

# Masters

# of the Value-Add

*Four ISOs leveraging new products and services for competitive advantage*

By Richard H. Gamble

## KEY NOTES

- ▶ Many companies find that packaging add-ons as part of a strategic, holistic solution brings success where individual products and services could not.
- ▶ Many ISOs use cash-advance as a strategy to generate leads. Merchants that use it often promote the idea to other merchants, creating new business for the ISOs that offer the service.
- ▶ Gift cards are being used to reduce attrition. Studies show that once merchants have a program in place, they're reluctant to give it up or change providers.

Differentiation—setting your company apart from the crowd—has become more than a business strategy for many ISOs. It can be a matter of survival. For those enterprises, the question is not whether they can find a way to market their services on something more than the price of card processing, but how to do it.

Offering merchants additional products and services that add value to the processing agreement is one approach that has paid off handsomely for some ISOs by bringing in new business and giving merchants a reason to think twice about jumping to competitors. For those who want to follow suit, finding successful strategies to emulate isn't difficult.

## Total Merchant Services: Making 'Free' Truly Free

When executives at Total Merchant Services decided in early 2005 to offer free terminals to merchants as part of their marketing strategy, they looked at a competitor's free terminal program and saw an opportunity to convert what was essentially a customer incentive into a true value-add proposition.

"Another ISO had recently come out with a free terminal program that had a \$79 annual fee billed in the second or third month of the merchant's contract," explains Ed Freedman, CEO and president of Total Merchant Services. "To us, this just looked like another way to bill a monthly rental fee. The only difference was that it was lumped into an annual fee as opposed to billing it monthly."

Total Merchant Services soon became the first company to offer a truly free terminal placement program. Merchants who take advantage of the program get the equipment at no charge and with no annual service fee, and then pay the same processing fees as merchants who aren't in the program. However, they do agree to accept a locked-down terminal, which can't be switched to another ISO.

"We created a full one-page form (that we still use today), which clearly explains how the free terminal placement program works," Freedman says. "This eliminated any confusion with our competitor's offering."

It also made clear the value to Total Merchant Services' merchant customers: high-quality equipment (for which they're not financially responsible) and reduced cost.

The positive results came quickly and grew.

"Within the first six months, our new account acquisition numbers doubled from 1,000 per month to 2,000 per month," says Freedman. "[The program] has far exceeded our expectations. In the past three years, we've seen our merchant numbers go from 1,000 per month to more than 4,500 per month—or from 12,000 per year to more than 50,000 new merchants per year."

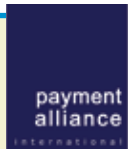
The free terminal placement program has been anything but stagnant over time;

Total Merchant Services has made adjustments about twice a year, such as increasing upfront bonuses for sales partners, adding wireless terminals to the program, and offering sales partners a hybrid program in which they get the free terminals but can opt to forgo their bonuses on placement to be able to sell or lease the terminal to merchants.

The economics of the program work well, Freedman says. "It takes about 18 months to recoup our money. That in-

cludes the cost of the equipment, upfront bonus payments, and deployment/merchant training costs. But our attrition rates are lower in large part because we're delivering locked-down terminal equipment that can't be reprogrammed by a competitor. If a competitor wants to move one of our merchants, they'll need to provide similar free equipment, lower rates and fees, and possibly even reimburse the merchant for the termination fee associated with our agreement."

## Payment Alliance International: Sticky Loans



Cash advance is perhaps the hottest add-on in today's credit-crunch economy, because "merchants see the benefit right away," says Donna Embry, senior vice president for strategic product development and marketing at Payment Alliance International, a Louisville, Kentucky-based ISO. "If they need cash, they're certainly interested in finding out how it works."

Payment Alliance launched its cash advance offering as part of a broader strategy that was aimed at giving merchants a wide range of add-on products and services that can be combined in many ways to create a tailored approach to a specific merchant's requirements.

"Not every merchant needs cash advance, and cash advance isn't right for some merchants," Embry says. Because of that, cash-advance programs include additional levels of consultation and qualification during the sign up.

Despite the additional work involved for both ISO and merchant by offering cash advance, ISOs can lend to or save merchants money—a powerful sales hook in the current economy, says Embry.

But unlike some other value-adds, cash advance has a reputation not only as a sales incentive, but as a lead generator. Merchants who find it a valuable way to smooth out cash flow promote the idea to others in their line of business, which tends to bring in new, unsolicited merchant accounts.

"There are not many things you can offer that prompt merchants to call and ask for an appointment to talk to a sales agent," Embry says. Cash advance turns out to be one of them.

Cash advance is a strong retention tool as well. Because a cash advance program is a recurring cycle of advances and repayments, merchants often come to depend on the steady cash flow, thereby reducing merchant attrition.

"We've seen significant reductions in our attrition," Embry says, "in part because merchants simply are reluctant to give up something that solves their working capital problems in a pretty painless way."

Companies like Payment Alliance International warn that while a merchant's need for working capital may be increasing during the current economic slow-down, cash advancers are taking on more risk while their access to credit shrinks. Consequently, they're tightening underwriting standards—and ISOs need to be careful not to pitch cash advance services to merchants that would likely be turned down.

But even in a credit crunch, the cash advance business is thriving. While the advancers have become more sophisticated in their underwriting, they aren't abandoning the business.



