White Paper
November 2008

Maintaining Trust in Micro-Ticket Leasing Operations

Executive Summary

The micro-ticket lease finance industry supplies a critical component of financial transaction processing for small- and medium-sized merchants.

What exactly does a micro-ticket lease finance company do?
It provides lease financing for the equipment needed to transmit purchase approvals for debit and credit card purchases.

What is the benefit of such a firm?
It enables small business owners to minimize up-front costs involved in accepting major credit and debit cards.

What is the industry's scope?
Micro-ticket leasing companies support merchants of various industries at locations worldwide.

How do these companies reach the merchant?
Due to the dispersed locations of business owners, micro-ticket leasing companies often partner with third-party organizations for sales and marketing. Known as "independent sales organizations" or "ISOs," these firms usually represent the financial organizations processing the credit and debit transactions.

Is this an equipment business?
No. The micro-ticket lease financing provides financing for the equipment already selected by the merchant in the course of securing their card processing services. By spreading the cost of this equipment over time, businesses can better manage their use of limited cash and credit line resources.

How is the transaction detailed?
Companies in our industry provide the ISO with lease documents detailing the terms and conditions of the lease finance transaction. When a merchant decides to lease the processing equipment, the lease document – signed by the merchant, the ISO and the lease finance company – becomes the business contract among all three parties.

Because ISOs may utilize different kinds of companies to support clients' credit and debit transaction needs, the services provided by the micro-ticket lease financing company must be clearly defined for the merchant.

The lease is the key in the relationship. How can companies most effectively structure lease agreements and merchant relationships? How can they work with ISOs to deliver the financing services vital to the merchant's business success? This paper addresses both of these large and important questions.

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Best Practices: Securing Leasing Services With Merchants

Establishing credit and debit card transaction processing involves interactions with credit and debit transaction processors, ISOs, equipment vendors and lease financiers. Transaction processors receive payment for their services based on the amount of transactions "batched" each month and processed for the merchants. ISOs receive an up-front commission for bringing together the transaction processors, equipment vendors and lease financiers in a relationship.

Success in micro-ticket lease financing is based on a long-term commitment and ongoing relations between the financing organization and the merchant. Lease financing benefits the business owner by establishing transaction processing for debit and credit card transactions with little up-front cost. The merchant typically agrees to pay a monthly leasing fee over a several-year period.

Many lease financing customers are new business owners.

Merchants entering lease financing arrangements are often new business owners with little experience in debit and credit card transaction processing. To make sure the interests of all involved parties (the merchant, ISO and lease finance company) are protected, the lease agreement should provide a clear understanding of the terms and conditions the merchant agrees to. Below is a description of lease components. If they are included in the lease document, that should ensure the merchant, ISO and leasing financier are aware of the commitment each party is making.

Structuring the Lease Agreement

Micro-ticket lease financing agreements are often non-cancelable.

Lease financing agreements for micro-ticketing processing equipment are often non-cancelable, meaning the merchant commits to make agreed-upon monthly payments for the entire lease, even if the equipment is damaged, lost, returned to the equipment vendor or no longer used. Since many merchants are new business owners, they need to understand this provision of the lease. If the lease is non-cancelable this provision should be noted clearly on more than one page of the lease agreement.

Lease fees and payment terms should be clearly stated on the first page of the lease agreement.

Many of the merchants entering lease finance agreements are new to retail markets; thus, they likely have a limited understanding of costs associated with establishing credit and debit card transaction processing. To ensure the lease financing costs are appropriately disclosed, all equipment lease financing fees and payment terms should be clearly stated on the first page of the lease agreement.

The lease should state that the equipment is leased "as is."

Although the lease financier is providing the funding needed to obtain the credit and debit transaction processing equipment, other vendors provide the equipment the business owner is leasing. Therefore, the lease financing company typically has no accountability for the condition of the equipment, either when it is first installed or throughout the lease's duration. The lease agreement should clearly state that equipment is leased "as is", and the leasing financier has no responsibility for equipment maintenance or repair.

Ending an agreement with a transaction processor does not impact the terms of an existing lease finance agreement.

