in the funding process and a bigger piece of the pie. After a year of working his own UCC leads from home, Otar was offered a partner position with a cash advance company, an attractive package with salary, commission and benefits.

Working in a senior role at a leading cash advance company gave Otar a broader view of the industry, an improved tolerance for risk, and a solid foundation for his subsequent success as an entrepreneur. With one and a half years of experience as an executive manager under his belt, Otar and a partner broke away and started their own company, working out of Otar's mother's basement. Otar described the early days as a democratic arrangement between friends — days of closing, borrowing, and "calling, calling, calling." A year later, the partners were funding an average of $2 million to $3 million in revenue per month.

Otar described his career as a rags-to-riches story with a real-life happy ending. He will never forget what it felt like to earn his first commission check or to find himself in his early 20s with a six-figure annual income. Most importantly, Otar, a self-described eternal optimist and four-time cancer survivor, is grateful to be alive.

After being diagnosed at 17 with testicular cancer and surviving multiple operations to become cancer free, Otar launched Campaign for Life Interrupted, promoting his cause on the talk show circuit.

In his interview with the Times Ledger newspaper in Queens, New York, Otar said that he wanted to spread hope to other young cancer patients and named the foundation "Life Interrupted" because, "When you have cancer, everything stops."

He also shared his story in the anthology "And We Write: Surviving Cancer; Let the Healing Begin", directing all proceeds from book sales to cancer research.

Reflecting on the extraordinary journey that brought him all the way to Wall Street, Chad credits his mother for her continuous encouragement, and for helping him become "the man I am today" – a man who is passionate about his business and deeply connected to his customers, partners, and friends.

ZACHARY RAMIREZ, Core Business Loans

Core Business Loans, established in January 2014 and based in Newport Beach, California, provides business loans and cash advance services to small and medium-sized businesses nationwide.

Core is focused on building partnerships with clients, brokers, and ISOs by providing low rates and high quality of service. Core believes in managed growth through long-term relationships that generate quality business over time.

Managing Partner Zachary Ramirez can see the John Wayne International Airport from his office window, a daily reminder of the hard work that goes into launching a new company.

Ramirez attributes his fast start in alternative lending to his background in equipment leasing and financing. Equipment lessors and cash-advance providers typically have a similar underwriting and funding process.

In fact, working capital loans and merchant cash advances are natural extensions of equipment financing, Ramirez said.

"I've worked in this industry for just over two years," Ramirez said. "I started out in equipment leasing, and gravitated towards working capital and cash advances after I learned the products and the space. After working in equipment leasing, which has a difficult and rigorous funding process, working capital seemed much easier. In addition, the demand for the product is growing exponentially."

Ramirez's first cash advance employer gave him inbound and outbound telemarketing scripts to recite verbatim to each prospective client. After several weeks he threw the scripts away, replacing them with his own fresh techniques, which proved highly successful. A short time later he was training the company's new recruits, and built their company into one of the largest ISOs on the West Coast in less than a year.

This type of overnight success can be both a blessing and a curse. After his highly successful stint growing his first cash advance company, Ramirez decided the time was right to start a new venture, a move that resulted in a stunning reversal of fortune and had him looking for a Plan B.

After losing the shirt off his back and hardly having two nickels to rub together, he regretfully gave up his dream and accepted a sales manager position at another established ISO.

The strategies that Ramirez used to get back on his feet became his guiding principles. He spent each night in the library during this time, perfecting and honing his already high-level sales abilities.

Brian Tracy's book "The Psychology of Selling", along with Neil Rackham's book "SPIN Selling", gave Ramirez the much-needed edge to hit the ground running again. The "Psychology of Selling" focuses on developing mental outlook, desire, and self-esteem, whereas "Spin Selling" focuses on pushing the deal to the maximum possible advance of the sale. Implementing these fresh new ideas, Ramirez managed to fund 14 units for a total of $71,387 of gross margin in just his second month at his new ISO.

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After a year of similar months, Ramirez saved enough money to cover a few years worth of expenses, allowing him to again pursue his dream of building the most competitive cash advance provider in the space.

He left his ISO to join the directors' board of Core Business Loans, serving as the VP of Sales.

Different strokes, remarkable similarities

While they couldn't be farther apart geographically, Otar and Ramirez have much in common. They're both in their 20s, entrepreneurial, and passionate about their profession. Both have found a way to quadruple earnings in less than three years. Both are high-energy extroverts whose primary motivation is not fortune or fame but a desire to make a difference.

Here in their words are some tips on how to make it in this business.

