* What the IFA ban means for MCAs

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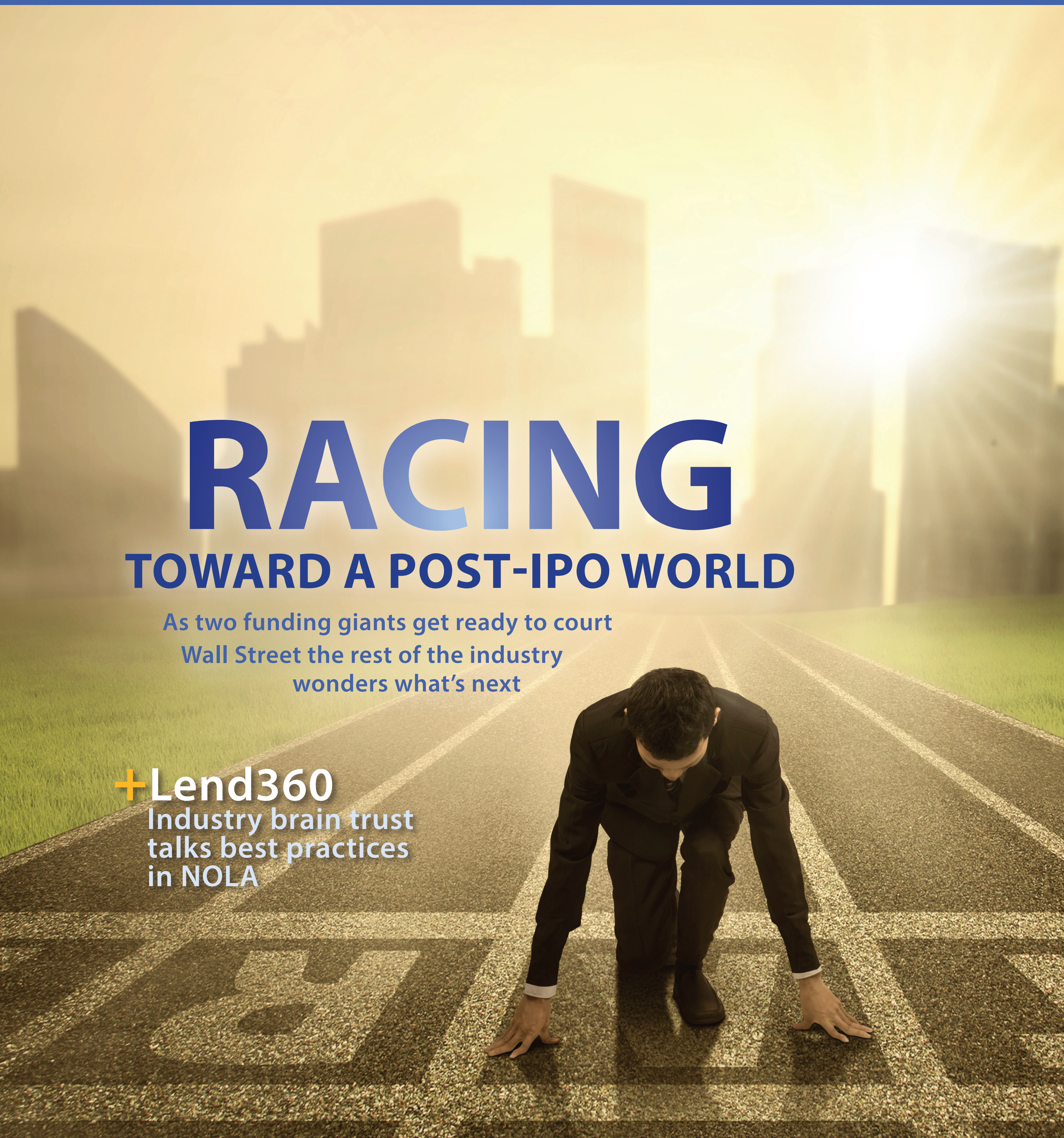

RACING
TOWARD A POST-IPO WORLD

As two funding giants get ready to court Wall Street the rest of the industry wonders what's next

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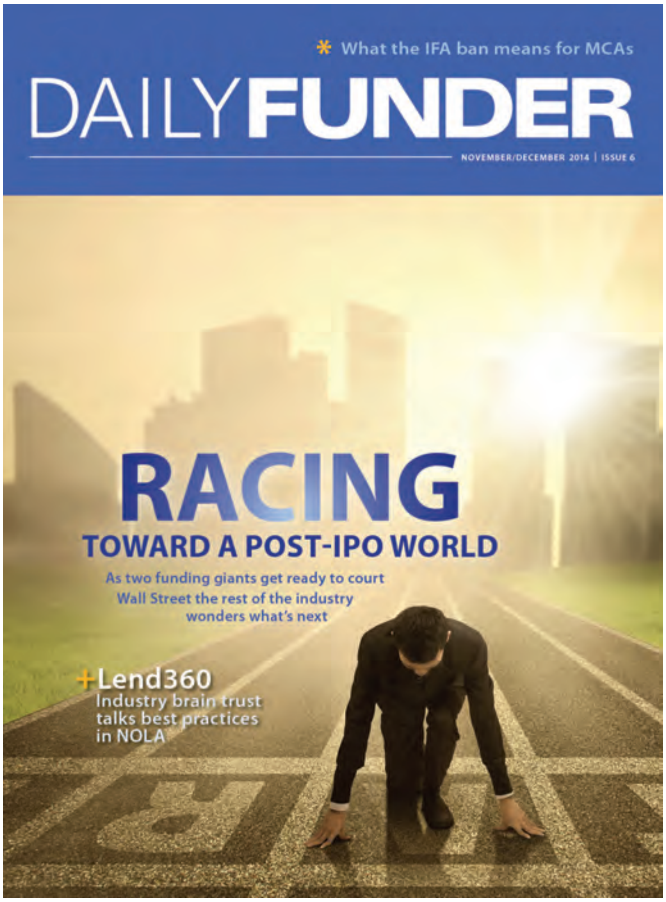

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THE END OF THE BEGINNING


MURRAY

This is the last issue of 2014 but it feels like closure of something more, the last issue of an era perhaps.

The startups of yesterday are all grown up. Soon, we'll be trading them on public exchanges. That means the products and services in alternative business financing are now bigger than just you, myself, and the funding partners we've all built relationships with. In our very first issue I referred to the industry as a footnote. I think we've overcome that label.

As we transition now from footnote to stock quote, there has never been a better time to construct a blueprint for longevity. The debate over best practices is unavoidable. It's everywhere, on the forum, at conferences, in news media, and in discussions behind closed doors. It's my belief the industry can find common ground and that it will continue to serve small businesses for generations to come.

2014 was an incredible year for capital raising, which means acquisitions and consolidations could be just around the corner. Rapid Capital Funding's acquisition of American Finance Solution is probably just the first of many we'll see.

And yet some things will never change. Just about every other day, I bump into kids just a few years out of college who tell me they want to leave their current job to start a business financing ISO. They're just as optimistic, excited and determined as my friends were who did just that many years ago. There's something about that conversation that feels like home.

If you just got into the business this year, congratulations. You're probably the last generation to have gotten in early. But that means you're responsible for what happens next. Know your products, know the laws surrounding them, and always be as fair and transparent as possible with your customers.

