



March 15, 2023

The Honorable Monique Limón
Chair, Senate Banking and Financial Institutions Committee
State Capitol
Sacramento, CA 95814

The Honorable Steve Glazer
State Capitol
Sacramento, CA 95814
By email: Sakshi.Walia@sen.ca.gov, Jesus.Nolasco@sen.ca.gov

Re: SB 33 (Glazer) Commercial Financing Disclosures – STRONG SUPPORT

Dear Senators Limón and Glazer:

On behalf of the California Association of Micro Enterprise Opportunity (CAMEO), the Responsible Business Lending Coalition (RBLC)¹, and the undersigned organizations, we write to applaud your leadership as sponsor of the first state bill to expand Truth-in Lending Act (TiLA) protections to small businesses. We voice strong support for SB 33 as an effort to preserve the commonsense protections that California businesses enjoy, thanks to the passage of SB 1235. SB 33 will eliminate the 2024 sunset date for SB 1235 and guarantee transparency for businesses and certainty for providers that the required financing disclosure rules implemented in December 2022 will remain in place.

SB 1235 empowers small business owners into making informed decisions by guaranteeing commonsense disclosure of pricing and terms. Since this disclosure bill was signed into law and implemented, nearly a dozen states have filed similar small business lending disclosure bills. New York state recently released the final rule for their small business lending disclosure law, which will take effect on August 1, 2023.

Passed in 1968, the federal Truth in Lending Act (TiLA) requires lenders to disclose key pricing and term information to consumers, enabling them to compare options and make informed credit decisions. However, the 1968 law does not extend to small business financing. The Federal Reserve, the U.S. Treasury Department, the Office of Comptroller of the Currency, and others have highlighted that lack of protections for small businesses is a critical gap in the regulatory framework.² In this gap, troubling lending practices

¹ California Micro Enterprise Network (CAMEO) is a statewide micro-business network made up of 400 organizations, agencies, and individuals dedicated to furthering Micro-Business development in California with small and micro-business financing, advocacy, public education, business management training, and technical assistance and the Responsible Business Lending Coalition (RBLC) is a national, cross-sector coalition that is organized around a shared commitment to innovation in small business lending and concerns about the rise of irresponsible small business lending. The mission of the RBLC is to promote a commercial financing landscape that is built on transparency, fairness, and that centers borrowers during the lending process.

² Treasury 2016: “*Small Business Borrowers Will Likely Require Enhanced Safeguards*”
<https://www.treasury.gov/connect/blog/Pages/Opportunities-and-Challenges-in-Online-Marketplace-Lending.aspx>

have emerged and providers are offering financing products with APRs as high as 94%, but these rates are not disclosed to the borrower. An Accion Opportunity Fund study found some California small businesses were paying, on average, nearly double what they could afford.³

In 2018, California became the first state in the nation to pass legislation that extended truth-in-lending disclosures to small business financing, allowing business borrowers to more easily comparison shop and evaluate the true cost of the money they are borrowing. Since the passage of SB 1235 in CA, New York passed a similar bill which takes effect on August 1, 2023. Bills largely modeled on California and New York have been introduced in other states including Connecticut, Maryland, and New Jersey. Additionally, a bicameral federal truth-in-lending bill was introduced in the 117th Congress and is expected to be reintroduced in the 118th Congress.

Unfortunately, SB 1235 authorization runs through January 1, 2024. By eliminating the 2024 sunset date for SB 1235, your bill, SB 33, would guarantee transparency for businesses and certainty for providers that the required financing disclosure rules implemented in December 2022 will remain in place. The bill protects California's economy by supporting responsible innovation and transparency in the commercial financing marketplace. The passage of SB 33 is yet another opportunity for California to set the standard for other states to follow.

We are pleased offer our strong support of SB 33 and we thank you for your leadership on this issue.

Continuing the disclosures are important because small business owners, especially first-time entrepreneurs, have little access to traditional bank loans. Many of these small business owners have a limited understanding of financial practices and do not have access to an attorney or accountant. They do not understand interest rates, prepayment penalties, or other complicated financing terms of the options that are available today. Moreover, many of the terms are not clearly written or proposed to the small business owner in a timely

Federal Reserve Governor Brainard *"raised concerns about the risk that some small business borrowers may have difficulty fully understanding the terms of the various loan products or the risk of becoming trapped in layered debt that poses risks to the survival of their businesses."* <https://www.federalreserve.gov/newsevents/speech/brainard20150930a.pdf>;

OCC: *"Should the OCC use its chartering authority as an opportunity to address the gaps in protections afforded individuals versus small business borrowers, and if so, how?"* <https://www.occ.gov/topics/responsible-innovation/comments/special-purpose-national-bank-charters-for-fintech.pdf>;

Federal Reserve Bank of Philadelphia President Harker: <https://youtu.be/6q6RWVsAaCY?t=1h34m45s>;

Federal Reserve Bank of New York President Dudley: *"There are individuals who try to take advantage of owners of new businesses by providing them with poor advice or overcharging them for credit... it would be helpful to have consistent standards and transparency requirements for organizations that lend to small businesses. Such standards and requirements exist for lending to households, and I believe the same justification exists to extend these requirements to small businesses."* <https://www.newyorkfed.org/newsevents/speeches/2015/dud150508.html>;

New Federal Reserve Research: *"When presented with sample online products, participants generally found the descriptions difficult to understand or lacking detail about costs and features."* <https://www.federalreserve.gov/publications/files/2018-small-business-lending.pdf>

³ A study of some California small businesses found they were paying average APRs of 94%, and as high as 350%. The average monthly loan payment was 178% the business' net incomes, pushing the small business from profitability into unprofitability. Opportunity Fund, "Unaffordable and Unsustainable: The New Business Lending," 2016. https://aofund.org/app/uploads/2021/03/Unaffordable-and-Unsustainable-The-New-Business-Lending-on-Main-Street_Opportunity-Fund-Research-Report_May-2016.pdf

Research by the Woodstock Institute also identifies APRs ranging up to 350%. Woodstock Institute, "Analysis of Business Loan Terms." <http://woodstockinst.org/research/fact-sheets/analysis-of-business-loan-terms/>

manner. An incomplete understanding of the product can lead small business owners to borrow more than they can afford to repay or trap them in cycles of high-cost debt. An inappropriate financing product can lead a small business to financial ruin, or even worse, closure of the business.

Federal Reserve Bank of Philadelphia President Harker spoke vividly of the need for transparency standards: “I hear these stories constantly about a small business in particular, getting into a situation where they didn’t quite know what they signed up for, and then they walk into their community bank and say, ‘I’ve got to get out of this deal, it’s killing me.’ And so, there are good actors and bad actors.” Small business owners agree. Polling by Small Business Majority found that 8 in 10 small business owners are in favor of regulating online lenders to ensure interest rates and fees are clearly disclosed to borrowers.⁴

SB 1235 as enacted in California, provided a sound solution for small business owners in the state seeking financing by requiring all providers to clearly communicate the cost and terms of the financing being offered. SB 33 secures the future of the commonsense and now-tested policy, ensuring transparency to small business borrowers in our state.

