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INNOVATOR OF THE YEAR Higher Power

In discovering an under-served market, Higher One builds a potential financial-services powerhouse



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Bootstrapping a company is a perilous process, requiring courage, determination, managerial and marketing skills and - more often than not - luck.

And even with what seems to be the right stuff, the odds of success can be long.

Business New Haven's 2008 Innovator of the Year, Higher One, has beaten the odds.

Co-founders Mark Volchek, Miles Lasater and Sean Glass met in the late 1990s as undergraduate students forming the Yale Entrepreneurial Society, and decided to start an Internet-based business expanding the use of student IDs for purchases and financial services. They launched it in New Haven in 2000.

Their company, named Higher One, turned profitable in 2006, and has blockbuster potential, according to those monitoring its development.

"So many times innovation is not so much about invention as it is about applying common sense to problem-solving," says Matthew Nemerson, president and CEO of the Connecticut Technology Council. In Higher One's case, innovation emerged from "some smart folks getting together and thinking about a market that needed to be served. In a sense this is the purest of companies, with a solution to a problem.

"We work with hundreds of companies," Nemerson adds, "with brilliant solutions to a problem that no one can identify."

The concept for Higher One began to coalesce in 1999, in discussions among Volchek, Lasater and Glass about the Yale Entrepreneurial Society's inaugural student business-plan



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competition.

"We were telling other folks to do business plans, and thought, 'Why don't we do one ourselves?'" recalls Volchek, 30, Higher One's chairman and chief financial officer. At the time he was earning a bachelor's and master's degree in economics at Yale. Lasater was studying computer science, and Glass was majoring in electrical engineering.

Over time, the Yale undergraduates zeroed in on what they perceived as several converging trends.

"One of the things we noticed was students used their ID cards for almost everything, including on-campus purchases, but few off-campus stores accepted the card," says Lasater, 30, Higher One's chief operating officer. "Seeing potential in the convenience and power of using that card, we thought, 'How can we make this bigger and better?'"

"We also were watching what was happening on the Internet, where financial services were beginning to be established online," Lasater adds. "We believed, and it's proving out now, that this would be embraced, and we were excited by the possibility from a business perspective and student perspective."

Consulting with several university chief financial officers, the budding entrepreneurs learned that most schools were surprisingly inefficient at refund disbursement.

"We came to understand it was really an unmet need, to move money from universities to students for things like financial aid and payroll, and from students and parents to the university, for tuition and payment," Lasater says.

"And that was the genesis of the idea," says Volchek. "Trying to make it easy for students to get money and spend it using their ID cards."

Joseph Mullinix remembers meeting Volchek, Lasater and Glass in those days, when he was Yale's vice president for finance and administration.

"We talked a lot about what was the target market and what colleges and universities would be interested in working with them," says Mullinix, who today is deputy president of administration at the National University of Singapore.

The conversations also centered on what kinds of products might be interesting to students and administrators, and the decision-making method at universities, which Mullinix describes as "a collaborative process, with people from different offices looking at things from different perspectives."

"I tried to give them some ideas," he says, "about what types of institutions, and which people in the administrative chain were likely to be most responsive."

Mullinix advised the undergrads to be patient, telling them, "Just because you haven't gotten an immediate 'yes' doesn't mean it is a 'no.'"

"Initially I was impressed by their enthusiasm," Mullinix recalls.

"But the more I met with them I was very, very impressed with their willingness to stick with this project for the long term and their commitment to success."

The three undergraduates also impressed David Cromwell, an adjunct professor of entrepreneurship at the Yale School of Management (SOM) and faculty advisor to SOM's Sachem Ventures, then a small venture capital fund for student enterprises.

"We were one of the first investors in Higher One, before they had any customers, and through that investment I became a member of their board of directors," says Cromwell, who spent six years as president and CEO of JPMorgan Capital Corp., the banking company's private equity investment group. "We thought their idea was good, but our main bet was on the people - as it always is. Can these guys pull it off? And we thought they could do it. They're very, very bright, hard-working and earnest, with very high levels of integrity."