And so I'll leave you with that. Together we'll close out a chapter, an era, and DailyFunder's last issue of 2014. I've got my funding pants on. Do you?

Sincerely,
Sean Murray

FUNDERS GET SET TO RACE INTO PUBLIC MARKETS

Two high-profile IPOs promise to bring attention to the industry, but analysts wonder if the momentum can carry on after the initial rush

BY AUTUMN CAFIERO GIUSTI

The names OnDeck and Lending Club might not be nearly as ubiquitous as JP Morgan Chase or Bank of America. But with the two alternative lending companies expected to go public before the end of the year, the general public could become a lot more aware of these two players — and the industry at large — in 2015.

Already, the companies have racked up some impressive publicity. Lending Club and OnDeck ranked at No. 5 and No. 11, respectively, on Forbes' 2014 list of America's Most Promising Companies.

Industry leaders predict that heightened media exposure from the two IPOs will put online nonbank

lending in front of even more business owners. What's more, having two public companies will lend credibility to nonbank lending, with borrowers, investors and consumers starting to take the space more seriously.

"If both companies can have a successful IPO that is in demand, people will look back at this time and say, 'That really was the start of when this industry was put on the map,'" said Peter Renton, founder of Denver-based Lend Academy, an online educational resource for the peer-to-peer lending industry.

In August, San Francisco-based P2P lender LendingClub Corp. filed for an initial public offering with a fundraising target of $500 million. Lending Club primarily collects money from outside investors and lends it to individuals but recently began funding loans to small businesses. If completed, the IPO could raise Lending Club's value to more than $4 billion.

Then, in September, reports surfaced that web-based small business lender OnDeck Capital Inc. had set the wheels in motion to file an IPO that could value the business at roughly $1.5 billion. The Financial Times reported that in August, OnDeck confidentially submitted a Form S-1, the paperwork that companies file to register with the U.S. Securities and Exchange Commission when they are planning to go public.

OnDeck is working with investment banks including

> "In the lending business, when you try to grow too fast, you can make some of these mistakes."
>
> —ROHIT ARORA

Morgan Stanley, Bank of America Merrill Lynch, JP Morgan Chase & Co., and Jefferies to underwrite the deal, according to the Financial Times.

The law states that companies can file an IPO confidentially if they have less than $1 billion in annual revenue. OnDeck generated $65 million in revenues in 2013. Lending Club ended 2013 with about $98 million in revenues.

There are potential downsides from the IPOs, though, with the risks of regulation and consolidation among the possibilities.

"I think it adds legitimacy and awareness to the industry. Obviously with any publicly traded company, it's going to add scrutiny to the industry as well," said David Goldin, CEO of New York-based business lender AmeriMerchant.

Industry leaders say the positives will far outweigh the negatives, though, and are optimistic about the future of nonbank lending.

Global ratings firm Fitch Ratings declared the IPO would be a "key milestone" in the evolution of peer-to-peer lending. In a recent report on P2P lending, Fitch researchers wrote, "A successful IPO could act as a catalyst and benchmark for other P2P institutions to pursue IPOs in order to raise capital and/or for investors to monetize their P2P investments. Publicly traded shares could also serve as a currency for acquisitions for industry consolidation or product/geographic expansion purposes."

GROWTH, WITH CAUTION

Rohit Arora, co-founder and CEO of New York-based online credit broker Biz2Credit Inc., said the two IPOs could create a better overall market in terms of transparency, increased exposure for the industry and greater recognition among small business owners. The caveat, he said, is that lenders will have to pace themselves.

The lending industry could gain integrity in the eyes of investors, and the cost of money could come down for lending companies. "Once you have a publicly traded company, that brings more transparency and scrutiny, creating legitimacy that will create more competition in the industry," Arora said.

The danger is that the industry could end up growing too quickly. The IPOs could trigger a mad rush for other players in the space to go public, start lending like crazy and lower their underwriting standards, Arora said. "In the lending business, when you try to grow too fast, you can make some of these mistakes," he said.

Arora said lenders can learn from companies like Groupon, whose unsustainable growth caused its stock value to plunge in the years after it went public. "Everyone knew that if Groupon didn't do well, the whole industry was going to suffer. That's where these companies need to figure that out."

Arora cautioned that public markets are very unforgiving and want growth every quarter, allowing publicly traded companies a very limited amount of time to recover from setbacks. "If things start blowing up or you have big portfolio losses, it's difficult to come back," he said.

What's more, lending companies might be ill equipped to endure a downturn. Arora noted that the mortgage sector has not fully recovered even after six years. "My worry is that some of these companies trying to go public don't have the kind of maturity or product base to weather that storm," he said.

Goldin contends that several alternative lenders are losing money. Although revenues are way up for both Lending Club and OnDeck — Lending Club tripled its earnings last year, and OnDeck's revenues doubled — their profitability is in question. In the first half of 2013, Lending Club had a net income of $1.74 million. In the first half of this year, the company lost $16.49 million due to a $23.69 million increase in its sales and marketing costs.

Meanwhile, OnDeck posted annual losses of $16.8 million and $24.4 million in 2012 and 2013, respectively, and losses of $14.4 million in the first half of 2014.

At the same time, Lending Club has issued more than $5 billion in loans since its inception, and OnDeck has delivered more than $1.5 billion in capital.

"It's not about how much capital you deploy. It's about how much money you collect back in. At some point, you need to turn a profit," Goldin said.

For now, it appears the industry has room to grow. Gary Chodes, CEO of Raiseworks, a New York-based small business lender, believes the alternative lending industry is still very early on in its growth cycle, and its volume will continue to grow by several hundred percent a year for a number of years. "I don't think there would be indications of anything else but continued growth," he said.

Chodes sees the IPOs as indicative of further progress that the alternative lending industry has made in playing a more meaningful part in fulfilling the capital needs of small to medium businesses and, in the case of Lending Club, consumers.

"It's a natural progression that both the consumer and business lending side grow and increase and diversify their sources of capital," Chodes said.

INDUSTRY ENTERS SPOTLIGHT

Along with sustainable growth, industry members are hoping that the IPOs could help provide the brand awareness that nonbank lending companies have lacked for so long.

"If you're thinking about a small business loan, you don't automatically think about OnDeck," Renton said.

A successful IPO could raise awareness for both the companies and the industry at large. Lending Club's IPO announcement brought unprecedented levels of media attention to alternative lending. "There was never a bigger day of press coverage for this industry than that day when Lending Club announced," Renton said.

Renton believes that compared to OnDeck, Lending Club's filing is a marketing exercise for the company. OnDeck is in a somewhat weaker position because Lending Club has experienced faster growth and has a slightly stronger brand, he said.

"When most companies do an IPO, the main goal is to raise money. You talk to Lending Club, and the main goal is to raise awareness. I don't know if that's the same with OnDeck," he said.

Chodes contends that the IPOs alone won't make borrowers any more aware of either company, or the industry as a whole. Rather, consumers and borrowers will learn about the companies in the same way they hear about all other products and services — through online, TV and radio advertising, as well as media coverage.

"Going public in and of itself is not going to build somebody's brand, with respect to the borrower," he said.

> "There was never a bigger day of press coverage for this industry than that day when Lending Club announced."
>
> —PETER RENTON

REGULATORY CONCERNS

The fear among industry members is that in the process of garnering public attention, the IPOs could grab the attention of regulators, too.

