HEARTLAND PAYMENT SYSTEMS INC
Form 10-K
March 02, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2014

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File No. 001-32594

HEARTLAND PAYMENT SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Delaware	22-3755714
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

90 Nassau Street, Princeton, New Jersey 08542
(Address of principal executive offices) (Zip Code)
(609) 683-3831
(Registrant's telephone number, including area code)

Securities registered pursuant to 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $0.001 par value	New York Stock Exchange

Securities registered pursuant to 12(g) of the Act:

(NONE)
(title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. x YES o NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. o YES x NO

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
x YES o NO
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x YES o NO

Indicate by check mark if disclosure of delinquent filer pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o YES x NO

The aggregate market value of the voting and non-voting common stock held by non-affiliates computed by reference to the price at which the common stock was last sold on the New York Stock Exchange on June 30, 2014 was approximately $1.5 billion.
As of February 23, 2015, there were 36,400,265 shares of the registrant’s Common Stock, $0.001 par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE
Specifically identified portions of the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the 2015 annual meeting of shareholders are incorporated by reference into Part III of this Annual Report on Form 10-K for fiscal year ended December 31, 2014.

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Heartland Payment Systems, Inc.
Annual Report on Form 10-K
For the Year Ended December 31, 2014

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FORWARD LOOKING STATEMENTS

Unless the context requires otherwise, references in this Annual Report on Form 10-K to “the Company,” “we,” “us,” and “our” refer to Heartland Payment Systems, Inc. and its subsidiaries.

Some of the information in this report may contain forward-looking statements that are based on our management's beliefs and assumptions and on information currently available to our management. Forward-looking statements include the information concerning our possible or assumed future results of operations, financial condition and prospects, business strategies, financing plans, competitive position, industry environment, potential growth opportunities, the effects of future regulation and the effects of competition. Forward-looking statements include all statements that are not historical facts and can be identified by the use of forward-looking terminology such as the words “anticipate,” “believe,” "estimate," “expect,” “intend,” “plan,” "predict," "will be," "will continue" or similar expression

Forward-looking statements involve risks, uncertainties and assumptions. Actual results may differ materially from those expressed in the forward-looking statements. You should understand that many important factors, in addition to those discussed elsewhere in this report, could cause our results to differ materially from those expressed in the forward-looking statements. Certain of these factors are described in Item 1A. Risk Factors and include, without limitation, unauthorized disclosure of user data through breaches of our computer systems or otherwise, our failure to comply with the applicable requirements of the Visa and MasterCard bankcard networks, our competitive environment, the business cycles and credit risks of our merchants, chargeback liability, merchant attrition, reliance on and problems with our sponsor banks, our relationships with third-party bankcard payment processors, our inability to pass increased interchange fees, assessments, and transaction fees along to our merchants, economic conditions, systems failures and government regulation.

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PART I.

ITEM 1. BUSINESS

Overview of Our Company

Heartland Payment Systems, Inc.
90 Nassau Street, Princeton, NJ 08542
(609) 683-3831

Our primary business is to provide Payment Processing services to merchants throughout the United States. This involves providing end-to-end electronic payment processing services to merchants by facilitating the exchange of information and funds between them and cardholders' financial institutions. To accomplish this, we undertake merchant set-up and training, transaction authorization and electronic draft capture, clearing and settlement, merchant accounting, merchant assistance and support, and risk management. We also sell and rent point-of-sale ("POS") devices. Our card-accepting customers primarily fall into two categories: small and mid-sized merchants (referred to as "Small and Midsized Enterprises," or “SME merchants”) and Network Services merchants, which are predominantly petroleum industry merchants of all sizes (referred to as “Network Services merchants”).
We provide additional services in our other business segments such as:

- Integrated commerce solutions, payment processing, higher education loan services and open and closed-loop payment solutions to higher-education institutions through Campus Solutions,
- School nutrition, POS solutions, and associated payment solutions, including online prepayment solutions, to kindergarten through 12th grade ("K-12") schools through Heartland School Solutions,
- Full-service payroll processing and related tax filing services, through Heartland Payroll Solutions,
- Other including (1) prepaid and stored-value card solutions through Micropayments, (2) POS solutions and other adjacent business service applications through Heartland Commerce and (3) marketing solutions including loyalty and gift cards which we provide through Heartland Marketing Solutions.

We were incorporated in June 2000, in the state of Delaware. As of December 31, 2014, we employed 3,734 full- and part-time personnel, including 1,154 sales professionals, 748 customer service, risk management, financial and operations support and underwriting employees, 439 systems and technology employees, 346 Heartland Payroll Solutions employees, 214 Heartland School Solutions employees, 396 Campus Solutions employees (including 179 employees who were added by our acquisition of TouchNet Information Systems, Inc., further discussed below), 193 accounting and administration employees, 38 Micropayments employees, and 206 Heartland Commerce employees (including 125 employees who were added by our acquisition of Xpient Solutions, LLC, further discussed below). Our sales professionals include 911 Relationship Managers and Territory Managers and 74 Senior Product Advisors, primarily payroll specialists. None of our employees were represented by a labor union, and we have experienced no work stoppages. We consider our employee relations to be good.
General Business Developments
Acquisitions
Campus Solutions
On September 4, 2014, we completed the acquisition of TouchNet Information Systems, Inc. (“TouchNet”), an integrated commerce solutions provider to higher-education institutions for a cash payment of $375 million, less a net working capital deficit, for all outstanding common shares. The purchase was funded primarily with a new five year, $375 million secured term loan. See “Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Credit Facilities,” for further discussion. TouchNet added over 600 higher education clients serving more than 6 million students, nearly one-third of the higher education enrollment in the United States.

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Heartland School Solutions

On April 1, 2014, we purchased the net assets of MCS Software Corporation ("MCS Software") for a $17.3 million cash payment. The purchase price was funded from a combination of operating cash and financing under our revolving credit facility. This acquisition further expanded our market-leading position in the K-12 school nutrition and POS technology industry.

Heartland Commerce

On October 31, 2014, we acquired the net assets of Xpient Solutions, LLC (“Xpient”) for a cash payment of $30.0 million, plus net working capital. The purchase price was funded from a combination of operating cash and financing under our revolving credit facility. Xpient provides POS software solutions to customers primarily in the food service industry.

On February 15, 2014, we purchased the assets of Merchant Software Corporation (referred to as "Liquor POS") for a $3.3 million cash payment. The purchase price was funded from operating cash flows. Liquor POS is a leading provider of POS systems to the liquor retail vertical and currently serves more than 3,400 merchants to whom we expect to offer additional products and services.

On September 11, 2013, we purchased 66.67% of the outstanding capital stock of Leaf Holdings, Inc. (“Leaf”) for a $14.5 million cash payment. The purchase price was funded from operating cash flows. Leaf provided us with a software-as-a-service (SaaS) POS system to deliver an open-architecture platform with the possibility of supporting numerous vertical-specific business applications. Leaf product development was aimed at providing a mobile payment platform built for local commerce, helping retail stores, restaurants, and other local merchants improve the speed and ease of checkout by offering easy-to-use business management, analytics, and customer engagement. On August 6, 2014, we entered into a Stock Purchase Agreement with the noncontrolling shareholders of Leaf under which we acquired all shares of Leaf common stock held by the noncontrolling shareholders. As a result of this transaction, Leaf became our wholly-owned subsidiary.

Heartland Commerce is comprised of existing POS businesses; Xpient, Liquor POS, Leaf and our other POS solutions, and will include the recently acquired POS businesses Automation, Inc. (d/b/a “pcAmerica” in January 2015) and Dinerware, Inc. (“Dinerware” in February 2015). Dinerware and pcAmerica are in the process of developing cloud-based POS systems that complement their well-established on-premise POS solutions. These cloud-based POS systems overlap with what was being developed by Leaf, and Dinerware and pcAmerica technologies and development plans provided insight into the status and positioning of Leaf’s technology in the marketplace. Consequently, management decided that it will stop POS development efforts at Leaf, and write down related POS assets.

Separately, we determined that our investment in TabbedOut, a mobile payments provider, was substantially impaired as of December 31, 2014 and recorded an impairment charge of $4.0 million related to that investment. In the fourth quarter ended December 31, 2014, we recorded total asset impairment charges of $41.4 million pre-tax, ($37.6 million after-tax, or $1.02 per share), related to the values ascribed to our investments at Leaf and in Prosper, an internally developed POS software technology, and our investment in TabbedOut.

Business Segment Overview

Payment Processing
Performance Update

At December 31, 2014, we provided our card payment processing services to 169,831 active SME merchants located across the United States. This compares to 166,697 active SME merchants at December 31, 2013. At December 31, 2014, we provided card payment processing services to approximately 2,181 Network Services merchants with approximately 42,397 locations, compared to 1,024 Network Services merchants with 42,669 locations at December 31, 2013.

Our total card processing volume for the year ended December 31, 2014 was $109.9 billion, a 7.4% increase from the $102.3 billion processed during the year ended December 31, 2013. Our SME card processing volume for the year ended December 31, 2014 was $81.1 billion, an 8.7% increase over $74.6 billion in 2013. Total card processing volume for 2014 also included $28.8 billion of settled volume for Network Services merchants, compared to $27.7 billion for 2013.

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In addition to settling card transactions, Network Services processes a wide range of payment transactions for its predominantly petroleum customer base, including providing 2.4 billion transaction authorizations (primarily for Visa and MasterCard) through its front-end card processing systems in 2014.

According to The Nilson Report, in 2013 we were the 5th largest merchant acquirer in the United States ranked by transaction count and the 9th largest merchant acquirer by processed dollar volume, which consisted of Visa, MasterCard, and Discover signature debit cards, and Interlink, Maestro and other PIN-based debit cards, in addition to Visa, American Express, MasterCard, Discover, Diners Club, Union Pay, and JCB credit cards. These rankings represented 3.5 billion transactions and 3.0% of the total U.S. bankcard processed dollar volume, respectively.

The following table summarizes revenue, net revenue (which we define as total revenue less interchange fees and dues, assessments and fees) and operating income for Payment Processing for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December 31,		
	2014	2013	2012
	(In thousands)		
Revenue	$2,111,487	$1,979,579	$1,922,154
Net revenue	472,731	443,189	438,613
Operating income	127,553	138,226	124,627

Business Structure

Our Payment Processing revenue from SME merchants and Network Services merchants is recurring in nature. We typically enter into three-year service contracts with our SME merchants and three-to-five-year agreements with Network Services merchants.

Most of our SME revenue is from fees for processing transactions, which are primarily a combination of a percentage of the dollar amount of each card transaction we process, a flat fee per transaction and monthly fees for services. We make mandatory payments of interchange fees to card issuing banks through card networks and dues, assessments and transaction authorization fees to Visa, MasterCard and Discover, and we retain the remainder as net revenue. For example, in a transaction using a Visa or MasterCard card, the allocation of funds resulting from a $100 transaction follows.

In contrast, our processing revenues from Network Services merchants generally consist of a flat fee per transaction, thus revenues are driven primarily by the number of transactions we process (whether settled or only authorized), not card processing volume.

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Our Merchant Base

We have developed significant expertise in industries that we believe present relatively low risks as the consumers are generally present and the products or services are generally delivered at the time the transaction is processed. These include:

- Restaurants
- Brick-and-mortar retailers
- Hotel and lodging
- Automotive sales and repair shops
- Convenience and liquor stores
- Professional service providers
- Gas stations

Generally, we define SME merchants as generating annual Visa and MasterCard card processing volume between \$50,000 and \$5,000,000. However, with the added functionality and cost benefits that our in-house processing platforms afford us, we also market to merchants with annual processing volume above \$5,000,000.

The following table summarizes our SME processing volume by merchant category for the month of December 2014, compared to the months of December 2013 and December 2012.

	Month of December		
	2014	2013	2012
Restaurants	35.1%	35.2%	36.0%
Retail	17.9%	17.8%	18.0%
Convenience, Fast Food & Liquor	11.4%	11.0%	11.2%
Professional Services	7.3%	7.4%	7.3%
Automotive	6.7%	6.8%	6.5%
Lodging	4.5%	4.6%	4.5%
Petroleum	1.6%	1.9%	1.9%
Other	15.5%	15.3%	14.6%
Total SME processing volume	\$6.6 billion	\$5.9 billion	\$5.7 billion

No single SME merchant accounted for more than 0.41% of our total SME Visa and MasterCard card processing volume in 2014, and during 2014, our top 25 SME merchants represented only 3.40% of our SME Visa and MasterCard card processing volume and 2.84% of our SME Visa and MasterCard gross processing revenue. In 2014, approximately 89% of our SME card processing volume came from merchants we installed in 2013 and earlier.

In December 2014, SME merchants located in the following states represented the following percentages of our SME card processing volume: California represented 10.7%, Texas represented 7.7%, Florida represented 4.8%, New York represented 4.7%, and Ohio represented 3.6%, respectively. No other state represented more than 3.5% of our total SME card processing volume. Our geographic concentration tends to reflect the states with the highest economic activity, as well as certain states where we have historically maintained a stronger sales force. This merchant and geographic diversification makes us less sensitive to changing economic conditions in any particular industry or region. We believe that the loss of any single SME merchant would not have a material adverse effect on our financial condition or results of operations.

Payment Processing Platforms

We have developed a number of proprietary payment processing systems to increase our operating efficiencies and customize our product offerings. These include:

- HPS Exchange, VAPS and NWS, our internal front-end authorization systems, provide authorization and data capture services that distribute processing and merchant data to card networks, merchants, and our sales force and customer service staff. These systems provide us greater control of the electronic transaction process, allow us to offer our merchants a differentiated product offering, and offer economies of scale that we expect will increase our long-term profitability.

HPS Exchange, VAPS and NWS enable us to provide more customized solutions to merchants that demand customized front-end solutions and take advantage of new terminal hardware platforms and technology like our end-

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to-end encryption solution (included in our Heartland Secure solutions), as well as near field communication ("NFC") and Europay, MasterCard and Visa (“EMV”) authentication standards. HPS Exchange, VAPS and NWS offer our merchants authorization and capture services in multiple industry verticals to a variety of POS systems including legacy terminals, petroleum pumps, middleware technologies, PC-integrated POS systems and web-based virtual terminals. In addition, HPS Exchange, VAPS and NWS offer third-party POS developers multiple protocols to meet their needs for integration.

During 2014, approximately 96% of the transactions of our SME merchants were processed on HPS Exchange, and 98% of all SME merchant accounts established in 2014 were placed on the system. During 2014, 100% of the transactions for our Network Services merchants were processed on VAPS or NWS.

- Passport, our internally developed back-end processing system, provides one settlement platform for SME merchants and Network Services merchants, providing value-added features such as Optimized Funding, multi-bank Next Day Funding, automated dispute resolution, advanced interchange management and single portal integration via InfoCentral. In addition, Passport generates significant cost savings and allows us greater economies of scale, by replacing third-party processors' per-transaction charges with more of a fixed-cost structure. This structure allows per-transaction savings as increasing numbers of transactions are processed on Passport. In addition, Passport provides us the opportunity to offer our merchants significantly greater amounts of information regarding their processing characteristics, in more usable formats, and to offer our services to larger merchants. At December 31, 2014 and 2013, substantially all of our SME merchants were processing on Passport, and all of our Network Services settlement merchants were processing on Passport.

Security, Disaster Recovery and Back-up Systems

In the course of our operations, we compile and maintain a large database of information relating to our merchants and their transactions, and large amounts of card information cross our network as we authorize transactions. We have placed significant emphasis on maintaining a high level of security in order to attempt to protect the information of our merchants and their customers. We maintain current updates of network and operating system security releases and virus definitions, and have engaged a third party to regularly test our systems for vulnerability to unauthorized access. Further, we encrypt the cardholder numbers and merchant data that are stored in our databases using what we believe are the strongest commercially available encryption methods.

Our internal network configuration provides multiple layers of security to isolate our databases from unauthorized access and implements detailed security rules to limit access to all critical systems.

Visa, STAR, NYCE and other debit card networks have established security guidelines for PIN-based debit transaction processing that is based upon ANSI standards that are published as the “ASC X9 TG-3 Retail Financial Services Compliance Guideline; Part 1: PIN Security and Key Management.” We have a regularly scheduled Security Review of our Key Management Procedures against this standard that is performed by an external auditor.

We also have engaged external auditors to perform an annual Standards for Attestation Engagements No. 16 ("SSAE 16") review and make available the “Report on Controls Placed in Operation and Tests of Operating Effectiveness.”

We operate our front-end processing, back-end processing, and other product platforms in two geographically dispersed outsourced data centers located in Texas and California. We establish system service level operational thresholds based on our large national merchants' requirements, and regularly exceed those levels, with system availability of greater than 99.9%. To achieve this standard, transactions are mirrored between the two data centers, and each center has the capacity to handle our full merchant transaction load. This duplicate processing capability ensures uninterrupted transaction processing during maintenance windows and other times processing may not be available. We regularly process through both data centers.

Sponsor Banks

Because we are not a "member bank" as defined by Visa and MasterCard, in order to process and settle these bankcard transactions for our merchants, we have entered into sponsorship agreements with member banks. Visa and

MasterCard rules restrict us from performing funds settlement or accessing merchant settlement funds and require that these funds be in the possession of the member bank until the merchant is funded.

A sponsorship agreement permits us to route Visa and MasterCard bankcard transactions under the member bank's control and identification numbers to clear credit and signature debit bankcard transactions through Visa and MasterCard. A sponsorship agreement also enables us to settle funds between cardholders and merchants by delivering funding files to the

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member bank, which in turn transfers settlement funds to the merchants' bank accounts. These restrictions place the settlement assets and liabilities under the control of the member bank.

The sponsorship agreements with the member banks require, among other things, that we abide by the bylaws and regulations of the Visa and MasterCard networks. If we were to breach a sponsorship agreement, the sponsor banks can terminate the agreement and, under the terms of the agreement, we would have 180 days to identify an alternative sponsor bank. As of December 31, 2014, we have not been notified of any such issues by our sponsor banks, Visa or MasterCard.

At December 31, 2014, we were party to three bank sponsorship agreements.

- Our primary sponsor bank for SME merchant processing is Wells Fargo Bank, N.A. (“Wells Fargo”). Either Wells Fargo or we can terminate the agreement if the other party materially breaches the agreement, including non-payment of fees due for processing our monthly settlement of transactions. The agreement may also be terminated if the other party files for or enters bankruptcy, if either party is required to discontinue performing its services under the agreement based upon a final order of a state or federal court or regulatory body or if there is a change in the majority ownership of the other party. Wells Fargo may terminate the agreement with us if we breach the by-laws and regulations of Visa or MasterCard, if either our registration or Wells Fargo's membership with Visa or MasterCard terminates, if any federal or state regulatory authority requests that the agreement be terminated or that Wells Fargo terminate its services or if applicable laws or regulations change to prevent Wells Fargo from performing its services under the agreement. Upon termination of the agreement for any reason, we will have 180 days to convert to another sponsor bank. The agreement, which we entered into with Wells Fargo on February 8, 2012, expires on February 8, 2016 and will automatically renew for successive three-year periods unless either party provides six months written notice of non-renewal to the other party. The sponsorship agreements we have with our other two sponsor banks involve substantially the same terms as apply with Wells Fargo.

- In November 2009, we entered into a sponsorship agreement with The Bancorp Bank ("TBB") to sponsor processing for our Network Services merchants and, as of October 2013, certain of our SME merchants. The agreement with TBB expires in February 2016 and will automatically renew for successive one-year periods unless either party provides six months written notice of non-renewal to the other party.