We also have included a letter to New York State Senator Kevin Thomas that outlines the importance of using APR in addition to total dollar cost.

Please know we will work to support and advance SB 33 in the months to come and if you have any questions, please feel free to contact hpickman@cameonetwork.org and info@borrowersbillofrights.org.

Sincerely,

1. The Responsible Business Lending Coalition⁵
2. Access Plus Capital
3. Accessity
4. Accion Opportunity Fund
5. Agriculture and Land-based Training Association (ALBA)
6. AmPac Tri-State CDC
7. Anchor Financial Services
8. Anew America Community Corporation
9. Asian Pacific Islander Small Business Program WBC LTSC Community Development Corp.
10. Bankers Small Business CDC of California
11. Bay Area Development Company
12. Bethel Los Angeles Community Development Corporation
13. California Asset-Building Coalition (CABC)
14. California Association for Micro Enterprise Development (CAMEO)
15. California Black Chamber of Commerce

⁴ Small Business Majority, “Small Business Owners Concerned with Predatory Lending, Support More Regulation of Alternative Lenders.” December 12th, 2017.

⁵ Executive Committee members include Accion Opportunity Fund, Camino Financial, Community Investment Management, Funding Circle, LendingClub, National Association for Latino Community Asset Builders, Opportunity Finance Network, Small Business Majority, and the Aspen Institute

16. California Capital Financial Development Corporation
17. California Hispanic Chambers of Commerce (CAHCC)
18. California Low-Income Consumer Coalition
19. California Reinvestment Coalition
20. California Small Business Development Center (SBDC) - Valley Community
21. California State University, Monterey Bay Institute for Innovation and Economic Development
22. Consumer Advocates Against Reverse Mortgage Abuse (CAARMA)
23. Consumer Federation of California
24. Crowdfund Better
25. Economic Development and Financing Corporation
26. El Pajaro Community Development Corporation
27. Fondo Adelante, Mission Economic Development Agency (MEDA)
28. Fresno Area Hispanic Foundation
29. Fresno Metro Black Chamber of Commerce
30. Funding Circle
31. Go Local Sonoma County
32. Greater Ontario Business Council
33. Halo Business Finance Corp
34. ICA Fund Good Jobs (Inner City Advisors)
35. Inclusive Action for the City
36. International Rescue Committee's Center for Economic Opportunity
37. Invest in Women Entrepreneurs Initiative
38. Jefferson Economic Development Institute (JEDI)
39. Latino Economic Development Center (LEDC)
40. LendingClub
41. Lighter Capital
42. Main Street Launch
43. Marian Doub Consulting
44. Maximum Reach for Economic Equity (FKA Sac Black Biz)
45. Microenterprise Collaborative of Inland Southern California
46. Momentum Capital
47. Multifunding
48. Oakland African American Chamber of Commerce
49. Oakland Citizens Committee for Urban Renewal (OCCUR)
50. Pacific Community Ventures (PCV)
51. Prospera Community Development
52. Public Law Center (PLC)
53. Renaissance Entrepreneurship Center
54. Richmond Main Street Initiative
55. San Francisco African American Chamber of Commerce (SFAACC)

56. San Mateo Area Chamber of Commerce
57. Silver Lining
58. Small Business California
59. Small Business Majority
60. Southeast Asian Community Center
61. Start Small Think Big
62. The C.O.O.K Alliance
63. The CraneWorks
64. Wadeco Business Center
65. Women's Economic Ventures (WEV)
66. Woodstock Institute
67. Working Solutions

RESPONSIBLE BUSINESS LENDING COALITION  **C.A.M.E.O.**





March 22, 2023

Chairman Kevin Thomas
Committee on Consumer Protection
Legislative Office Bldg., Room 947
Albany, NY 12247

Re: Introduction of S5470

Dear Chairman Thomas,

Thank you for your leadership in introducing S5470. We have valued working with your office over the past year and look forward to speaking with you soon. In the following letter, we share thoughts on the bill and respond to a few questions raised by high-cost financing companies.

The Responsible Business Lending Coalition (RBLC) is a unique nonprofit/industry coalition of advocacy groups, community development financial institutions, and fintech companies. We are the only coalition representing the nonprofit sector, the financing industry, and small businesses themselves on these financing issues.⁶

The RBLC came together out of concern about the predatory small business lending each of our organizations began encountering several years ago. In 2015, the RBLC became the first coalition to raise the call for small business truth-in-lending standards and launched the *Small Business Borrowers' Bill of Rights*.⁷ Over 110 small business lenders, brokers and lead generators, and advocacy organizations have endorsed these standards.

We have worked closely with the New York State CDFI Coalition, the Upstate Black Chamber of Commerce, the National Urban League, other organizations, and especially the leadership of your office, to help develop S5470. We hope to work with you to pass this bill. As drafted, it will be a monumental advancement for small business protection, the development of a fair and competitive small business financing market, and the prosperity of Main Street families in New York State.

The Central Importance of APR

First, we hope to address why APR is essential. The lack of transparency in small business financing today is the lack of APR.

We understand that your office was provided a statement about APR made in 2013 by the CFPB. We believe these CFPB quotes about APR may not have been presented with appropriate context. In the very

⁶ Members of the RBLC include Accion Opportunity Fund, Community Investment Management, Funding Circle, LendingClub, Opportunity Finance Network, Small Business Majority, StreetShares, and the Aspen Institute.

⁷ The Small business Borrowers Bill of Rights, and the list of its endorsers and signatories, can be found at <http://www.borrowersbillofrights.org/bill-of-rights.html>

same passage that was quoted, the CFPB concluded that APR, “provides a good way of comparing the entire costs of the loan over the entire term.”⁸

That is the CFPB’s position. The CFPB’s website today states that, “The APR, or annual percentage rate, is the standard way to compare how much loans cost. It lets you compare the cost of loan products on an “apples-to-apples” basis. Your lender must disclose the APR before you agree to the loan.”⁹

Here is a screenshot of the CFPB’s website on the value of APR for comparing products of different types and term lengths:¹⁰

Tip: Focus on APRs. If you want to compare the cost of a payday loan to the cost of an installment loan or a credit card, focus on the APRs.