Maximizing Income

There are many ways to make money in alternative lending. It's not uncommon to receive upfront commissions as soon as a deal is funded. Ancillary revenue streams from a variety of sources such as processing residuals and renewals can enhance and stabilize monthly income. DailyFunder asked the top producers for recommendations on how to make more than six figures in this business.

Otar has a counterintuitive approach to maximizing income by putting the best interests of clients, partners, and employees before his own. In his words, if you do the right thing, the money will follow.

"We don't charge upfront fees and broker fees," Otar said. "We do right by them and they come back. That's why my book has a high retention rate. And we ask for [credit card] processing revenue only if it's necessary to change their processing. It's always a good idea to have that in your back pocket. And always try to save them something. And remember not every deal is a one-size-fits-all. You need to look for other options for your clients."

Ramirez believes that the most important thing about making money in this industry is consistency with prospecting and maximizing every opportunity.

"In every step of the sales process, go for the maximum possible advance of the sale: whatever gets you to the next step. For example, if you're on the first call with a client, what's the best outcome you can get from the call? Wouldn't it be walking through the application process on the phone? Go for it! What do you have to lose? The client saying no gets you the same result as never having asked."

He went on to say that a truly "maxed out" deal is one that capitalizes on every opportunity: funding the deal, switching their processor over, getting a written testimonial, getting a referral, and of course, getting the RENEWAL.

Sources of Leads

There are numerous ways to get revenue in this business, from ISO partners, personal referrals, online lead aggregators, to local community banks. While Otar calls UCCs his "sweet spot," he is also a big believer in referrals.

"Talk to your parents," Otar said. "They know people who own businesses. Think outside the box by focusing on underserved, vertical industries. Grow your referral network by connecting with lenders with different areas of specialization such as asset-based lending, purchase orders, small SBA and receivables."

Ramirez said his favorite leads are the deals that his "wonderful ISOs send me!"

"But really, the best lead is an unsolicited referral. The next best is a solicited referral. I've tried virtually every lead source, SEO, direct mail; email blast, fax blast, UCCs, aged leads, you name it," Ramirez said. "In the end, all leads are managed with the same strategy: push each call to the furthest point to increase conversion rates, measure your metrics at each stage of the sale, and ultimately keep your CPA (cost per acquisition) as low as possible."

Staying in the Game

There can be bad days, even bad months, in this business. DailyFunder asked Otar and Ramirez how they stay motivated and in the game.

"The summer months were always a tricky matter to me," Otar said, "Because everybody is in summer mode, no one is looking for money, they aren't worried, and they're all relaxed. I deal with this by staying calm, and just continuing to do what I always do, which is to stay focused, stay connected, and keep on making calls."

Ramirez described funding as an emotion-driven business and cautioned against becoming emotionally invested in any deal.

"Don't get excited until it is funded," he said. "

A good rule of thumb is to be skeptical of every deal, yet confident in your own work ethic and abilities. Over time, no single deal will make or break you."

Ramirez said that fear of rejection and lack of self-esteem have an inverse relationship to success.

"Boost your self-esteem and you'll increase your conversion rate. It's that simple," Ramirez said.

Ramirez said that typically to stay motivated he reads daily affirmations, which include quotes and messages such as, "I am the best salesman in this industry," and "It is going to be a great day."

"Affirmations get you pumped up and ready to hammer the phones," Ramirez said. "I set DAILY quotas and goals for myself and my team that are measurable, such as 'I will make 125 prospecting calls today.' This way I can measure key performance indicators on a daily basis to ensure we are on track for monthly targets."

Advice for the worst of times

In addition to the customary peaks and valleys of career selling, there can be hard knocks, situations that can prompt even the most experienced and successful agents to consider other, albeit less profitable, ways of making a living.

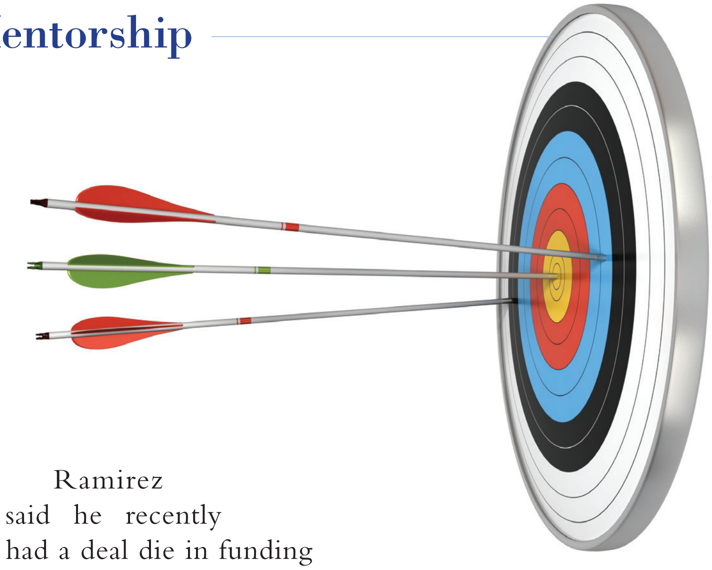
DailyFunder asked Otar and Ramirez to share how they have dealt with sales nightmares.