## Electronic Cash Systems: Quick Check Clearing

While many, if not most, merchants can and do accept checks from their customers, offering them the ability to process those checks electronically—and without the hassle of dealing with bounced checks—can be an effective growth tool for ISOs.

“It’s part of being able to offer merchants a complete solution for their business,” says Electronic Cash Systems President/CEO Fadi Cheika. “And that gives us the opportunity to talk to more merchants, because we’re talking to them about more than just card acceptance and negotiating over fees.”

ECS offers merchants check conversion and guarantee along with traditional card processing, but the company finds mer-

chants are most excited about a Check 21 service, which allows them to scan a check and then send the digital image to ECS for clearing (as a check).

“We take it from there and do everything else for them—provide quality assurance, clear it through the Federal Reserve and make lump-sum deposits of all checks into their bank account,” says Cheika.

A big part of the value to merchants and ISOs—apart from being able to offer customers the choice of writing a check and using a credit card—is that the check processing is typically provided by a company that specializes in check processing. That company absorbs the losses and inherits the job of collecting on bounced checks. Because writing bad checks is a crime, the guarantor has the staff and tools to recoup the lost money.

While only about 1,000 ECS customers use the Check 21 service, it produces almost the same payments volume as its other principal products—credit card transactions, ATM transactions, ACH

transactions, gift cards and bill payment says Cheika.

But the ability to offer Check 21, along with check conversion and check guarantee, is a potent way to build the ISO’s business. And each new customer brought in by the check processing service adds to the volume on all offerings. The result is a balanced and diverse revenue stream, with each service making up a roughly equal portion of ECS’ business.

Companies like ECS that are succeeding with check processing point to significant growth potential for this add-on, especially considering a large market doesn’t take card payments, but does take checks: utility companies, property management companies, clinics, commercial suppliers, and others.

“Finding products that have that kind of growth potential has been the key to growing our business,” Cheika says. “To attract new merchant accounts, we have to be able to give them something they need, but don’t have, and we have to move into markets that are expanding. Check processing has fit those conditions perfectly.”

## International CyberTrans: Loyalty Rewards

The old standbys of gift card and loyalty programs still have fans, especially when those programs incorporate high-tech enhancements. The favorite add-on at Nashville-based International CyberTrans (ICT) is a dual gift and loyalty smart card, says CEO Joyce Cook. “The value is loaded directly onto the card chip,” she explains, and merchants need

a smart-card reader, which gives ICT another piece of equipment to sell. “Merchants like it because the technology eliminates the transaction fee. Plus, it is more flexible and multi-functional than most other gift card programs.”

But technology aside, ICT has found that the benefits to merchants from gift and loyalty programs not only make them easy to sell, but give sales agents a hook to get them in the door to talk to a merchant.

“We don’t have to start the conversation with a discussion of credit and debit card processing fees,” Cook explains.

As is true for most good value-add programs, gift and loyalty cards have benefits that are easy for merchants to understand, and also strengthen the business relationship between merchant and ISO, Cook says. Merchants get cash on the spot and the benefits of float. Then the card either brings the recipient into the store to buy, with opportunities to reload the card

and get repeat business, or the merchant keeps the cash as breakage. Either way, merchants make money. And the longer a merchant uses a gift and loyalty program, the more difficult it becomes to switch to a new provider. Cook points to studies that show attrition falls from 18 to 20 percent annually to just 5 or 6 percent.

ICT’s programs have created a steady flow of new business and falling attrition rates—the keys to a thriving ISO business.

Best of all, the price point to justify gift and loyalty programs has fallen to the point where more small merchants are signing up, expanding the market. “We are offering the programs to merchants who wouldn’t have considered it before,” Cook points out.

While nothing may beat the familiar closed-loop gift card for building retention, merchants also are showing more interest in open-loop prepaid cards that carry the Visa or MasterCard logo and can be used anywhere that accepts those brands. A merchant can sell a \$50 open-loop gift card for \$54.95 and pocket the difference. They can also make money putting in a rack and selling closed-loop gift cards for popular retail chains. And prepaid cards are proliferating as health-care, gift, and corporate rewards cards.



# But Wait, There's More

While these companies demonstrate the **value** and the **success potential** of value-adds, they certainly aren't the only success stories. Among the more innovative options, a few ISOs are selling Web site design services to merchants, first launching a static billboard site and then moving to an interactive site that accepts credit or debit card payments.

Others are selling full POS systems and the associated processing. A few are even offering telecommunications lines as part of their portfolios.

A growing trend is packaging add-ons as part of a strategic, holistic solution, which "takes you out of the commodity world of selling credit card processing and into helping a merchant manage his business with a service that happens to include card processing," says Embry.

A holistic solution could mean helping merchants both make and receive payments. On the receiving end, it would in-

clude all card payments—credit, debit, and prepaid—plus a full line of check services, including POS and back-office conversion, verification, guarantee, imaging, and remote deposit. For cash-taking merchants, a holistic solution could include ATM installation; for liquor stores, it could include age verification. Background checks on employees are another option, as well as proprietary and branded gift cards, mall cards, and PCI compliance aids.

Business analytics software to measure performance may also be part of a strategic solution. "It's a long list," Embry says. "The

trick is to apply a decision tree and package the right bundle of services to provide the right holistic solution for each merchant you sell to."

At the end of the day, it's all about thinking big. While many add-ons were originally introduced as revenue builders, the end game for smart ISOs has become building enduring relationships with more holistic, strategic solutions. **TT**

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