Regulators could very well become more mindful of the space following the IPOs, but Arora contends that they would be doing so at a time when things are going well. Companies are better off dealing with regulatory scrutiny early on than they are growing without any oversight, only to have regulators clamp down on them once they have gotten big, he said. "I think any sector should look at regulations when things are good, not when things are bad," Arora said.

Some industry leaders believe the IPOs will have little to no effect on the regulatory landscape. Chodes


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doubts that an IPO would affect the lender-borrower relationship, or the regulations that govern it.

"I don't think the fact that there's been a public offering has any bearing on those regulations, because it's the same regulatory framework whether it's public or private," he said.

The regulatory landscape appears to have more stability on the consumer lending side than on the business side. Renton said there isn't much impetus to change in Washington when it comes to consumer lending. "I've spoken to regulators who are happy with the status quo and haven't seen much need to change, " he said.

Lending Club might have less to worry about on the regulatory front than OnDeck, Renton said. Small business lending is different from consumer lending, and the challenge OnDeck faces is that some people don't like the interest rates they charge. Even though they offer loans with interest rates that are lower than the typical cash advance, their rates are still much higher than what SBA-type lenders provide.

And whereas Lending Club has received very little bad press, OnDeck and the merchant cash advance industry as a whole have received some unflattering media coverage, with critics calling it payday lending for businesses.

"For venture capital and private equity firms, it's going to be a race to the finish line. This might accelerate their decision to make investments." —DAVID GOLDIN

For the time being, Goldin contends that alternative lending companies are giving no reason for regulators to step in. "Why would they regulate it if the business owners are happy with it?" Goldin asked.

The levels of regulatory scrutiny could all come down to the business practices of the individual companies.

"Business-to-business lending has never been regulated in the history of our country. It's just a question of if the companies are performing responsibly," Goldin said.

If business owners continue to benefit from the existence of alternative lenders, regulation is unlikely – unless those businesses start complaining to politicians, things could change, Goldin said.

"As long as there's a sense of strong self-regulation, it will be some time before regulators step in. However if there are questionable business practices, that could accelerate the regulation," he said.

Goldin said an IPO isn't going to clue in regulators about something they don't already know.

"I was personally invited over the summer to meet with a government agency, and they are fully aware of all of the products in this market," he said.

MORE COMPETITION, INVESTORS

Not only could the IPOs bring about media coverage and exposure, but they could help build integrity for nonbank lending. That translates to increased competition and more investors, ultimately creating cheaper capital in the marketplace.

"For venture capital and private equity firms, it's going to be a race to the finish line. This might accelerate their decision to make investments," Goldin said.

If the IPOs are successful, they could help other companies in the same space raise more money in the marketplace, because they will see investors putting more money into Lending Club and OnDeck. "Hopefully, it should mean that the cost of lending and money will go down because of increased competition," Arora said.

On the flip side, there could also be more consolidation in the industry, because if the companies do well, they will gain in size and strength, Arora said.

Chodes believes the industry will remain large and continue to support the more than two dozen major players that are growing by more than 100 percent each year.

"On the small business side, no alternative lender has more than a few percent market share, OnDeck included," he said.

On the peer-to-peer lending side, an IPO from Lending Club could propel the company's lead so far ahead of others that it might be difficult for a new entrant to start from scratch, unless they come in with a different marketing angle or offer a unique product, he said.

Competitors might be in a weaker position than these two leaders, but Renton said it doesn't have to be a zero-sum game. The industry is growing rapidly, and online lending is still scratching the surface.

"I don't think they're going to be able to dominate their competitors. The industry is just too big for that," Renton said.

Going public likely will cement OnDeck and Lending Club's positions as leaders in the space, Renton said.

"Obviously there will be other IPOs in this industry, but no one can ever claim to be the first other than these two companies," he said.

In raising money for an IPO, the two companies will be at an advantage because they will have a lot of cash on their balance sheets that their competitors won't have. That could lead to some consolidation.

"I think both companies are going to look to make acquisitions to expand their market. They might take on some of their smaller competitors," Renton said.

MORE TO COME?

Given what's at stake in terms of public awareness, regulation and competition for the alternative lending industry, all eyes will be on Lending Club and OnDeck for at least the next 12 months to see how, or if, these IPOs shake out.

If they go well, the industry could gain an advantage in all three of these areas. But if not, the entire sector could be tarnished.

"The performance of the stock for the next year is critical for the industry," Arora said.

Goldin said that although OnDeck and Lending Club might not become household names right away, they could at least get on the radar of the general business community.

"Will they become a name like JP Morgan Chase or Bank of America? Highly unlikely. But I think more and more people will definitely become aware of the key alternative lending names," he said.

When the industry does achieve mainstream status, Renton said people will start referring to it as "online lending" instead of "alternative lending." Although the industry is still in its infancy, Renton believes that in a decade or two, nonbank lending will be the way most people obtain financing for a business, house or car.

"These are the first two companies going public, but they certainly won't be the last," he said.

MAJOR INDUSTRY MERGER OF 2014

On Oct. 8, Miami-based Rapid Capital Funding announced they had acquired one of the industry's oldest companies, Anaheim-based American Finance Solutions. Craig Hecker, CEO of Rapid Capital Funding told DailyFunder why he did the deal.

Hecker: AFS has always been very good at the sales partner business, which is a business line that RCF has never focused on. RCF is and has always been a direct-to-customer originator.

I feel that the landscape in the industry is changing right now in that all of the companies that have always been almost 100 percent sales partner business are now trying to figure out how to get into direct origination. I believe there to be a massive opportunity to work with the best-in-breed sales partners that we can be helpful to, by providing them resources such as leads, capital, infrastructure, and technology.

My analogy is the stock market….Buy when the public is selling and sell when the public is buying. Since RCF has built our robust direct origination channel, we can now enter the sales partner space with a vengeance at a time when our competitors are abandoning sales partner business and trying to direct originate.