Otar said his "nightmare," actually had a pretty good ending and began when he had his first monster deal.

"From the time that my client said, 'OK and let's do this right away' to the day that he got funded, I don't think I had two hours sleep," Otar said. "Sometimes when things go too smoothly, you just feel weird inside. This was definitely one of those too-good-to-be true situations, and the four longest days of my life. When it was over, and I got paid, I did what any self-respecting broker would do. I bought a Rolex to remind me of how far I've advanced in my career, and how much I have to keep on pushing."

Ramirez implied that every deal has its own little nightmare.

"Unfortunately, sales nightmares are standard-issue in this business," Ramirez said. "Every day there are deals that randomly die in funding, go with a competitor, get funded from a family member, or any other number of circumstances."



Ramirez said he recently had a deal die in funding that absolutely needed the money to meet their $40,000 payroll.

"The deal died in funding because the merchant could not keep their rent up-to-date. Now they've lost their business, and I can't help but feel partially responsible," Ramirez said.

Best Years Ahead

Both Otar and Ramirez are optimistic about the future and abundant opportunities in non-bank finance.

"Make sure to maximize EVERY single opportunity," Ramirez said. "Switch their processor over. Ask them to write a testimonial for you. Get a referral or two from them. Above all, secure the renewal. If you aren't maximizing every opportunity, you will lose in this business."

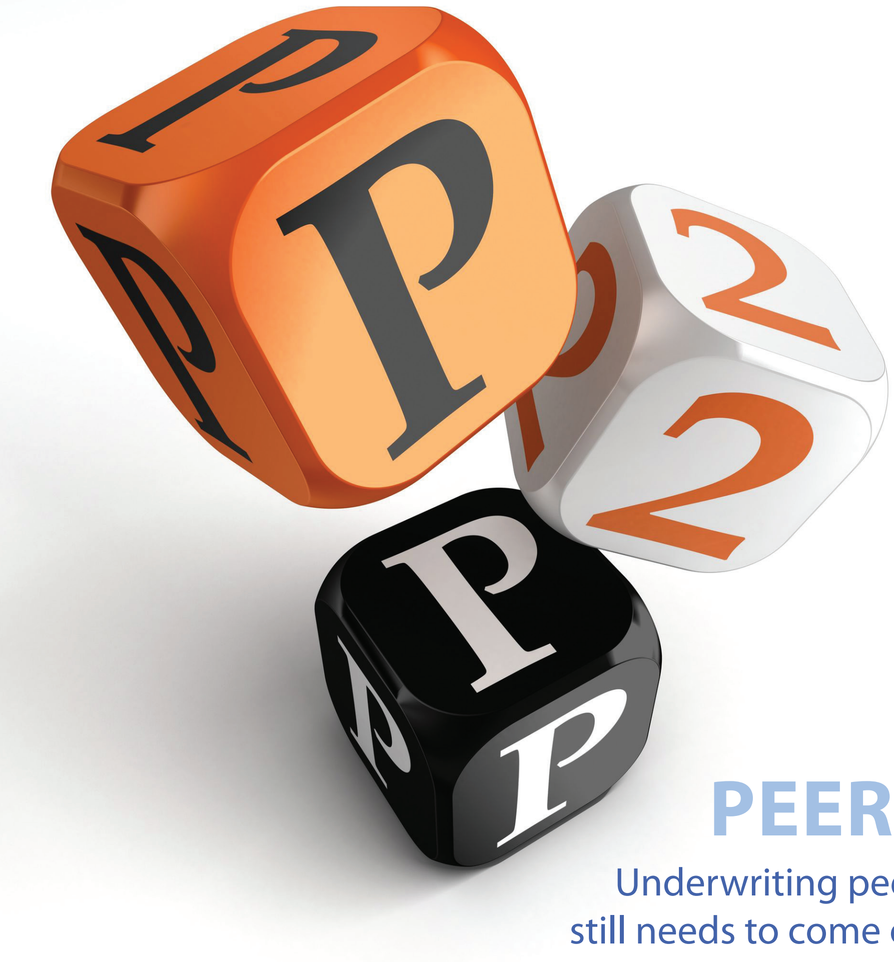
Ramirez said to set long-term goals for yourself.

