

California Department of Business Oversight

INITIAL STATEMENT OF REASONS

Hearing Date: No hearing date is scheduled. A public hearing will be held if any interested person, or his or her duly authorized representative, submits a written request for a public hearing to the contact person listed no later than 15 days prior to the close of the written comment period.

Written Public Comment Period: September 11, 2020 through October 28, 2020.

Subject Matter of Proposed Regulations: Commercial Financing Disclosures

California Code of Regulations Section Being Amended or Repealed: None.

California Code of Regulations Sections Being Adopted: Title 10, Subchapter 16, Sections 2057, 2060, 2061, 2062, 2063, 2064, 2065, 2066, 2067, 2068, 2070, 2071, 2089, 2091, 2092, 3000, 3001, 3002, 3003, 3010, 3020, 3021, 3022, 3023, 3024, 3025, 3026.

Effective Date of the Regulations

The Department anticipates that the proposed regulations will go into effect, if adopted on or before January 1, 2021, on July 1, 2021. Since the proposed regulations will require affected businesses to implement new practices and procedures, July 1, 2021 represents a 6-month delay from the anticipated date of adoption in order to come into compliance. If, however, the proposed regulations are adopted after January 1, 2021, the effective date will adjust accordingly to maintain a 6-month delay in effectiveness.

Specific purpose of each adoption, amendment, or repeal:

On September 30, 2018, Governor Brown signed SB 1235 (Chapter 1011, Statutes of 2018) into law. SB 1235 requires a “provider” – a person who extends a specific offer of “commercial financing” (as defined in Financial Code section 22800, subdivision (d)) to a recipient – to give the recipient certain disclosures at the time the provider extends the offer. SB 1235 mandates the Department to draft regulations implementing the specific requirements of the disclosures to be provided to recipients, including: definitions, methods of calculation for certain disclosure items, the method of expressing the annualized rate disclosure, the time, manner and format of the disclosures, and many other details. The Department seeks to add new Code of Regulation sections to comply with the legislature’s mandate.

The goal of the new disclosures is to provide recipients more information about the actual costs and terms of financing agreements, as well as help them comparison shop for financing. Increased protection of businesses seeking commercial financing (many of whom are small businesses) is a key goal of the disclosures, as well.

Pursuant to its authority to promulgate rules and regulations under Sections 22802, 22803, and 22804 of the Financial Code, the Department proposes to add sections 2057, 2060, 2061, 2062, 2063, 2064, 2065, 2066, 2067, 2068, 2070, 2071, 2089, 2090, 2091, 2092, 3000, 3001, 3002, 3003, 3010, 3020, 3021, 3022, 3023, 3024, 3025, 3026 to the California Code of Regulations.

Factual Basis/Rationale

Pursuant to the legislative mandate contained in Financial Code section 22804, the Department proposes to draft these regulations that will govern the required disclosure definitions, contents, methods of calculation, and requirements concerning the disclosure timing, manner and formatting. The Commissioner has determined that these proposed regulations are reasonable and necessary to comply with the legislature's mandate as well as to accomplish the stated goals of the regulations.

Section 2057: The purpose of proposed section 2057 is to clarify terms used in the statute relating to the disclosure requirements. The clarifications are necessary to provide the public with guidance on compliance with the law and are intended to reflect meanings commonly understood by industry and other stakeholders. The provisions benefit the public by providing clarity regarding the meaning of terms and phrases as used in law.

Section 2057(a)(1): Financial Code section 22800, subdivision (n) defines "recipient" to mean "a person who is presented a specific commercial financing offer by a provider that is equal to or less than five hundred thousand dollars (\$500,000)." Financial Code section 22800, subdivision(d)(1) defines "commercial financing" to mean "an accounts receivable purchase transaction, including factoring, asset-based lending transaction, commercial loan, commercial open-ended credit plan, or lease financing transaction intended by the recipient for use primarily for other than personal, family or household purposes." Because of the broadly different types of transactions (and how those transactions operate) contained within the definition of "commercial financing", a regulation clarifying how the \$500,000 threshold might be reached or established for the different types of transactions was established in section 2071. Proposed subdivision (a)(1) of section 2057 establishes definitions of a term ("approved advance limit") that is used in section 2071 to help clarify how the \$500,000 threshold might be reached for certain factoring transactions.