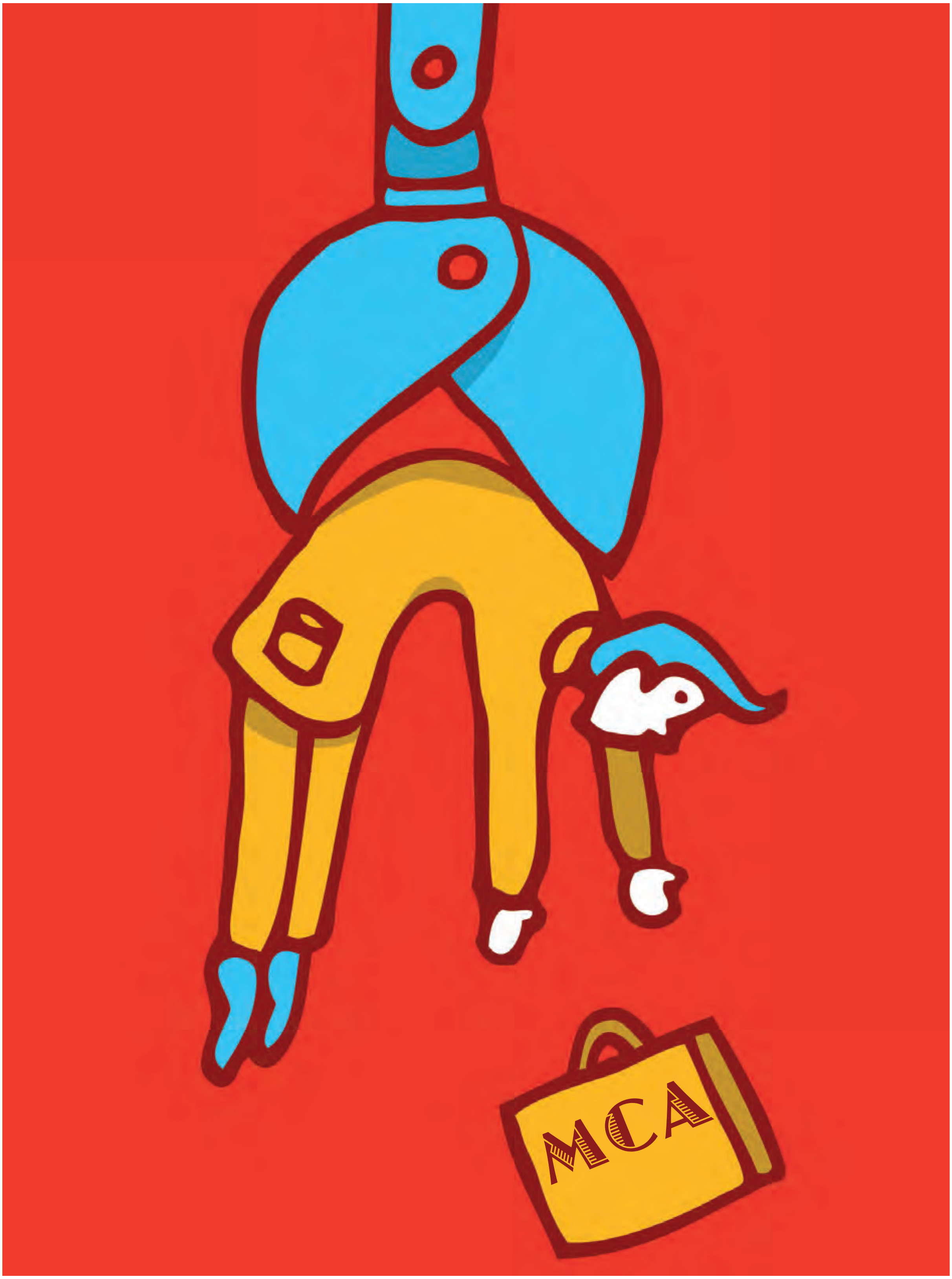
DailyFunder: What made AFS stand out?

Hecker: I identified AFS as a great acquisition target because they have been in the space since 2006 with almost all tenured employees that have been there since inception. This was a huge win for RCF to be able to get this much human capital at once!

DailyFunder: Did the deal lead to any major human resource changes?

Hecker: With the acquisition, RCF was able to repurpose several key staff members to our retention department to better service our growing portfolio.

Hecker also confirmed that Scott Griest, AFS' CEO will stay on to play an integral role in the Rapid Capital Funding family. Visit their website at www.rapidcapitalfunding.com


MCA

"It is clear why they kicked them out, but the merchant cash advance community seems to have no idea why they did it,"

DARREN LATIMER, CHIEF EXECUTIVE OFFICER OF GIBRALTAR BUSINESS CAPITAL

REMOVED

An influential financial trade group has said that businesses conducting MCAs are no longer welcome

BY MICHAEL GIUSTI

Merchant cash advance companies have one fewer networking opportunity now that a major trade group has banned them from membership.

The International Factoring Association voted this summer to exclude merchant cash advance companies from membership in their organization. But following that decision, many people in the alternative business lending industry are left scratching their heads and wondering what sparked the decision, whether it is an overreaction, and what it means moving forward.

According to Bert Goldberg executive director of the International Factoring Association, based in Avila Beach, California, the decision was based on a number of reasons primarily relating to what IFA members characterized as unfair, unethical and potentially illegal business practices on the part of some merchant cash advance companies.

"Basically – there has been a lot of, maybe, bad players in the merchant cash advance space," Goldberg said.

Following the decision to exclude MCA companies, Goldberg said he personally contacted the IFA member companies that were going to be affected by the ban.

"Most of them came back and said this was a good decision," Goldberg said. "I thought I would have received more issues. But the people who were members said the board was making the right decision and doing the right thing."

Alison Leon, vice president of marketing for Business Financial Services based in Coral Springs, Florida, said she was disappointed when she received word of the ban.

Business Financial Services offers both term business loans, as well as merchant cash advance services.

Leon said she suspects the ban was a response to an outdated reputation as much as anything else.

"Some of it has to do with the connotation from years back — associating us with some of the more payday lending schemes that are out there," she said.

Leon said she worries that the good players are getting unfairly lumped in with a very small minority of bad players.

"We have never done anything to tarnish the factoring association," she said.

Indeed, Goldberg said that neither he, nor the IFA board believed that merchant cash advance is universally problematic, but they still felt that the ban was appropriate, particularly because of the actions of what he characterizes as some of the newer, smaller industry players.

"We are not saying they are all bad. We are saying there are some bad players who could spark regulatory agencies to take a closer look, and we don't want to be lumped in with them if something happens," Goldberg said.

Darren Latimer, chief executive officer of Gibraltar Business Capital, based in Northbrook, Illinois, took the news in stride. Gibraltar offers merchant cash advances as a part of its portfolio, but he said he still recognizes an issue within the industry.

"It is clear why they kicked them out, but the merchant cash advance community seems to have no idea why they did it," Latimer said.

Because merchant cash advance is such a small portion of Gibraltar's portfolio, Latimer said his company was not asked to leave the IFA.

Jeremy Brown, CEO of Rapid Advance, based in Bethesda, Maryland, agrees that problems may be brewing in some corners of the merchant cash advance community.

"Their concerns are legitimate," Brown said.

"Problematic" Practices

Goldberg said that a number of business practices caught the attention of the IFA board after some factoring companies raised concerns. In the most grievous instances, Goldberg said that IFA members described merchant cash advance companies calling customers of factoring companies and misrepresenting themselves as being associated with the factor in order to poach business away.

Steven Kurtz, co-general council of the IFA, and a

"We are not saying everyone is bad. They are not,"

BERT GOLDBERG EXECUTIVE DIRECTOR OF THE INTERNATIONAL FACTORING ASSOCIATION partner in Levinson, Arshonsky and Kurtz LLP, based in Sherman Oaks, California, said that he also had been receiving an increasing number of complaints stemming from the actions of a few merchant cash advance companies.

Kurtz said members complained of MCAs and independent sales organizations calling factor customers and claiming that there was an issue regarding their factoring deal or implying that the factor was having problems, and then using what he described as "aggressive tactics" to win over the factors' customers.

"I think that merchant cash advance has a lot of bad players in the industry now and if it is not policed … an outside agency will,"

BERT GOLDBERG EXECUTIVE DIRECTOR OF THE INTERNATIONAL FACTORING ASSOCIATION

"It is kind of like the wild west for merchant cash advance," Kurtz said.

Kurtz said another tactic that riled factoring companies was the use of reverse UCC lien searches to prospect business.

"That tactic is frowned upon by the IFA," Kurtz said. "There are other ways to do business. It may not be dishonest, but it's frowned upon."

Kurtz said factoring companies also did not appreciate what he described as merchant cash advance companies pushing business into situations that might be in violation of their contract with the factor.