What the CFPB found in 2013 is that, specifically in the mortgage context, consumers sometimes confused the APR generally *with the interest rate*. Unlike in small business financing, in mortgage lending consumers are always told an interest rate, as well the APR which includes both the interest rate and fees and so is a slightly higher number. Unlike in small business financing, in mortgage lending the interest rate and APR are generally very close—within 0.03% on to bankrate.com today.¹¹

In the status quo that high-cost alternative small business finance companies defend, these companies tell customers neither. Small business owners are often shown no interest rate or APR at all, while they may be paying these companies APRs averaging 94% and upwards of 350%.¹² Small business owners are paying rates vastly different than their expectations and “have no common basis for cost comparison,” in the words of the Federal Reserve research.¹³

The CFPB explained that the basis for its 2013 comments about APR was its Quantitative Study, showing 66-80% of consumers studied correctly identified the APR, depending on the formatting of the disclosure they were presented, but the rest did not.¹⁴ Small business face a much more severe problem with the

⁸ Volume 78, No. 251, Federal Register, December 31, 2013, p. 79880. www.govinfo.gov/content/pkg/FR-2013-12-31/html/2013-28210.htm

⁹ www.consumerfinance.gov/ask-cfpb/my-payday-lender-said-my-loan-would-cost-15-percent-but-my-loan-documents-say-the-annual-percentage-rate-apr-is-almost-400-percent-what-is-an-apr-on-a-payday-loan-and-how-should-i-use-it-en-1625/. The same phrase appears throughout CFPB materials, on payday lending, auto, mortgage, credit card, etc.

¹⁰ Id.

¹¹ “Current Mortgage and Refinance Rates for March 2020.” Bankrate.com. March 2020. www.bankrate.com/mortgage

¹² Opportunity Fund, “Unaffordable and Unsustainable: The New Business Lending on Main Street,” May 2016. www.opportunityfund.org/wpcontent/uploads/2019/09/Unaffordable-and-Unsustainable-The-New-Business-Lending-on-Main-Street_Opportunity-Fund-Research-Report_May-2016.pdf

¹³ Federal Reserve Board of Governors, “Uncertain Terms: What Small Business Borrowers Find When Browsing Online Lender Websites,” Dec 2019. (Page 18) <https://www.federalreserve.gov/publications/files/what-small-business-borrowers-find-when-browsing-online-lender-websites.pdf>

¹⁴ The CFPB wrote that, “the Quantitative Study asked the consumer respondents in the study, “[w]hat is the Annual Percentage Rate (APR) for this loan?” For the consumers using the Bureau’s integrated disclosures, 79.5 percent gave the correct answer to this question, while for consumers using the early TILA disclosure statement and RESPA GFE, only 65.7

disclosures used today. In the Federal Reserve's [testing](#), small business owners reviewed online disclosures used in the market today that lack APR. Zero percent of small business owners identified the effective interest rate. Zero.

The Federal Reserve researchers presented small business owners with a series of typical online business loan disclosures used in the market today by higher-cost financing companies. They asked the small business owners if anything seemed confusing or if any additional information was needed. Typical replies included "No, it's pretty straightforward," and "I can't think of anything more I would like to see, really." However, when asked what rate they would pay, the small business owners did not know, and often appeared not to realize that they did not know. Answers included 28%, 5%, 9.8%, and the highest guess was a "a whopping 30%." The actual rate was 60%. None realized it was that high.¹⁵ As you might expect, small business owners often do not know what rate they would be effectively be charged if it is not disclosed to them transparently. As a result, small business are hindered from making informed cost comparisons, are often overcharged, and often end up in financing that is unaffordable.¹⁶

The CFPB's conclusion, in the same document quoted to you, was that APR should be clearly distinguished from the interest rate and *is* valuable for cost comparison: "The Bureau is, however, improving the APR disclosure through a descriptive statement that clearly distinguishes the APR from the interest rate. The Bureau may also develop supplemental educational materials in booklets and its Web site that will further **explain how the APR differs from the interest rate, how it provides a good way of comparing the entire costs of the loan over the entire term**, and why consumers may want to use both the ``In 5 Years'' and APR figures to think about their financial futures."¹⁷ (emphasis added)

As to the CFPB's finding that applicants can confuse APRs, interest rates, and other forms of rates, we agree! And we are grateful that your S5470 is written to address that very problem. The Federal Reserve's research has repeatedly found that small business owners often mistake any percentage number or "rate" for the interest rate. The Federal Reserve found that this confusion is being actively exploited by high-cost small business financing companies, who present different forms of "rate" that are much lower than the

percent gave the correct answer, a difference of 13.8 percentage points." -Volume 78, No. 251, Federal Register, December 31, 2013, p. 79881. <https://www.govinfo.gov/content/pkg/FR-2013-12-31/html/2013-28210.htm>.

The Quantitative Study referenced is: Kleimann Communication Group. 2013. "Know Before You Owe: Quantitative Study of the Current and Integrated TILA-RESPA Disclosures." See pages 45 and 50-51. https://files.consumerfinance.gov/f/201311_cfpb_study_tila-respa_disclosure-comparison.pdf

¹⁵ Federal Reserve Bank of Cleveland, "Alternative Lending through the Eyes of 'Mom & Pop' Small-Business Owners," August 2015. <https://www.clevelandfed.org/en/newsroom-and-events/publications/special-reports/sr-20150825-alternative-lending-through-the-eyes-of-mom-and-pop-small-business-owners.aspx>

¹⁶ See, e.g. Opportunity Fund, "Unaffordable and Unsustainable: The New Business Lending on Main Street," May 2016. https://www.opportunityfund.org/wpcontent/uploads/2019/09/Unaffordable-and-Unsustainable-The-New-Business-Lending-on-Main-Street_Opportunity-Fund-Research-Report_May-2016.pdf

¹⁷ The reference to "in five years" further illustrates why the CFPB's 2013 comments on APR in mortgage lending are not applicable to small business financing. Mortgage loans are long-term, generally 15-30 years, and refinanced often. In this case, the APR's spreading of upfront fees across an entire 30-year term may undercount the cost of the fee, if the mortgage is refinanced after only a few years. The CFPB therefore considered indicating the cost, including fees, after only 5 years. This is not applicable to small business financing, where the loans being considered are often only 3-36 months. Volume 78, No. 251, Federal Register, December 31, 2013, p. 79880. <https://www.govinfo.gov/content/pkg/FR-2013-12-31/html/2013-28210.htm>

true interest rate or APR. Below is an excerpt from this Federal Reserve research, demonstrating how this customer confusion is being exploited today:¹⁸

Participants noted that the varying product descriptions provided no common basis for cost comparisons, and several suggested that APR would be helpful for that purpose. In fact, determining the equivalent APR on some products may be challenging, given the non-standard terminology and structure of products offered by online lenders. Table 3 presents APR-equivalents for a common scenario in which \$50,000 is repaid in six months according to the terms and rates promoted on the lenders' sites.

Table 3. Estimated APRs for select online products		
Rate advertised on website	Product details	Estimated APR equivalent
1.15 factor rate	<ul style="list-style-type: none"> Total repayment amount \$59,000 Fees: 2.5% set-up fee; \$50/month administrative fee Term: none (assume repaid in six months) Daily payments (assume steady payments five days/week) 	Approximately 70% APR
4% fee rate	<ul style="list-style-type: none"> Total repayment amount \$56,500 Fee rate: 4% (months 1–2), 1.25% (months 3–6) Fees: none Monthly payments Term: six-month term 	Approximately 45% APR
9% simple interest	<ul style="list-style-type: none"> Total repayment amount \$54,500 Fees: 3% origination fee Weekly payments Term: six-month term 	Approximately 46% APR

Source: Authors' calculations, based on product descriptions on company websites.