- On March 24, 2011, we entered into a sponsorship agreement with Barclays Bank Delaware to sponsor processing for certain of our Network Services merchants. The agreement with Barclays Bank Delaware expires in March 2016 and will automatically renew for successive one-year periods unless either party provides six months written notice of non-renewal to the other.

Following is a breakout of our total Visa and MasterCard settled card processing volume for the month of December 2014 by percentage processed under our individual bank sponsorship agreements:

Sponsor Bank	% of December 2014 Card Processing Volume
Wells Fargo Bank, N.A.	70%
The Bancorp Bank	21%
Barclays Bank Delaware	9%

Customer Acquisition

Unlike many of our competitors who rely on Independent Sales Organizations or salaried salespeople and telemarketers, we have built a direct, primarily commission-based, sales force. Our sales model divides the United States into seven primary markets overseen by Senior Vice Presidents and Vice Presidents of Sales. These Vice Presidents are responsible for hiring Relationship Managers and increasing the sales of our products in their markets. We measure the overall production of our sales force by new gross margin installed, which reflects the expected annual gross profit from a merchant contract after deducting processing and servicing costs associated with that revenue. We measure installed margin primarily for our SME card processing, payroll processing and loyalty and gift card marketing businesses. In 2014, our newly installed gross margin for the year increased 17% from the gross margin we installed during the year ended December 31, 2013 compared to an increase of 22% in 2013. We attribute this increase in newly installed gross margin to higher volumes and margins at newly installed merchants and improved individual productivity achieved by our salespersons as well as growth in the sales force. Our combined Relationship Managers, Territory Managers, and Senior Product Advisors ("SPAs") amounted to 985 and 902 at December 31, 2014 and 2013, respectively. We expect to drive

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increases in year-over-year installed margin in future periods primarily by increasing the number of SPAs and Relationship and Territory Managers.

We designed our sales force compensation structure to motivate our Relationship Managers to establish profitable long-term relationships with low-risk merchants and create a predictable and recurring revenue stream. Compensation for Relationship Managers is entirely commission-based, with commissions paid as a percentage of the financial value of new merchant accounts installed, which is measured in terms of the annual gross margin we estimate we will receive from the merchant accounts installed. This is calculated by deducting the cost of processing (on a per-transaction basis) and servicing (measured in dollars per month) from the expected first-year net revenue the account is expected to generate.

The Relationship Manager and SPA generally will be paid a signing bonus equal to 50% of the first 12 months' estimated gross margin. The Relationship Manager and SPA will also receive, beginning the month installed, 15% of the gross margin generated from the merchant each month as residual commissions for as long as the merchant remains our customer.

In addition, the Division Manager will receive an amount equal to 25% of the amount paid to the Relationship Manager (split with a Territory Manager, if one exists for the account). The Vice Presidents will receive an amount equal to 25% of the amount paid to the Division Manager. For example, if a merchant account has $1,000 of estimated annual gross margin for the first 12 months and estimated monthly gross margin of $83.33, our sales force would be compensated as follows:

Signing Bonus:			
Estimated gross margin for first 12 months	$1,000		
Signing bonus paid to:			
Relationship Manager /SPA	$500	50.0	%
Division Manager (plus Territory Manager)	$125	12.5	%
SVP/VP	$31	3.13	%
Residual Commission:			
Estimated monthly gross margin	$83.33		
Monthly residual commission paid to:			
Relationship Manager /SPA	$12.50	15.0	%
Division Manager (plus Territory Manager)	$3.12	3.75	%
SVP/VP	$0.78	0.94	%

Marketing

Our marketing efforts have historically focused on industry verticals and marketing partnerships. We focus our marketing efforts on industries in which we believe our direct sales model is most effective and on merchants with certain key attributes. These attributes include owners who are typically on location, interact with customers, value a local sales presence, and consult with trade associations and other civic groups to make purchasing decisions.

We also determine which additional markets to enter into based on the following criteria:

- Average potential customer revenue;
- Number of locations to be serviced;
- Underwriting risk; and
- Required technological upgrades.

We have focused significantly on the hospitality industry and, in particular, independent restaurants. The number of restaurants to which we provide our payment processing services was approximately 42,000 as of December 31, 2014. We have also historically had success in marketing our products and services through relationships with key trade associations, agent banks and value-added resellers.

As of December 31, 2014, we had preferred partner agreements with more than 269 trade associations, approximately 38 percent of which are in the hospitality industry. Of these partnerships, 48 are state restaurant associations and another 40 are state lodging associations. In addition, we were the American Hotel & Lodging Association's and National Restaurant Association's endorsed provider for credit card processing, gift card marketing and payroll services.

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In exchange for an association's endorsements and recommendation of our products and services to their members, and upon the installation of a new merchant that is a member of the association, we pay to the trade association a signing bonus and residual commission.

We offer programs to banks across the United States that allow them access to leverage our extensive sales and support teams and other resources. The program provides our partner banks a source to refer their customers for merchant services as well as payroll processing and other electronic payment processing services. We offer on-site sales, training, installation, and ongoing service and support to the referred merchants. In exchange for a bank's endorsement of our products and services, we typically pay the bank a monthly residual fee based on the referred merchant's processing volumes or margin. As of December 31, 2014, we provide these services to more than 1,539 banking locations in the United States.

In order to further market our products and services, we enter into arrangements with value-added resellers and third-party software developers. Value-added resellers typically sell complementary products and services such as hardware and software applications and POS hardware, software and communication network services to merchants in markets similar to ours. Our agreements with value-added resellers provide that, in exchange for their endorsement of our products and services and upon the installation of a new merchant referred by them, we will pay the value-added reseller a portion of the sales commission from the Relationship Manager responsible for that merchant and/or a transaction fee.

As we continue to expand our product offerings, we intend to introduce capabilities that will allow our systems to be compatible with third-party software developers while working to reduce merchants' third-party up-front costs for processing with us. We are committed to passing along our cost efficiencies to our merchants and their POS providers to encourage joint technology partnerships.

Merchant and Transaction Risk Management

We focus our sales efforts on low-risk bankcard merchants and have developed systems and procedures designed to minimize our exposure to potential merchant losses.

We have developed significant expertise in industries that we believe present relatively low risks as the customers are generally present and the products or services are generally delivered at the time the transaction is processed. These industries include restaurants, brick-and-mortar retailers, professional service providers, convenience and liquor stores, automotive sales and repair shops, gas stations, lodging establishments and others. The following table summarizes our SME merchants by industry as of December 31, 2014.

Restaurants	24.7%
Retail	18.7%
Professional Services	12.8%
Convenience, Fast Food & Liquor	11.4%
Automotive	7.7%
Lodging	3.1%
Petroleum	1.7%
Other	19.9%

Effective risk management helps us minimize merchant losses relating to chargebacks, reject losses and merchant fraud for the mutual benefit of our merchants and ourselves. We believe our knowledge and experience in dealing with attempted fraud has resulted in our development and implementation of effective risk management and fraud prevention systems and procedures for the types of fraud discussed in this section. In 2014, 2013 and 2012, we experienced merchant losses of $7.3 million, $3.1 million and $2.0 million, respectively, or 0.90 basis points, 0.41 basis points and 0.28 basis points, respectively, of our SME card processing volume. In 2014, our losses included $4.6 million resulting from chargebacks from a single merchant who entered bankruptcy in the fourth quarter.

We employ the following systems and procedures to minimize our exposure to merchant and transaction fraud:
Underwriting. Our sales force sends new applications to their regional service team for scoring and account set up. Higher-risk applications are routed to our credit underwriting department for review and screening. Our underwriting department's review of these applications serves as the basis for our decision whether to accept or reject a merchant account. The review also provides the criteria for establishing cash deposit or letter of credit requirements, processing limits, average transaction amounts and pricing, which assists us in monitoring merchant transactions for those accounts that exceed those pre-determined

thresholds. The criteria set by our underwriting department also assist our risk management staff in advising merchants with respect to identifying and avoiding fraudulent transactions. Depending upon their experience level, our underwriting staff has the authority to render judgment on new applications or to take additional actions such as adjusting processing limits supported by prior processing history, analyzing average charge per transaction information or establishing cash deposits/letters of credit, reserves, and delayed funding requirements for new and existing merchants. Our underwriting department prepares accounts that are risk-sensitive for our Credit Committee review. The Credit Committee consists of a Manager of Underwriting, Manager of Risk Review, Director of Underwriting and Vice President of HSC Operations. Merchant accounts that exceed certain committee thresholds are reviewed by our CEO, Vice Chairman or Chief of Operations. Our sponsor banks also review and approve our merchant underwriting policies and procedures to ensure compliance with Visa and MasterCard operating rules and regulations.

Merchant Monitoring. We employ several levels of merchant account monitoring to help us identify suspicious transactions and trends. Daily merchant activity is sorted into a number of customized reports by our systems. Our risk management team reviews any unusual activity highlighted by these reports, such as larger than normal transactions or credits, and monitors other parameters that are helpful in identifying suspicious activity. We have daily windows to decide if any transactions should be held for further review, which provides us time to interview a merchant or issuing bank to determine the validity of suspicious transactions. We have also developed a fraud management system for HPS Exchange that is fully integrated with our internal customer relationship management software and has detailed review capabilities to further streamline our monitoring of those transactions. We also place merchants who require special monitoring on alert status and have engaged a web crawling solution that scans all merchant websites for content and integrity.

Investigation and Loss Prevention. If a merchant exceeds any parameters established by our underwriting and/or risk management staff or violates regulations established by the applicable bankcard network or the terms of our merchant agreement, one of our investigators will identify the incident and take appropriate action to reduce our exposure to loss and the exposure of our merchant. This action may include requesting additional transaction information, withholding or diverting funds, verifying delivery of merchandise or even deactivating the merchant account. Additionally, Relationship Managers may be instructed to retrieve equipment owned by us.

Collateral. We require some of our merchants to establish cash deposits or letters of credit that we use to offset against liabilities we may incur. We hold such cash deposits or letters of credit for as long as we are exposed to a loss resulting from a merchant's payment processing activity. In addition, we maintain a five-day delayed deposit policy on transactions processed by our Internet merchants and newly established merchants who have not previously processed bankcards to allow for additional risk monitoring. We also place a “hold” on batches containing questionable transactions, diverting the funds to a separate account pending review. As of December 31, 2014, these cash deposits and delayed and “held” batches totaled approximately $6.2 million.

Industry Overview

The payment processing industry provides merchants with credit, debit, gift and loyalty card and other payment processing services, along with related information services. The industry continues to grow as a result of wider merchant acceptance, increased consumer use of bankcards and advances in payment processing and telecommunications technology. According to The Nilson Report, total expenditures for all card type transactions by U.S. consumers are expected to grow to $6.6 trillion by 2018, representing a compound annual growth rate of 10.0%. The proliferation of bankcards has made the acceptance of bankcard payments a virtual necessity for many businesses, regardless of size, in order to remain competitive. This increased use of bankcards and prepaid cards, payment processing via smart phones, enhanced technology initiatives, efficiencies derived from economies of scale and the availability of more sophisticated products and services to all market segments has resulted in a highly competitive and specialized industry.

The payment processing industry is dominated by a small number of large, fully integrated payment processors that sell directly to, and handle the processing needs of, the nation's largest merchants. These integrated processors serve a broad market spectrum from large to small merchants and some provide banking, ATM and other payment-related services and systems in addition to card payment processing. Large national merchants with multiple locations and high volumes of bankcard transactions typically demand and receive the full range of payment processing services at low per-transaction costs.

SME merchants' payment processing needs generally are served by a large number of smaller payment processors, including banks and Independent Sales Organizations, that generally procure most of the payment processing services they offer from large payment processors. It is difficult, however, for banks and Independent Sales Organizations to customize payment processing services for the SME merchant on a cost-effective basis or to provide sophisticated value-added services.

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Accordingly, services to the SME merchant market segment historically have been characterized by basic payment processing without the availability of the more customized and sophisticated processing, information-based services or customer service that are offered to large merchants. The continued growth in bankcard transactions is expected to cause SME merchants to increasingly value sophisticated payment processing and information services similar to those provided to large merchants. Heartland employees handle all aspects of the merchant’s payments needs, including sales, underwriting and risk management and servicing, as well as ancillary services like equipment deployment and repair and transaction tokenization and encryption services.
We compete with other providers of payment processing services on the basis of the following factors:

- Sales force size and effectiveness
- Range of product offering
- Quality of service
- Reliability of service
- Professional association endorsements
- Ability to evaluate, undertake and manage risk
- Speed in approving merchant applications
- Price
- Brand name

Some of our large competitors have substantially greater capital resources than we have. Others operate as subsidiaries of financial institutions or bank holding companies, which could allow them to own and conduct depository and other banking activities that we do not have the regulatory authority to own or conduct. Further, since they are affiliated with financial institutions or banks, these competitors may not incur the costs associated with being sponsored by a bank for registration with card networks and they can settle transactions quickly for the merchants with a deposit account at the bank. In addition, large, global technology companies are emerging in the non-bankcard payment space.

Competitive Advantage
We believe our competitive strengths related to card payment processing, particularly for SME merchants, include the following:

- Large, Experienced, Efficient, Direct Sales Force

We sell and market our SME card payment processing services through a nationwide direct sales force of 911 Relationship Managers and Territory Managers, and 74 Senior Product Advisors, as of December 31, 2014, who work exclusively for us. Our sales professionals have local merchant relationships and industry-specific knowledge that allow them to effectively compete for merchants. These relationships are also supported by our customer service and support teams located in our service center. We believe our control of sales, underwriting and servicing both enhances our SME merchant retention and reduces our risks. We also believe that internally generated SME merchant contracts generally are of a higher quality and are more predictable than contracts acquired from third parties and the costs associated with such contracts generally are lower than the costs associated with contracts acquired from third parties. Many of our competitors rely on third party distribution channels, including Independent Sales Organizations (“ISOs”) and Value-Added Resellers (“VARs”) that often generate merchant accounts for multiple payment processing companies, maintain ownership of the merchant relationships and may demand, over time, an increasing level of compensation from their processors.

We grow our SME payment processing business exclusively through internal expansion by generating new SME merchant contracts submitted by our own direct sales force.

- Strong Position and Substantial Experience in Our Target Markets

As of December 31, 2014, we were providing card payment processing services to 169,831 active SME merchants located across the United States. We believe our understanding of the needs of SME merchants and the risks inherent in doing business with them, combined with our efficient direct sales force, provides us with a competitive advantage over larger service providers that access this market segment through third-party sales channels. We also believe that we have a competitive advantage over service providers of a similar or smaller size that may lack our extensive experience and resources, and so do not benefit from the economies of scale that we have achieved.

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At December 31, 2014, we also provided card payment processing services to approximately 2,181 Network Services merchants with approximately 42,397 locations. These Network Services merchants are predominantly in the petroleum industry. We believe that our understanding of the processing needs of petroleum merchants and the products we offer them provides us with a competitive advantage.

• Expertise and Focus

Historically, we have focused our sales efforts on SME merchants who have certain key attributes and on industries in which we believe our direct sales model is most effective and the risks associated with card processing are relatively low. These attributes include owners who are typically on location, interact with customers in person, value a local sales and servicing presence and often consult with trade associations and other civic groups to help make purchasing decisions.

To further promote our products and services, we have entered into referral arrangements with various trade associations, with an emphasis on restaurant and hospitality groups. We believe that these partnerships have enabled us to gain exposure and credibility within the restaurant and hospitality industries and have provided us with opportunities to market our products to new merchants.

Our historical focus on SME merchants has diversified our merchant portfolio and we believe has reduced the risks associated with revenue concentration. In 2014, no single SME merchant represented more than 0.41% of our total SME Visa and MasterCard processing volume, consistent with prior years.

Our Network Services business has further diversified our total merchant portfolio, adding a substantial base of large national merchants, predominantly in the petroleum industry.

• Merchant-Centric Culture

We have built a corporate culture and established practices that we believe improve the quality of services and products we provide to our merchants. We developed and endorsed the Merchant Bill of Rights, an advocacy initiative that details ten principles we believe should characterize all merchants' processing relationships. The Merchant Bill of Rights allows our sales team to differentiate our approach to bankcard processing and we believe that a focus on these principles will enhance our merchant relationships, and so reduce merchant attrition. We believe that our culture and practices allow us to maintain strong merchant relationships and differentiate ourselves from our competitors in obtaining new merchants.

Our merchant-centric culture spans from our sales force, which maintains a local market presence to provide rapid, personalized customer service, through our service center, which is segmented into regional teams to optimize responsiveness, and to our technology organization, which has developed a customer management interface and information system that alerts our Relationship Managers to any problems a merchant has reported and provides them with detailed information on the merchants in their portfolio. Additionally, we believe that we are one of the few companies that fully disclose our pricing to merchants. We think this approach contributes substantially to building long-term merchant relationships.

• Scalable Operating Structure

Our scalable operating structure generally allows us to expand our operations without proportionally increasing our fixed and semi-fixed support costs. In addition, our front-end and back-end card processing technology platforms were designed with the flexibility to support significant growth and drive economies of scale with low incremental transaction costs. Most of our operating costs are tied to the number of individuals we employ. We have in the past used, and expect in the future to use, technology to leverage our personnel, which should cause our personnel costs to increase at a lower rate than our card processing volume.

• Advanced Technology

We employ information technology systems, which use the Internet to improve management reporting, enrollment processes, customer service, sales management, productivity, merchant reporting and problem resolution. We believe that these systems help attract both new merchants and Relationship Managers and provide us with a competitive advantage over many of our competitors who rely on less flexible legacy systems. We also offer a full suite of data security solutions, including encryption, tokenization and EMV, all wrapped with a data breach warranty that responds to an increasingly security-focused SME merchant.

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We actively leverage the latest advances in technology to provide the best payments experience for merchants within liability levels that we believe exceed industry norms.

Campus Solutions

In September 2014, we acquired TouchNet Information Systems, Inc. ("TouchNet") for a cash payment of $375 million, less a net working capital deficit, for all outstanding common shares. TouchNet, an integrated commerce solutions provider to higher-education institutions, added more than 600 higher education clients serving over 6 million students, which is nearly one-third the higher education enrollment in the United States, to Heartland's Campus Solutions business. This acquisition allows Heartland to offer the higher education market an end-to-end integrated commerce and payments solution that is unmatched in the industry. Since 1989, TouchNet has been a pioneer in delivering innovative payment solutions. Colleges and universities have relied on TouchNet to unify and secure payment and related business transactions throughout the campus enterprise. TouchNet enables institutions of higher education to process and manage the myriad of campus payments—from student tuition to parking to alumni donations to campus events—on one platform and through one service provider.

In December 2012, we added to our Campus Solutions segment by acquiring ECSI, which provides a suite of solutions to support administrative services for higher education including student loan payment processing, delinquency and default services, refund management, tuition payment plans, electronic billing and payment, tax document services, and business outsourcing. ECSI's core services support the management, payment and collection of student loans including Perkins and institutional financing. Since its founding in 1972, ECSI has printed and mailed 500 million billing statements, processed over 400 million tuition and loan payments and managed accounts for approximately 7 million students and borrowers. ECSI also processes nearly 5 million tax documents every year.

Campus Solutions also provides open- and closed-loop payment solutions for college or university campuses to efficiently process small-value electronic transactions. Campus Solutions currently serves more than 2,600 colleges and universities across multiple higher education sectors including nonprofit, for-profit, private, and community colleges.