He said that in most cases, factoring deals provide that clients can't take on additional debt.

"But some merchant cash advance companies go out and target clients that are using factoring, and they were causing breaches of their factoring agreements," Kurtz said.

He added that since factoring deals use deposits or inventory as a form of collateral, many merchant cash advance deals that are paid through those deposits or through purchases made from that inventory, again walk businesses into situations that breach their contracts. He said merchant cash advance companies are also disregarding their junior position as lienholders.

Rapid Advance's Jeremy Brown said he, too, has seen some smaller merchant cash advance companies write deals that disregard factoring contracts in much the same way as they practice stacking against other MCAs.

"It is a short-term mentality rather than taking a long view of how to establish beneficial business relationships and how to play nice in the sandbox," he said.

Goldberg said that in addition to competitive tensions, the IFA board is worried that regulatory agencies may begin to increase their scrutiny on the business lending sector in coming years.

Kurtz said that increased regulatory scrutiny may come as a result of what he described as "creeping consumerism," or business owners and regulators trying to apply consumer protections on business loans. And in that environment, he said that the typically high interest rates involved in merchant cash advance deals may catch the attention of agencies like the federal Consumer Financial Protection Bureau and state regulators.

"The fact that many of these MCA deals are structured as a purchase of accounts, IFA is concerned with those problems also being attributed with factoring because the people who regulate this may not understand the difference," Kurtz said.

Uncertain future

Following the ban, many IFA members that offer merchant cash advance deals in addition to other financial products appear to be in a sort of limbo. Goldberg said that for many organizations, whether they may stay members is not entirely clear-cut.

"We are telling some members that their factoring division is still eligible, but their MCA division or department is not," he said.

Business Financial Services and Gibraltar Business Capital are two of those businesses that offer merchant cash advances as a part of a portfolio, and that have not been asked to leave outright.

Still, this was the first year Business Financial Services had gone to an IFA show, and Leon said she was excited by the opportunity to potentially partner with many of the organization's members, and she said she was worried what the IFA's decision to distance itself from merchant cash advance may ultimately mean for

those potential partnerships.

Brown also said he is worried about what the decision might mean for partnerships between MCAs and factors.

"I think it affects us to some extent because if there is a factor who doesn't know Rapid Advance personally, they might have a preconceived notion about merchant cash advance companies because of IFA's stance, and that could limit a potentially beneficial partnership," Brown said.

Some further tensions might come in when it comes to the strategic goals of the IFA, some members are saying. That is because merchant cash advance and factoring may both have lobbying agendas that are at cross positions on some issues, and that could make it difficult for the trade group to faithfully serve both types of members.

Other IFA members suggested that the move may have come from a natural tension that had been building between factoring companies and the more nimble merchant cash advance companies that now are taking business away from factoring companies that aren't able to react to market changes quite as fast.

> "It is kind of like the wild west for merchant cash advance,"
>
> STEVEN KURTZ, CO-GENERAL COUNSEL OF THE IFA.

Can they coexist?

Despite competitive tensions, many industry insiders say that merchant cash advance could very easily coexist with factoring — if some best practices can be sorted out.

"We are not saying everyone is bad. They are not. That is why they were members," Goldberg said. "But I think that merchant cash advance has a lot of bad players in the industry now, and if it is not policed, if someone doesn't come in and take the lead within the industry so it can police itself, an outside agency will."

The natural fit that is possible between merchant cash advance companies and factoring companies is obvious in the many companies that offer both products at the same time.

"A lot of factoring companies are doing business with merchant cash advance companies, and there are a lot of companies that offer both products, and we expect that would continue," Goldberg said. "We are not inherently at odds."

Kurtz agrees that there could be a happy future for the two types of funders.

"I'm not saying it is bad. Merchant cash advance is a great idea," Kurtz said. "It is an innovative source of financing. It is a necessary product. It is just the way some of the players have been operating that has caused problems."

Gibraltar is one of the companies that offers both products in its portfolio, and Latimer agreed that cooperation is more than possible — if some controls can be put in place.

"We like the space, but we don't like the murky players who are involved along the fringes," Latimer said.

Goldberg said he and the IFA board had discussed the possibility of creating a set of professional standards, best practices, or a code of ethics for the merchant cash advance space. But, in the end, they decided to instead go the route of limiting membership.

"The way we are set up is not to come up with merchant cash advance rules," Goldberg said. "We are a factoring association."

Kurtz said that any limitations or standards really have to come from within the merchant cash advance space.

A handful of merchant cash advance industry leaders are trying to do just that. Brown said he is working with several larger players within the industry, in cooperation with the North American Merchant Advance Association to develop a white paper to establish best practices for the industry.

"We believe there are some best practices we should be adhering to. There is a groundswell from a number of companies that would support something that would cover best practices," Brown said.

Several companies are involved in the effort, Brown said, and when it is done, it will be the IFA's white paper, and will be presented to the IFA board for consideration.

"We want to bring everyone into compliance and educate factors on what they should expect in terms of best practices," Brown said.

The challenge with crafting this kind of document, Brown said, is that each cash advance company is independent, and they are not coming to the problem from the position of someone who could actually regulate the industry.

"In the end, each company can still conduct business as they see fit," Brown said. "The industry is full of some strong personalities that run some very dynamic entrepreneurial businesses. They have strong opinions, and we will have to tread very cautiously."

> "We have never done anything to tarnish the factoring association,"
>
> ALISON LEON, VICE PRESIDENT OF MARKETING FOR BUSINESS FINANCIAL SERVICES

Brown said that the issue of stacking is an example of one of the contentious issues that may ultimately be addressed in the white paper.

Brown said the Electronic Transactions Association is also updating its white paper on merchant cash advance best practices, which was originally authored in 2008.

While nothing is certain, Goldberg says he can potentially see a future where merchant cash advance and factoring operates together.

"I could see us possibly lifting the ban if standards are put in place by the industry," Goldberg said.

Until those final decisions are made, merchant cash advance companies appear to be unwelcome within the membership roles of the IFA, and companies that offer both factoring and merchant cash advance may continue their existence in limbo.

"We don't have any hard feelings, yet, because the IFA has been open to discussions," Leon said. "If they are willing to allow lenders who offer other products to continue membership, then that would be a good thing, because we see such a huge value in the organization and the people who are a part of it."

Leon said she would be truly disappointed if the IFA ultimately rules to expel all merchant cash advance companies outright and closes the door to future partnerships.

"The most positive thing I can say is they haven't shut the door completely, yet," Leon said.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From left: DailyFunder's Michael Giusti leads a lively CEO Panel with AmeriMerchant's David Goldin, Rapid Advance's Jeremy Brown, Elevate's Greg Hall, Cashland Online's Samantha Bentson, and MacFarlane Group's Mark Curry.

LEND360

Alternative business lenders rubbed elbows with alternative consumer lenders

BY SEAN MURRAY

The 2014 Lend360 conference in New Orleans brought consumer lenders and business lenders together for a three-day event that set attendees off on a collaborative mission, to do what's best for the customer.

Heavy hitters from both sides of the lending aisle coalesced with industry attorneys, politicians, and institutional investment groups. Lend360 at its core was a brain trust for standards and best practices.

Two industry captains, David Goldin of AmeriMerchant and Jeremy Brown of RapidAdvance, walked the crowd of nearly 500 people through the history and methodologies of merchant cash advance financing. Several consumer lenders described the two-man panel as a wake up call. "Wow, there's a real market there," said a lead generator who asked not to be identified. Goldin and Brown were up on stage twice at the conference.