As you can see, in the left column, small businesses were quoted rates such as 1.15, 4%, and 9%, while never being told that the actual APRs they would be charged were approximately 70%, 45%, and 46% respectively. These types of “non-standard” rates used today mislead small businesses to the benefit of high-cost financing companies. The Federal Reserve researchers found that, “when asked to compare a sample short-term loan product with a 9 percent “simple interest” rate to a credit card with a 21.9 percent interest rate, most participants incorrectly guessed the short-term loan to be less expensive.”¹⁹

¹⁸ Federal Reserve, Dec 2019. (Page 18) <https://www.federalreserve.gov/publications/files/what-small-business-borrowers-find-when-browsing-online-lender-websites.pdf>

¹⁹ Federal Reserve, 2019, pg. 19.

This confusion between different forms of rate is why the RBLC advocates for the one standardized form of rate, APR, which the CFPB describes as, “the standard way to compare how much loans cost. It lets you compare the cost of loan products on an ‘apples-to-apples’ basis.”²⁰ It is also why the RBLC has pushed so hard for the language in S5470 §710, which prohibits misleading forms of “rates” the Federal Reserve highlights above. We consider this one of the most important sections of the bill:

33 § 710. Additional information. Nothing in this article shall prevent a
34 provider from providing or disclosing additional information on a
35 commercial financing being offered to a recipient, provided however,
36 that such additional information shall not be disclosed as part of the
37 disclosure required by this article. If other metrics of financing cost
38 are disclosed or used in the application process of a commercial financ-
39 ing, these metrics shall not be presented as a "rate" if they are not
40 the annual interest rate or the annual percentage rate. The term "inter-
41 est", when used to describe a percentage rate, shall only be used to
42 describe annualized percentage rates, such as the annual interest rate.
43 When a provider states a rate of finance charge or a financing amount to
44 a recipient during an application process for commercial financing, the
45 provider shall also state the rate as an "annual percentage rate", using
46 that term or the abbreviation "APR".

Another implication of the CFPB’s 2013 research is that the formatting of a disclosure, even if it includes the same information, can lead to different levels of borrower comprehension. For this reason, we support delegating the development of the required disclosure formatting to DFS so it can be fine-tuned as needed.

Why should be APR be disclosed, rather than the interest rate?

Interest rate cannot be the “common basis for cost comparison” called for by the Fed (above) because some forms of financing today have no interest rate. (Interest is charged at a fixed rate for traditional loans and lines of credit, but not for merchant cash advances, some non-amortizing “fixed fee” loans, factoring, and so on.) However, APR can be calculated for all forms of financing and enables comparison across all of them.

In addition, interest rate does not include fees and other charges. It can fail to represent the cost of a financial product if the fees are significant. In small business financing today, fees can represent a large part, or even 100% of the cost.²¹ Thus, if interest rate were disclosed without APR some providers would disclose interest rates of 0% while charging APRs of 350% or higher. APR captures all appropriate charges in one number that “lets you compare the cost of loan products on an ‘apples-to-apples’ basis,” in the words of the CFPB.²²

²⁰ <https://www.consumerfinance.gov/consumer-tools/credit-cards/answers/key-terms/>

²¹ This was not as significant problem in the mortgage TILA/RESPA issues considered by the CFPB in 2013, because mortgage interest rates and fee are structures are fairly standardized, and fees do not represent the large part of the cost.

²² <https://www.consumerfinance.gov/consumer-tools/credit-cards/answers/key-terms/>. Similarly, in the mortgage context the CFPB website reads, “The APR takes into account both interest and loan fees. It shows which loan is less expensive over the full term of the loan.

Why not just disclose the total cost of capital in dollar terms, without APR?

Dollar cost alone does not enable applicants to compare the cost of financing with different term lengths, or of different amounts. In this way, it would mislead applicants towards shorter-term financing. Small businesses would pay more, even in dollar terms, to use this financing over equivalent periods of time. APR enables apples-to-apples comparison between products of different term lengths.

The problem of relying on dollar cost was described especially well by MFTransparency, which established transparency standards in the international microfinance industry:

“When you take out a loan you are essentially ‘renting’ money. You are given money that is owned by someone else and you agree to pay them ‘rent’ (interest) for this privilege. This is just like renting anything else, an apartment for example. If you rent an apartment, a room that costs \$1,000 dollars per day is very different than a room that costs \$1,000 dollars per month. Using Total Cost of Credit is like looking at the price of an apartment, but not taking into account how long you will be able to stay!

But APR is like looking at a standardized cost per year for that same apartment:

- \$1,000 per day = \$365,000 per year
- \$1,000 per month = \$12,000 per year”²³

The CFPB website today illustrates the same point, encouraging consumers to use APR to compare the cost of a 14-day payday loan to a credit card:

“For example, if your payday lender is charging you a \$15 fee for every \$100 borrowed, that would be a simple interest rate of 15 percent. But if you have to repay the loan in two weeks, that 15 percent finance charge equates to an APR of almost 400 percent because of the very short term.

Here’s why: Consider the daily interest cost, \$1.07 (or \$15 divided by 14 days), then multiply that out for a full year (365 days, so \$390.55). So, borrowing \$100 would cost you \$391 if the term were extended to one year – that’s 391 percent of the borrowed amount.

By comparison, the cost of borrowing the same \$100 on a credit card with a 15 percent APR is \$15 for one year, or about 57 cents for two weeks.

You don’t need to worry about the math. **Just keep in mind that the APR does matter because it provides a shorthand way for you to compare the cost of two or more loans.** Remember, your lender must disclose the annual percentage rate (APR) and other costs before you agree to the loan.”²⁴ (emphasis added)

Senator Proxmire, sponsor of the federal Truth in Lending Act, addressed the need for APR as a standardized, all-in, annualized rate on the floor of the Senate in 1967:

²³ MicroFinance Transparency, “Total Cost of Credit vs. APR,” 2010. <http://www.mfransparency.org/total-cost-of-credit-vs-apr>

²⁴ <https://www.consumerfinance.gov/ask-cfpb/my-payday-lender-said-my-loan-would-cost-15-percent-but-my-loan-documents-say-the-annual-percentage-rate-apr-is-almost-400-percent-what-is-an-apr-on-a-payday-loan-and-how-should-i-use-it-en-1625/>

“Just as the consumer is told the price of milk per quart and the price of gasoline per gallon, so must the buyer of credit be told the "unit price." Historically in our society that unit price for credit has been the annual rate of interest or finance charge applied to the unpaid balance of the debt. Without easy knowledge of this unit price for credit, it is virtually impossible for the ordinary person to shop for the best credit buy. This is true, of course, because different offerings of credit may vary with respect to the amount of debt, the number of payment periods under which it is to be repaid, and the amount to be paid per period.”²⁵

Just as in S5470, Senator Proxmire’s Truth in Lending Act addressed the need for occasional estimation as well. In cases when an exact APR cannot be calculated, Senator Proxmire noted that the Truth in Lending Act “makes it abundantly clear that lenders need only state an approximate annual rate and would not be held to absolute accuracy down to the last decimal point.”²⁶

Additionally, measures of dollar cost consider only a single loan. However, the reality is that the business model of many small business financing companies is to encourage borrowers to renew their short-term financing over and over, year after year, similar to a payday loan. Many celebrate this on their websites! To quote one alternative financing company:

“[Company name] has designed an excellent Renewal Program for our customers. Once your Merchant Cash Advance or Business Loan payback is 50% complete, you’ll be eligible to renew with us for additional funding.