Occasionally, a merchant may decide to terminate an agreement with a transaction processing firm prior to the end of the equipment financing lease. Although agreements for processing the transactions and leasing the equipment may have been obtained through the same ISO, the merchant signed a separate lease agreement when the service was initiated. The business owner should be aware that a decision to end an agreement with a transaction processor will not affect the terms set forth in an existing lease financing agreement. In any event, the business owner is obligated to continue to honor the terms of the agreement and remit lease payments.

The merchant, ISO and financier should initial each page of the lease to confirm understanding of its provisions.

All parties to the lease – the merchant, ISO and lease financier – should indicate their understanding of and agreement with the various lease components by initialing each section when the lease is executed.

By considering these provisions when devising the lease, the lease financier can meet the needs of the business owner and establish a positive, lasting relationship that will benefit the merchants, the ISOs and the lease finance company.

The ISO relationship: Critical to lease finance success

Most micro-ticket lease financing organizations utilize ISOs for sales and marketing efforts. Therefore, the ISO is often the "face" the merchant sees. The lease finance company depends on the ISO to generate new business and establish relationships with business owners. To that end, it is imperative that the ISO understands the lease's terms and conditions. The ISO must work to make sure the merchant understands the limits of the ongoing relationship with the lease finance company at the moment when the lease is executed.

The business relationship between the merchant and the lease finance company should begin on solid footing. A clearly defined and frequently monitored set of business guidelines should be established between ISO and lease financier. Below are some general guidelines to consider when establishing these relationships:

The ISO must be trained on the lease terms and conditions before initiating business on behalf of the lease financing company.

The terms and conditions of the lease financing agreement mark the relationship between the business owner and the financing company. The lease financing company must train the ISO on its contract terms and conditions before the ISO begins sales efforts on its behalf. The ISO must appropriately represent the lease financing company with its customers. Penalties for misrepresentation of any financier services must be established when the ISO relationship is initiated.

All operating issues impacting the ISO relationship should be clearly established up-front, before the ISO begins sales and marketing efforts on the behalf of the lease financier.

Issues include:

- Financial compensation, i.e., the payment structure for business the ISO brings to the lease financing company, must be agreed upon.

- The ISO must demonstrate a clear understanding of the lease financing contract's components – chief among them, the ISO must understand the contract terms are not negotiable. Should the merchant request any contract changes, the ISO should advise the lease finance company. Any contract exceptions would have to be agreed to in writing before the ISO could advise the merchant.

- If the merchant fails to adhere to the terms set forth in the lease financing agreements, the financier may decide to penalize the merchant or terminate the relationship. The ISO must be aware of procedures and penalties for failure to adhere to the lease agreement, and advise the merchant of those provisions when securing the lease.

- Record keeping requirements must be defined by the lease financier, and agreed to by the ISO. Why? Because the ISO executes the lease documents on behalf of the lease finance company. Periodic audits of lease documents should be conducted to ensure adherence to the guidelines.

- The ISO often represents several companies when setting up transaction processing for merchants. To ensure the interests of all parties are protected, the ISO must sign an agreement confirming intent to maintain confidentiality of the terms and conditions set forth by each party.

- The lease financing company should establish certain baseline criteria to be considered when merchants seek financing for transaction processing equipment. The ISO should use these criteria as a "vetting" mechanism when prospecting for new customers. Following are some examples:

    - Merchant documentation (i.e., financial statements or a business plan);
    - Allowable exceptions on credit reports;
    - Previous forays into business ownership, particularly in the retail space;
    - Underwriting guidelines.

An audit routine for the ISO must be established.

For the benefit of all involved parties, the lease financing company will establish an audit routine for the ISO. Methods for addressing any irregularities discovered during these reviews should be established when the ISO relationship with the lease finances company begins, including any grounds for ending the relationship.

The lease financier should annually share their "best practices" with the ISO.

The ISO should be made aware of any changes in the lease financiers' business practices. The lease financier's "best practices" should be reviewed annually with the ISO.

Conclusion

Micro-ticket lease financing is critical to small business owners' success.

By providing financing for an optimum credit and debit card transaction processing solution for merchants, retail customers are able to purchase goods and services securely and easily.

In clearly defining lease provisions and operating standards for ISOs, lease financiers ensure a successful business that benefits all concerned.