"We don't really consider banks as a competitor," Goldin explained. Much like the consumer lenders in attendance, merchant cash advance companies described helping the underbanked, customers who can't get a bank loan.

Brown, who like Goldin is also a founding member of the North American Merchant Advance Association, believes there are similarities in both industries up to a point. "Past a certain dollar amount, we want an underwriter," Brown said in response to a question about whether underwriting should be fully computerized.

Brown doesn't want to be in an environment without human involvement in underwriting. "The deals are too big and the assets are less tangible," he explained.

That stood in stark contrast to the belief held by some of the small dollar consumer lenders on the panel whose customers prefer a completely automated experience.

Governor Bobby Jindal of Louisana told the crowd that they help people achieve their dreams

Lisa McGreevy, president of the Online Lenders Alliance and Sean Murray, chief editor of DailyFunder

Indeed, the conference hosted many short-term installment lenders, some of whom make loans to consumers for less than $1,000. A full manual human evaluation of such loans would increase the costs of them astronomically, and this in an industry that is already criticized for its high costs.

One couldn't help but notice that merchant cash advance companies face a similar dilemma — pricey financing and constant criticism. The products aren't the same, nor is the customer base, but the phrase oft-repeated at Lend360 by consumers lenders to the merchant cash advance crowd was, "you guys are where we were seven years ago."

The message communicated there was that merchant cash advance companies weren't prepared to take on regulatory threats. There's been a torrent of debate regarding action the CFPB might invoke under Section 1071 of the Dodd-Frank Act, but attorney Robert Cook of Hudson Cook, LLP informed a packed room that contrary to what everyone thinks, the industry is already regulated by a different agency: the FTC.

"The FTC already has the right to punish unfair or deceptive products and marketing," Cook said.

And deception could be a matter of common sense. "Talk to merchants like they're very unsophisticated," Cook added.

When pressed for an example on deception, Cook warned, "If you only advertise the factor rate and not the other fees upfront, that is deceptive and the FTC might be interested in that."

The seven-year lag consumer lenders were talking about was not entirely predicated on the regulatory environment. There were consumer lead generators in attendance that claimed to be funding a loan almost every second of the day.

Operating on that level, one wonders if the volume could be duplicated in the business-lending world.

A recent article by Businessweek cast the cost of an exclusive merchant cash advance lead to be around $200, not far off from the premium price of consumer loan leads.

Leads were a big conversation on the second day, when the agenda was dominated by business lending sessions and merchant cash advance panels. Some of the speakers walked off stage after having mentioned doing hundreds of millions of dollars in funding and they were getting scooped up by the curious lead generators who had overheard them from their booths.

It's probably no coincidence that an afternoon breakout session on business lending was standing room only. There, Jared Weitz, CEO of United Capital Source, and Mark Cerminaro, CRO of RapidAdvance, broke down the specifics on the type of clients best suited for their products.

Tim Graczewski of Creditera, a company that helps small businesses build their business credit scores, provided some excellent insight into why such businesses are not actually bankable.

While both sides talked business, three guests talked politics.

Louisiana Gov. Bobby Jindal gave his stump speech but told the crowd that it was entrepreneurs like them that created opportunities.

Sen. David Vitter of Lousiana talked about the nuts and bolts of Operation Choke Point with attendees over breakfast.

And Congressman Sean Duffy of Wisconsin couldn't be there in person so he videotaped an address to the Lend360 crowd to voice his support.

Everywhere you turned, ethics were boiled into the message. Ryan McCurry, the president of ACH Works, made it a point to say that they only want to work with reputable companies. Heather Francis, EVP of Merchant Cash Group and Jim Salters, CEO of The Business Backer both argued that it takes work to do things right.

"Conduct spot checks," Francis said. "That includes spot checks on merchant interviews to find out what the ISOs told them," she added.

Cook seconded that. "Drop bad ISOs that misrepresent your product," he warned.

Meanwhile Salters' own experience in the industry has convinced him that there needs to be more than just transparency over certain practices, but the actual elimination of some. Of note was his stance on refi 's and a methodology he calls double dipping. Using a second advance to satisfy part of the balance of the first advance is unethical according to a video his company published on YouTube. In that same video, Salters' company describes double dipping as paying for an entire tank of gas when your gas tank is already half full.

And as for stacking, Cook advised, "Don't stack. It hurts you, the merchant and the industry."

The constant reinforcement of ethical practices inspired several attendees to collaborate further, beyond the conference. "Anything we can do to participate in the longevity of the industry, let us know," said the partners of Florida-based Fusion Capital to DailyFunder.

OLA members advised the merchant cash advance crowd to be customer-focused even without impending regulatory scrutiny. Having weathered many storms themselves, it was tough to ignore. OLA's standards extend from the lenders all the way to the lead generators. That should interest merchant cash advance ISOs who may be wondering what role they have in ethics and best practices.

Lend360 proved how much in common both industries have with each other. This phrase echoed over and over again, "You guys are where we were seven years ago." That means incredible opportunities await and there's a chance to dictate how the future will play out. Lend360 was absolutely about business, but above all, ethical business.

Are you doing your part to be an industry good citizen?

John Hecht of Jefferies and Brendan Carroll of Victory Park Capital on the Investor Roundtable

The Online Lenders Alliance team that put the conference together

Conference brought together diverse pieces of the online lending world

The online lending industry is changing, and those in attendance at LEND360 put themselves ahead of the curve. Traditional consumer lenders are beginning to show interest in new installment products, lines of credit, peer-to-peer, merchant cash advance, auto, auto title and retail installment lending.

When we first began to plan LEND360, we knew we had to put together a conference that would be aimed at companies and leaders who are looking to diversify and offer a variety of different products to myriad customers.

LEND360 brought together nearly 500 attendees from six different countries. This year, we welcomed 201 new faces to the conference, with 15 percent of attendees representing the small business lending and merchant cash advance industries.

Through a partnership with DailyFunder, we were able to bring together consumer and small business lenders for three days of sharing collaborative ideas and best practices. The results were incredible and awe-inspiring.

I believe DailyFunder's Sean Murray put it best in his closing remarks, "We may in some way have thought that lending is kind of like a junior high school dance, with all of the consumer lenders on one side of the room and all of the business lenders on the other. All it takes is that one boy to ask that one girl if she'd like to dance, and before you know it, you start to wonder what everyone was so nervous about when they got there."

LEND360 demonstrated that synergy can occur in the online lending space, and there is much to be learned from one another. The energy was high when we left New Orleans, and we hope to continue the dialogue we started, and search for new ways we can share ideas and spark innovation.

The conference may be over, but our work has just begun. As laid out in my closing remarks, these are the action items we must focus on, together:

Implement the "Look for the Seal" campaign

In an industry plagued by nasty headlines about the questionable tactics of a few bad apples, members of the Online Lenders Alliance serve as a beacon of trust for customers looking to do business with reputable lenders.

Sound business practices and objective standards are essential to ensuring industry excellence and longevity. OLA members can embed the OLA seal on their websites to show customers and regulators that they adhere to the strictest industry best practices.

As announced at LEND360, we are launching a campaign to inform customers to look for the OLA seal when searching for an online lender.