Over 70% of our merchants take advantage of this option, many of them renewing for a third or fourth time. Our cash advance and business loan terms are less than a full year, which means just a few months after funding, you’ll have a chance to get funded again...

Our goal is to make a lasting connection with every merchant, and be there for them whenever they need a financing boost. That’s what our Renewal Process is all about.”²⁷

When the business model is to encourage borrowers to renew their short-term financing every time it is 50% repaid as part of “a lasting connection,” it would be misleading to compare only the dollar costs of single transactions. Small businesses must be empowered to compare the price of using a 6-month merchant cash advances on an ongoing basis, to that of a 3-year loan, or a 1-year line of credit. Indeed, that is exactly the sort of choice small business are making every day.

There is no solution, other than APR, for transparent disclosure and a “common metric of cost comparison.” Not interest rate, not dollar cost, not new metrics invented by high-rate financing providers, and not the status quo in which so small businesses are being overcharged and misled.

²⁵ Senator Proxmire, William, “Congressional Record - Senate,” Jan 1967.
<https://web.archive.org/web/20120415005111/http://www.llsdc.org/attachments/wysiwyg/544/TILA-LH-CR-1967-01-31.pdf>

²⁶ Id.

²⁷ <https://www.capify.com/renewal-process-70-merchants-renew/>

These are among the reasons why the need for APR transparency in small business financing has been raised by:

- The National Consumer Law Center²⁸
- The Bloomberg News editorial board (“Protect Small Businesses from Predatory Lending”)²⁹
- The Bipartisan Policy Center³⁰
- Former SBA Administrator Karen Mills³¹
- US Treasury officials³²
- Federal Reserve Governor Lael Brainard³³
- Federal Reserve Board of Governors Community Advisory Council³⁴
- At least three research studies published by the Federal Reserve³⁵
- The Conference of State Bank Supervisors’ Fintech Industry Advisory Panel
- 110+ industry and nonprofit signatories and endorsers of the Responsible Business Lending Coalition’s *Small Business Borrowers Bill of Rights*³⁶
- A dozen member companies of the Innovative Lending Platform Association³⁷
- Numerous news articles, (e.g. McClatchy, “Even Finance Whizzes Say It’s Impossible to Compare Online Small Business Loan Options.” June 2018)³⁸
- And not least, the New York Department of Financial Services³⁹

In contrast, APR disclosure in small business financing appears to be opposed primarily by high-cost financing companies that do not disclose APR.

²⁸ See NCLC’s letter in Appendix B of the RBLC’s comment letter:

http://www.borrowersbillofrights.org/uploads/1/0/0/4/100447618/sb_1235_support_coalition_and_rblc_comment_-_small_business_disclosures_file_no_pro_01-18.pdf

²⁹ <https://www.bloomberg.com/amp/opinion/articles/2018-11-28/confessions-of-judgment-small-business-and-predatory-lending>

³⁰ <https://bipartisanpolicy.org/wp-content/uploads/2018/07/Main-Street-Matters-Ideas-for-Improving-Small-Business-Financing.pdf>

³¹ http://www.hbs.edu/faculty/Publication%20Files/17-042_30393d52-3c61-41cb-a78a-ebbe3e040e55.pdf

³² <https://www.treasury.gov/connect/blog/Pages/Opportunities-and-Challenges-in-Online-Marketplace-Lending.aspx>, https://www.progressivepolicy.org/wp-content/uploads/2017/11/PPI_SmallBizCredit_2017.pdf,

³³ Board of Governors of the Federal Reserve System, “Remarks by Lael Brainard: Community Banks, Small Business Credit, and Online Lending,” 2015. www.federalreserve.gov/newsevents/speech/brainard20150930a.pdf

³⁴ See page 7, <https://www.federalreserve.gov/aboutthefed/files/cac-20181005.pdf>

³⁵ Federal Reserve Bank of Cleveland, “Alternative Lending through the eyes of ‘Mom & Pop’ Small-Business Owners,” August 2015. <https://www.clevelandfed.org/newsroom-and-events/publications/special-reports/sr-20150825-alternative-lending-through-the-eyes-of-mom-and-pop-small-business-owners.aspx>

Federal Reserve Board of Governors, “Browsing to Borrow: ‘Mom & Pop’ Small Business Perspectives on Online Lenders,” June 2018. <https://www.federalreserve.gov/publications/files/2018-small-business-lending.pdf>

Lipman, Barbara and Ann Marie Wiersch, Board of Governors of the Federal Reserve System, “Searching for Small Business Credit Online,” Consumer and Community Context, Nov 2019, Vol 1, No 2, <https://www.federalreserve.gov/publications/files/consumer-community-context-201911.pdf>

³⁶ <http://www.borrowersbillofrights.org/signatories.html>

³⁷ <https://innovativelending.org/>

³⁸ <https://www.mcclatchydc.com/news/nation-world/national/article212491199.html>

³⁹ https://www.dfs.ny.gov/docs/reportpub/online_lending_survey_rpt_07112018.pdf

Other topics of clarification

RBLC comments included in blue.

Definitions.

Commercial financing: eliminate "other form of financing"

RBLC feels “other form of financing” was wisely included, at the recommendation of Assembly committee staff, to close loopholes. These industries are adept at finding loopholes--the merchant cash advance itself exists as a loophole to lending law. Additionally, some CDFI members inquired about the treatment of contract-based financing, for example. I believe it would be treated as “accounts receivable financing.” But if not, this “other forms” section enables DFS to address it and maintain a level playing field of transparency. To address the concern about equity, this could be defined modified to, or defined as, “non-equity financing.”

Open line of credit instead of commercial line of credit. We changed commercial line of credit to closed end so this is just consistency.

We believe that “commercial line of credit” would be better named “open-end financing,” for consistency.

However, commercial line of credit must be considered open-end credit, not closed-end. (Closed-end credit refers to credit with a known series of payments, like a regular loan. Open-end credit refers to lines of credit that can be drawn down, repaid, and then drawn down again, like credit cards or other commercial lines of credit.)

Leases

We share the SBFA’s view that, “many businesses obtain all of their equipment through equipment leases. If the goal of the Bill is to inform small business owners and make it possible for them to compare financing costs, all products should be included in the Bill.” Structuring financing as a lease, instead of a loan, is one way that financing providers evade lending law. We absolutely welcome SBFA’s suggestions on how to improve the inclusion of lease financing in this bill.

Accounts receivable: covers gross revenue and credit card MCAs but not forward looking factoring transactions- buy accounts based on future clients based on past sales history. Are we intentionally excluding these?