Because some factoring transactions are structured in a manner that makes it difficult to perform a simple calculation of whether or not the recipient is being offered a transaction in excess of \$500,000, this subdivision is necessary to help clarify if the disclosures required by Financial Code section 22800 *et seq.* must be given to a recipient of a factoring transaction subject to a factoring agreement, including a factoring agreement that differentiates between the amounts to be paid to the recipient depending on the type of legally enforceable claim.

Section 2057(a)(2): Similar in purpose and intent to subdivision (a)(1) of section 2057, proposed subdivision (a)(2) of section 2057 establishes definitions of a term (“approved credit limit”) that is used in section 2071 to help clarify how the \$500,000 threshold might be reached for open-ended credit plan agreements or asset-based lending transactions.

Because open-ended credit plans and asset-based lending transactions are structured in a manner that makes it difficult to determine whether or not a recipient is being offered a transaction in excess of \$500,000, this subdivision is necessary to help clarify if the disclosures required by Financial Code section 22800 *et seq.* must be provided to recipients of those types of transactions.

Section 2057(a)(3): This Section clarifies that for a transaction to qualify as asset-based lending, it must be a loan under California law. The purpose of this section is to ensure that providers who do not characterize their products as loans do not mistakenly classify their products as “asset-based lending” and use disclosures designed for a regulated loan product. The section is necessary to ensure that asset-based lending disclosures are only made for regulated loan transactions.

Section 2057(a)(3)(i): Financial Code Section 22800, subdivision (c) defines “asset-based lending transaction” to mean “a transaction in which advances are made from time to time contingent on a recipient forwarding payments received from one or more third parties for goods the recipient has supplied or services the recipient has rendered to that third party or parties.” Subdivision (a)(3) of section 2057 clarifies the meaning of the phrase “forwarding payments.” It provides that “forwarding payments” includes arrangements in which a recipient and the financier create an account in which third party obligors deposit payments, arrangements in which a recipient repays advances with the proceeds the recipient collects from the sale or disposition of goods or services financed with such advances, and arrangements in which the recipient directs third party obligors to make payments directly to the financier.

The subdivision is necessary to clarify the meaning of the phrase “forwarding payments” and ensure that a common practice in asset-based lending transactions would not, if used, result in being excluded from the definition.

Section 2057(a)(4): Financial Code section 22802, subdivision (a) provides, in relevant part, that “a provider subject to this division shall disclose all of the information in subdivision (b) or in Section 22803, if applicable, to a recipient at the time of extending a specific commercial financing offer to that recipient” Subdivision (a)(4) of section 2057 clarifies the meaning of the phrase “at the time of extending a specific commercial financing offer.” It provides that the phrase means (1) the time when a specific amount, rate or price, in connection with a commercial financing, is quoted to a recipient, based upon information from, or about, the recipient, and (2) any subsequent time when the terms of an existing commercial financing contract are amended or supplemented, prior to the recipient agreeing to the changes, if the resulting changes to the contract would result in an increase to the finance charge, payments, term, or annual percentage rate, regardless of whether those terms were previously disclosed to the recipient.

This subdivision is necessary to clarify the timing of when a disclosure must actually be made. Because of the great variance in how commercial financing providers do business and solicit interest in their products, without this clarification, it is unclear as to when a provider must provide a borrower the required disclosures, especially if the borrower and provider have a pre-existing relationship. This subdivision is further necessary to ensure a legislative intent of SB 1235 is carried out: that borrowers have increased availability of information to make an informed decision on proposed financing offers. To that end, the disclosures must be provided at an early enough stage of the borrowing process to permit a borrower to reasonably use the information provided in the disclosure to compare and contrast other, similar offers.

Section 2057(a)(5): Financial Code section 22804, subdivision (a)(1) mandates the Commissioner to establish regulations governing, among other things, the methods of calculation for each of the disclosure items required by Financial Code section 22802, subdivision (b) and section 22803, subdivision (a). Subdivision (a)(5) of section 2057 establishes a definition for “benchmark rate”, which means a rate index based upon general market conditions that is commonly used to calculate the interest rate in adjustable-rate transactions in the credit industry. This definition is used throughout the regulations where the disclosures require a calculation of interest.