Watch this short video on the OLA seal campaign: http://tinyurl.com/LookForTheSeal

Stay in communication with each other

While in New Orleans, we laid the foundation to work together to do what is best for customers. Consumer and small business lenders have a lot to learn from one another, and we hope to continue the conversation over the course of the year. Keep an eye on the LEND360 website for information on future collaborative opportunities.

Be vigilant as an industry against Operation Choke Point

Operation Choke Point is but one example of the challenges faced by the online lending industry by state and federal governments. Technology and innovation continue to move quickly to meet growing consumer demand, but changes to state and federal laws and regulations are slow to adapt. We must work together to encourage the stability of the online lending industry.

Work toward passage of payments legislation

Rep. Blaine Luetkemeyer, a Republican from Missouri, introduced HR 4986, the "End Operation Choke Point Act," to do exactly what the title suggests. Luetkemeyer recognizes the need for borrowers to have access to innovative financial products, and the demand for the online lending marketplace.

Update and expand our best practices

As the online lending industry evolves, so must our best practices. Our member companies set the standard for how the industry conducts business. We are constantly looking for ways to improve the industry and better serve customers effectively.

Again, I thank everyone who joined us for LEND360. We cannot wait to keep the conversation going and we hope you will join us for the 2015 LEND360 event, Oct. 13-16 in Atlanta.

Lisa McGreevy, President + CEO, Online Lenders Alliance

Ron Suber of Prosper explained the challenge in alternative lending is finding the borrowers

Industry attorney Robert Cook preached guidelines for best practices

Tim Graczewski of Creditera, Mark Cerminaro of RapidAdvance, and Jared Weitz of United Capital Source discussed their customer-base.

David Goldin of AmeriMerchant and Jeremy Brown of RapidAdvance provided excellent insight into the business lending industry

David Aidi of Atalaya Capital Management, Jeff Marron of Sheridan Asset Management, and Craig Hecker of Rapid Capital Funding raised the roof on a raising capital panel

SHARKS IN ANGEL'S CLOTHING

Alternative business lenders are praised by some while demonized by others

BY DALE LASZIG AND SEAN MURRAY

Something seems to be fishy about the public's perception of alternative lending.

The same businesses that have been panned and described in various news media as "predatory" by many industry critics are also being featured and celebrated on television shows that extoll the benefits of non-bank finance. Is there a television double standard?

Perhaps epitomizing that seemingly schizophrenic view is Total Merchant Resources, based in Piscataway, New Jersey. Total Merchant Resources caused a stir on ABC's reality TV show "Shark Tank," when the partners made a deal with Kevin O'Leary. When CEO Jason Reddish and President Val Pinkhasov described themselves as mini sharks, the blank stares of the bigger sharks made it clear that cash advance was a relatively new concept.

And yet there was something very familiar about the Total Merchant Resources model, they took big risks on small businesses, with terms you wouldn't find at a bank.

America loves "Shark Tank" and all of the deal making that goes along with it. Millions of viewers respect the game even if it's real life and even if some of the terms would be virtually unconscionable for a consumer.

But the rules are different for businesses, as Wicked Good Cupcakes would learn when they filmed their stint on "Shark Tank" back in June 2012. Based in Massachusetts, the mother-and-daughter team Tracey Noonan and Danielle Vilagie made a deal with Kevin O'Leary, a transaction that would cost them 45 cents per cupcake in perpetuity.

It wasn't equity and it wasn't exactly a loan, though if imagined as a loan, this deal demanded payments for the rest of their lives. In return they got capital and access to a broad network of dedicated supporters who were eager to advise on an array of topics, including how to execute business strategy and deal with issues.

"So instead of paying accountants, attorneys and marketing people – we got a royalty deal and we were one of the first people he offered it to," husband and father Scott Noonan said about Kevin O'Leary, adding that industry critics may not fully appreciate all the value that's bundled into the 45 cents a jar.

"If I had to pay Mullen or Arnold, it would cost far more than 45 cents a jar," he said. "This may not be the right deal for everyone, but we did as much in sales in the first week as we did in the entire previous year."

Noonan went on to say that life after "Shark Tank" is not Utopia and that business owners have to be ready to execute. And while a 45-cent-per-unit royalty in perpetuity attracted criticism from some fans, others were envious of how it allowed them to grow.

"We hear people say you were lucky. No such thing as luck – luck is what happens when practice meets opportunity," Noonan said.

Today, Noonan is experiencing great success. "It opened up Kevin O'Leary's vast network of business specialists, attorneys, and marketing experts. The power is enormous. And he introduced us to Marcus Lemonis, a celebrity on television and in the gluten-free space, who brought us into his 'Crumbs Empire,'" he said.

While part of the show's intent is to deliver entertainment value, Ami Kassar, CEO of MultiFunding LLC, a Philadelphia-based consulting firm, warned against the mainstream media's tendency to paint alternative financing with a broad brush.

What works for the businesses that appear on "Shark Tank" might not work for the individual circumstances of other entrepreneurs. Specifically, Kassar claimed that there are too many disparate parts of non-bank finance for the entire ecosystem to fit neatly into one category or industry.

"We have to be very careful not to call it all the same thing. There are alternative lenders who create reasonable lending programs," Kassar said.

Widely-known as a critic of merchant cash advance, Kassar addressed "Shark Tank" in an Inc. column, "I would love to see a lender on the show, sitting side-by-side with the investors, asking the entrepreneur questions about

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their cash flow, collateral, and credit," he wrote.

Notably, Kassar seems to argue that the stakes aren't high enough. "It would be fascinating to watch an entrepreneur have to make a decision in front of millions of watchers between taking a loan and keeping control of their company but have to risk their house as collateral or taking an investment," he wrote.

That's where the line would probably start to get murky. In the Wicked Good Cupcakes deal, Kevin O'Leary didn't ask for a house, but rather a return commensurate with the risk and his efforts, which was priced at 45 cents a cupcake forever.

And for those under the impression that there is nothing in between short-term lending and "Shark Tank," they'd be wrong. Halfway in between TV and reality, but set completely in reality and not on TV, is Guppy Tank

Darrin Ginsberg, founder and CEO of Super G Holdings in Newport Beach, California saw a need for a non-televised, localized version of "Shark Tank."

Ginsberg created The Guppy Tank, a place where entrepreneurs can pitch business concepts to business mentors and potential investors in a relaxed setting, potentially securing equity investments, cash flow loans, or combinations of equity and loans.

"The 'Shark Tank' only allows you to ask for equity," Ginsberg said, "and if you don't get the full amount you are asking for, you get nothing. That's where The Guppy Tank differs."

He went on to say that asking for debt instead of equity can be a better choice for a start-up with little to show beyond a dream and a business plan.

And yet in June 2013, "Shark Tank" investor and celebrity entrepreneur Mark Cuban famously said in a Bloomberg interview, "If you're starting a business and you take out a loan, you're a moron."

Cuban's words left little room for misinterpretation. "There's so many uncertainties involved with starting a business, yet the one certainty that you'll have to have is paying back your loan," he added.

The caveat is that business owners not able to get equity investors can jeopardize themselves personally through debt. That seems to be where the merchant cash advance product comes in. It's not equity, it's not debt, and these transactions are typically not personally guaranteed.

Oddly enough, merchant cash advances resemble a Kevin O'Leary royalty in perpetuity deal, where funds are delivered to the investor at the pace that sales are generated. The difference being that merchant cash advances terminate after a predetermined dollar amount has been delivered rather than continue for a lifetime.