Besides payment processing, our OneCard product enables personal identification, door access, cashless vending transactions, cashless laundry, meal plans and cashless printing at campus facilities. Our innovative Give Something Back Network adds Internet and phone-accessible closed-loop debit card-based financial services to the students, faculty, staff and local community merchants of an educational institution. In addition, our RefundSelect program, which we introduced in 2010, addresses the major operational needs of campuses by providing an open-loop debit card platform onto which schools load financial aid refunds. At December 31, 2014, we had 59 colleges enrolled in the RefundSelect program. We issued 450,000 refunds for approximately $801 million in 2014. We currently have 239 OneCard and RefundSelect college and university accounts.

The Campus Solutions industry is competitive with no single competitor providing the complete set of solutions that we provide. However, companies such as Higher One, Nelnet and Tuition Management Systems are larger competitors that compete with some of the solutions provided by us. Competition is primarily based on the products and services offered, innovation, customer service, reputation and price. Products must be compliant with various government regulations, which impede new, smaller entrants. We believe our Campus Solutions business is well positioned to gain customers and generate additional revenue by selling additional products to our existing base of customers.

The following table summarizes revenue and operating income (loss) for Campus Solutions for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December 31,		
	2014	2013	2012
	(In thousands)		
Revenue	$61,538	$36,186	$8,065

Operating income (loss)	12,653	3,930	(16)

Heartland School Solutions

Heartland School Solutions provides cafeteria POS solutions to more than 34,000 schools, making us the largest provider of kindergarten through 12th grade (K-12) food-service technology in the nation. In conjunction with this core POS business, approximately 80% of our customer schools actively use Heartland's online prepayment solutions to allow parents to fund accounts for school lunches or other on-campus activities. Parents can opt to establish recurring payments with customized low balance thresholds, make one-time payments, or simply see what their students ate for lunch that day. With a consistently high annual renewal rate for its POS customers, those platforms serve as a reliable base on which to offer

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additional value-added products and services. We offer back-office management software, hardware, annual technical support, and training to our customer school districts.

Heartland School Solutions has been built through a series of six acquisitions in 2010, 2011, 2012, and 2014. On April 1, 2014, Heartland completed its most recent acquisition in this market, MCS Software. Following the acquisitions, we focused on merging the management and operational structures of the six acquired businesses that make up the School Solutions group. The more than 200 combined School Solutions professionals now operate under a single management structure and go-to-market strategy. While continuing to maintain certain legacy POS platforms for the foreseeable future, we combined all online prepayment activity into two platforms: MySchoolBucks and MyLunchMoney. Together these two systems have more than 5 million registered users. During 2014, we made a significant investment in our consumer-focused marketing strategy in order to encourage more widespread adoption of our online payment products, which, along with our acquisition of MCS Software, resulted in total growth in processing volume of 24% in 2014.

The K-12 food service technology industry is competitive, with our largest competitor being Horizon Software International and other smaller, privately held companies. Competition in the K-12 food-service technology industry is primarily based on the products and services offered, innovation, customer service, ease of use, reputation and price. Products must be in compliance with government regulations for schools in the districts we serve. Payment processing is becoming an increasingly important element of the overall offering for schools, which provides us with a competitive advantage, as we are the only payment processor in the K-12 industry. We believe we are well positioned to gain new school customers and generate additional revenue with our existing customers primarily through greater adoption of payment processing services.

The following table summarizes revenue and operating income for Heartland School Solutions for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December 31,		
	2014	2013	2012
	(In thousands)		
Revenue	$57,570	$50,541	$36,614
Operating income (a)	10,874	16,348	8,766

(a) See Note 1 Organization and Operations in the Notes to Consolidated Financial Statements for a discussion of an Out-of-Period Adjustment recorded in the year ended December 31, 2014.

Heartland Payroll Solutions

We operate a full-service nationwide payroll processing service. Our payroll services include check printing, direct deposit, related federal, state and local tax deposits, time clock sales and integrations, accounting documentation and human resources information. In order to improve operating efficiencies and ease of use for our customers and to decrease our own processing costs, we offer electronic and paperless payroll processing that allows an employer to submit its periodic payroll information to us via the Internet. If a customer chooses the online option, all reports and interactions between the employer and Heartland Payroll Solutions can be managed electronically, eliminating the need for cumbersome paperwork. Approximately half of our payroll customers currently submit their information electronically. However, if a customer chooses not to submit their payroll data online, they may submit such information via phone or facsimile. Regardless of input method, clients can choose to have Heartland Payroll Solutions print and ship their payroll package or to receive this information electronically.

On December 31, 2012, we acquired Ovation, adding more than 10,000 customers to our payroll business. As of December 31, 2014, 2013 and 2012, we provided payroll processing services to 25,764, 24,088 and 22,553 customers, respectively. In 2014, 2013 and 2012, we added 5,821, 5,797 and 2,984 new payroll processing customers, respectively.

We operate a comprehensive payroll management platform, which streamlines all aspects of the payroll process to enable time and cost savings. We consider our payroll platform to be state of the art, enabling us to process payroll on a large scale and provide customizable, cost-effective solutions for businesses of all sizes. It enables faster processing and continuous updates to help businesses remain compliant with payroll, tax and human resources regulations. The platform features web-hosted access, enabling businesses and their accountants to securely access all payroll data from virtually anywhere with SSL-encryption protection. It also provides robust, easy-to-use reporting for better business analysis. The Heartland Payroll platform is equipped to interface with certain leading providers of accounting services and time and attendance applications, as well as restaurant and retail POS systems. Our platform also includes an Employee Self-Serve web portal that allows employees to review copies of their paychecks, vouchers, and payroll detail, and maintain their individual demographic information.

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The payroll processing services industry is highly competitive, with services provided by outsourced providers like Heartland Payroll Solutions, but also accounting firms and self-service options. Overall the industry is comprised of two major segments: large national full-service payroll providers, and numerous much smaller national, regional, local and online providers. While large national payroll service firms such as ADP, Paychex, Ceridian, and Intuit are highly recognized, the full service payroll industry market is very fragmented. We compete with both segments. Competition in the payroll processing industry is primarily based on service responsiveness, payroll accuracy, quality, reputation, range of product offering and price. The payroll industry faces continually evolving tax, regulatory and technology environments, which for smaller competitors create increasingly complex tax, compliance tracking (e.g. Affordable Care Act) technology, third-party integrations, customer service and platform development challenges that they may lack the technical and financial resources to overcome. We believe Heartland Payroll Solutions is well positioned to continue to gain market share from those challenged providers. Additionally, we believe our competitive position is enhanced through our ability to offer payment processing services to payroll customers, and vice versa, and thus offer an integrated services suite, which will provide our customers with efficient and convenient options.

The following table summarizes revenue and operating income for Heartland Payroll Solutions for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December 31,		
	2014	2013	2012
	(In thousands)		
Revenue	$50,394	$44,565	$21,368
Operating income	9,076	3,404	2,424

Heartland Commerce

Heartland Commerce provides a comprehensive suite of POS solutions, payment processing capabilities and other adjacent business service applications, serving the hospitality and retail industries. Heartland Commerce is comprised of existing POS businesses; Xpient, Liquor POS, and our other POS solutions, and will include the recently acquired pcAmerica and Dinerware POS businesses.

In October 2014, we purchased Xpient, a leading food service industry enterprise-level POS software provider. This acquisition adds 25,000 installed locations to our POS business. Xpient provides advanced technology to 11 of the top 25 quick-service and fast casual restaurant brands, including Taco Bell, Jack in the Box and Panera Bread. Acquiring Xpient allows Heartland to meet the critical technology needs of its restaurant industry customers. The expanded portfolio will allow restaurants of all sizes to seamlessly manage kitchen throughput even during the busiest times, whether generated at the drive-thru, front counter or through mobile applications. Xpient's solutions help streamline front-of-house operations, onsite and mobile orders, and mobile payments functionality.

In February 2014, we acquired Liquor POS, a leading provider of POS systems to the liquor retail vertical. It currently serves more than 3,400 merchants to whom we expect to offer our products and services.

In January 2015, we acquired pcAmerica, a leading retail and restaurant provider of POS systems which streamline its customers daily operations, including customer transactions, inventory tracking, employee labor, and marketing reports, and are designed to meet the evolving needs of retail stores or restaurants. Some notable pcAmerica users include Flowers Foods, Goodwill Stores, Baskin-Robbins, Tasti D-Lite and various United States Embassies and Consulates.

In February 2015, we acquired Dinerware a provider of restaurant POS software solutions to the hospitality industry. Dinerware customers include upscale restaurants, cafes, nightclubs, bar and grills, fast casual restaurants, counter service establishments, quick serve restaurants, hotels, casinos, cafeterias, golf courses, and wineries.

Previously, we acquired a 67% ownership interest in Leaf in September 2013 and acquired the remaining 33% interest in August 2014. Leaf provided us with a software-as-a-service (SaaS) POS system to deliver an open-architecture platform supporting numerous vertical-specific business applications.

Dinerware and pcAmerica are in the process of developing cloud-based POS systems that complement their well-established on-premise POS solutions. These cloud-based POS systems overlap with what was being developed by Leaf, and Dinerware and pcAmerica technologies and development plans provided management insight into the status and positioning of

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Leaf’s technology in the marketplace. Consequently, management decided that it will stop POS development efforts at Leaf, and write down related POS assets.

Separately, we determined that our investment in TabbedOut, a mobile payments provider, was substantially impaired as of December 31, 2014 and recorded an impairment charge of $4.0 million related to that investment. In the fourth quarter ended December 31, 2014, we recorded total asset impairment charges of $41.4 million pre-tax, ($37.6 million after-tax, or $1.02 per share), related to the values ascribed to our investments at Leaf and in Prosper, an internally developed POS software technology, and our investment in TabbedOut, a mobile payments provider.

The POS solutions industry has become increasingly competitive, and integrated with payments, with some of the large POS companies forging key partnerships with payments companies, and other merchant acquirers selling their services through POS VARS. As a way to surpass the competition, Heartland’s strategy is to not only establish partnerships with POS dealers but to also own select best of breed POS technologies. This enables us to offer a truly integrated POS platform that becomes the focal point for many of Heartland's value added applications including payment processing, table management, payroll, security, and online ordering.

Micropayments

We began addressing the small-value transaction market in 2006. We manufacture and sell solutions comprising unattended online wireless credit card-based payment systems, and unattended value top-up systems for off-line closed-loop smart (chip) card based payment systems. Our electronic cash systems provide small-value transaction processing for commercial laundry machines and vending machines, which are located in apartment laundries, cruise ships, corporate and university campuses, and penitentiaries. These systems offer consumers convenient ways to use their debit and credit cards to purchase and reload electronic cash cards, and to spend the value on the card for small-value purchases in both attended and unattended POS locations. In addition, we provide merchants financial settlement between the electronic cash card issuer and the vendor/merchant who accepts the card as payment. Our WaveRider system allows laundry patrons to use their debit or credit card to pay directly for their laundry right at the washer or dryer, simply by swiping their card. We believe there is increasing consumer demand for, and merchant interest in, card-based solutions for small denomination transactions, and expect to make additional investments in the future in developing solutions in this area.

The unattended payments industry is competitive with the largest competitor being USA Technologies. Other competitors include vending machine manufacturers and privately held companies focusing on specific vertical markets. Competition is primarily based on the products and services offered, ease of installation and setup, innovation and price. As payment processing is a core component of the services offered, we believe that we have a distinct advantage over many of our competitors. As unattended payments become more commonplace and expected, we believe that we will continue to add new customers.

The following table summarizes revenue and operating income for Micropayments for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December 31,		
	2014	2013	2012
	(In thousands)		
Revenue	$16,950	$12,634	$8,201
Operating income	3,568	1,336	142

Heartland Marketing Solutions

Heartland Marketing Solutions ("HMS") delivers a full suite of consumer engagement solutions for merchants. These include mobile and card-based gift and rewards marketing services to merchant locations through real-time communications with the merchant POS, enabling us to leverage existing installations across our merchant base and enhancing our overall value proposition to the merchant community. In addition to gift and rewards, HMS also delivers vertical use case driven mobile applications, such as the Heartland ToGo product, a mobile and online ordering solution that is integrated with gift and rewards. In addition to servicing the SME merchant market, HMS also provides these solutions to regional and national brands.

The Marketing Solutions space continues to evolve and become even more relevant as merchants are looking for deeper engagement with their customers. In 2014, HMS launched several enhancements such as a suite of Application Programming Interfaces ("APIs"), integration into several mobile application providers, a full suite of digital card distribution to the SME space and has developed the groundwork for a robust data and analytics solution. As of December 31, 2014,

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Heartland Marketing Solutions has 11,669 active merchant locations and loaded $340 million on approximately 7.1 million consumer gift cards, compared to 10,426 active merchant locations and $241 million loaded on approximately 5.5 million cards as of December 31, 2013.

In addition, there has been prolific emergence of mobile application providers to enable merchants to create a branded mobile application to compete with other large brands. HMS has reacted by developing a robust set of APIs to enable integration in the fast-moving market to allow for quick integration into multiple third-party solutions. This option enables merchants to partner with any application developer to integrate gift and rewards into the application of their choosing. HMS has integrated with several vertical use case driven mobile applications and launched Heartland ToGo, a mobile and online ordering solution with embedded gift and rewards in August of 2014. As of December 31, 2014, Heartland has boarded more than 150 merchants on the Heartland ToGo solution.

The core gift space, historically defined as merchant branded gift card, is highly competitive. Most solutions are currently sold and provisioned by merchant processors. Competition usually focuses on one of two markets depending on their merchant base: medium to large merchant providers where solutions are highly flexible, feature-rich and allow for customization, and small merchant providers where solutions are still feature-rich, but have been streamlined to minimize implementation costs. Competition includes First Data Gift Card, StoredValueSystems (owned by FleetCor), Valutec (owned by Fidelity National Information Services) and Givex. We believe that very few gift card providers have a robust rewards platform, so merchants usually have to go to two different providers to satisfy their gift and rewards needs. Heartland Marketing Solutions is one of the few providers whose platform was specifically built to support both gift and rewards implementations.

The following table summarizes revenue and operating income (loss) for HMS for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December 31,		
	2014	2013	2012
	(In thousands)		
Revenue	$9,364	$9,649	$13,477
Operating income (loss)	378	(248)	1,666

Intellectual Property

Most of our services and products are based on proprietary software or processes that are updated to meet customer needs and remain competitive. Our proprietary software is critical, as it allows us to offer distinctive services and products to customers, which differentiates us from our competitors. We own and are pursuing numerous patents with the United States Patent and Trademark Office. In addition, we own various trademarks and have applied for numerous others.

WHERE YOU CAN GET ADDITIONAL INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy our reports or other filings made with the SEC at the SEC's Public Reference Room, located at 100 F Street, N.E., Washington, DC 20549. You can obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. You can also access these reports and other filings electronically on the SEC's web site, www.sec.gov.

In addition, certain of our SEC filings, including our Annual Report on Form 10-K, our Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and amendments to these reports, can be viewed, free of charge, and printed from the investor information section of our website at www.heartlandpaymentsystems.com, as soon as reasonably practicable after filing with the SEC. Certain materials relating to our corporate governance, including our code of ethics for chief executive and senior financial officers, code of business conduct and ethics, corporate governance guidelines and board committee charters, are also available in the investor relations section of our website.

The information on the websites listed above, is not and should not be considered part of this Annual Report on Form 10-K or any other report or document we file with the SEC and is not incorporated by reference in this document or any other report or document we file with the SEC. These websites are, and are only intended to be, inactive textual references.

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In May 2014, we submitted to the New York Stock Exchange the CEO certification required by Section 303A.12(a) of the New York Stock Exchange Listed Company Manual without qualification.

ITEM 1A. RISK FACTORS

An investment in our common stock involves a high degree of risk. You should consider carefully the following risks and other information contained in this Annual Report on Form 10-K and other SEC filings before you decide whether to buy our common stock. If any of the events contemplated by the following discussion of risks should occur, our business, results of operations and financial condition could suffer significantly. As a result, the market price of our common stock could decline, and you may lose all or part of the money you paid to buy our common stock.

Risks Relating to Our Business

Unauthorized disclosure of merchant, cardholder or other user data, whether through breach of our computer systems (such as the Processing System Intrusion discussed in Item 3 Legal Proceedings) or otherwise, could expose us to liability and protracted and costly litigation, as well as harm our reputation.

We collect and store sensitive data about merchants, including names, addresses, social security numbers, driver's license numbers and checking account numbers. In addition, we maintain a database of cardholder and other user data relating to specific transactions, including bankcard numbers, in order to process the transactions and for fraud prevention. Any loss of data by us or our merchants could result in significant fines and sanctions by the card networks or governmental bodies, which could have a material adverse effect upon our business, financial position and/or results of operations. In addition, a significant breach could result in our being prohibited from processing transactions for card networks.

Our computer systems have been, and could be in the future, subject to penetration by hackers and our encryption of data may not prevent unauthorized use. In this event, we may be subject to liability, including claims for unauthorized purchases with misappropriated bankcard information, impersonation or other similar fraud claims. We could also be subject to liability for claims relating to misuse of personal information, such as unauthorized marketing purposes. These claims also could result in protracted and costly litigation. In addition, we could be subject to penalties or sanctions from the card networks, or our reputation could be harmed, which may deter clients from using our services.

Although we generally require that our agreements with our service providers who have access to merchant and customer data include confidentiality obligations that restrict these parties from using or disclosing any customer or merchant data except as necessary to perform their services under the applicable agreements, we cannot assure you that these contractual measures will prevent the unauthorized use or disclosure of data. In addition, our agreements with financial institutions require us to take certain protective measures to ensure the confidentiality of merchant and consumer data. Any failure to adequately enforce these protective measures could result in protracted and costly litigation.

The Heartland Secure solution could be breached at one or many merchant locations. In the event of a breach of the Heartland Secure solution, we could face material financial liability.

In 2015, we began offering a warranty to merchants using the Heartland Secure™ solution, a comprehensive credit/debit card data secure payment solution combining EMV, the Heartland E3® end-to-end encryption technology and tokenization. Through the warranty, Heartland agrees not to pass on to covered merchants those costs, fees and fines from card brands that result from a breach.

The Heartland Secure solution could be breached at one or many merchant locations. In the event of a breach of the Heartland Secure solution, we could face liability for the costs associated with the breach, and the fees and fines assessed by the card brands. In addition, we may face liability arising from: (i) claims for unauthorized purchases with misappropriated bankcard information, (ii) impersonation or other related fraud claims; (iii) products liability claims; and/or (iv) breach of warranty claims. We could face protracted and costly litigation relating to such claims. If the Heartland Secure solution is breached, our reputation could be harmed, which may deter clients from using our services, and such a breach may have a material adverse effect upon our financial position and results of operations.

If we fail to comply with the applicable requirements of the Visa and MasterCard bankcard networks, Visa or MasterCard could seek to fine us, suspend us or terminate our registrations. Fines could have an adverse effect on our operating results and financial condition, and if these registrations are terminated, we will not be able to conduct our primary business.

On occasion, we have received notices from Visa and MasterCard of non-compliance and fines, which have typically related to excessive chargebacks by a merchant or data security failures on the part of a merchant. If we are unable to recover fines from our merchants, we will experience a financial loss. The termination of our registration, or any changes in the Visa or MasterCard rules that would impair our registration, could require us to stop providing Visa and MasterCard payment processing services, which would make it impossible for us to conduct our business on its current scale.