This subdivision is necessary to ensure clarity as to how adjustable-rate interest transactions are to be calculated when complying with the proposed regulations.

Section 2057(a)(6): This section defines the term “broker” to mean “any person other than a financier who communicates a financing amount, rate or price relating to a commercial financing to a recipient based upon information from, or about, the recipient.” This section was added to address an inconsistency in the

law relating to commercial financing offers and transactions when a person communicating related information may not quite meet the definition of provider or financier. This section is necessary, in connection with related regulations addressing the conduct of brokers (section 3023), in order to clarify the responsibilities of persons meeting the definition of broker as well as the responsibilities of financiers using a broker for commercial financing transactions.

Section 2057(a)(7): This section is necessary to ensure clarity when referencing the California Financial Code within the proposed regulations.

Section 2057(a)(8): Financial Code section 22800, subdivision(d)(1) defines “commercial financing” to mean “an accounts receivable purchase transaction, including factoring, asset-based lending transaction, commercial loan, commercial open-ended credit plan, or lease financing transaction intended by the recipient for use primarily for other than personal, family or household purposes.” While the statute does not expressly use the term “closed-end”, by using the term “open-ended”, it implicitly establishes that some transactions are inherently “closed” if they are not “open-ended”. Subdivision (a)(8) of section 2057 defines the term “closed-end transaction” and by doing so intends to clarify differences in such transactions from others. This is necessary in order to ensure clarity throughout the regulations when discussing commercial financing transactions.

Section 2057(a)(9): Financial Code section 22800, subdivision (b)(3) and section 22803, subdivision (a)(3) require the disclosure of a term or estimated term. For open-ended credit plans and asset-based lending transactions, the Department has interpreted this requirement to mean the length of time that it is anticipated will be necessary for the recipient to fulfill its obligations under the financing agreement with respect to a particular loan advance (section 2057(a)(25)(C)). For a factoring disclosure made pursuant to Financial Code section 22803, the Department has interpreted this requirement to mean the maximum length of time between when a financier will accept a legally enforceable claim and when that legally enforceable claim will become due and payable by the legally enforceable claim’s account debtor. Each of these clarifying definitions of “term” (see section 2057(a)(25)) is designed to reflect the length of time it will take for a financier to be repaid in connection with a specific advance. The Department recognizes that with open-ended credit plans, asset-based lending transactions, and general factoring agreements, there may also be a time period during which a recipient may make draws under the agreement. The purpose of this section is to help recipients better understand their commercial financing disclosures, by disclosing “term” and “draw period” separately. This section is necessary because it defines the time period during which a recipient may make draws under the agreement so that providers can disclose this metric as the “draw period” separately from the “term”.

Section 2057(a)(10): Financial Code section 22802, subdivision (b)(2) and section 22803, subdivision (a)(2) require one of the disclosures made to recipients by a provider be “the total dollar cost” of the financing. Subdivision (a)(10) of section 2057 defines “finance charge” to mean “the amount of any and all costs of credit, represented as a dollar amount.” Since there may be many different costs and fees associated with a particular commercial financing, especially between the different types of commercial financing, a separate rule was added in section 3010 discussing how the finance charge must be calculated. This provision is necessary to ensure uniformity in how the “total dollar cost of financing” is described and specified in both the regulations and the disclosures by using a well-known, industry standard term to express the concept.

Section 2057(a)(11): Subdivision (a)(11) of section 2057 defines “financer” to mean “the person who provides or will provide the commercial financing to the recipient, or any nondepository institution which enters into a written agreement with a depository institution to arrange for the extension of commercial financing by the depository institution to a recipient via an online lending platform administered by the nondepository institution.” This section is intended to address a situation, given the statute’s definition of “provider”, where the individual who *extends an offer of commercial financing* to a recipient might not necessarily be the same entity that is *financing* the transaction (see also: the definition of “broker”). This section is necessary, along with related sections (see section 3023), to clarify what the responsibilities of persons meeting the definition of “financer” should be since by using a broker to extend offers of commercial financing it would otherwise be unclear which entity, financer or broker, is responsible for making disclosures in certain common commercial financing scenarios.