The similarities did not go unnoticed. Just a year after the handshake that sealed O'Leary's $200,000 investment and 50 percent equity stake in Total Merchant Resources, O'Leary announced a strategic alliance with Atlanta-based online lender IOU Central that provides loans of up to $100,000 to small-to-midsized businesses.

While IOU is not exactly merchant cash advance, they have made waves in that industry with a competing product. In a press release, O'Leary is quoted as saying, "We've chosen IOU as O'Leary Financial Group's small business lending partner because they share our way of thinking."

The partnership is one of many bridges between TV fantasy and reality.

The media gives favorable coverage to "Shark Tank's" investors while often chastising short-term business lenders. And that's what's fishy, since one of the only remaining distinctions between the two is that one has millions of viewers.

Going on "Shark Tank" is hard, regardless of what deals you're offered.

Reddish of Total Merchant Resources had been warned by friends in the reality show business of the transformative power of television editing. His heart was pounding at the thought of looking really dumb in front of millions of people.

Some times the exposure works against the entrepreneur. The upside from publicity is not guaranteed.

Both Reddish and Pinkhasov however were grateful to the show's staff for presenting them in a positive light, while regretting the subsequent bashing they received from critics in print media.

Reddish went on to enjoy other public appearances, including speaking engagements in New York City, Atlanta with Super Bowl winner Randy Cross on Super Bowl Sunday, and Washington D.C. at Georgetown Law School's graduation ceremony. Reddish said that none of these events would have occurred without the television exposure.

Wicked Good Cupcakes used the long interval between the taping in June 2012 to the airing in April, 2013 to put a process in place that would help them scale.

Noonan noted that only a small percentage of "Shark Tank" deals are actually consummated with investors. He said that despite all the planning that no entrepreneur can be fully ready for prime time.

And Kassar said that small business owners must choose wisely to keep payments manageable because they never know when the next tsunami will hit.

"Every time that they need money they have to decide between equity and debt, and what is a better option – it's not a black and white question. Every situation is different," Kassar said.

Of course, in today's world there is more than just equity and debt. Whether it's O'Leary's royalty deal or a merchant cash advance, or something else completely, it's a pretty great time to be in business. What entrepreneurs are seeing on TV is happening in the real world too. There's no place for a double standard.

Kevin O'Leary took the bait, and came back a year later, wanting more. As other celebrities like Larry King attach their brand to alternative lending, TV and reality are blurring.

In Noonan's case, their dreams were realized when Mark Cuban ate five cupcakes.

There's a really simple reason why the general public was willing to give the royalty terms the benefit of the doubt, because the deal was priced in cupcakes. Perhaps the final missing link between what's on TV and what's in real life is in the presentation.

Loans and merchant cash advances get wrapped up in thick stacks of legalese. It may be necessary and it may be binding, but it lacks a certain luster, something to simplify what it's all about. Could a holdback percentage or recurring payment be communicated in a friendlier way, say in the dollar and cents of cupcakes, hamburgers, shovels, or whatever it is the business sells?

Forty five cents a cupcake sounds neutral, warm, even yummy. And even if the cost is wildly unfavorable, the only thing the media, the public, and anyone else is going to be thinking about after they do the math, is "those must be some wicked good cupcakes."

BAD ADS

The danger of offering "lowest rates" and the importance of substantiating claims in advertisements

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

A merchant cash advance company needs advertising to attract customers. Unfortunately, many MCA companies and their independent sales organizations do not understand the legal limitations placed on advertising.

MCA companies and ISOs unknowingly risk legal penalties by advertising in a way that may be deceptive or making claims that they cannot substantiate. The penalties for deceptive or unsubstantiated claims can hurt.

The Federal Trade Commission is the cop on the beat when it comes to enforcing the truthfulness of business-to-business advertising. The FTC recently sued an ISO for allegedly making statements that constituted a deceptive act or practice in violation of the FTC Act, 15 U.S.C. § 45(a).

In 2013, the FTC sued Merchant Services Direct LLC, an ISO in Spokane, Washington, that sold credit card processing services. According to the FTC, Merchant Services Direct specifically targeted small storefront businesses and sole proprietorships.

In court filings and its press release, the FTC alleged that the ISO advertised on its website that it had "Guaranteed Lowest Rates," claimed merchants could "save 30%" with "whole sale [sic] processing" or have "anywhere from 20% to 30% savings when switching to" its service. Claiming that these advertisements were "unsubstantiated," the FTC asked the U.S. District Court for the Eastern District of Washington for an order freezing business's assets and to stop the allegedly deceptive acts and practices.

Merchant Services Direct has denied the FTC's allegations regarding the alleged deceptive advertising.

MCA companies and ISOs should pay attention to the Merchant Services Direct case.

Congress gave the FTC the power to regulate and punish unfair or deceptive acts or practices in or affecting commerce, and directed the FTC to prevent individuals and businesses from using such acts and practices.

The FTC has clarified over time what actions or practices it considers "unfair" or "deceptive." An act or practice is "unfair" if it causes injury to the buyer that outweighs potential benefits to competition.

An act or practice is "deceptive" if it will likely mislead someone, acting reasonably under the circumstances, to that person's detriment.

Tied to these requirements is the concept of "substantiation." The FTC took the position in a 1983 policy statement that the "failure to possess and rely upon a reasonable basis for objective claims constitutes an unfair and deceptive act or practice…." In other words, a business needs data to prove that the claims made in an ad are accurate.

Specific claims will be subject to more demanding substantiation requirements.

Problematic advertisements may include those that


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promise the "lowest" rates or a specific rate of savings. Additionally, a funder advertising a rate or factor "as low as" a certain amount raises a simple question: just how many customers actually get that low rate or factor?

An MCA company should be able to provide examples of customers who have received the rates or services advertised. The failure to have solid substantiation for advertised claims can expose a funder to undesirable penalties, possibly including a civil order from the FTC, monetary penalties, and even a lawsuit in federal court.

Among the possible penalties, perhaps the most likely would be a cease and desist order from the FTC requiring an MCA company or ISO to change its advertising and not to commit the violation again in the future.

Violation of a cease and desist order can trigger civil penalties of up to $16,000 per violation or per day. The FTC also can file a complaint in federal district court for a broad range of equitable relief. A court could require the defendant to give up all the money made from the deceptive conduct, or return money to victims harmed by deceptive ads.

In addition, a court could grant injunctive relief by setting standards that the defendant must comply with in the future.

Civil penalties are not the only risk a small-business funder must manage. The media attention that may follow an FTC action is not the sort of publicity a funder wants. A reputation as a "bad actor" may scare away future customers and investors.

To avoid penalties from the FTC, an MCA company or ISO should consider several proactive steps. First, its management team along with in-house and outside counsel should review all statements made on its website or other advertisements regarding services and rates.

Extra care must be taken to ensure that specific rates and service offerings are accurate and substantiated.

Second, an MCA company or ISO should create a legal review process for all future advertising and website launches that involve any claim about a product or service.

As federal regulators review small-business funding with increasing scrutiny, a prudent small-business funder should exercise care and vigilance. In a modern era where websites and corporate blogs may be updated instantly, and advertisements can be captured by anyone on the Internet, establishing good policies and procedures can prevent a major legal headache in the future.

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