"Break those goals into yearly steps. Break those yearly steps into monthly steps. Finally break those monthly steps into DAILY ACTIONS," Ramirez said. "Write those daily actions down (100 calls per day, three hours of talk time, two applications per day, etc) and hold yourself to those standards EVERY DAY. Once you create a daily routine and have the integrity to hold yourself to it, you will see measurable results almost immediately."

"Just call nonstop and don't give up!" said Otar. "Keep on making those calls. Keep on fighting!"

He added that it's better to down-sell than to walk away from a deal.

"This is a relationship business," he said. "Remember to leave the door open. You can always make your money the second time around."



PEER REVIEW

Underwriting peer to peer lending still needs to come of age

BY DAVID T. SCHAEFER | CEO | ORION FIRST FINANCIAL

The peer-to-peer lending space has proven itself a disruptive element in the financial world — this much cannot be denied.

As with any emerging market space, there comes along with it radical speculation of untapped potential and naysayers who see economic harbingers of a subprime past. The truth of the matter is that disruptive innovation — with all its technology, transparency and more efficient delivery systems — is quickly changing the commercial lending landscape.

This forward-looking disruption finds its roots in a collective of individuals who realize a for-the-people product can yield better results for individual investors and borrowers across the board.

There is a new level of transparency brought about by improved technology, which results in lower interest rates for prospective borrowers, both consumer and commercial alike. The circumvention of traditional lending institutions has created a whole new market for individual and institutional investors.

The challenge is to take the advantages of this new paradigm yet include the best practices of the traditional lending industry.

Every investor wants to see predictable and stable returns on their

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investment. Some of these emerging lending platforms are developing and testing new algorithms to underwrite the credit risk of small business loans.

It will take time to prove out how these algorithms perform through the different phases of an economic cycle. In the meantime, investors will be charging a greater premium to cover this underwriting risk.

Combining the best time-tested underwriting practices of the traditional model will accelerate the time it will take to reduce this premium. The sooner the best of these models converge the sooner we can realize a peer-to-peer industry that deploys healthy, risk-based capital across a broad range of credit tiers.

There are a few distinct factors that are deserving of special attention as we discuss the future of the small business lending space:

First and foremost is the fundamental element of scoring. Right now, credit underwriting in this new market is being mostly dictated by proprietary algorithms.

Most of us can only venture to guess the ingredients going into the secret sauce being used by companies in the P2P space in order to evaluate risk. The fact remains that we have years and years of historical performance data that can be evaluated to extrapolate certain risk factors in the small business space.

Combining consumer bureau data on the owners of the business, commercial credit bureau data, industry classification codes and other business specific attributes are being utilized today to rank-order risk in the small business lending space.

There is a certain truth to the adage "you can price for anything." However, statistical models and algorithms and seemingly meaningful data provide rather limited insight into real-world performance.

This brings us to the next piece of the puzzle — servicing and collections. No matter how good you are at underwriting there will always be slow paying customers and defaults.

What's needed is a safety net throughout the life of the loan — and this net consists of a scrupulous servicing platform supported by staff experienced in commercial collections best practices. Due diligence and meticulous servicing of accounts are going to be integral to the success of this burgeoning industry.

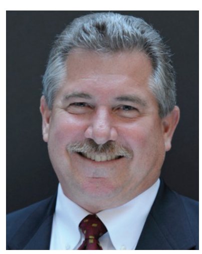
Technology to support the collection cycle, combined with skilled and well-managed staff, will have a significant impact on the overall performance of an asset class — especially as one ventures into higher risk credits.

Collection protocols need to be in place to properly manage this risk, however, care and attention must be focused on the efficient use of human resources to carry out these protocols.

Lenders have the option to build this system internally, or outsource these functions, but either way this will be a vital requirement for long-term success.

This is an exciting time in the small business lending market space. Those of us involved either directly or tangentially understand the inherent risks and rewards that come along with a market in flux.

We seek greater stability at every touch point as the market continues to scale. But more than anything we want to help people and communities grow by deploying capital to small business across America, and this can only be done if we have systems in place that reduce default and mitigate risk.



David Schaefer is the founder and Chief Executive Officer of Orion First Financial, LLC. Orion is a servicer and underwriter focused exclusively on supporting those lending in the small business space.

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