Section 2057(a)(12): Certain types of financing transactions have an adjustable interest rate that cannot be calculated in advance for the entire term of the transaction. The Department has determined that for the purposes of making required disclosures, the provider shall use the initial interest rate that would be in place at the time of disclosure when calculating the interest rate for any part of the term of the transaction where the interest rate cannot be calculated in advance (section 2060(a)(10)). The Department’s purpose in allowing this simplifying assumption is to promote uniformity in disclosures where there are adjustable interest rates of this type. This section is necessary so that the Department can require calculations and disclosures based upon the initial interest rate in other parts of these rules.

Section 2057(a)(13): The purpose of this section is to enable disclosures for transactions where charges accrue over time based (at least in part) on the outstanding principal balance. It is necessary to define the rate at which such

charges accrue as the “interest rate” so that the interest rate may be disclosed in other sections and incorporated into calculations for other disclosures.

Section 2057(a)(14): The purpose of this section is to ensure that providers make disclosures that incorporate all payments a recipient will be required to make. This section is necessary because certain financing transactions include required payments that are not paid at regular intervals (periodic payments).

Section 2057(a)(15): Financial Code section 22804, subdivision (a)(1) mandates the Commissioner to establish regulations governing, among other things, the methods of calculation for each of the disclosure items required by Financial Code section 22802, subdivision (b) and section 22803, subdivision (a). Subdivision (a)(15) of section 2057 establishes a definition for “margin”, which means, in a commercial financing with an adjustable interest rate, the adjustment to the benchmark rate designated in the contract used to calculate the interest rate. This definition is used throughout the regulations where the disclosures require a calculation of adjustable interest.

This subdivision is necessary to ensure clarity as to how adjustable-rate interest transactions are to be calculated when complying with the proposed regulations.

Section 2057(a)(16): The purpose of this section is to help recipients better understand the costs and benefits of prepayment in cases where all or part of the finance charge is a fixed cost (rather than interest that accrues over time). This section is necessary because it defines the amount (that must be disclosed to the recipient) of non-interest finance charges that a recipient must pay if they prepay on a financing agreement.

Section 2057(a)(17): Certain types of sales-based financing base a recipient's payment amounts upon the recipient's cash flow through a particular bank account or credit card processor, or some other metric of the recipient's business receipts. For circumstances like this, the Department has determined that disclosures should explain this process (see e.g. Section 2065, subdivision (a)(3)(C)) so that small business owners can better understand how their payments are calculated. This section is necessary because it creates a definition that is used in other sections to require disclosure of how payments are calculated in circumstances like those described above.

Section 2057(a)(18): The purpose of this section is to ensure that providers make disclosures that incorporate all payments a recipient will be required to make. This section is necessary because many financing transactions require payments at regular intervals.

Section 2057(a)(19): Financial Code section 22800, subdivision (m) defines “provider” to mean “a person who extends a specific offer of commercial

financing to a recipient.” The section further states that “provider” also includes “a nondepository institution, which enters into a written agreement with a depository institution to arrange for the extension of commercial financing by the depository institution to a recipient via an online lending platform administered by the nondepository institution.” Subdivision (a)(19) of section 2057 makes two clarifications on the definitions in the statute.

First, it clarifies that “provider” also includes “financers” (defined in subsection (a)(11)) in certain situations, such as when a financier communicates certain information to a broker (defined in subsection (a)(6)). This section is necessary to address the concern discussed in the discussion on subsection (a)(11) where it is unclear who is responsible for making disclosures to a recipient in certain common commercial financing transaction situations.

Second, it clarifies the phrase “administered by” to exclude arrangements where a non-depository institution provides technology or support services for a depository institution’s commercial financing program, provided that the non-depository institution has no interest, or arrangement or agreement to purchase any interest in the commercial financing extended by the depository institution in connection with such program, and the commercial financing program is not branded with a trademark owned by the non-depository institution. This clarification is necessary to ensure that a company’s business relationship with a provider that is purely technical support or technology-related is not burdened by the disclosure requirements of the statute.