The “accounts receivable” section may need some cleanup, or deletion, with two respects:

1) To clarify that it should not include MCAs. MCAs are to be considered “sales-based financing” rather than “accounts receivable financing.” This should be clarified. (With respect to “forward-looking factoring transactions,” this appears to be another word for a merchant cash advance. They should be treated as “sales-based financing” like other MCAs.)

2) To better address factoring. There are disclosures asked here for “accounts receivable financing” that are not appropriate for “factoring.” For example, a traditional factoring does not include any periodic payments, or any concept of prepayment. So no “payment amount” or “prepayment” disclosures are appropriate here.

Our suggestion would be to delete the “accounts receivable” definition and revise the “accounts receivable” section to the previous form where it focused on factoring. It may be that the products intended to be addressed with this section can be treated as “open-end financing.” If not, DFS can develop additional “accounts receivable” disclosure requirements if needed, under the “other form of financing” section.

Accounts receivable and sales based: MCAs can fall under both categories; I don't think this matters for the disclosures but does this limit or restrict potential DFS regs if DFS wants to force additional disclosures based on product?

MCAs are to be considered “sales-based financing” rather than “accounts receivable financing.” We agree this must be clarified.

Recipient: should clarify that recipient can never be a broker because we don't want a disclosure going to the wrong person

Great point! We agree that “recipient should only be a small business owner or his or her authorized representative.”

We do believe it is important that a broker may be a “provider.” The Truth in Lending Act requires disclosure of APR at a must earlier stage, when small business may be in a comparison shopping phase when they may be working with a broker, through it's Advertising section.

<https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1026/24/>. This bill does not go this far.

Here is a passage from Federal Reserve research, drawing on the Federal Reserve Small Business Credit Survey, indicating that nearly ½ of small businesses considering online credit rely on brokers, and that these brokers have the same misaligned incentives that led mortgage brokers to steer borrowers into

expensive subprime mortgages, pre-2008 crisis.

The SBCS responses suggest where these small-business owners may be likely to go instead for financing advice: a loan broker, cited by nearly half (47 percent) of online applicants as their second major source of financial information. Brokers often compete actively to deliver clients to online alternative lenders, and can obtain substantial upfront referral fees. Bank officers, of course, routinely suggest their banks' own products. However, because brokers may refer borrowers to certain online lenders based on higher commissions rather than on product suitability, their role in online lending is controversial. Recent research suggests that the majority of small-business borrowers do not comparison-shop online when applying for a loan.¹³ The implication is that by relying on brokers instead of comparison-shopping, small businesses may not end up with the most appropriate, affordable product.

Specific offer:

This definition of when a disclosure must be made is intended to be broad, as SBFA notes that it is. The goal is that the disclosure not be pushed to the end of the financing process. The Federal Reserve's 2019 study concluded that:

When small business borrowers receive disclosures may be nearly as important as what is disclosed. Nearly all focus group participants said they would want clear upfront information to help them make borrowing decisions, stating they would want the level of detail that is provided in the disclosure as early as possible in the process. Many remarked that presenting the product rate and terms at loan closing is too late, as they have already invested time in the application process, shared their financial data with the lender, and may have already committed the expected loan proceeds.

If a provider is not yet able to provide a price, they should not quote a specific amount to the recipient. If the provider can commit to providing some amount of capital, but they cannot yet quote a price, the "specific offer" disclosure would not be triggered by quoting amount ranges such as, "between \$30,000 and \$50,000," or "up to \$50,000."

Purchaser/Provider/Recipient: confusing, definitions don't align with how products actually work

We recommend the "purchaser" definition be deleted. It is not needed in addition to "recipient."

Sales-based financing:

This category was created with the intention to include all MCAs and other products repaid as a percentage of sales such as the PayPal transactions.

Here is the definition in the draft regulations written by the CA state financial regulator, which we recommend adopting:

“Sales-based financing” means a transaction that is repaid by a recipient to the finance company as a percentage of sales or revenue, in which the payment amount increases and decreases according to the volume of sales made or income received by the recipient. Sales-based financing also includes transactions with a “true-up mechanism.”

The value of their reference to a “true-up mechanism,” not currently included in S5470, is that many MCAs don’t actually have the technology or processes to have the payment amount rise as fall with sales as those changes occur. Instead, the MCA sets a fixed daily payment amount, and the small business can apply to “true-up” the amount to account for their actual sales and be refunded if they overpaid. In practice, many may simply overpay. We suggest this be included.

We disagree with the argument that “sales-based financing” as drafted would not include MCAs repaid as a % of specific revenue streams, such as credit cards. We also disagree that there is a problem that, “transactions have fixed payments and they would be excluded as well.” We believe it is sufficiently clear that these would be “closed-end credit.”

Exemptions:

We share the SBFA’s view that, “The Bill may want to specifically exempt equity transactions and transaction over a certain threshold. This Bill’s disclosure requirements are not necessary for large transactions (*e.g.* over \$1,000,000). As currently drafted, the Bill would apply to a \$50,000,000 loan made by Goldman Sachs.”

Disclosure Requirements

APR:

Thank you for raising this. We hope it is addressed satisfactorily above, and would be delighted to discuss it further.

We highlight SBFA’s statement that, “All providers today disclose the financing amount, the total repayment amount, the payment amounts, other fees, prepayment costs and collateral. These items are

required in order to have an enforceable contract... Many providers do not disclose the financing charge, although it is readily apparent by deducting the financing amount from the total repayment amount.”

There would be no contribution in a bill that required these disclosures alone. That would create only the appearance of a transparency bill and undermine efforts for an effective transparency bill like S5470. S5470 provides real value by requiring additional disclosure that are not consistently taking place. Specifically: APR, payment amount, and prepayment costs.

Finance Charge: Is the finance charge definition different from TILA? Does it make a serious difference to have fees included as finance charge? Does it make a serious difference if fees are considered outside of finance charge? Is this just a stall tactic?

The “finance charge” language may be able to be tightened up. The “total cost of financing” described in S5470 aligns with the TILA “finance charge” in principle but not in letter. Both include fees that are required to get the financing. Here is the definition of “finance charge” in TILA:

“The finance charge is the cost of consumer credit as a dollar amount. It includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction.” The is more discussion here: <https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1026/4/>

Perhaps the S5470 “finance charge” approach could be updated to better align with TILA with the following language:

1) Define “finance charge,” referencing and based in TILA, as:

“the cost of financing as a dollar amount. It includes any charge payable directly or indirectly by the recipient and imposed directly or indirectly by the provider as an incident to or a condition of the extension of financing. It includes all charges that would be included under 12 C.F.R. part 1026.4 if the transaction were subject to 12 C.F.R. part 1026.4.

In any open-end credit transaction, the finance charge shall assume the maximum amount of credit available to the recipient, in each case, is drawn and repaid at the minimum rate.” [The current text of s5470 705(B) reads “held for the duration of the term or draw period” instead of “repaid at the minimum rate,” but we favor the later.]