We rely on sponsor banks, which have substantial discretion with respect to certain elements of our business practices, in order to process bankcard transactions. If these sponsorships are terminated and we are unable to secure new bank sponsors, we will not be able to conduct significant portions of our business.

Over 73% of our revenue is derived from processing Visa and MasterCard bankcard transactions. Because we are not a bank, we are not eligible for membership in the Visa and MasterCard networks and are, therefore, unable to directly access the bankcard networks. Instead, Visa and MasterCard operating regulations require us to be sponsored by a member bank in order to process bankcard transactions. We are currently registered with Visa and MasterCard through Wells Fargo Bank N.A. since February 2012, The Bancorp Bank since November 2009, and Barclays Bank Delaware since March 2011.

Our sponsorship agreements with Wells Fargo Bank N.A., The Bancorp Bank and Barclays Bank Delaware expire February 2016, February 2016 and March 2016, respectively. If our sponsorships are terminated and we are unable to secure another bank sponsor or sponsors, which could arise due to future consolidation of sponsor banks or because sponsor banks exit this line of business, we will not be able to process Visa and MasterCard transactions. Furthermore, some agreements give the sponsor banks substantial discretion in approving certain aspects of our business practices, including our solicitation, application and qualification procedures for merchants, the terms of our agreements with merchants and our customer service levels. Our sponsor banks' discretionary actions under these agreements could be detrimental to our operations.

Current or future bankcard network rules and practices could adversely affect our business.

We are registered with the Visa and MasterCard networks through our bank sponsors as an Independent Sales Organization with Visa and a Member Service Provider with MasterCard. We are currently a sales agent and service agent for American Express and a registered acquirer with Discover. The rules of the bankcard networks are set by their boards, which may be strongly influenced by card issuers, and some of those card issuers are our competitors with respect to these processing services. Many banks directly or indirectly sell processing services to merchants in direct competition with us. These banks could attempt, by virtue of their influence on the networks, to alter the networks' rules or policies to the detriment of non-members like us. The termination of our registration or our status as an Independent Sales Organization or Member Service Provider, or any changes in card network or issuer rules that limit our ability to provide payment processing services, could have an adverse effect on our bankcard processing volumes, revenues or operating costs. In addition, if we were precluded from processing Visa and MasterCard bankcard transactions, we would lose the majority of our revenues.

Any new laws and regulations, or revisions made to existing laws, regulations, or other industry standards affecting our business may have an unfavorable impact on our operating results and financial condition.

Our business is impacted by laws and regulations that affect the bankcard industry. In July 2010, Congress passed The Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), which significantly changed financial regulation. Changes included restricting amounts of debit card fees that certain issuer banks can charge merchants and allowing merchants to offer discounts for different payment methods. The impact which new requirements imposed by the Dodd-Frank Act or other new regulation will have on our operating results is difficult to determine, as their implementation could result in the need for us to modify our services and processing platforms. As new requirements are mandated, these regulations could adversely affect our operating results and financial condition. Furthermore, the requirements of the new regulations and the timing of their effective dates could result in changes in our clients' business practices that may alter their delivery of their products and services to consumers and the timing of their investment decisions, which could change the demand for our services as well as alter the type or volume of transactions that we process on behalf of our clients.

Additionally, all persons engaged in commerce, including, but not limited to, us and our merchant and financial institution customers, are subject to Section 5 of the Federal Trade Commission Act prohibiting unfair or deceptive acts or practices, or UDAP. The Federal Trade Commission, or FTC, has authority to take action against nonbanks that engage in UDAP and to the extent we are processing payments for a merchant engaged in UDAP, we may be subject to action by the FTC.

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On July 26, 2011, the Financial Crimes Enforcement Network of the U.S. Department of the Treasury, or FinCEN, issued a final rule regarding the applicability of the Bank Secrecy Act's regulations to “prepaid access” products and services. This rulemaking clarifies the anti-money laundering obligations for entities engaged in the provision and sale of prepaid services such as prepaid cards. We have registered with FinCEN as a “money services business-provider of prepaid access” in accordance with the rule. Notwithstanding previously implemented anti-money laundering procedures pursuant to various contractual obligations, the rule increases our regulatory risks and, as with other regulatory requirements, violations of the rule could have a material adverse effect on our business, financial condition and results of operations.
We are required to assist our Sponsor banks in complying with certain of their regulatory obligations. In particular, the anti-money laundering provisions of the USA PATRIOT Act require that customer identifying information be obtained and verified. In addition, both we and our Sponsor banks are subject to the laws and regulations enforced by the Office of Foreign Assets Control, or OFAC, which prohibit U.S. persons from engaging in transactions with certain prohibited persons or entities. Our failure to comply with any of these laws or rights could materially and adversely affect our business, financial credit and results of operations.

We are subject to laws and regulations relating to the collection, use, retention, security and transfer of personally identifiable information and data regarding our customers and their financial information. In addition, we are bound by our own privacy policies and practices concerning the collection, use and disclosure of user data, which are posted on certain of our website pages. New legislation and regulations in this area have been proposed, both at the federal and state level. Such measures, including pending Federal legislation, would potentially impose additional obligations on us, including requiring that we provide notifications to consumers and government authorities in the event of a data breach or unauthorized access or disclosure, beyond what state law already requires.

These and other laws and regulations could adversely affect our business, financial condition and results of operations. In addition, even an inadvertent failure to comply with laws and regulations, given rapidly evolving social expectations of corporate fairness, could damage our business or our reputation.

Governmental regulations designed to protect or limit access to consumer information could adversely affect our ability to effectively provide our services to merchants.

Governmental bodies in the United States and abroad have adopted, or are considering the adoption of, laws and regulations restricting the transfer of, and safeguarding, non-public personal information. For example, in the United States, all financial institutions must undertake certain steps to ensure the privacy and security of consumer financial information. While our operations are subject to certain provisions of these privacy laws, we have limited our use of consumer information solely to providing services to other businesses and financial institutions. We limit sharing of non-public personal information to that necessary to complete the transactions on behalf of the consumer and the merchant and to that permitted by federal and state laws. In connection with providing services to the merchants and financial institutions that use our services, we are required by regulations and contracts with our merchants to provide assurances regarding the confidentiality and security of non-public consumer information. These contracts require periodic audits by independent companies regarding our compliance with industry standards and best practices established by regulatory guidelines. The compliance standards relate to our infrastructure, components, and operational procedures designed to safeguard the confidentiality and security of non-public consumer personal information shared by our clients with us. Our ability to maintain compliance with these standards and satisfy these audits will affect our ability to attract and maintain business in the future. The cost of such systems and procedures may increase in the future and could adversely affect our ability to compete effectively with other similarly situated service providers.

Global economics, political and other conditions may adversely affect trends in consumer spending, which may adversely impact our revenue and profitability.

A recessionary economic environment could have a negative impact on our merchants, which may, in turn, adversely impact our revenue and profitability, particularly if the recessionary environment disproportionately affects some of the market segments that represent a larger portion of our card processing volume, like restaurants. If our merchants make fewer sales of their products and services, we will have fewer transactions to process, resulting in lower revenue. In addition, we have a certain amount of fixed and semi-fixed costs, including rent, processing contractual minimums and salaries, which could limit our ability to quickly adjust costs and respond to changes in our business and the economy.

In a recessionary environment our merchants could also experience a higher rate of business closures, which could adversely affect our business and financial condition. During prior recessions, including the 2008-2009 recession, we experienced negative same-store sales growth (or contraction) and an increase in business closures. In the event of a closure of a merchant, we are unlikely to receive our fees for any transactions processed by that merchant in its final month of operation.

We have faced, and will in the future face, chargeback liability when our merchants refuse or cannot reimburse chargebacks resolved in favor of their customers, reject losses when our merchants go out of business, and merchant fraud. We cannot accurately anticipate these liabilities, which may adversely affect our results of operations and financial condition.

In the event a billing dispute between a cardholder and a merchant is not resolved in favor of the merchant, the transaction is normally “charged back” to the merchant and the purchase price is credited or otherwise refunded to the cardholder. If we or our clearing banks are unable to collect such amounts from the merchant's account, or if the merchant refuses or is unable, due to closure, bankruptcy or other reasons, to reimburse us for the chargeback, we bear the loss for the amount of the refund paid to the cardholder. The risk of chargebacks is typically greater with those merchants that promise future delivery of goods and services rather than delivering goods or rendering services at the time of payment. We may experience significant losses from chargebacks in the future. Any increase in chargebacks not paid by our merchants may adversely affect our financial condition and results of operations.

Reject losses arise from the fact that we typically collect our fees from our SME merchants on the first day after the monthly billing period. This results in the build-up of a substantial receivable from our customers, which significantly exceeds the receivables of any of our competitors which generally assess their fees on a daily basis. If a merchant has gone out of business during the billing period, changes their demand deposit account, or institutes blocks on its demand deposit account, we may be unable to collect such fees. In addition, if our sponsor bank is unable, due to system disruption or other failure, to collect our fees from our merchants, we would face a substantial loss.

We have potential liability for fraudulent bankcard transactions initiated by merchants. Merchant fraud occurs when a merchant knowingly uses a stolen or counterfeit bankcard or card number to record a false sales transaction, processes an invalid bankcard or intentionally fails to deliver the merchandise or services sold in an otherwise valid transaction. We have established systems and procedures designed to detect and reduce the impact of merchant fraud, but we cannot assure you that these measures are or will be effective. It is possible that incidents of fraud could increase in the future. Failure to effectively manage risk and prevent fraud would increase our chargeback liability. Increases in chargebacks could have an adverse effect on our operating results and financial condition.

In the years ended December 31, 2014, 2013 and 2012, we incurred charges relating to chargebacks, reject losses and merchant fraud of $7.3 million, $3.1 million and $2.0 million, respectively, or 0.90 basis points, 0.41 basis points and 0.28 basis points, respectively of our SME card processing volume. In 2014, our losses included $4.6 million resulting from chargebacks from a single merchant who entered bankruptcy in the fourth quarter.

We rely on various financial institutions to provide clearing services in connection with our settlement activities. If we are unable to maintain clearing services with these financial institutions and are unable to find a replacement, our business may be adversely affected.

We rely on various financial institutions to provide clearing services in connection with our settlement activities. If such financial institutions should stop providing clearing services, we must find other financial institutions to provide those services. If we are unable to find a replacement financial institution we may no longer be able to provide processing services to certain customers, which could negatively impact our revenue and earnings.

Increased merchant attrition that we cannot offset with increased card processing volume from same store sales growth or new accounts would cause our revenues to decline.

We experience attrition in merchant card processing volume resulting from several factors, including business closures, transfers of merchants' accounts to our competitors and account closures that we initiate due to heightened credit risks. During the years ended December 31, 2014, 2013 and 2012, we experienced average annualized attrition in our SME card processing volume of 12.7%, 12.9% and 12.8%, respectively. Substantially all of our SME processing contracts may be terminated by either party on relatively short notice. We cannot predict the level of attrition in the future, and it could increase. Increased attrition in merchant card processing volume may have an adverse effect on our financial condition and results of operations. If we are unable to establish accounts with new merchants or otherwise increase our card processing volume in order to counter the effect of this attrition, our revenues will decline.

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If we cannot pass increases in bankcard network interchange fees, assessments and transaction fees along to our merchants, our operating margins will be reduced.

We pay interchange fees and other network fees set by the bankcard networks to the card issuing bank and the bankcard networks for each transaction we process. From time to time, the bankcard networks increase the interchange fees and other network fees that they charge payment processors and the sponsor banks. At their sole discretion, our sponsor banks have the right to pass any increases in interchange fees on to us and have always done so in the past. We are allowed to, and in the past we have been able to, pass these fee increases along to our merchants through corresponding increases in our processing fees. However, if we are unable to do so in the future, our operating margins will be reduced.

The payment processing industry is highly competitive and we compete with certain firms that are larger and that have greater financial resources. Such competition could increase, which would adversely influence our prices to merchants, and as a result, our operating margins.

The market for payment processing services is highly competitive. Other providers of payment processing services have established a sizable market share in the small and mid-sized merchant processing sector. Maintaining our historic growth will depend on a combination of the continued growth in electronic payment transactions and our ability to increase our market share. According to The Nilson Report, we accounted for approximately 4.5% of the 77.2 billion of purchase transactions processed by all U.S. bankcard acquirers in 2013. The competition we face may affect the prices we are able to charge. If the competition causes us to reduce the prices we charge, we will have to aggressively control our costs or our profit margins will decline. In addition, some of our competitors are financial institutions, subsidiaries of financial institutions or well-established payment processing companies. Our competitors that are financial institutions or subsidiaries of financial institutions do not incur the costs associated with being sponsored by a bank into the card networks and can settle transactions more quickly for their merchants than we can for ours. These competitors have substantially greater financial, technological, management and marketing resources than we have. This may allow our competitors to offer more attractive fees to our current and prospective merchants, or other products or services that we do not offer. This could result in a loss of customers, greater difficulty attracting new customers, and a reduction in the price we can charge for our products and services.

The payment processing market in which we compete is subject to rapid technological changes. These markets are characterized by technological change, new product introductions, evolving industry standards and changing customer needs. In order to remain competitive, we are continually involved in a number of projects to offer our customers convenient and efficient solutions for their payment needs. These projects carry the risks associated with any development effort, including cost overruns, delays in delivery and performance problems. In addition, many of our competitors may have the ability to devote more financial and operational resources than we can to the development of new technologies and services, including Internet payment processing services and mobile payment processing services that provide improved operating functionality and features to their product and service offerings. If more successful than ours, their development efforts could render our product and services offerings less desirable to customers, again resulting in the loss of customers or a reduction in the price we could demand for our offerings.

Our systems and our third-party providers' systems may fail due to factors beyond our control, which could interrupt our service, cause us to lose business and increase our costs.

We depend on the efficient and uninterrupted operation of our computer network systems, software, data center and telecommunications networks, as well as the systems of third parties. Our systems and operations or those of our third-party providers could be exposed to damage or interruption from, among other things, fire, natural disaster, power loss, telecommunications failure, unauthorized entry and computer viruses. Our property and business interruption insurance may not be adequate to compensate us for all losses or failures that may occur. Defects in our systems or those of third parties, errors or delays in the processing of payment transactions, telecommunications failures or other difficulties could result in:

- loss of revenues;
- loss of merchants, although our contracts with merchants do not expressly provide a right to terminate for business interruptions;
- loss of merchant and cardholder data;
- harm to our business or reputation;
- exposure to fraud losses or other liabilities;
- negative publicity;
- additional operating and development costs; and/or
- diversion of technical and other resources.

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If we fail to protect our intellectual property rights and defend ourselves from potential patent infringement claims, our competitive advantages may diminish or our ability to offer services to our customers could be restricted.

Our patents, trademarks, proprietary software and other intellectual property are critical to our future success. We rely on proprietary technology. It is possible that others will independently develop the same or similar technologies. Assurance of protecting our rights and proprietary information cannot be guaranteed. Our patents could be challenged, invalidated or circumvented by others and may not be of sufficient scope or strength to provide any meaningful protection or advantage. If we are unable to maintain the proprietary nature of our technologies, we could lose competitive advantages and be materially adversely affected. Adverse determinations in judicial or administrative proceedings could prevent us from precluding others from selling competing services, and thereby may have a material adverse effect on our business and results of operations.

Additionally, claims have been made, and other claims may be made in the future, with regard to our services or technology infringing on a patent or other intellectual property rights of others. Third parties may have, or may eventually be issued, patents that could be infringed by our services or technology. Any of these third parties could make a claim of infringement against us with respect to our services or technology. We may also be subject to claims by third parties for breach of copyright, trademark, license usage or other intellectual property rights. Any claim from third parties may result in a limitation on our ability to use the intellectual property subject to these claims, restrict us from delivering the related service or result in an unfavorable settlement that could be material to our operating results, financial condition and cash flow. Also, in recent years, individuals and groups have been purchasing intellectual property assets for the sole purpose of making claims of infringement and attempting to extract settlements from companies like ours. Even if we believe that intellectual property related claims are without merit, defending against such claims is time consuming and expensive and could result in the diversion of the time and attention of our management and employees. Claims of intellectual property infringement also might require us to redesign affected services, enter into costly settlement or license agreements, pay costly damage awards, or face a temporary or permanent injunction prohibiting us from marketing or selling certain of our services. Even if we have an agreement for indemnification against such costs, the indemnifying party, if any in such circumstances, may be unable to uphold its contractual obligations. If we cannot or do not license the infringed technology on reasonable terms or substitute similar technology from another source, our revenue and earnings could be adversely impacted.

Finally, we use open source software in connection with our technology and services. Companies that incorporate open source software into their products have, from time to time, faced claims challenging the ownership of open source software. As a result, we could be subject to suits by parties claiming ownership of what we believe to be open source software. Some open source software licenses require users who distribute open source software as part of their software to publicly disclose all or part of the source code to such software and/or make available any derivative works of the open source code on unfavorable terms or at no cost. While we monitor the use of open source software in our technology and services and try to ensure that none is used in a manner that would require us to disclose the source code to the related technology or service, such use could inadvertently occur and any requirement to disclose our proprietary source code could be harmful to our business, financial condition and results of operations.

Adverse conditions in markets in which we obtain a substantial amount of our card processing volume, such as our largest SME merchant markets of California, Texas, Florida, New York and Ohio, could negatively affect our results of operations.

Adverse economic or other conditions in California, Texas, Florida, New York and Ohio would negatively affect our revenue and could materially and adversely affect our results of operations. In December 2014, SME merchants located in the following states represented the following percentages of our SME card processing volume: California represented 10.7%, Texas represented 7.7%, Florida represented 4.8%, New York represented 4.7% and Ohio represented 3.6%, respectively. As a result of this geographic concentration of our merchants in these markets, we are exposed to the risks of downturns in these local economies and to other local conditions, which could adversely affect the operating results of our merchants in these markets. No other state represented more than 3.5% of our SME card processing volume in December 2014.

If we lose key personnel or are unable to attract additional qualified personnel as we grow, our business could be adversely affected.

We are dependent upon the ability and experience of a number of our key personnel who have substantial experience with our operations, the rapidly changing payment processing industry and the selected markets in which we offer our services. It is possible that the loss of the services of one or a combination of our senior executives or key managers, particularly Robert O. Carr, our Chief Executive Officer, would have an adverse effect on our operations. Our success also depends on our ability to continue to attract, manage and retain other qualified middle management and technical and clerical personnel as we grow. We may not continue to attract or retain such personnel.

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If we are unable to attract and retain qualified sales people, our business and financial results may suffer.

Unlike many of our competitors who rely on Independent Sales Organizations or salaried salespeople and telemarketers, we rely on a direct sales force whose compensation is entirely commission-based. Through our direct sales force of approximately 911 Relationship Managers and Territory Managers and 74 product specialists (SPAs), we seek to increase the number of merchants using our products and services. We intend to significantly increase the size of our sales force. Our success partially depends on the skill and experience of our sales force. If we are unable to retain and attract sufficiently experienced and capable Relationship Managers, Territory Managers and SPAs, our business and financial results may suffer.

Any potential strategic acquisitions or buyouts of our sales persons portfolio equity that we make could disrupt our business and harm our financial condition.