Section 2057(a)(20): Financial Code section 22800, subdivision (n) defines “recipient” as “a person who is presented a specific commercial financing offer by a provider that is equal to or less than five hundred thousand dollars (\$500,000).” Subdivision (a)(20) of section 2057 clarifies the phrase “person who is presented a specific commercial financing offer” to mean “the expected primary borrowers on a commercial loan, open-ended credit plan, or asset-based lending transaction, sellers in accounts receivable purchase transactions (including factoring), and lessees in lease financing transactions.” Because of the broadly different types of commercial financing transactions (and how those transactions differ in operation), this clarification is necessary to eliminate confusion as to who the recipient is in a particular transaction, and thus ensure the correct, intended individual is presented with the mandated disclosures.

Section 2057(a)(21): The purpose of this section is to create a distinct term for a concept that requires the evaluation of a completed financing agreement. This section is necessary because calculation of the retrospective annualized rate is essential to performing the self-audit process in subdivision (a)(5) of section 2092.

Section 2057(a)(22): Financial Code section 22800, subdivision (c) defines “asset-based lending transaction” to mean “a transaction in which advances are made from time to time contingent on a recipient forwarding payments received from one or more third parties for goods the recipient has supplied or services the recipient has rendered to that third party or parties.” A variety of commercial transactions fit under this definition, but subdivision (a)(22) of section 2057 defines “sales-based financing” to mean those transactions “that are repaid by the recipient to the financier as a percentage of the recipient’s sales or income, and in which the payment amount increases or decreases according to the volume of sales made or income received.” It also includes within the definition any transactions with a “true-up mechanism” (defined in section 2057(a)(28)).

Section 2057(a)(23): The purpose of this section is to create a distinct term for a sales-based financing term more particularly described in subsection (a)(28)(A) of section 2057. The term is used in section 3003 and is necessary to ensure the requirements of that rule are as clear as possible.

Section 2057(a)(24): The purpose of this section is to define a commonly-used term that describes a sales-based financing feature. It is necessary in order to ensure clarity in various sections requiring a disclosure of a sales-based financing offer payment terms.

Section 2057(a)(25): Financial Code section 22802, subdivision (b)(3) and section 22803, subdivision (a)(3) require one of the disclosures made to recipients by a provider be “term or estimated term” of the financing. Subdivision (a)(25) of section 2057, in recognition that each different type of commercial financing transaction has a different concept of “term”, defines “term” separately per type of commercial financing transaction. This section is necessary in order to ensure clarity with respect to the information being disclosed to a recipient depending on the type of commercial financing transaction offer they might be receiving.

Section 2057(a)(26): Certain types of sales-based financings are structured such that the recipient makes set payments that are subject to reconciliation at a later date or dates to ensure that the cumulative amount of payments reflects a certain percentage of sales or income. The reconciliation can result in a change to the payment amount going forward, or a lump sum payment to or from the recipient. This section defines that payment or change as a “true-up”. The purpose of this section is to ensure that all costs associated with a financing are accurately presented to the recipient. This section is necessary because true-ups can increase or decrease the total cost of financing, and defining “true-up” is necessary to require disclosure of reasonably-anticipated true-ups in other sections.

Section 2057(a)(27): For sales-based financing disclosures, a provider must disclose reasonably anticipated true-ups and calculate other disclosures based upon reasonably anticipated true-ups (§§ 2065(a)(5)(B)(iii), 3003(b)(5)). The purpose of this section is to ensure disclosures are based only on accurate estimates of future performance. The Department has learned through its experience in the commercial finance space that many small business are unaware of true-up features in their contracts and do not take advantage of them. As such, it is necessary to define what constitutes a reasonably anticipated true-up, such that disclosures are based only on true-ups that the provider believes are likely to occur.

Section 2057(a)(28): Certain types of sales-based financings are structured such that the recipient makes set payments that are subject to reconciliation at a later date or dates to ensure that the cumulative amount of payments reflects a certain percentage of sales or income. The reconciliation can result in a change to the payment amount going forward, or a lump sum payment to or from the recipient. This section defines this process as a “true-up mechanism.” The purpose of this section is to ensure that all costs associated with a financing are accurately presented to the recipient. This section is necessary because true-ups can increase or decrease the total cost of financing, and defining the true-up mechanism is necessary to require disclosure of reasonably anticipated true-ups in other sections.

Section 2057(a)(29)(A): In factoring transactions, the recipient of the financing is not the person with the primary obligation to pay the legally enforceable claim assigned to the financier by the recipient. The purpose of this section is to provide clarity by creating a distinct term for the person with the primary obligation to pay. This section is necessary because while some factoring providers refer to this person as the account debtor, this section will provide further certainty as to what the term means.

