



*Advancing Economic Security  
and Community Prosperity*

January 22, 2018

Commissioner Jan Lynn Owen  
Department of Business Oversight  
1515 K Street, Suite 200  
Sacramento, California 95814-4052

Re: Small Business Disclosures, FILE NO: PRO 01-18

Dear Commissioner Owen:

The comment letter submitted by the Responsible Business Lending Coalition contains many important recommendations. We wanted to highlight one because we feel this recommendation is necessary to close a potential loophole that could be used by unscrupulous lenders to undermine SB 1235.

The Military Lending Act (MLA) establishes a 36-percent Annual Percentage Rate (APR) cap on loans made to active duty members of the military, their spouses, and their dependents. We have seen lenders try to evade state interest rate caps by shifting their fees to the various categories of fees that are *not* included in the APR under Regulation Z of the Truth In Lending Act (TILA).<sup>1</sup> For example, some lenders charge “junk fees” for add-on products that provide little to no benefit to the borrower. “Credit protection” and “identity monitoring” are examples of such products.<sup>2</sup> To prevent such evasion, the MLA established an annualized rate that includes more types of fees than are included under TILA. The additional types of fees included in the APR under the MLA are described in the *OCC Comptroller’s Handbook, Military Lending Act* (page 8).<sup>3</sup>

Even outside the context of interest rate caps, some lenders would be motivated to hide the true cost of their loans to make their products appear more affordable to borrowers and to evade regulatory scrutiny. In the context of payday loans, triple-digit interest rates inspired state initiatives to cap interest rates. Largely due to the lack (until now) of a disclosure requirement, widely available data does not exist in the context of small business lending. Woodstock analyzed a small set of small business loans made by non-bank financial technology (fintech) lenders, and some of the APRs were alarming, including a high of 367.7 percent!<sup>4</sup> Some of these high-cost fintech loans are essentially payday loans for small

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<sup>1</sup> The Federal Reserve describes this phenomenon in an MLA exam procedures handbook in footnote 6 on page one. [https://www.federalreserve.gov/supervisionreg/caletters/Attachment\\_CA\\_Letter\\_16-6\\_MLA\\_Exam\\_Procedures.pdf](https://www.federalreserve.gov/supervisionreg/caletters/Attachment_CA_Letter_16-6_MLA_Exam_Procedures.pdf)

<sup>2</sup> CFPB, *What are credit card “add-on products?”* (Aug. 8, 2016). <https://www.consumerfinance.gov/ask-cfpb/what-are-credit-card-add-on-products-en-1541/>

<sup>3</sup> OCC, *Comptroller’s Handbook, Military Lending Act* (May 2018). <https://www.occ.gov/publications/publications-by-type/comptrollers-handbook/military-lending-act/pub-ch-mla.pdf>

<sup>4</sup> Woodstock Institute, *Analysis of Business Loan Terms* (July 12, 2016). [http://www.woodstockinst.org/wp-content/uploads/2016/07/Woodstock\\_Analysis\\_of\\_Online\\_SB\\_Loan\\_Terms.pdf](http://www.woodstockinst.org/wp-content/uploads/2016/07/Woodstock_Analysis_of_Online_SB_Loan_Terms.pdf)

businesses. To the extent SB 1235 helps bring predatory practices to light, it will pave the way, if necessary, for additional protections for small business borrowers.

Thus, to bring greater transparency to the industry and to enable small business owners to make informed business decisions as to credit, the annualized rate that is disclosed under SB 1235 should reflect the included charges under Regulation Z of TILA *and* the additional included charges under the MLA.

Very truly yours,

WOODSTOCK INSTITUTE

#### About Woodstock Institute

Woodstock Institute is a leading nonprofit research and policy organization in the areas of equitable lending and investments; wealth creation and preservation; and safe and affordable financial products, services, and systems. Since 1973, Woodstock has conducted high-quality research and used our findings to advocate with policymakers and financial institutions for access to safe and affordable financial products, services, and investments in underserved low- and moderate-income (LMI) communities, and for a more equitable financial system. We serve as a bridge between community-based organizations, policymakers, and financial institutions, to effect changes that directly benefit LMI people and communities of color.