We expect to evaluate potential strategic acquisitions of complementary businesses, products or technologies. We may not be able to successfully finance or integrate any businesses, products or technologies that we acquire. Furthermore, the integration of any acquisition may divert management's time and resources from our core business and disrupt our operations. We may spend time and money on projects that do not increase our revenue. To the extent we pay the purchase price of any acquisition in cash, it would reduce our cash reserves or increase our borrowings, and to the extent the purchase price is paid with our stock, it could be dilutive to our stockholders. We, from time to time, evaluate potential acquisitions of businesses, products and technologies, and anticipate continuing to make these evaluations.

We also regularly buy out the residual commissions of our Relationship Managers and sales managers, at multiples that typically amount to 2 1/2 years of such commissions. If the merchants included in the portfolios we purchase do not generate sufficient incremental margin after the purchase, we will not achieve a positive return on the cash expended.

Our operating results are subject to seasonality, which could result in fluctuations in our quarterly net income.

We have experienced in the past, and expect to continue to experience, seasonal fluctuations in our revenues as a result of consumer spending patterns. Historically our revenues have been strongest in our second and third quarters, and weakest in our first quarter.

We may become subject to additional U.S., state or local taxes that cannot be passed through to our merchants, which could negatively affect our results of operations.

Companies in the payment processing industry, including us, may become subject to taxation in various tax jurisdictions based on our net income or revenues. Taxing jurisdictions have not yet adopted uniform positions on taxation. If we are required to pay additional taxes on our net income or revenues and are unable to pass the tax expense through to our merchants, our costs would increase and our net income would be reduced.

We may need to raise additional funds to finance our future capital needs, which may prevent us from growing our business.

We may need to raise additional funds to finance our future capital needs, including developing new products and technologies, and operating expenses. We may need additional financing earlier than we anticipate if we:

- expand faster than our internally generated cash flow can support;

- purchase portfolio equity (the portion of our commissions that we have committed to our sales force for as long as the merchant processes with us, which we may buy out at an agreed multiple) from a large number of Relationship Managers or sales managers;
- add new merchant accounts faster than expected;
- need to reduce pricing in response to competition;
- repurchase our common stock or pay dividends; or
- acquire complementary products, business or technologies.

If we raise additional funds through the sale of equity securities, these transactions may dilute the value of our outstanding common stock. We may also decide to issue securities, including debt securities that have rights, preferences and privileges senior to our common stock. We may be unable to raise additional funds on terms favorable to us or at all. If financing is not available or is not available on acceptable terms, we may be unable to fund our future needs. This may prevent us from increasing our market share, capitalizing on new business opportunities or remaining competitive in our industry.

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Risks Related to Our Company

Borrowings under our Credit Agreement could adversely affect our financial condition, and the related debt service obligations may adversely affect our cash flow and ability to invest in and grow our businesses.

The interest rates on debt outstanding under our Credit Agreement are floating based on the LIBOR rate; accordingly, if the LIBOR rate increases, our interest expense will be higher on the portion of our debt outstanding not managed with interest rate swaps. At December 31, 2014, there was $559.8 million outstanding under our Credit Agreement. We are party to fixed-pay amortizing interest rate swaps having a notional amount of $15.0 million at December 31, 2014. These interest rate swaps convert $15.0 million of our borrowings under our Credit Agreement to fixed rate. These interest rate swaps amortize at $3.75 million per quarter in 2015 until their expiry in November 2015. At December 31, 2014 the fair value of these interest rate swaps, a liability of $0.1 million, was recorded in accrued expenses and other liabilities.

We intend to fulfill our total debt service obligations primarily from cash generated by our operations. Such funds will not be available to use in future operations, or investing in our businesses. This may adversely impact our ability to expand our businesses or make other investments. If we are unable to meet our debt obligations, we could be forced to restructure or refinance our obligations, to seek additional equity financing or to sell assets, which we may not be able to do on satisfactory terms or at all. As a result, we could default on those obligations and in the event of such default, our lenders could accelerate our debt or take other actions that could restrict our operations.

Our borrowing agreements contain restrictions which may limit our flexibility in operating and growing our business.

Our borrowing agreements contain covenants regarding our maintenance of certain leverage and fixed charge coverage ratios. Our borrowing agreements also include covenants that limit our ability to engage in specified types of transactions, including among other things:
- incur additional indebtedness or issue equity;
- pay dividends on, repurchase or make distributions in respect of our common stock;
- make certain investments (including acquisitions) and distributions;
- sell certain assets;
- create liens;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets;
- enter into certain transactions with respect to our affiliates,
- ability to enter into business combinations, and
- certain other financial and non-financial covenants.

We were in compliance with these covenants as of December 31, 2014. Failure to be in compliance with these covenants could result in an event of default which, if not cured or waived, could result in the acceleration of all or a portion of our outstanding indebtedness, which would have a material adverse effect on our business, financial condition and results of operations.

Our balance sheet includes significant amounts of goodwill and intangible assets. The impairment of a significant portion of these assets would negatively affect our business, financial condition, and results of operations.

As a result of recent acquisitions, a significant portion of our total assets consist of goodwill and intangible assets. Combined goodwill and intangible assets, net of amortization, accounted for approximately 45% and 27% of the total assets on our balance sheet at December 31, 2014 and 2013, respectively. We may not realize the full carrying value of our intangible assets and goodwill. We test goodwill for impairment at least annually and during interim periods if an event occurs or changes in circumstances suggest a potential decline in the fair value of goodwill. We also evaluate intangible assets on an ongoing basis for indicators of impairment. A significant amount of judgment is involved in determining if an indicator or change in circumstances relating to impairment has occurred. If testing indicates that impairment has occurred, we would be required to write-off the impaired portion of goodwill and such intangible assets, resulting in a charge to our earnings. An impairment of a significant portion of goodwill or intangible assets could have a material adverse effect on our business, financial condition, and results of operations. Our impairment testing in 2014 indicated an impairment of goodwill and intangible assets relating to our Leaf reporting unit and related POS assets resulting in pre-tax impairment charges of $37.4 million, of which $18.5 million was related to goodwill.

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The costs and effects of pending and future litigation, investigations or similar matters, or adverse facts and developments related thereto, could materially affect our business, financial position, results of operations and cash flow.

We are from time-to-time involved in various litigation matters and governmental or regulatory investigations or similar matters arising out of our current or future business. Our insurance or indemnities may not cover all claims that may be asserted against us, and any claims asserted against us, regardless of merit or eventual outcome, may harm our reputation. Furthermore, there is no guarantee that we will be successful in defending ourselves in pending or future litigation or similar matters under various laws. Should the ultimate judgments or settlements in any pending litigation or future litigation or investigation significantly exceed our insurance coverage, they could have a material adverse effect on our business, financial condition, results of operations and cash flow. For more information about our legal proceedings, refer to “Item 3: Legal Proceedings” herein.

Future sales of our common stock, or the perception in the public markets that these sales may occur, could depress our stock price.

Sales of substantial amounts of our common stock in the public market, or the perception in the public markets that these sales may occur, could cause the market price of our common stock to decline. This could also impair our ability to raise additional capital through the sale of our equity securities. At December 31, 2014, we had 36,344,921 shares of our common stock outstanding. In addition, as of December 31, 2014, we had outstanding stock options and restricted share units totaling 1,439,612 shares issued under our amended and restated 2008 Equity Incentive Plan and our 2000 Incentive Stock Option Plan, of which 187,643 were vested. Assuming the exercise of all outstanding options to acquire our common stock and the vesting of all restricted share units and performance share units, our current stockholders would own on a fully-diluted basis 95% of the outstanding shares of our common stock, and the number of shares of our common stock available to trade could cause the market price of our common stock to decline. In addition to the adverse effect a price decline could have on holders of our common stock, such a decline could impede our ability to raise capital or to make acquisitions through the issuance of additional shares of our common stock or other equity securities.

Failure to maintain effective systems of internal control over financial reporting and disclosure controls and procedures could cause a loss of confidence in our financial reporting and adversely affect the trading price of our common stock.

Effective internal control over financial reporting is necessary for us to provide accurate financial information. Section 404 of the Sarbanes-Oxley Act requires us to evaluate the effectiveness of our internal control over financial reporting as of the end of each fiscal year and to include a management report assessing the effectiveness of our internal control over financial reporting in our Annual Report on Form 10-K. If we fail to maintain the adequacy of our internal control, we may not be able to conclude and report that we have effective internal control over financial reporting. If we are unable to adequately maintain our internal control over financial reporting, we may not be able to accurately report our financial results, which could cause investors to lose confidence in our reported financial information, negatively affecting the trading price of our common stock, or our ability to access the capital markets.

Provisions in our charter documents and Delaware law could discourage a takeover that our stockholders may consider favorable or could cause current management to become entrenched and difficult to replace.

Provisions in our amended and restated certificate of incorporation, in our bylaws and under Delaware law could make it more difficult for other companies to acquire us, even if doing so would benefit our stockholders. Our amended and restated certificate of incorporation and bylaws contain the following provisions, among others, which may inhibit an acquisition of our company by a third party:

- advance notification procedures for matters to be brought before stockholder meetings;
- a limitation on who may call stockholder meetings;
- a prohibition on stockholder action by written consent; and
- the ability of our Board of Directors to issue up to 10 million shares of preferred stock without a stockholder vote.

If any shares of preferred stock are issued that contain an extraordinary dividend or special voting power, a change in control could be impeded.

We are also subject to provisions of Delaware law that prohibit us from engaging in any business combination with any "interested stockholder," meaning, generally, that a stockholder who beneficially owns more than 15% of our stock cannot acquire us for a period of three years from the date this person became an interested stockholder unless various conditions are met, such as approval of the transaction by our Board of Directors. Any of these restrictions could have the effect of delaying or preventing a change in control.

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We may be unable or we may decide not to pay dividends on our common stock at a level anticipated by stockholders, which could depress our stock price.

The payment of dividends on our common stock in the future will be at the discretion of our Board of Directors and will depend on, among other factors, our earnings, stockholders' equity, cash position and financial condition. No assurance can be given that we will be able to or will choose to pay any dividends in the future.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not Applicable.

ITEM 2. PROPERTIES

At December 31, 2014, we owned one facility and leased thirty three facilities which we use for operational, sales and administrative purposes.

Our principal executive offices are located in approximately 9,300 square feet of leased office space on Nassau Street in Princeton, New Jersey. The Nassau Street lease expires in June 2023. We own 58 acres of land in Jeffersonville, Indiana, on which we constructed our operations and service center. The state-of-the-art facility is comprised of 238,000 square feet of space supporting customer service, operations, deployment, day care, fitness, cafeteria, and large company meetings.

As of December 31, 2014, we also leased the following facilities located throughout the United States to operate our business. Multi-purpose facilities include administrative, sales, operations, technology and facilities shared by multiple business segments.

Segment	Square Feet	Expiration
Multi-purpose	298,029	1/31/2015 to 12/31/2026
Campus Solutions	79,449	2/28/2015 to 12/31/2019
Heartland School Solutions	41,015	3/31/2015 to 6/30/2023
Heartland Payroll Solutions	53,781	7/31/2015 to 7/31/2019
Heartland Commerce	50,852	6/30/2015 to 6/30/2017
Heartland Marketing Solutions	10,838	12/31/2016
	533,964	

We believe that our facilities are suitable and adequate for our current business operations and, if necessary, could be replaced with little disruption to our company. We periodically review our space requirements and may acquire new space to meet our business needs or consolidate and dispose of or sublet facilities which are no longer required.

ITEM 3. LEGAL PROCEEDINGS

Processing System Intrusion Legal Proceedings

On January 20, 2009, we publicly announced the discovery of a criminal breach of our payment systems environment (the “Processing System Intrusion”). The Processing System Intrusion involved malicious software that appears to have been used to collect in-transit, unencrypted payment card data while it was being processed by us during the transaction authorization process. We believe the breach did not extend beyond 2008.

Several lawsuits were filed against us and our sponsor banks in connection with the Processing System Intrusion, including putative class action lawsuits brought by financial institutions and banks, which sought to represent all financial institutions that issued payment cards to cardholders whose transaction information was alleged to have been placed at risk in the course of the Processing System Intrusion. These actions were centralized before the United States District Court for the Southern District of Texas as part of a multi-district litigation captioned In re Heartland Payment Systems, Inc. Customer Data Security Breach Litigation, MDL No. 2046, 4:09-md-2046. These actions sought compensatory damages, including recovery of the cost of issuance of replacement cards and losses by reason of unauthorized transactions, as well as injunctive relief, attorneys' fees and costs.

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On February 26, 2015, the financial institutions named as plaintiffs in the putative financial institution class actions and/or in the actions that were transferred to or otherwise made part of the centralized multi-district litigation agreed to dismiss their claims with prejudice. As part of this dismissal, we made no payments to the named plaintiffs.

Other Legal Proceedings

In the ordinary course of our business, we are party to various legal actions, which we believe are incidental to the operation of our business. We believe that the outcome of the proceedings to which we are currently a party will not have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II.

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock trades on the New York Stock Exchange under the ticker symbol “HPY.” The following table sets forth the high and low sales prices of our common stock and dividend paid per share for the four quarters during the years ended December 31, 2014 and 2013:

	High	Low	Dividend Per Share
2013			
Quarter Ended:			
March 31, 2013	$33.70	$29.30	$0.07
June 30, 2013	$37.39	$30.29	$0.07
September 30, 2013	$40.38	$36.73	$0.07
December 31, 2013	$50.36	$37.57	$0.07
2014			
Quarter Ended:			
March 31, 2014	$50.44	$38.67	$0.085
June 30, 2014	$43.52	$37.25	$0.085
September 30, 2014	$49.46	$40.61	$0.085
December 31, 2014	$56.28	$46.67	$0.085

Holders of Common Stock

The number of stockholders of record of our common stock as of February 23, 2015 was 16.

Dividends

Our Board of Directors has declared a quarterly cash dividend on our common stock each quarter since the third quarter of 2006. The payment of dividends on our common stock in the future will be at the discretion of our Board of Directors and will depend on, among other factors, our earnings, stockholders' equity, cash position and financial condition. On February 13, 2015, our Board of Directors declared a quarterly cash dividend of $0.10 per share of common stock, payable on March 13, 2015 to stockholders of record as of March 2, 2015.

Securities Authorized For Issuance Under Equity Compensation Plans

We maintain the Heartland Payment Systems, Inc. Amended and Restated 2008 Equity Incentive Plan under which shares of our common stock are authorized for issuance. For more information on this plan, see Note 14, Stock Incentive Plans. Information regarding the common stock issuable under this plan as of December 31, 2014 is set forth in the following table:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders	1,439,612	$35.40	1,439,612
Equity compensation plans not approved by security holders	None	N/A	None
Total	1,439,612	$35.40	1,439,612

Purchases of Equity Securities by the Issuer

Open Repurchase Authorization. On May 8, 2014, our Board of Directors authorized the repurchase of up to $75 million of our outstanding stock. We intend to fund any repurchases with cash flow from operations, existing cash on the balance sheet, and other sources including our 2014 Revolving Credit Facility. The manner, timing and amount of repurchases, if any, will be determined by management and will depend on a variety of factors, including price, corporate and regulatory requirements, market conditions and other corporate liquidity requirements. The repurchase program may be modified or discontinued at any time. As of December 31, 2014, we have not repurchased any shares under the May 8, 2014 authorization.

Performance Graph

The following graph compares the percentage change in cumulative total stockholder return on our common stock for the past five years with the cumulative total returns over the same period of (i) the S&P 500 Index and (ii) the S&P Information Technology Index.

The below comparison assumes $100 was invested on December 31, 2009 in our common stock and in the S&P 500 Index and the S&P Information Technology Index, and assumes reinvestment of dividends, if any. Historical stock prices are not indicative of future stock price performance.

	Base Period	Period Ended				
	12/31/2009	12/31/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014
Heartland Payment Systems, Inc.	$100.00	$117.73	$187.49	$228.91	$389.80	$425.11
S&P 500	100.00	115.06	117.49	136.30	180.44	205.14
S&P Information Technology Index	100.00	110.19	112.85	129.57	166.41	199.89

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ITEM 6. SELECTED FINANCIAL DATA

The following table sets forth our selected historical consolidated financial information and other data for the years ended December 31, 2014, 2013, and 2012, which are derived from our consolidated financial statements included elsewhere in this report. Historical consolidated financial information for 2011 and 2010 are derived from our consolidated financial statements for those years (not included herein). The information in the following table should be read together with “Management's Discussion and Analysis of Financial Condition and Results of Operations” and our consolidated financial statements and the related notes included elsewhere in this report.

	Year Ended December 31,				
	2014	2013	2012	2011	2010
Income Statement Data:	(In thousands, except per share data)				
Total revenues	$2,311,381	$2,135,372	$2,013,436	$1,985,577	$1,855,839
Total costs of services	2,001,342	1,835,706	1,763,701	1,783,731	1,710,335
General and administrative	190,554	173,568	139,934	125,765	99,912
Goodwill impairment charge	18,490	—	—	—	—
Asset impairment charges	18,875	—	—	—	—
Total expenses	2,229,261	2,009,274	1,903,635	1,909,496	1,810,247
Income from operations	82,120	126,098	109,801	76,081	45,592
Net income from continuing operations	31,868	74,102	64,353	42,988	34,183
Net income attributable to Heartland	33,879	78,626	65,889	43,939	34,537
Basic earnings per share:					
Income from continuing operations	$0.93	$2.03	$1.67	$1.10	$0.90
Income from discontinued operations	$—	$0.11	$0.04	$0.03	$0.01
Basic earnings per share	$0.93	$2.14	$1.71	$1.13	$0.91
Diluted earnings per share:					
Income from continuing operations	$0.91	$1.96	$1.60	$1.07	$0.87
Income from discontinued operations	$—	$0.10	$0.04	$0.02	$0.01
Diluted earnings per share	$0.91	$2.06	$1.64	$1.09	$0.88
Weighted average number of common shares outstanding:					
Basic	36,354	36,791	38,468	38,931	37,994
Diluted	37,187	38,053	40,058	40,233	39,310
Dividends declared per share	$0.34	$0.28	$0.24	$0.16	$0.04
Other Data:					
Net revenue*	$672,625	$598,982	$529,895	$470,896	$436,374
Operating margin	12.2 %	21.1 %	20.7 %	16.2 %	10.4 %

*Net revenue is defined as total revenues less Interchange fees and dues, assessments, and fees.

	As of December 31,				
	2014	2013	2012	2011	2010
Balance Sheet Data:	(In thousands)				

Total assets	$1,387,773	$900,305	$813,414	$596,921	$561,464
Current portion of borrowings	36,792	—	102,001	15,003	38,286
Long-term borrowings	523,122	150,000	50,000	70,000	85,000
Total liabilities	1,137,013	633,642	602,253	376,869	383,870
Total stockholders' equity	250,760	260,475	209,786	219,410	177,293

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the consolidated financial statements and the accompanying notes to consolidated financial statements and the risk factors included elsewhere in this report.

Overview

General

Our primary business is to provide payment processing services to merchants throughout the United States. This involves providing end-to-end electronic payment processing services to merchants by facilitating the exchange of information and funds between them and cardholders' financial institutions. To accomplish this, we undertake merchant set-up and training, transaction authorization and electronic draft capture, clearing and settlement, merchant accounting, merchant assistance and support, and risk management. Our card-accepting customers primarily fall into two categories: our core small and mid-sized merchants (referred to as "Small and Midsized Enterprises," or “SME merchants”) and Network Services merchants, predominately petroleum industry merchants of all sizes (referred to as “Network Services merchants”).