Section 2057(a)(29)(B): The purpose of this section is to provide clarity by creating a distinct term for the price a financier agrees pay for the assignment a legally enforceable claim. This section is necessary because while some factoring providers refer to this amount as the purchase price, this section will provide further certainty as to what the term means.

Section 2057(a)(29)(C): The purpose of this section is to provide clarity by creating a distinct term for the fee a financier charges when it acquires a legally enforceable claim. This section is necessary because while some factoring providers refer to this amount as the factoring fee, this section will provide further certainty as to what the term means.

Section 2057(a)(29)(D): The purpose of this section is to provide clarity by creating a distinct term for the amount the financier remits to the recipient upon

assignment of a legally enforceable claim. This section is necessary because there is no generally accepted term in the industry for this amount.

Section 2057(a)(29)(E): The purpose of this section is to provide clarity by creating a distinct term for the reserve a financier maintains to secure the financier in the event of non-payment of a legally enforceable claim, or to secure the financier in the event of nonpayment of other legally enforceable claims assigned or to be assigned by the recipient to the financier. This section is necessary because while some factoring providers refer to this amount as the reserve, this section will provide further certainty as to what the term means.

Section 2057(a)(29)(F): The purpose of this section is to provide clarity by creating a distinct term for the type of factoring transaction in which the financier maintains a reserve amount. This section is necessary because while some factoring providers refer to this amount as the reserve, there is no commonly used shorthand term to describe factoring transactions that require a reserve.

Section 2057(b): This section is to eliminate any possibility of confusion when the regulations refer to the commonly used term “average,” and its definition.

Section 2057(c): This section is necessary to avoid confusion by ensuring that any terms defined in Financial Code section 22800 *et seq.* that are also used in the proposed regulations have the same definitions.

Section 2060(a): This section contains general formatting and content requirements for the different types of disclosures that must be made depending on the type of commercial financing offer a recipient is being given. It is necessary to ensure that there is relative uniformity in design and formatting of the disclosures to maximize a recipient’s ability to compare and contrast offers from different providers (or from the same provider for different terms).

Section 2060(a)(1): This section requires that every disclosure made pursuant to Division 9.5 of the Financial Code begin with the words “OFFER SUMMARY.”

The Department chose the heading “OFFER SUMMARY” because Financial Code section 22802, subdivision (a), requires a provider to make disclosures at the time an “offer” is extended to the recipient. This section is necessary to ensure uniformity in design and formatting of all disclosures required by Division 9.5 of the Financial Code, so that recipients of commercial financing are better able to compare and contrast competing commercial financing offers.¹ Using the

¹ See Bill Analysis, 04/16/18- Senate Banking And Financial Institutions, https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201720180SB1235# “Author’s Statement: According to the author, “With the explosion of the online lending sector and the spread of innovative finance products, potential customers and borrowers find it difficult to compare and contrast the many offers available and determine which would be best, and least costly, for their business.”

same language, “OFFER SUMMARY” language at the top of every disclosure provides a signals to recipients that they can compare different disclosures from different providers, or different offers from the same provider, that are provided to the recipient.

Section 2060(a)(2): This section requires the bottom of the disclosure to include a statement informing the recipient that California law requires the disclosure to be made. Informing the recipient that the disclosure is legally required creates an indicia of trust. This requirement is necessary because recipients who understand the disclosures are legally required will be more prepared and more likely to compare disclosures from different providers.

This section also requires providers to include a signature line where the recipient can acknowledge receipt of the disclosure and enter the date when they sign the disclosure. Financial Code section 22802, subdivision (a), requires providers to obtain the recipient’s signature “before consummating the commercial financing transaction.” Requiring a signature line is necessary to implement Financial Code section 22802, subdivision (a)’s signature requirement. Requiring a field where the recipient may enter the date of signature is necessary to ensure that providers obtain the signature “before consummating the commercial financing transaction” (Fin. Code § 22802, subd. (a)) because it creates a record that demonstrates whether the provider obtained the disclosure before or after consummating the commercial financing transaction.