\dropcap\From the outset, Volchek, Lasater and Glass "were very close as a working team, which impressed me, because when you have a group where there is a bond, it dramatically increases the chances of success," says attorney Frank Marco, the Wiggin & Dana partner who incorporated their company, originally known as UNECT, in March 2000. (The name was changed to Higher One, reflecting the company's focus on the higher education market.)

"They struck me back then as rising above the pack with their vision and drive," adds Marco, who specializes in emerging companies.

Start-ups, he observes, have "several mountains to climb.

"Obviously, you've got the technology mountain, the challenge of making the concept for the company work," Marco says. "Then there's the management team, who all should be rowing the boat in the same direction. You've got your capital hurdles: You can have the best idea in the world but are you going to get the funding for it? Then the marketing hurdle - is anyone going to buy it? - and getting it into the market through all the right channels."

Higher One's management team confronted the challenges, one by one.

In 2002, the company recruited and hired Dean Hatton as its president and CEO, shortly after signing its first client, the University of Houston.

"They had reached a point in development of the company when they wanted to start raising institutional money," says Hatton, 47. "And in doing so they knew they would need to reach out and hire some experienced management."

Hatton's experience included a stint as president and CEO of Yclip Inc., a direct marketing promotion company he sold to First Data Corp., executive vice president and COO of Carlson Wagonlit Travel, and senior vice president at Citigroup, where he was CEO of Travelers Property Casualty Direct.

"It was really a good fit right from the start," he says. "I also had spent 15 years in banking, most in direct banking, dealing directly with consumers, and had done some [product and distribution] assignments at Travelers."

"We also had good chemistry and complementary management styles, which divided up early on from a matter of interest, although we've always overlapped from a perspective of managing the corporation," Hatton adds. "Mark was interested in financial, legal and negotiation, Miles in operations and technology, and

Sean in marketing."

\dropcap\When Hatton signed on, the company hadn't progressed much beyond the concept stage and "didn't even" have a bank partner.

"We knew what we wanted to do and had to do," Hatton says. "We first had to build the technology platform to reach out to universities and students, and most of the early time was spent on that. We had to build a customer-service infrastructure, and we had to build a sales model and a sales team.

"And, of course, we had to raise money to make this happen." To date, Higher One has raised around \$17 million from angel investors and venture capitalists.

The company moved as it grew, from its first "office," in Lasater's Blake Place apartment, a place furnished with "\$4 plastic chairs and tables made of cinderblocks and countertop pieces," to 59 Elm Street and then to 122 Court Street. In 2004, Higher One relocated to 25 Science Park, where it occupies 30,000 square feet, and is negotiating for an additional 15,000 square feet at the same location.

"We continued to sign up clients over the years and launch innovations," Lasater says, such a payroll service for universities and a service enabling parents to send students money for free from any U.S. bank account.

Higher One's flagship products include OneDisburse, a refund-management disbursement service of university funds, and OneFinance, a set of banking services including a no-minimum-balance, no-monthly-fee checking account with OneCard, a debit MasterCard for ATM withdrawals and purchases.

The latest innovation, which Higher One is piloting, is OnePay, which allows students and parents to make tuition payments using any checking account or credit card.

The company also has broken ground working with state and federal regulators on novel ways verify student IDs.

"Banks check people's IDs when they come in to open an account, but we had to do that differently, developing ways for students to upload their IDs using a third-party database," Volchek says. The company has 150 employees, including 110 full-time and 40 part-time (in customer service), according to Volchek, who expects more hiring in 2008, but for fewer full-time positions.

Higher One today has "partnerships" with 94 colleges and universities (none in Connecticut) and has dispensed about \$2.3 million in disbursements to nearly one million students and faculty.