In any accounts receivable purchase or factoring transaction, the finance charge includes the discount taken on the face value of the accounts receivable.”

In addition, the following text, drawing on the California regulation, could be included in S5470 or could be left to the DFS to define:

“In any lease financing transaction, finance charge includes the sum of the lease payments and, if there is a fixed-price purchase option or a purchase option with a price that can be calculated at the time of disclosure, the purchase price listed in the contract that the lessee may pay to acquire the leased goods at the end of the lease, minus: a) if the finance company selects, manufactures or supplies the goods to be leased, the price that the finance company would sell the goods in a cash transaction, or b) if the finance company does not select, manufacture or supply the goods to be leased, the price the finance company will pay to acquire the property to be leased.”

- 2) Replace the “total cost of financing” sub-sections (703(b), 704(b), 705(b) etc.) with a reference to the now-defined “finance charge.” E.g. “The finance charge, as a dollar amount.”
- 3) If seeking to close existing loopholes, consumer advocates have also suggested that the finance charge definition should be based on the Military Lending Act, rather than TILA. The Military Lending Act definition of APR brought in a number of charges advocates feel should also be included.⁴⁰

Simple Interest and Credit Cards: Is simple interest rate really what is required for credit cards? If simple interest rates are what people are really used to seeing, why is this bill advocating an APR standard that has been abandoned?

Credit card APR is not the simple interest rate. Credit card APRs do not include fees, however. The proposed approach to open-end credit APR addresses a loophole that would otherwise enable any provider classifying their charges as “fees” to disclose a 0% APR. (This loophole would apply to the entire MCA industry, and some others.) The proposed approach is based on small business financing industry practice (it’s required by both the Small Business Borrowers’ Bill of Rights and the SMART Box) and has already

⁴⁰ New York could consider including additional finance charge items addressed in the Military Lending Act. Quoted here from the FDIC Consumer Compliance Examination Manual, V13.4:

“The following charges included in the MAPR (“charges”) must be included in the calculation of the MAPR for both closed- and open-end credit, as applicable:

- Any credit insurance premium or fee, any charge for single premium credit insurance, any fee for a debt cancellation contract, or any fee for a debt suspension agreement;
- Any fee for a credit-related ancillary product sold in connection with the credit transaction for closed-end credit or an account for open-end credit; and
- Except for a bona fide fee (other than a periodic rate) charged to a credit card account, which may be excluded if the bona fide fee is reasonable:
 - o Finance charges associated with the consumer credit;
 - o Any application fee charged to a covered borrower who applies for consumer credit, other than an application fee charged by a Federal credit union or an insured depository institution when making a short-term, small amount loan provided that the application fee is charged to the covered borrower not more than once in any rolling 12-month period (see note below); and
 - o In general, any fee imposed for participation in any plan or arrangement for consumer credit. (See “No Balance During a Billing Cycle” section below for more information on the MAPR calculation rules when there is no balance during a billing cycle for open-end credit).

These charges are to be included in the MAPR calculation even if they would be excluded from the calculation of the finance charge under Regulation Z.”

<https://www.fdic.gov/regulations/compliance/manual/5/v-13.1.pdf>

been adopted by the CA regulator. It is discussed in more detail in the RBLC Jan 2019 comment to CA, pages 42-43.

The CFPB indicates that APR is valuable for comparing cost of credit cards with other types of credit: “To calculate the APR, the interest rate and fees are compared to the amount you borrow and calculated over a one-year period. **This allows you to compare the costs of a credit card to a six-month installment loan, or a two-week payday loan. It is also why APRs are often different from simple interest rates.**”⁴¹ (emphasis added)

The reference to “simple interest rate” is also an example of the confusion about that term, even among finance professionals.⁴² S5470 is written to address this confusion, which will be of great benefit to small businesses.

Can you respond to these points on pages 9-11: 1, 2, 3, 5, 6

1) “APR... will be misleading as the fixed fee loan products have no accruing rate.”

Small businesses are grossly misled by the disclosure practices of fixed-fee products today. This has been established by repeated Federal Reserve studies, the experience of our organizations every day, and has been decried by regulators, advocates, community groups, and industry. With respect to the concern raised here that borrowers will mistake the APR as the rate accruing interest, this will be addressed through clarifying language in the disclosure. The disclosure is intended to make clear that the “fixed fee” is a fixed fee, that no savings or limited savings occurs on prepayment, and that the estimated APR is a provided to enable borrowers to make cost comparisons but is not the interest rate that will be charged. DFS will prescribe the clarifying language.

2) “APR is a complicated mathematical calculation.”

Calculating APR may be unfamiliar to financing companies that have not been doing it. (Though, frankly, a finance company that cannot figure out how to calculate an APR may want to consider another line of work.) Fortunately, DFS can make calculations accessible for less familiar financing providers by posting plug-and-play formulas that can be used in Microsoft Excel or Google Sheets. These calculations are

⁴¹ <https://www.consumerfinance.gov/ask-cfpb/my-payday-lender-said-my-loan-would-cost-15-percent-but-my-loan-documents-say-the-annual-percentage-rate-apr-is-almost-400-percent-what-is-an-apr-on-a-payday-loan-and-how-should-i-use-it-en-1625/>

⁴² The term “simple interest” it is commonly used differentiates open-end credit or credit card’s “compound” interest vs. installment loans “simple” interest. But the term “simple interest” is also sometimes used by the financing industry to describe the total interest charges as a percentage of the original balance. This number is much lower than the actual annualized interest rate or APR, and the Fed identified this practice as confusing to borrowers. In the Fed research example, they contrast a disclosed “9% simple interest” to the APR of 46%.

described, with mathematical demonstration of their accuracy with regard to TILA, in the RBLC September 2019 Comment to CA, page 17.⁴³

3) “Two products with identical pricing and terms will have different APRs if one is a monthly pay product and one is a daily pay product.”

Far from being a problem, this is accurate and mathematically correct. If a loan is repaid in daily payments as compared to monthly payments, it is repaid more quickly. The borrower will have a lower balance during the month as they will have returned more of the capital to the provider. If they are being charged the same finance charge for use of that lower balance, they are being charged a higher price. APR accurately reflects that. This is discussed in with examples in the RBLC’s Jan 2019 Comment to CA, pages 17-20.

4) Claim: Rate may be important for consumers financing lifestyle needs, but rate is not important for small businesses. Business operates in dollars and so small business don’t need to see an annualized rate.

Although you did not request a response on #4, we believe it is illustrative. The fact is, much more than consumers’ lives, business actually *does* operate on annualized rates. The basic metric of business is the profit margin, a percentage rate. And when considering a specific investment, the basic metric of business is the Return on Investment (ROI.)

It is a problem today for a small business, desperate for capital, to borrow at undisclosed annualized rates of 50% or 350% and invest that capital in a restaurant with a profit margin of 5%. They are losing money. It is a problem today for a retailer to borrow at undisclosed annualized rates of 50% or 350% to buy inventory they will sell at a return on investment of 20%. They are losing money. A business might choose to make these loss-making investments strategically, but they should be given the information to make this choice with eyes wide open.