We provide additional services such as:

- Integrated commerce solutions, payment processing, higher education loan services and open and closed-loop payment solutions to higher-education institutions through Campus Solutions,
- School nutrition, point-of-sale solutions ("POS"), and associated payment solutions, including online prepayment solutions, to kindergarten through 12th grade ("K-12") schools through Heartland School Solutions,
- Full-service payroll processing and related tax filing services throughout the United States provided by Heartland Payroll Solutions, and
- Other including (1) prepaid and stored-value card solutions throughout the United States and Canada provided by Micropayments, (2) POS solutions and other adjacent business service applications through Heartland Commerce, and (3) marketing solutions including loyalty and gift cards which we provide through Heartland Marketing Solutions.

Payment Processing

At December 31, 2014, we provided our card payment processing services to 169,831 active SME merchants located across the United States. This compares to 166,697 active SME merchants at December 31, 2013. At December 31, 2014, we provided card payment processing services to approximately 2,181 Network Services merchants with approximately 42,397 locations, compared to 1,024 Network Services merchants with 42,669 locations at December 31, 2013. The increase in the number of Network Services merchants in 2014 primarily reflects adding smaller-size merchants (merchants with single or few locations), predominantly in the petroleum industry. While the decrease in the number of Network Services merchant locations for 2014 reflects a decline in the number of locations we serve for a large retail merchant, partially offset by the locations added by those smaller-size petroleum industry merchants.

Our total card processing volume for the year ended December 31, 2014 was $109.9 billion, a 7.4% increase from the $102.3 billion processed during the year ended December 31, 2013. Our SME card processing volume for the year ended December 31, 2014 was $81.1 billion, a 8.7% increase over $74.6 billion in 2013. This increase in processing volume reflects same store sales growth and the addition of SME merchants whose processing volume exceeded that of merchants who attrited during the year. The increase in SME processing volume also reflects the impact of the new American Express Card Acceptance Program (referred to as "OptBlue") to new and existing merchants. We converted a majority of our existing merchants currently processing under the former sales and servicing agreement with American Express to OptBlue during the third quarter of 2014. Our card processing volume for 2014 also includes $28.8 billion of settled volume for Network Services merchants, compared to $27.7 billion for 2013. Card processing volume for the years ended December 31, 2014, 2013 and 2012 was as follows:

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	Year Ended December 31,		
	2014	2013	2012
	(In millions)		
SME merchants	$81,077	$74,578	$71,724
Network Services merchants	28,848	27,710	27,894
Canada (a)	—	59	770
Total card processing volume (b)	$109,925	$102,347	$100,388

(a) Canadian operations were discontinued as result of the sale of CPOS in January 2013.
(b) Card processing volume includes volume for credit and signature debit transactions.

Merchant attrition is expected in the card payment processing industry in the ordinary course of business. We experience attrition in merchant card processing volume resulting from several factors, including business closures, transfers of merchants' accounts to our competitors and account closures that we initiate due to heightened credit risks. We measure SME processing volume attrition relative to all SME merchants that were processing with us in the same month a year earlier. During the year ended December 31, 2014, we experienced 12.7% average annualized attrition in our SME card processing volume compared to average attrition of 12.9% and 12.8% for the years ended December 31, 2013 and 2012, respectively.

In our SME business, we measure same store sales growth, or contraction, as the change in card processing volume for all card merchants that were processing with us in the same month a year earlier. In 2014, same store sales grew 2.0% on average, compared to 2.0% and 2.2% same store sales growth in 2013 and 2012, respectively. Same store sales growth or contraction results from the combination of the increasing or decreasing use by consumers of bankcards for the purchase of goods and services at the POS, and sales growth or contraction experienced by our retained SME merchants. Historically, our same store sales experience has tracked overall economic conditions. The following table compares our same store sales growth or contraction during 2014, 2013 and 2012:

Same Store Sales Growth (Contraction)	2014	2013	2012
First Quarter	(0.2)%	2.2%	3.4%
Second Quarter	2.4%	1.9%	2.2%
Third Quarter	1.8%	1.6%	1.8%
Fourth Quarter	3.9%	2.4%	1.5%
Full Year	2.0%	2.0%	2.2%

We measure the overall production of our sales force by new gross margin installed, which reflects the expected annual gross profit from a merchant contract after deducting processing and servicing costs associated with that revenue. We measure installed margin primarily for our SME card processing, payroll processing and loyalty and gift card marketing businesses. In 2014, our newly installed gross margin for the year increased 17% from the gross margin we installed during the year ended December 31, 2013 compared to increases of 22% and 12% in 2013 and 2012, respectively. We attribute this increase in newly installed gross margin to higher volumes and margins at newly installed merchants and improved individual productivity achieved by our salespersons as well as growth in the sales force. Our combined Relationship Managers, Territory Managers, and Senior Product Advisors ("SPAs") totaled to 985, 844 and 739 at December 31, 2014, 2013 and 2012, respectively. We expect to drive increases in year-over-year installed margin in future periods primarily by increasing the number of SPAs and Relationship and Territory Managers.

The card revenue we earn in our SME business is recurring in nature, as we typically enter into three-year service contracts with our card processing SME merchants that, in order to qualify for the agreed-upon pricing, require the merchant to achieve card processing volume minimums. Our SME revenue is generated primarily from payment processing fees, which are a combination of a fee equal to a percentage of the dollar amount of each transaction we process plus a flat fee per transaction. We make mandatory payments of interchange fees to the card issuer through the card networks and dues, assessments and other network fees to Visa, MasterCard and Discover. Our SME gross card processing revenue is largely driven by the Visa and MasterCard volume processed by our merchants. We also realize card processing revenues from processing transactions for our SME merchants accepting American Express and from processing Discover transactions.

In contrast to SME card processing revenues, revenues from our Network Services merchants are largely driven by the number of transactions we process (whether settled, or only authorized), not our processing volume, as the merchants which comprise Network Services' customer base pay on a per transaction basis for processing services. The number of Network Services transactions increased in 2014 primarily due to an increase in the number of transactions at our large petroleum merchants.

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Additionally, we provide authorization, settlement and account servicing services on our front and back end systems for American Express transactions for SME merchants and merchants originally signed to American Express by other processors. For those services we receive compensation from American Express on a per transaction basis. The number of transactions we processed for Network Services merchants and American Express for the years ended December 31, 2014, 2013 and 2012 were as follows:

	Year Ended December 31,		
	2014	2013	2012
Network Services merchants:	(In thousands)		
Authorized	2,384,723	2,347,776	2,481,174
Settled	1,083,606	967,230	957,756
Total Network Services	3,468,329	3,315,006	3,438,930
American Express (a)	17,150	32,016	32,306
Total	3,485,479	3,347,022	3,471,236

(a) Includes only those transactions not eligible for residual compensation

Our ability to manage our front-end authorization systems, HPS Exchange, VAPS and NWS, provides us greater control of the electronic transaction process, allows us to offer our merchants a differentiated product offering, and offers economies of scale that we expect will increase our long-term profitability. During the years ended December 31, 2014, 2013 and 2012, approximately 96%, 96% and 95%, respectively, of our SME transactions were processed through HPS Exchange. All of our Network Services transactions were processed through VAPS or NWS.

We provide clearing, settlement and merchant accounting services through our own internally developed back-end processing system, Passport. Passport enables us to customize these services to the needs of our Relationship Managers and merchants. At both December 31, 2014 and 2013, substantially all of SME merchants were processing on Passport and all Network Services settled transactions were processed on Passport.

We sold our interest in Collective POS Solutions Ltd. ("CPOS") in a transaction settled in January 2013. CPOS has historically represented an insignificant component of our financial position and results of operations. However, as further disclosed elsewhere in the notes to consolidated financial statements, we recognized a gain on the sale of CPOS in the first quarter of 2013. As a result, we presented the net assets of CPOS as held for sale at December 31, 2012 and presented the results of operations for CPOS as a discontinued operation for all periods presented.

Campus Solutions

Campus Solutions provides payment processing, integrated commerce solutions, higher education loan services and open- and closed-loop payment solutions to campuses throughout the United States and Canada.

We provide a suite of solutions to support administrative services for higher education including student loan payment processing, delinquency and default services, refund management, tuition payment plans, electronic billing and payment, tax document services, and business outsourcing. Our OneCard product enables personal identification, door access, cashless vending and laundry transactions, meal plans and cashless printing at campus facilities. Our innovative Give Something Back Network adds internet and phone accessible closed-loop debit card based financial services to the students, faculty, staff and local community merchants of an educational institution.

On September 4, 2014, we acquired TouchNet Information Systems, Inc. ("TouchNet"), an integrated commerce solutions provider to higher-education institutions. TouchNet became a part of our Campus Solutions business. See "—Liquidity and Capital Resources — Acquisitions" for additional information on this transaction. TouchNet added over 600 higher education clients serving over six million students which is nearly one-third of higher education enrollment in the United States.

As of December 31, 2014, we provided services to more than 2,600 colleges and universities supporting approximately $16 billion in higher education payments, 23 million payment transactions, 1.5 million active student and student borrower loan/tuition accounts, 5 million tax documents annually and over $650 million in annual reimbursements.

Heartland School Solutions

We provide school nutrition, POS solutions, and associated payment solutions including online prepayment, to K-12 schools throughout the United States. At December 31, 2014, our Heartland School Solutions business provided services to more than 34,000 public and private schools, as compared to over 29,000 public and private schools at December 31, 2013. Our Heartland School Solutions business has been built through a series of six acquisitions, including the April 2014 acquisition of

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MCS Software. This acquisition continues the expansion of our market-leading position in the K to 12 school nutrition and POS technology industry. The more than 34,000 K-12 schools that Heartland School Solutions serves nationwide, represents a 35% share of the public schools in the U.S.

Heartland Payroll Solutions

We provide payroll processing services throughout the United States. On December 31, 2012, we acquired Ovation Payroll, Inc. ("Ovation") adding more than 10,000 customers to our existing payroll business. At December 31, 2014, we processed payroll for 25,764 customers, an increase of 7.0% from 24,088 payroll customers at December 31, 2013. In 2014, 2013 and 2012, we added 5,821, 5,797 and 2,984, respectively, new payroll processing customers. We operate a comprehensive payroll management platform, which we refer to as HPS (formerly PlusOne Payroll, and Heartland Ovation Payroll or HOP), that streamlines all aspects of the payroll process to enable time and cost savings.The HPS platform enables us to process payroll on a large scale and provide customizable solutions for businesses of all sizes.

Heartland Commerce

We provide leading-edge POS solutions, payments processing capabilities and other adjacent business service applications, serving the hospitality and retail industry through our recently organized Heartland Commerce business.

On October 31, 2014, we acquired the net assets of Xpient Solutions, LLC (“Xpient”) for a cash payment of $30.0 million, plus net working capital. The purchase price was funded from a combination of operating cash and financing under our 2014 Revolving Credit Facility. Xpient provides POS software solutions to customers primarily in the food service industry. Xpient’s applications include back office and enterprise management; solutions that help efficiently take orders, manage labor, control inventory, support customer loyalty programs, and manage data.

On February 15, 2014, we purchased the assets of Merchant Software Corporation (referred to as "Liquor POS") for a $3.3 million cash payment. The purchase price was funded from operating cash flows. Liquor POS is a leading provider of POS systems to the liquor retail vertical. It currently serves over 3,400 merchants to whom we expect to offer our products and services.

Heartland Commerce is comprised of existing POS businesses; Xpient, Liquor POS, and our other POS solutions, and will include the recently acquired Automation, Inc. (d/b/a “pcAmerica” in January 2015) and Dinerware, Inc. (“Dinerware” in February 2015) POS businesses (see "— Liquidity and Capital Resources — Acquisitions and Divestitures" for more detail). Dinerware and pcAmerica are in the process of developing cloud-based POS systems that complement their well-established on-premise POS solutions. These cloud-based POS systems overlap with what was being developed by Leaf, and Dinerware and pcAmerica technologies and development plans provided management insight into the status and positioning of Leaf’s technology in the marketplace. Consequently, management decided that it will stop POS development efforts at Leaf, and write down related POS assets.

Separately, we determined that our investment in TabbedOut, a mobile payments provider, was substantially impaired as of December 31, 2014 and recorded an impairment charge of $4.0 million related to that investment. In the fourth quarter ended December 31, 2014, we recorded total asset impairment charges of $41.4 million pre-tax, ($37.6 million after-tax, or $1.02 per share), related to the values ascribed to our investments at Leaf and in Prosper, an internally developed POS software technology, and our investment in TabbedOut, a mobile payments provider.

2014 Financial Highlights

For 2014, we recorded net income from continuing operations attributable to Heartland of $33.9 million, or $0.91 per share compared to $74.7 million or $1.96 per share, in 2013. Net income from continuing operations for 2014 reflects the following:

- Asset impairment charges related to our investment in Leaf and other POS assets, and our investment in the stock of TabbedOut, of $41.4 million pre-tax ($37.6 million after-tax, or $1.02 per share). We recently acquired pc America and Dinerware for its Heartland Commerce segment (see "— Overview — Heartland Commerce"). Heartland Commerce provides a comprehensive suite of POS solutions, payments processing capabilities and other adjacent business service applications. Heartland Commerce is comprised of existing POS businesses; Xpient, Liquor POS, Leaf and our other POS solutions, and will include pcAmerica and Dinerware. Dinerware and pcAmerica are in the process of developing cloud-based POS systems that complement their well-established on-premise POS solutions. These cloud-based POS systems overlap with what was being developed by Leaf, and Dinerware and pcAmerica technologies and development plans provided insight into the status and positioning of Leaf's technology in the marketplace. Consequently, we decided that we will stop POS development efforts at Leaf. This decision caused a significant adverse change in the extent or manner in which the long-lived asset group for Leaf will be used, including Prosper, an internally developed POS software technology. These circumstances also resulted in the implied fair value of the Leaf reporting unit being significantly below its carrying value, which caused a Goodwill Impairment charge for the full balance of Leaf Goodwill as of December 31, 2014, as well as, asset impairment charges for Prosper and for the Leaf intangible and long-lived assets.

During the fourth quarter of 2014, we reviewed our investment in the stock of TabbedOut and estimated that the fair value of its investment in Tabbedout was substantially impaired, and therefore, an impairment charge was recorded as of December 31, 2014.

- Pre- and after-tax gain of $3.6 million, or $0.10 per share, recognized as a result of our August 6, 2014 acquisition of all shares of Leaf common stock held by noncontrolling shareholders and the concurrent release from a contingent earn-out liability to those noncontrolling shareholders.

Our income from operations, which we also refer to as operating income, decreased $44.0 million to $82.1 million for 2014, from $126.1 million for 2013. Our Operating Margin, which we measure as operating income divided by net revenue, was 12.2% for 2014, compared to 21.1% for 2013. Operating income and Operating Margin decreased for 2014 primarily as a result of the POS asset and goodwill impairment charges described above. Excluding the impact of the goodwill and asset impairment charges during the fourth quarter, our operating income would have been $119.5 million or 17.8% for 2014. Our operating results for 2014 also reflect 12.3% year-over-year growth in net revenue, partially offset by increases of 20.1% in processing and servicing costs and 9.8% in general and administrative expenses. We define net revenue as total revenues less interchange fees and dues, assessments and fees. The following is a summary of our operating results for the year ended December 31, 2014.

- Net revenue increased 12.3% to $672.6 million during 2014, from $599.0 million during 2013. The increase in net revenue was driven by growth in card processing net revenue from our SME merchants and increases in revenues across all other non-card payment processing businesses including Heartland School Solutions, Heartland Payroll Solutions, Campus Solutions and Other Revenues (predominately related to an increase in net revenue relating to our Micropayments business and the acquisition of Xpient on October 31, 2014). The growth in these non-card payment processing businesses was aided in part by the 2014 acquisition of TouchNet which added $19.9 million in revenue since its September 4, 2014 acquisition. See "— Liquidity and Capital Resources — Acquisitions" for further information on these acquisitions.

- SME card processing volume increased 8.7% to $81.1 billion, compared to $74.6 billion in 2013. We earn percentage-based revenues on our SME processing volume. The year-over-year increase reflects same store sales growth and the addition of SME merchants whose processing volume and net revenue exceeded that of merchants who attrited in the same period. The increase in SME processing volume also reflects the conversion of new and existing merchants to OptBlue. We converted a majority of our existing merchants currently processing under the former sales and servicing agreement with American Express to OptBlue during the third and fourth quarters of 2014.

- Our processing and servicing expenses for 2014 increased by $47.8 million, or 20.1%, compared with 2013. The increase in processing and servicing expenses for the year ended December 31, 2014 reflects the acquisitions of MCS Software, TouchNet and Xpient, as well as, increased costs associated with processing and servicing higher SME bankcard processing volume, increased sales compensation, higher merchant losses as a result of chargebacks from a single merchant who entered bankruptcy in the fourth quarter and increased cost of sales and servicing related to higher Heartland School Solutions, Heartland Payroll Solutions, Campus Solutions, and Other revenues (primarily our Micropayments business). The increase in processing and servicing expenses also reflects approximately $6.5 million of expenses which were classified as general and administrative expense in the prior year. This reclassification brings operating expenses in our legacy payroll business and Ovation business into alignment.

Our general and administrative expenses for the year ended December 31, 2014 increased by $17.0 million, or 9.8%, from $173.6 million in 2013 to $190.6 million in 2014. General and administrative expenses increased primarily due to a $15.2 million increase in personnel costs and an increase of $2.7 million in occupancy costs. The increase in personnel and occupancy costs primarily reflects the acquisitions of Leaf in September 2013, MCS Software in April 2014, TouchNet in September 2014 and Xpient in October 2014, as well as other headcount increases. The remaining increase in general and administrative expenses resulted from our acquisitions, including $3.7 million of acquisition-related expenses. Partially offsetting these increases was a decrease due to the reclassification of $6.5 million of payroll related expenses from general and administrative to processing and servicing expense for our payroll business as well as lower equipment lease and information technology related expenses.

See "— Results of Operations — Year Ended December 31, 2014 Compared to Year Ended December 31, 2013" for a more detailed discussion of our full year operating results.

Components of Revenues and Expenses

Revenue. We classify our revenues into five categories: (i) Payment Processing, (ii) Campus Solutions, (iii) Heartland School Solutions, (iv) Heartland Payroll Solutions and (v) Other.

Payment Processing revenue primarily consists of discount, per-transaction and periodic (primarily monthly) fees from the processing of Visa, MasterCard, American Express and Discover transactions for SME merchants and per-transaction fees for the authorization and settlement of transactions for Network Services merchants. Also included in this category are American Express servicing fees, merchant service fees, fees for processing chargebacks and termination fees on terminated contracts. Interchange fees, which are our most significant expense, are set by the card networks and paid to the card issuing banks. For the majority of SME card processing revenue, we do not offset processing revenues and interchange fees because our business practice is to advance the interchange fees to most SME merchants when settling their daily transactions (thus paying the full amount of the transaction to the merchant), and then to collect the full discount fees from merchants on the first business day of the next month. For SME merchants to whom we do not advance interchange, we record card processing revenues net of interchange fees. As Network Services does not advance interchange fees to its merchants, we record card processing revenues net of interchange fees. We record Payment Processing revenue at the time services are provided.

Campus Solutions revenue includes fees associated with providing integrated commerce solutions to support administrative services for higher education, as well as, student loan payment processing, delinquency and default services, refund management, tuition payment plans, electronic billing and payment, tax document services and business outsourcing. Campus Solutions revenue also includes fees from the sale and maintenance of open- and closed-loop payment hardware and software solutions for college or university campuses to process small value electronic transactions.