"Our revenues are similar to how banks makes money," Volchek explains, based on things like card transaction fees and miscellaneous banking fees, including foreign ATM fees, stop-payment fees, wire transfers and bad checks.

Hatton will not reveal how much Higher One earned in 2006, its first year of profitability, but acknowledges the amount was less than the \$2 million profit reported in a local press account.

"In 2007, we've just about doubled revenue from 2006, and more than tripled profitability," he says. "For 2008, we think that we will grow substantially but won't quite double revenue. We should grow around 75 percent, while profitability will certainly more than double again."

In 2007, Higher One ranked No. 85 on Inc. magazine's list of the 5,000 fastest-growing companies in America - and No. 6 in the financial-services industry. Inc. reported company revenue as \$894,759 in 2003 and \$16.5 million in 2006.

Higher One also was named a "Rising Star" in Deloitte & Touche USA's 2006 Technology Fast 50 program for Connecticut. The award honors the state's fastest-growing companies based on aggregate revenue growth over three years (2004 to 2006).

Such a track record opens up all sorts of options.

"Becoming public is a possibility, but we can't rule out any possibility," Hatton says. "Certainly there have been people interested in our company; we've grown quickly and we provide a service nobody else does.

"We get interest from strategic partners all the time."

Yale SOM professor Cromwell says Higher One's growth has been remarkably trouble-free.

"The business, because of its nature, is highly unpredictable," he says, "and these guys have done better than any venture group I have ever seen at hitting their financial plans. They feel awful if they're off by one percent.

"They have never lost a client," Cromwell adds. "Clients renew, so you know what the revenues and profit were for last year, and you've got a predictable cash flow."

There have been a few glitches.

Volchek recalls an uncomfortable moment he and his colleagues had to inform their first client about a sudden change of plan.

"We thought we would be working with VISA and had printed up marketing materials," Volchek says, "but we signed with MasterCard, which was more flexible for us."

Hatton contends that Higher One's innovativeness is embedded in its corporate culture.

"We have this belief that there is a way to figure anything out," he says. "On top of that we have a very collaborative environment. Ideas come from anywhere in the company and we build on them."

Last November, for example, Higher One launched a new service, sending students a text message on their cell phone when financial-aid money became available in their account. Hatton says the service was based on an idea sent to the company's online suggestion box from a business-development employee.

"We also get a lot of ideas from the people in customer service, on how to improve efficiency or the work environment."

Innovations also stem from schools asking for new services.

Hatton describes Higher One as "very open since the very beginning.

"We've shared financials with the entire company, which is a bit unusual but it's worked well for us," he says. "At quarterly all-hands meetings, we review financials - anything we're not prevented from sharing or shouldn't because of common sense. And every employee has stock options."

Community service is an important part of the overall company package, too.

In March 2007, New Haven Mayor John DeStefano Jr. appointed Volchek to the city of New Haven's Development Commission. He also is chairman of the Tweed New Haven Airport Authority (chosen in September 2007 to replace Lawrence J. DeNardis).

Lasater is a member of the Port Authority of New Haven and is on Yale's Advisory Committee on Investor Responsibility.

Glass, who left his post as Higher One's chief marketing officer in January 2008 to work on a new business venture in London, is on the Connecticut Technology Council board.

"It's great to see everybody involved," Nemerson says, which shows how new companies "can be serious and important civic players - and a great role model for Yale and New Haven."

Mayor DeStefano thinks so, too.

"Seeing people like Mark Volchek stepping up to leadership in the New Haven community is a great template for what else could happen here," DeStefano says, adding he envisions more business startups from the university, "and not just in the life sciences."

Higher One seems poised to build on its success, developing more innovative products to enhance and expand its core market.

At the moment, Hatton says, the company is "primarily focused on signing up more universities" and launching the OnePay product. Cromwell offers a broader perspective.

"Sooner or later we're going to go public or somebody will buy the company," he says. "And these guys are going to get very

rich."