Section 2060(a)(3): This section requires a term or estimated term to be disclosed in units of years and months, with any remaining days listed as a portion of a month to the nearest two decimal points. Requiring the same formatting for the “term” disclosed by all providers is necessary because it helps recipients more easily compare different disclosures from different providers. Requiring fractions of months to be displayed to the nearest two decimal points is necessary to reduce visual clutter on the disclosure page (i.e., 1 year, 2.33 months take up less space than 1 year, 2 months, 10 days).

Section 2060(a)(4): This section allows providers to assume when making disclosures that there are 30 days in every month and 360 days in a year. The purpose of this section is to reduce provider costs and regulatory burdens associated with providing the disclosures. The simplifying assumption is necessary to achieve this purpose because it allows providers to make disclosure calculations without regard for the time of year when the disclosure is made.

Section 2060(a)(5): This section requires any annual percentage rate (APR) disclosure to be expressed to the nearest ten basis points (e.g. APR – 29.33%). The purpose of requiring the same formatting for the APR disclosed by all providers is to help recipients more easily compare different disclosures from

different providers. This requirement is necessary because variability in disclosure formatting will make it more difficult for recipients to compare disclosures.

The purpose of requiring APR disclosure to ten basis points is to help recipients better differentiate between different products with different costs. This requirement is necessary, particularly for longer term commercial financing transactions, because APR differences that are a fraction of 1% can reflect significant differences in the cost of financing.

Section 2060(a)(6): This section requires disclosures to be presented to the recipient in a document separate from other documents. The purpose of this requirement is to encourage recipients to notice and review the disclosures required by statute. This requirement is necessary because a recipient is less likely to review disclosures if they are included in a voluminous document.

This section also allows the disclosure to be mailed or transmitted in a package with other documents. The purpose of this permissive language is to reduce compliance costs. This permissive language is necessary because it allows a provider to avoid paying duplicative postage costs for documents that could be mailed together, and because transmitting the disclosures separately creates an additional administrative burdens for providers and recipients.

Section 2060(a)(7): This section allows flexible formatting for disclosures. The purpose of this section is to permit sufficient formatting flexibility for the disclosures so that providers can offer disclosures through a variety of display mediums, such as paper or mobile electronic devices. The section is necessary because alternatives, such as requiring set font sizing, may not reasonably result in clear and conspicuous disclosures on all display mediums (e.g. a cell phone).

This section prohibits using formatting to make any enumerated term required by Financial Code section 22802, subdivision (b) more clear or conspicuous than any other terms. The purpose of this section is to ensure that recipients receive disclosures that represent a neutral presentation of the relevant terms required by statute. This section is necessary because otherwise providers could hide unfavorable offer terms by highlighting or otherwise emphasizing other terms on the form.

Section 2060(a)(8): This section is intended to accommodate a recipient's possible preference to enter into a commercial financing transaction using electronic methods (e-mail, internet, etc.) when the disclosure is provided electronically. Since Financial Code section 22802, subdivision (a) requires providers to obtain the recipient's signature "before consummating the commercial financing transaction," it is necessary that a mechanism exist for the

signature to be obtainable electronically, should the recipient prefer that method of transmission.

This section is also intended to help recipients compare disclosures and ensure that providers give recipients accurate disclosures, by requiring, when disclosures are provided electronically, that providers provide the recipient with the ability to receive a copy of the disclosure. This requirement is necessary to help recipients compare disclosures because if a recipient cannot create a copy of the disclosure that the recipient can keep, the recipient will not be able to compare the disclosure with other disclosures at a later date. This requirement is necessary to ensure that providers give accurate disclosures, because a provider is more likely to provide an accurate disclosure if the provider knows that the recipient may also have a copy of the disclosure in the recipient's records.

Section 2060(a)(9): This section sets out guidelines for how providers (except those of sales-based financing) who need to make assumptions to make required disclosures can do so. The purpose of this section is to permit flexibility for unforeseen circumstances where a provider must use assumptions in order to provide the disclosures required by law. This section is necessary, because absent specific guidelines for incorporating assumptions, providers may be reluctant to incorporate necessary assumptions or disclose when disclosures are estimates based upon those assumptions.

This section does not apply to sales-based financing, because Sections 2091 and 2092 more specifically deal with assumptions relating to sales-based financing, based upon circumstances (e.g. uncertainty concerning a recipient's future income) that the Department has been able to anticipate and consider.