Moreover, without APR, borrowers of are inhibited from comparing financing options to see which is cheapest, over time. Transparent price disclosure is necessary for the financing market to be competitive. This was a primary goal of the 1967 Truth in Lending Act. Senator Proxmire stated that, “The market system requires information in order to function-information on the part of both buyers and sellers. When information channels become clogged, competition breaks down. The essence of the truth-in-lending bill is to restore full information in the consumer credit field to insure a full disclosure of the cost of credit and thus to permit the market system to function more effectively.”⁴⁴

5) “TILA and its implementing regulations never envisioned daily pay products.”

⁴³http://www.borrowersbillofrights.org/uploads/1/0/0/4/100447618/rblc_coalition_comment_on_ca_dbo_small_business_financing_disclosures_-_pro_01-18_-_sept_2019.pdf

⁴⁴ Congressional Record - Senate (1967)

False. The National Consumer Law Center, which literally “wrote the book”⁴⁵ on TILA that many finance attorneys consult to interpret the law, refuted this argument when it was made to the CA legislature with reference to weekly payments. Below is an excerpt from NCLC’s letter (included in full in the RBLC Jan 2019 comment to CA, Appendix B):

The analysis of S.B. 1235 prepared for the Senate Committee on Banking and Financial Institutions for its April 18 hearing expresses concern that the Truth in Lending Act APR disclosure does not take into account the possibility of a weekly (rather than monthly) payment schedule or accommodate varying payment amounts. In fact, the Truth in Lending Act explicitly *requires* the APR disclosure to take weekly payment schedules and varying payment amounts into account. Appendix J to TILA’s Regulation Z gives specific instructions for making these calculations. The regulation for computing the APR, 12 C.F.R. § 1026.22(b)(1) provides:

(b) Computation tools.

(1) The Regulation Z Annual Percentage Rate Tables produced by the Bureau may be used to determine the annual percentage rate, and any rate determined from those tables in accordance with the accompanying instructions complies with the requirements of this section.

Volume I of the tables applies to single advance transactions involving up to 480 monthly payments or 104 *weekly* payments. It may be used for *regular transactions and for transactions with any of the following irregularities: an irregular first period, an irregular first payment, and an irregular final payment.* Volume II of the tables applies to transactions involving multiple advances and *any type of payment or period irregularity.*

(Emphasis added.)

⁴⁵ <https://library.nclc.org/til>

The widespread availability of computerized calculation tools has made APR calculations even easier today. Many APR calculators are available free on the internet, including one provided by the federal Office of the Comptroller of the Currency, the regulator of national banks: <https://www.occ.treas.gov/tools-forms/tools/compliance-bsa/aprwin-software.html>. The TILA regulations explicitly endorse the use of these APR calculators:

(2) Creditors may use any other computation tool in determining the annual percentage rate if the rate so determined equals the rate determined in accordance with appendix J to this part, within the degree of accuracy set forth in paragraph (a) of this section.

12 C.F.R. § 1026.22(b)(2).

The analysis prepared for the committee also expresses concern about certain types of business financing in which the repayment period is not known with certainty in advance. The APR can be easily accommodated to this type of lending by estimating the repayment period. Responsible business lenders already provide an APR using such an estimate – see, for example, <https://www.americanmerchantbrokers.com/merchant-cash-advance-calculator.html>. This approach would simply codify the existing best practices of the small business lending industry. The Truth in Lending regulations already endorse the use of estimates when the information necessary for a completely accurate disclosure is unknown to the creditor:

Basis of disclosures and use of estimates. Disclosures shall reflect the terms of the legal obligation between the parties. If any information necessary for accurate disclosure is unknown to the creditor, it shall make the disclosure based on the best information reasonably available and shall state clearly that the disclosure is an estimate.

12 C.F.R. § 1026.5(c).

6) Claim: Small businesses using sales-based products will be confused between the APR and the “split rate,” which is the % of sales that goes towards repaying the financing.

This is a valid concern. As we’ve noted, the Federal Reserve research has found that small business owners often assume any percentage number to be the annualized rate. However, the worst form of this confusion is what is happening today, without APR disclosure. Small business owners are being shown a 4% “rate” (the split rate), and believing that this is equivalent to their annual interest rate or APR, and are never told they will be charged an APR of 50% or 350%.

Federal reserve research has shown that this is misleading small businesses into taking expensive financing, when more affordable options are available: “when asked to compare a sample short-term loan product with a 9 percent “simple interest” rate to a credit card with a 21.9 percent interest rate, most participants incorrectly guessed the short-term loan to be less expensive.”⁴⁶

⁴⁶ Federal Reserve, 2019, pg. 19.

Preemption: The way we have talked about this and correct me if I am wrong: TILA applies only to consumer loans, business loans were left out of TILA intentionally, this is disclosure for business loans, TILA doesn't touch on business loans, so there is no preemption because there is no conflict.

Here's from the National Consumer Law Center on this question: "Since the Truth in Lending Act and Regulation Z don't apply to business credit (with one exception - the provisions about issuance of credit cards and unauthorized use apply to business as well as consumer credit cards), the preemption rules just don't come into play. The whole reason for your bill is that TILA doesn't apply. *If you wanted to be super-safe I suppose you could add something in your bill saying that your bill is inapplicable to any transaction for which TILA requires disclosure of the terms of the transaction, but I think that would be a belt-and-suspenders approach.*"

Term: Where historical and opt-in came from. SBFA says they don't know these standards.

The historical and opt-in approach was proposed by the RBLC. It has been adopted by the CA regulator. We believe the Historical Method proposed is the most accurate than can be used in the absence of reporting to DFS without risk of gaming by providers. The Opt-In Program provides additional flexibility to providers, and to prevent gaming, pairs it with the additional accountability of reporting to the DFS.

The historical method is simple—project sales based on the historical average. This is how many MCA providers project terms today. Because it is prescriptive, it prevents providers from manipulating their estimates to disclose unreasonably low APRs.

If a sales-based financing provider believes their internal method of determining the required estimates are more accurate, the Opt-In Program provides a way for the provider to use that method. They can use whatever method they choose, so long as they report on its accuracy to DFS. This pairs the flexibility with some accountability.

SBFA notes that, "We suggest this language be amended to actually reflect what is done in the industry to estimate terms." In fact, the proposed approach is designed to enable providers to do exactly "what is done in the industry to estimate terms"—with the addition of accountability to prevent deceiving customers.

Moreover, it is important to note here the SBFA's acknowledgement that it is already MCA industry standard practices to estimate term, and thus also the annualized rate. This is not a surprise. Finance companies do not give out money without an expectation of when it will be repaid. Similarly, they do not give out money without an expectation of an annualized rate of return. In fact, these high-rate financing providers sometimes advertise their high annualized gross yields or APRs to their investors. We believe the borrowers paying those yields deserve to know them as well.

We look forward to speaking with you soon. Please do not hesitate to contact us for any reason at any time, at kim@borrowersbillofrights.org.