Heartland School Solutions' revenue includes fees from sales and maintenance of cafeteria POS solutions and associated payment solutions, including online prepayment solutions, back office management and hardware and technical support.

Heartland Payroll Solutions revenue includes fees charged for payroll processing services, including check printing, direct deposit, related federal, state and local tax deposits and providing accounting documentation and interest income earned on funds held for customers. Revenues are recorded at the time service is provided.

Other revenues include Micropayments' fees from selling hardware and software for unattended online wireless credit card based payment systems, and unattended value top up systems for off-line closed-loop smart (chip) card based payment systems. Also included in this category are Heartland Marketing Solutions' fees from selling mobile and card-based marketing services, gift cards and rewards services as well as fees from selling, renting and deploying POS devices. Other revenues also include Heartland Commerce, which provides leading-edge POS solutions, payments processing capabilities and other adjacent business service applications, serving the hospitality and retail industry. Revenues are recorded at the time of shipment or at the time services are provided.

Net Revenue. We define net revenue as total revenues less interchange fees and dues, assessments and fees. Management uses net revenue to assess our operating performance, including operating margin.

Expenses. In addition to interchange fees, we also pay Visa, MasterCard, American Express and Discover, as well as certain PIN networks, dues, assessments and fees, which are a combination of a percentage of the dollar volume processed and per-transaction fees. Interchange fees and dues, assessments and fees are recognized at the time transactions are processed. It is our policy to pass along to our merchants any changes in interchange fees and card network dues, assessments and fees. Since the card networks regularly adjust those rates, our gross card processing revenue will increase or decrease, but all the impact of such changes will be paid to the card issuing banks and our net revenue and income from operations will not be affected.

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Costs of services also include processing and servicing costs, customer acquisition costs, and depreciation and amortization. Processing and servicing costs include:

- processing costs, which are either paid to third parties, including our bank sponsors, or represent the cost of our own authorization/capture and accounting/settlement systems. During 2014 and 2013, costs we paid to third parties represented about 34% and 39% of our processing costs, respectively;
- residual commission payments to our Relationship Managers, sales managers, trade associations, agent banks and value-added resellers, which are a percentage of the gross margin we generated from our merchant contracts during the accounting period;
- the costs of operating our service center and other customer support locations, including telecommunications costs, personnel costs, occupancy costs, losses due to merchant defaults, depreciation and amortization, and other direct servicing costs; and
- the costs of merchant supplies, bankcard terminals, POS systems, hardware and software deployed in our businesses.

Customer acquisition costs reflect the amortization over the initial three-year contract term of the cash signing bonus paid, and the deferred acquisition costs accrued for vested Relationship Managers and sales managers, as well as changes in the accrued buyout liability, which reflect the impact of buying out residual commissions and volume attrition (see "— Critical Accounting Estimates — Accrued Buyout Liability") .

Depreciation and amortization expenses consist of depreciation on our investments in property, equipment and software, and our amortization of acquired intangible assets. Depreciation and amortization expenses are primarily recognized on a straight-line basis over the estimated useful life of the asset, except for the amortization of customer relationships intangible assets which is recognized using a proportional cash flow method.

General and administrative expenses include personnel and other administrative expenses related to our information technology infrastructure costs, our marketing expenses and other administrative functions.

Critical Accounting Estimates

The discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses. Actual results could differ from those estimates. Our significant accounting policies are more fully described in Note 2 to our consolidated financial statements included elsewhere in this report. The critical accounting estimates described here are those that are most important to the depiction of our financial condition and results of operations, including those whose application requires management's most subjective judgment in making estimates about the effect of matters that are inherently uncertain. The line items on our income statement and balance sheet, which are impacted by management's estimates, are described below.

Revenue

Our card processing revenue is derived from processing and settling Visa, MasterCard, American Express and Discover bankcard transactions for our merchant customers. Our most significant expense related to the generation of those revenues is interchange fees, which are set by the card networks, and paid to the card issuing banks. For our SME merchant card processing, we do not offset card processing revenues and interchange fees in our income statement because our business practice is to advance the interchange fees to most of our SME merchants when settling their daily transactions (thus paying the full amount of the transaction to the merchant), and then to collect our full discount fees from our merchants on the first business day of the next month. We fund interchange advances to our SME merchants from a combination of our operating cash, processing cash and advances from our sponsor banks. We believe this policy aids in new business generation, as our merchants benefit from bookkeeping simplicity. However, this practice results in our carrying a large receivable from our merchants at each period-end, and a corresponding but smaller payable to our sponsor banks, which are settled on the first business day after the period-end. As we are at risk for the advance receivables, we record the associated revenues on a gross processing revenue basis in our consolidated Statements of Income. We have merchant portability, credit risk, and the ultimate responsibility to the merchant and, as such, revenue is reported at the time of settlement on a gross basis. Payment processing services are transaction based and priced either as a fixed fee per transaction or calculated as a percentage of the transaction value. The fees are charged for the processing services provided and do not include the gross sales price paid by the ultimate buyer to the merchant. Certain of our competitors report their processing revenue net of interchange fees. This is because the card issuing banks make their payments to these competitors net of those interchange fees, and these acquirers pay this reduced amount to their merchants. For our Network Services merchants, we also record a portion of our processing revenues net of interchange fees because the daily cash settlement with Network Services' merchants is net of interchange fees.

We also evaluate contractual arrangements for indications that multiple element arrangements may exist including instances where more-than-incidental software deliverables are included. Both Campus Solutions and Heartland School Solutions have arrangements that contain multiple elements, such as hardware, software products, including perpetual licenses and Software-as-a-Service (“SaaS”) services, maintenance, and professional installation and training services. We allocate revenues to each element based on the selling price hierarchy. The selling price for a deliverable is based on vendor specific objective evidence (“VSOE”) of selling price, if available, or estimated selling price (“ESP”) if VSOE of selling price is not available. We establish ESP, based on our judgment, considering internal factors such as margin objectives, pricing practices and controls, customer segment pricing strategies and the product life cycle. In arrangements with multiple elements, we determine allocation of the transaction price at inception of the arrangement based on the relative selling price of each unit of accounting.

In multiple element arrangements where more-than-incidental software deliverables are included, we have applied the residual method to determine the amount of software license revenues to be recognized. Under the residual method, if fair value exists for undelivered elements in a multiple-element arrangement, such fair value of the undelivered elements is deferred with the remaining portion of the arrangement consideration recognized upon delivery of the software license or services arrangement. We allocate the fair value of each element of a software related multiple-element arrangement based upon its fair value as determined by VSOE, with any remaining amount allocated to the software license. If evidence of the fair value cannot be established for the undelivered elements of a software arrangement then the entire amount of revenue under the arrangement is deferred until these elements have been delivered or objective evidence can be established.

Capitalized Customer Acquisition Costs

Capitalized customer acquisition costs consist of (1) up-front signing bonuses paid to Relationship Managers, SPAs and sales managers, referred to as the "salesperson" or "salespersons," for the establishment of new merchant relationships, and (2) deferred acquisition cost representing the estimated cost of buying out the commissions of vested salespersons at some point in the future. Capitalized customer acquisition costs represent incremental, direct customer acquisition costs that are recoverable through gross margins associated with SME merchant contracts. The capitalized customer acquisition costs are amortized using a method which approximates a proportional revenue approach over the initial three-year term of the merchant contract.

The amount of the up-front signing bonus paid for new SME card, payroll and loyalty marketing accounts is based on the estimated gross margin for the first year of the merchant contract. The gross signing bonuses paid during 2014, 2013 and 2012 were $42.7 million, $32.7 million and $32.4 million, respectively. The signing bonus paid, amount capitalized, and related amortization are adjusted at the end of the first year to reflect the actual gross margin generated by the merchant contract during that year. The net signing bonus adjustments made during 2014, 2013 and 2012 were $(4.0) million, $(3.7) million and $(3.1) million, respectively. Negative signing bonus adjustments occur when the actual gross margin generated by the merchant contract during the first year is less than the estimated gross margin for that year, resulting in the overpayment of the up-front signing bonus, which overpayment would be recovered from the relevant salesperson. Positive signing bonus adjustments result from prior underpayments of up-front signing bonuses, and would be paid to the relevant salesperson.

The deferred acquisition cost component of capitalized customer acquisition costs is accrued for vested salespersons over the first year of SME card, payroll and loyalty marketing merchant processing, consistent with the build-up in the accrued buyout liability, which is described below.

Management evaluates the capitalized customer acquisition costs for impairment by comparing, on a pooled basis by vintage month of origination, the expected future net cash flows from underlying merchant relationships to the carrying amount of the capitalized customer acquisition costs. If the estimated future net cash flows are lower than the recorded carrying amount, indicating an impairment of the value of the capitalized customer acquisition costs, the impairment loss will be charged to operations. We have not recognized an impairment loss of this type in 2014, 2013 or 2012.

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Accrued Buyout Liability

We pay our salespersons residual commissions based on the gross margin generated from the monthly processing activity of SME, payroll, and loyalty marketing merchant accounts signed by them. We refer to these residual commissions as the "owned" portion of such commissions, or "portfolio equity." The salesperson has no obligation to perform additional services for the merchant for so long as the merchant continues processing with us. We have the right, but not the obligation, to buy out some or all of these commissions, and intend to do so periodically. We accrue the buyout liability, which represents the estimated current settlement cost of buying out all vested and expected-to-vest salespersons for the owned portion of such commissions. We also record a deferred acquisition cost asset related to those buyouts, and amortize that asset as an expense over the initial three year contract term.

We consider a salesperson to be vested once they have established merchant relationships that generate the equivalent of $10,000 of monthly gross margin. Vested status entitles the salesperson to his or her residual commissions for as long as the merchant processes with us, even if the salesperson is no longer employed by us.

The accrued buyout liability is based on the merchants we have under contract at the balance sheet date, the gross margin we generated from those accounts in the prior twelve months, the “owned” commission rate, and the fixed buyout multiple of 2.5 times the commissions. The liability related to a new merchant is therefore zero when the merchant is installed, and increases over the twelve months following the installation date. A small portion of our accrued buyout liability, approximately 6%, relates to salespersons who have opted to receive a multiple of 2.0 times commissions in exchange for a larger company contribution towards health insurance.

For unvested salespersons, the accrued buyout liability is accrued over the expected vesting period; however, no deferred acquisition cost is capitalized as future services are required in order to vest. In calculating the accrued buyout liability for unvested salespersons, we have assumed that 31% of unvested salespersons will vest in the future, which represents our historical vesting rate. A 5% increase to 36% in the expected vesting rate would have increased the accrued buyout liability for unvested salespersons by $0.2 million and $0.1 million at December 31, 2014 and 2013, respectively.

Buyout payments made to salespersons reduce the outstanding accrued buyout liability. Given our view of the duration of the cash flows associated with a pool of merchant contracts, we believe that the benefits of such buyouts significantly exceed the cost, which typically represents 2 ½ years of commissions. If the cash flows associated with a pool of bought out contracts does not exceed this cost, we will incur an economic loss on our decision to buyout the contracts. During 2014, 2013, and 2012, we made buyout payments of approximately $11.6 million, $13.7 million and $11.9 million, respectively.

Processing Liabilities

Processing liabilities result primarily from our card processing activities and include merchant deposits maintained to offset potential liabilities arising from merchant chargebacks. At December 31, 2014 and 2013, processing liabilities totaled approximately $119.4 million and $130.9 million, respectively. In the fourth quarter of 2012, we accelerated the end-of-day presentment of transaction funding files to the bankcard networks, resulting in our sponsor banks receiving settlement cash one day earlier and increasing our funding obligations to our SME merchants, which we carry in processing liabilities.

Disputes between a cardholder and a merchant periodically arise as a result of, among other things, the cardholder's dissatisfaction with merchandise quality or merchant services. Such disputes may not be resolved in the merchant's favor. In these cases, the transaction is "charged back" to the merchant, which means the purchase price is refunded to the customer by the card-issuing bank and charged to the merchant. If the merchant is unable to fund the refund, we must do so. We also bear the risk of reject losses arising from the fact that we collect our fees from our merchants on the first day after the monthly billing period. If the merchant has gone out of business during such period, we may be unable to collect such fees. We maintain cash deposits or require the pledge of a letter of credit from certain merchants, generally those with higher average transaction size where the card is not present when the charge is made or the product or service is delivered after the charge is made, in order to offset potential contingent liabilities such as chargebacks and reject losses that would arise if the merchant went out of business. At December 31, 2014 and 2013, we held SME merchant deposits totaling \$6.2 million and \$7.7 million, respectively. Most chargeback and reject losses are charged to processing and servicing as they are incurred. However, we also maintain a loss reserve against losses including major fraud losses, which are both less predictable and involve larger amounts. The loss reserve was established using historical loss rates, applied to recent card processing volume. At December 31, 2014 and 2013, our loss reserve totaled \$3.4 million and \$1.5 million, respectively. Aggregate SME merchant losses were \$7.3 million, \$3.1 million and \$2.0 million, or 0.90 basis points, 0.41 basis points and 0.28 basis points, respectively, of our SME card processing volume for the years ended December 31, 2014, 2013 and 2012. In 2014,

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our losses included $4.6 million resulting from chargebacks from a single merchant who entered bankruptcy in the fourth quarter. Chargeback losses originating from Network Services card processing on Passport during the year ended December 31, 2014, 2013 and 2012 were immaterial.

Share-based Compensation
We expense employee share-based payments under the fair value method. Share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over the requisite service period.

Restricted Share Units. We grant three types of Restricted Share Units (“RSUs”); service-based RSUs, performance-based RSUs (“PRSUs”), and total shareholder return RSUs (“TRSUs”). With regard to PRSUs and TRSUs, estimates and judgments are made concerning ultimate achievement of performance targets which impact the amount of share-based compensation recorded.

In the fourth quarters of 2012, 2013 and 2014, the Compensation Committee of our Board of Directors approved grants of PRSUs having rights to earn 0% to 250% of a target number of shares of our common stock depending on the achievement of grant-specific performance targets and service vesting as shown in the following table:

	Performance Awards by Grant Date		
	4th Quarter 2012	4th Quarter 2013	4th Quarter 2014
PRSUs granted at target	60,507	115,223	47,421
% of Target shares earned	23%	(a)	(a)
Vesting during 2015	50%	—	—
Vesting during 2016	50%	—	—
Vesting during 2017	—	50%	
Vesting during 2018	—	50%	50%
Vesting during 2019	—	—	50%
Grant Performance Target	(b)	(c)	(d)

(a) PRSUs are still in the performance period.

(b) The target number of shares for these PRSUs would have been earned had we achieved a pro forma diluted earnings per share compound annual growth rate ("CAGR") of fifteen percent (15%) for the two-year period ending December 31, 2014. Based on actual CAGR achieved, these PRSUs were earned at 23% of target. Prior to the fourth quarter of 2014, we had been expensing these PRSUs to target, and in the fourth quarter reduced the cumulative stock compensation expense recorded on these PRSUs by $1.1 million.

(c) The target number of shares for these PRSUs will be earned only if we achieve a pro forma diluted earnings per share growth rate of forty percent (40%) over the three-year period ending December 31, 2016. Shares actually earned could range from 0% to 250% of target determined by the actual growth rate achieved over the three-year period ending December 31, 2016. We have recorded expense on these PRSUs based on achieving the 40% target.

(d) The target number of shares for these PRSUs will be earned only if we achieve a pro forma diluted earnings per share growth rate of forty percent (40%) over the three-year period ending December 31, 2017. Shares actually earned could range from 0% to 225% of target determined by the actual growth rate achieved over the three-year period ending December 31, 2017.We have recorded expense on these PRSUs based on achieving the 40% target.

Pro forma diluted earnings per share for (b), (c) and (d) performance targets are calculated excluding non-operating gains and losses, if any, and excluding the after-tax impact of share-based compensation expense. The closing price of our common stock on the grant date equals the grant date fair value of these nonvested Restricted Share Units awards and will be recognized as compensation expense over their vesting periods.

In the fourth quarters of 2012, 2013 and 2014, the Compensation Committee of the Company's Board of Directors approved grants of TRSUs having rights to earn 0% to 225% of a target number of shares of the Company’s common stock depending on the achievement of grant-specific measures of total shareholder returns and service vesting as summarized below:

In the fourth quarter of 2012, the Compensation Committee of our Board of Directors approved target grants of 72,345 Relative Total Shareholder Return Restricted Share Units (referred to as “Relative TRSUs”). These Relative TRSUs are nonvested share awards for which vesting percentages and ultimate number of units vesting will be calculated based on the total shareholder return of our common stock as compared to the total shareholder return of 86 peer companies. The payout schedule can produce vesting percentages ranging from 0% to 225%. Total shareholder return will be calculated based upon the average closing price for the 30 calendar day period ending December 9, 2015, divided by the closing price on December 10, 2012. The target number of units is based on achieving a total shareholder return equal to the 65th percentile of the peer group. We recorded expense on these Relative TRSUs based on achieving the target. A lattice valuation model was applied to measure the grant date fair value of these Relative TRSUs.

In the fourth quarter of 2013, the Compensation Committee approved target grants of 57,598 Relative TRSUs. These Relative TRSUs are nonvested share awards for which vesting percentages and ultimate number of units vesting will be calculated based on the total shareholder return of our common stock as compared to the total shareholder return of 91 peer companies. The payout schedule can produce vesting percentages ranging from 0% to 200%. Total shareholder return will be calculated based upon the average closing price for the 30 calendar day period ending December 6, 2016, divided by the closing price on December 6, 2013. The target number of units is based on achieving a total shareholder return equal to the 65th percentile of the peer group. We recorded expense on these Relative TRSUs based on achieving the target. A lattice valuation model was applied to measure the grant date fair value of these Relative TRSUs.

In the fourth quarter of 2013, the Compensation Committee approved target grants of 59,533Absolute Total Shareholder Return Restricted Share Units (referred to as “Absolute TRSUs”). These Absolute TRSUs are nonvested share awards for which vesting percentages and ultimate number of units vesting will be calculated based on our three or four year total shareholder return of our common stock. The payout schedule can produce vesting percentages ranging from 0% to 200%. Total shareholder return will be calculated based upon the average closing price for the 30 calendar day period ending December 6, 2016 or December 6, 2017, divided by the closing price on December 6, 2013. The target number of units is based on achieving a total shareholder return of 33% over three years or 46% over four years. We recorded expense on these Absolute TRSUs based on achieving the target. A lattice valuation model was applied to measure the grant date fair value of these Absolute TRSUs.

In the fourth quarter of 2014, the Compensation Committee approved target grants of 52,321Absolute TRSUs. These Absolute TRSUs are nonvested share awards for which vesting percentages and ultimate number of units vesting will be calculated based on our three or four year total shareholder return of our common stock. The payout schedule can produce vesting percentages ranging from 0% to 200%. Total shareholder return will be calculated based upon the average closing price for the 30 calendar day period ending December 18, 2017 or December 18, 2018, divided by the closing price on December 18, 2014. The target number of units is based on achieving a total shareholder return of 33% over three years or 46% over four years. We recorded expense on these Absolute TRSUs based on achieving the target. A lattice valuation model was applied to measure the grant date fair value of these Absolute TRSUs.

Goodwill

Goodwill represents the excess of acquisition costs over the fair values of net assets acquired in business combinations. We test goodwill for impairment at least annually and between annual tests if an event occurs or changes in circumstances suggest a potential decline in the fair value of the reporting unit. A significant amount of judgment is involved in determining if an indicator or change in circumstances relating to impairment has occurred. Such changes may include, among others: a significant decline in expected future cash flows; a sustained decline in market capitalization; a significant adverse change in legal factors or in the business climate; unanticipated competition; and slower growth rates. We perform annual goodwill impairment testing in the fourth quarter. The impairment test for goodwill is a two-step approach. In the first step, the fair value of each reporting unit is compared to the reporting unit's carrying value, including goodwill. If the fair value of a reporting unit is less than its carrying value, the second step of the goodwill impairment test is performed to measure the amount of impairment, if any. In the second step, the fair value of the reporting unit is allocated to the assets and liabilities of the reporting unit as if it had been acquired in a business combination and the purchase price was equivalent to the fair value of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is referred to as the implied fair value of goodwill. The implied fair value of the reporting unit's goodwill is then compared to the actual carrying value of the goodwill. If the implied fair value of goodwill is less than the carrying value of goodwill, an impairment loss is recognized for the difference.

Significant estimates and assumptions are used in our goodwill impairment review and include the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units and determining the fair value of each reporting unit. The fair value of each reporting unit is determined based on a combination of techniques,

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including the present value of future cash flows, applicable multiples of competitors and multiples from sales of like businesses, and requires us to make estimates and assumptions regarding discount rates, growth rates and our future long-term business plans. Changes in any of these estimates or assumptions could materially affect the determination of fair value and the associated goodwill impairment charge for each reporting unit.

The implied fair value of the Leaf reporting unit's goodwill was determined at December 31, 2014 to be significantly below its carrying amount, resulting in a goodwill impairment charge equal to the full balance of Leaf goodwill of $18.5 million during the fourth quarter of 2014. See “— Overview — Heartland Commerce” for further details.

Our goodwill testing indicated that no other impairment existed and the fair value of each of the other reporting units subject to the impairment evaluation substantially exceeded their respective carrying values as of December 31, 2014 and 2013. At December 31, 2014 and 2013, goodwill of $425.7 million and $191.0 million, respectively, was recorded in our Consolidated Balance Sheets. We may be required to record goodwill impairment losses in future periods, whether in connection with our next annual impairment testing in the fourth quarter of 2015 or prior to that, if any such indicators constitute a triggering event in other than the quarter in which the annual goodwill impairment test is performed. It is not possible at this time to determine if any such future impairment loss would result or, if it does, whether such charge would be material.

Income Taxes

We account for income taxes by recognizing deferred tax assets and liabilities, which are recorded to reflect the future tax consequences attributable to the effects of differences between the carrying amounts of existing assets and liabilities for financial reporting and for income tax purposes. Judgments are required in determining the amount and probability of future taxable income, which in turn is critical to a determination of whether a valuation allowance against the deferred tax assets is appropriate.

We also account for the recognition and measurement of tax benefits associated with uncertain tax positions. This requires evaluations of individual tax positions to determine whether any part of that position can be recognized or continues to be recognized in the financial statements. An uncertain tax position exists if it is unclear how a transaction will be treated under tax law. We had approximately $7.3 million of total gross unrecognized tax benefits as of December 31, 2014, approximately $4.9 million of which would impact the effective tax rate.

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Results of Operations

Year Ended December 31, 2014 Compared to Year Ended December 31, 2013

The following table shows certain income statement data as a percentage of net revenue for the periods indicated (in thousands of dollars):

	2014	% of Net Revenue	2013	% of Net Revenue	Change Amount	%
Net revenue:						
Total revenue	$2,311,381		$2,135,372		$176,009	8.2 %
Less: Interchange	1,422,894		1,335,487		87,407	6.5 %
Less: Dues, assessments and fees	215,862		200,903		14,959	7.4 %
Total net revenue	672,625	100.0 %	598,982	100.0 %	73,643	12.3 %
Expenses:						
Processing and servicing	285,011	42.4 %	237,232	39.6 %	47,779	20.1 %
Customer acquisition costs	46,977	7.0 %	42,109	7.0 %	4,868	11.6 %
Depreciation and amortization	30,598	4.5 %	19,975	3.3 %	10,623	53.2 %
General and administrative	190,554	28.3 %	173,568	29.0 %	16,986	9.8 %
Goodwill impairment charge	18,490	2.7 %	—	— %	18,490	100.0 %
Asset impairment charges	18,875	2.8 %	—	— %	18,875	100.0 %
Total expenses	590,505	87.8 %	472,884	78.9 %	117,621	24.9 %
Income from operations	82,120	12.2 %	126,098	21.1 %	(43,978)	(34.9)%
Other income (expense):						
Interest income	125	— %	124	— %	1	0.8 %
Interest expense	(8,057)	(1.2)%	(5,429)	(0.9)%	(2,628)	(48.4)%
Other, net	(444)	(0.1)%	(241)	— %	(203)	(84.2)%
Total other expense	(8,376)	(1.2)%	(5,546)	(0.9)%	(2,830)	(51.0)%
Income from continuing operations before income taxes	73,744	11.0 %	120,552	20.1 %	(46,808)	(38.8)%
Provision for income taxes	41,876	6.2 %	46,450	7.8 %	(4,574)	(9.8)%
Net income from continuing operations	31,868	4.7 %	74,102	12.4 %	(42,234)	(57.0)%
Income from discontinued operations, net of income tax	—	— %	3,970	0.7 %	(3,970)	(100.0)%
Net income	31,868	4.7 %	78,072	13.0 %	(46,204)	(59.2)%
Less: Net (loss) income attributable to noncontrolling interests						
Continuing operations	(2,011)	(0.3)%	(610)	(0.1)%	(1,401)	(229.7)%
Discontinued operations	—	— %	56	— %	(56)	(100.0)%
Net income attributable to Heartland	$33,879	5.0 %	$78,626	13.1 %	$(44,747)	(56.9)%

Revenue. The following tables summarize total revenue and total net revenue (which we define as total revenue less interchange fees and dues, assessments and fees) by segment for the years ended December 31, 2014 and 2013 (in thousands of dollars):

	Year Ended December 31,		Change from Prior Year	
Total revenue:	2014	2013	Amount	%
Payment Processing	$2,111,487	$1,979,579	$131,908	6.7 %
Campus Solutions	61,538	36,186	25,352	70.1 %
Heartland School Solutions (a)	57,570	50,541	7,029	13.9 %
Heartland Payroll Solutions	50,394	44,565	5,829	13.1 %

Other	30,392	24,501	5,891	24.0	%
Total revenue	$2,311,381	$2,135,372	$176,009	8.2	%

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Total net revenue:	Year Ended December 31, 2014	2013	Change from Prior Year Amount	%	
Payment Processing	$472,731	$443,189	$29,542	6.7	%
Campus Solutions	61,538	36,186	25,352	70.1	%
Heartland School Solutions (a)	57,570	50,541	7,029	13.9	%
Heartland Payroll Solutions	50,394	44,565	5,829	13.1	%
Other	30,392	24,501	5,891	24.0	%
Total net revenue	$672,625	$598,982	$73,643	12.3	%

(a) See below for discussion of Out-of-Period Adjustments.

Payment Processing

Payment Processing net revenue increased $29.5 million, or 6.7%, from $443.2 million in 2013 to $472.7 million in 2014. This increase was driven by a $26.1 million or 6.6% increase in SME net revenue, reflecting a 8.7% increase in SME processing volume from $74.6 billion in 2013 to $81.1 billion in 2014. This increase in processing volume reflects the addition of SME merchants whose processing volume exceeded that of merchants who attrited and the impact of same store sales growth in 2014. The increase in SME processing volume also reflects the conversion of new and existing merchants to OptBlue. We converted a majority of our existing merchants currently processing under the former sales and servicing agreement with American Express to OptBlue during the third and fourth quarter of 2014. Our reported SME processing volume includes processing volumes for merchants in our Heartland School Solutions, Campus Solutions, and Other businesses. However, net revenue related to that processing volume is included in the net revenue reported for those businesses.

Campus Solutions

Campus Solutions net revenue increased 70.1% from $36.2 million in 2013 to $61.5 million in 2014. The increase included $19.9 million of revenue added by TouchNet since its September 4, 2014 acquisition. The remaining increase in Campus Solutions net revenue is due to higher student loan servicing related revenue, as well as growth in transaction processing revenue related to our student tuition payment processing and tuition payment plan products.

Heartland School Solutions

Heartland School Solutions net revenue increased 13.9% from $50.5 million in 2013 to $57.6 million in 2014. The increase in Heartland School Solutions net revenue is due primarily to an increase in transaction processing revenue (partially aided by the April 2014 acquisition of MCS Software) and equipment-related revenues as a result of a sale of equipment and related installation services to a large new school district customer. Partially offsetting the increase in net revenue for Heartland School Solutions is a decrease associated with out-of-period adjustments. In the second quarter of 2014, we recorded out-of-period adjustments decreasing its revenue and increasing bad debt expense (included in Processing and Servicing in its Condensed Consolidated Statements of Income) by $1.4 million and $0.9 million, respectively. These adjustments related to immaterial errors that originated in the prior year in our Heartland School Solutions business. These adjustments included revenue which was incorrectly recorded in prior periods and a reassessment of the collectability of certain customer accounts receivable. These out-of-period adjustments reduced earnings before income taxes and net income in 2014 by $2.3 million and $1.4 million, respectively, and reduced diluted earnings per share by $0.04.

Heartland Payroll Solutions

Heartland Payroll Solutions net revenue increased 13.1% from $44.6 million in 2013 to $50.4 million in 2014. The increase in payroll processing net revenue is primarily due to a 7.0% increase in payroll processing customers from 24,088 at December 31, 2013 to 25,764 at December 31, 2014.

Other

Other net revenue increased 24.0% from $24.5 million in 2013 to $30.4 million in 2014, primarily due to growth in Micropayments revenue which reflects higher equipment sales and payment processing for unattended payment locations such as laundry facilities, kiosks and vending machines. The increase also included $1.4 million of revenue added by Xpient since its October 31, 2014 acquisition.

Total expenses. Total expenses increased 24.9% from $472.9 million in 2013 to $590.5 million in 2014, due to the increases in processing and servicing, depreciation and amortization, customer acquisition costs, general and administrative expenses and asset impairment charges related to our investment in Leaf and other POS assets . These increases are further discussed below and resulted in total expenses representing 87.8% of total net revenue in 2014, compared to 78.9% in 2013.

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Processing and servicing expense for the year ended December 31, 2014 increased by $47.8 million, or 20.1%, compared with the year ended December 31, 2013. The increase in processing and servicing expense reflects the acquisitions of MCS Software, TouchNet and Xpient, as well as, increased costs associated with processing and servicing higher SME bankcard processing volume, increased sales compensation, higher merchant losses as a result of chargebacks from a single merchant who entered bankruptcy in the fourth quarter and increased cost of sales and servicing related to higher Heartland School Solutions, Heartland Payroll Solutions, Campus Solutions, and Other revenues (primarily our Micropayments business). The increase in processing and servicing expenses also reflects approximately $6.5 million of expenses which were classified as general and administrative expense in the prior year. This reclassification brings operating expenses in our legacy payroll business and Ovation business into alignment. As a percentage of total net revenue, processing and servicing expense increased to 42.4% for the year ended December 31, 2014 compared with 39.6% for the year ended December 31, 2013.

Customer acquisition costs for the year ended December 31, 2014 increased by $4.9 million, or 11.6% compared with the year ended December 31, 2013. As reflected in the table below, this increase reflects higher amortization on increased capitalized deferred acquisition costs resulting from improved levels of new installed margin and the impact of subsequent changes in the estimated accrued buyout liability due to lower merchant attrition and same-store sales growth. As a percentage of total net revenue, customer acquisition costs remained consistent at 7.0% for the year ended December 31, 2014 and 2013.

Customer acquisition costs for the years ended December 31, 2014 and 2013 included the following components (in thousands of dollars):

	Year Ended December 31,	
	2014	2013
Amortization of signing bonuses, net	$30,345	$27,767
Amortization of capitalized customer deferred acquisition costs	21,281	17,881
Increase in accrued buyout liability	20,182	17,620
Capitalized customer deferred acquisition costs	(24,831)	(21,159)
Total customer acquisition costs	$46,977	$42,109

Depreciation and amortization expenses increased 53.2% from $20.0 million in 2013 to $30.6 million in 2014. The increase in depreciation and amortization expenses include increases in acquisition related amortization of intangible assets in 2014 compared to 2013. As a percentage of total net revenue, depreciation and amortization expenses increased to 4.5% for the year ended December 31, 2014 compared with 3.3% for the year ended December 31, 2013. See "— Liquidity and Capital Resources — Acquisitions" for further information on these acquisitions.

Most of our investments in information technology have supported the continuing development of HPS Exchange, Passport and other processing-related initiatives. Depreciation and amortization expense recorded on these investments is included in processing and servicing expense. Additionally, we capitalized salaries, fringe benefits and other expenses incurred by our employees that worked on internally developed software projects and outsourced programming. Amortization does not begin on the internally developed software until the project is complete and placed in service, at which time we begin to amortize the asset over expected lives of three to five years. The amount capitalized increased from $38.4 million in 2013 to $40.3 million in 2014. The total amount of capitalized costs for projects placed in service in 2014 and 2013 was $36.5 million and $25.7 million, respectively.

General and administrative expenses increased $17.0 million, or 9.8%, from $173.6 million in 2013 to $190.6 million in 2014. General and administrative expenses increased primarily due to a $15.2 million increase in personnel costs and an increase of $2.7 million in occupancy costs. The increase in personnel and occupancy costs primarily reflects the acquisitions of Leaf in September 2013, MCS Software in April 2014, TouchNet in September 2014 and Xpient in October 2014, as well as other headcount increases. The remaining increase in general and administrative expenses resulted from our acquisitions, including $3.7 million of acquisition-related expenses. Partially offsetting these increases was a decrease due to the reclassification of $6.5 million of payroll related expenses from general and administrative to processing and servicing expense for our payroll business as well as lower equipment lease and information technology related expenses. General and administrative expenses as a percentage of total net revenue for 2014 was 28.3%, a slight decrease from 29.0% for 2013.

We recorded pre-tax asset impairment charges related to our investment in Leaf and other POS assets of $37.4 million, including $18.5 million for goodwill impairment.

We recently acquired pc America and Dinerware for its Heartland Commerce segment (see "— Overview — Heartland Commerce"). Heartland Commerce provides a comprehensive suite of POS solutions, payment processing capabilities and other adjacent business service applications. Heartland Commerce is comprised of existing POS businesses; Xpient, Liquor POS, Leaf and our other POS solutions, and will include pcAmerica and Dinerware. Dinerware and pcAmerica are in the process of developing cloud-based POS systems that complement their well-established on-premise POS solutions. These cloud-based POS systems overlap with what was being developed by Leaf, and Dinerware and pcAmerica technologies and development plans provided insight into the status and positioning of Leaf's technology in the marketplace. Consequently, we decided that we will stop POS development efforts at Leaf. This decision caused a significant adverse change in the extent or manner in which the long-lived asset group for Leaf will be used, including Prosper, an internally developed POS software technology. These circumstances also resulted in the implied fair value of the Leaf reporting unit being significantly below its carrying value, which caused a Goodwill Impairment charge for the full balance of Leaf Goodwill as of December 31, 2014, as well as, asset impairment charges for Prosper and for the Leaf intangible and long-lived assets.

Income from operations. Our income from operations, which we also refer to as operating income, decreased to $82.1 million for 2014, from $126.1 million for 2013, as a result of increases in processing and servicing expenses, depreciation and amortization, general and administrative expenses, and goodwill and asset impairments, partially offset by an increase in net revenue. Our operating margin, which we measure as operating income divided by net revenue, was 12.2% for 2014, compared to 21.1% for 2013. Excluding the impact of the goodwill and asset impairment charges during the fourth quarter, our operating income would have been $119.7 million or 17.8% for 2014.

Interest expense. Interest expense for 2014 and 2013 was $8.1 million and $5.4 million, respectively. Interest expense in both periods includes interest incurred under our credit facilities and interest we recorded on payables to our sponsor banks. The increase in interest expense reflects higher borrowings under our 2014 Revolving Credit Facility (as defined in —Liquidity and Capital Resources—Credit Facilities herein) as well as interest expense on $375 million under our 2014 Term Credit Facility (as defined in —Liquidity and Capital Resources—Credit Facilities herein) that was used to fund the TouchNet Acquisition. See "— Liquidity and Capital Resources — Credit Facilities" for more detail on our borrowings.

Other income (expense), net. Other, net for 2014 includes the following:

•Pre and after-tax gain of $3.6 million relating to a release from a contingent earn-out liability to the noncontrolling shareholders of Leaf. As a result of the Stock Purchase Agreement we entered into on August 6, 2014 with the noncontrolling shareholders of Leaf, we were released from a contingent earn-out liability to those noncontrolling shareholders. The non-cash impact of the gain associated with the release of the contingent earn-out liability is recorded in "Other, net" in the Consolidated Statements of Income and "Write-off of fixed assets and other" in the Consolidated Statement of Cash Flows.

•Pre-tax charge of $4.0 million relating to an other than temporary impairment ("OTTI") of an investment in the stock of TabbedOut. See "— 2014 Financial Highlights," for information on this OTTI.

Income taxes. Income tax expense for 2014 was $41.9 million, reflecting an effective tax rate of 56.8%. This compares to income tax expense of $46.5 million for 2013, an effective tax rate of 38.5%. The overall increase in our effective tax rate for 2014 is due to a $6.5 million increase in the valuation allowance against deferred tax assets and the impact of a non-deductible goodwill impairment charge. Our effective tax rate without these two charges would have been 39.2%. The increase in the valuation allowance resulted from Leaf's operating losses during the 66.67% ownership period from January 1 to August 5, 2014 and from the write down of our investment in TabbedOut. On August 6, 2014, we acquired 100% of the common stock shares of Leaf. As a result, we will be able to utilize the losses generated from Leaf against consolidated taxable income for the period beginning on and after August 6, 2014. See “— Liquidity and Capital Resources — Acquisitions" for a description of the transaction involving Leaf’s ownership interests. The effective tax rate for 2014 and 2013 benefited from recognition of research and development credits. On December 19, 2014, the Tax Increase Prevention Act of 2014 was enacted which included an extension of the federal research and development credit retroactively for one year and is reflected in 2014. On January 2, 2013, the American Taxpayer Relief Act of 2012 ("ATR Act") was enacted which included an extension of the federal research and development credit retroactively to 2012 and prospectively through 2013. We recognized the effects of the research and development credits in 2013 in conjunction with filing our 2012 tax return. The favorable impact of the research and development credits on the effective tax rate for 2013 was partially offset by a valuation allowance recorded against the deferred tax assets arising from Leaf’s operating losses and an increase in the state tax rates.

Net income attributable to Heartland. As a result of the above factors, we recorded net income of $33.9 million for 2014. This compares to a net income of $78.6 million for 2013.

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Year Ended December 31, 2013 Compared to Year Ended December 31, 2012
The following table shows certain income statement data as a percentage of net revenue for the periods indicated (in thousands of dollars):

	2013	% of Net Revenue	2012	% of Net Revenue	Change Amount	%
Net revenue:						
Total revenue	$2,135,372		$2,013,436		$121,936	6.1 %
Less: Interchange	1,335,487		1,284,038			