Section 2060(a)(9)(A): The purpose of this section is to ensure that information disclosed to recipients is reliable. This section is necessary because information is most likely to be reliable when it is based on "the best information reasonably available to the provider at the time of the disclosure."

Section 2060(a)(9)(B): The purpose of this section is to ensure that recipients understand the disclosures they are provided. This section is necessary because absent mandating that providers disclose that a given term is an "Estimate", a recipient would likely assume that the disclosed term is not an estimate.

Section 2060(a)(9)(C): The purpose of this section is to ensure that recipients understand the disclosures they are provided. This section is necessary because requiring that a provider state clearly any assumptions or estimates that are the basis for the disclosure helps the recipient understand why a disclosed term is an estimate.

Section 2060(a)(10): This section sets out guidelines for how providers who need to make assumptions about the applicable interest rate for a transaction should do so. The purpose of this section is to ensure that providers apply consistent assumptions about the applicable interest over the course of a transaction. This section is necessary to achieve this consistency because it directs all providers to use the initial interest rate for any period of time when interest cannot be calculated in advance.

Sections 2061-2068: Each of these sections describes disclosure tables consisting of certain number of rows and three columns. Generally, the first column contains the title of the disclosure element (e.g. Annual Percentage Rate), the second column contains the required disclosure (e.g. 39%), and the third column contains a space where an explanation of the required disclosure is permitted or required. The purpose of this structure is to allow recipients to easily compare offers from different providers and identify important information on the page. Tables are necessary to help recipients identify important information because they help providers present the required disclosures in an organized fashion. Using a similar table format for all disclosures is also necessary to help recipients compare offers from different providers, because consistent formatting will help recipients spot and compare the same relevant terms (e.g. Funding You Will Receive, Annual Percentage Rate, etc.) on multiple disclosure forms.

With certain exceptions and variations, the sections require disclosure of the following elements in the following order:

1. Funding You Will Receive
2. Annual Percentage Rate (APR)
3. Finance Charge
4. Payment
5. Term
6. Prepayment (Policies)

As discussed further below, these disclosures correspond to the required disclosures under Financial Code sections 22802(b) and 22803(b).

“Funding Your Will Receive” corresponds to 22802(b)(1) and 22803(a)(1) (“amount of funds provided” and “amount financed”, respectively).

“Annual Percentage Rate (APR)” corresponds to 22802(b)(6) and 22803(a)(6) (the “total cost of the financing expressed as an annualized rate”).

“Finance Charge” corresponds to 22802(b)(2) and 22803(a)(2) (the “total dollar cost of the financing” and “total dollar cost”, respectively).

“Payment” corresponds to 22802(b)(4) and 22803(a)(4) (“method, frequency and amount of payments”).

“Term” corresponds to 22802(b)(3) and 22803(a)(3) (“term or estimated term”)

“Prepayment” corresponds to 22802(b)(5) and 22803(a)(5) (“description of prepayment policies”).

Section 2061(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2061(a)(2): These sections describe what information must appear in the first row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount of funds provided.” (Financial Code section 22802(b)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although there are other methods of validly expressing the “amount of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2061(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total cost of financing expressed as an annualized rate.” (Financial Code section 22802(b)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers. Because of the variable components that may be included in the calculation of APR, the subparagraphs (a)-(d) are necessary to ensure the recipient understands the meaning of the specific disclosure being made to them. Without such clarifying statements, the risk of a recipient misunderstanding what the APR percentage represents would be significantly greater.

Section 2061(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost of the financing.” (Financial Code section 22802(b)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2061(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(b)(4).) Because of the general variability between

commercial financing products, and variability even between products of the same type, provisions were included here to ensure clear reporting of each possible situation concerning how variable payments might occur. These provisions are necessary to avoid confusion as to how different payment situations should be disclosed.

Section 2061(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2061(a)(7-9): These sections describe what information must appear in the sixth and seventh rows of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22802(b)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed finance charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2061(a)(10): These sections describe the situation where a periodic payment might be permitted that is not monthly and how to alter the table accordingly. These sections are necessary to effect the legislative intent requiring disclosure of the “amount of payments.” (Financial Code section 22803(b)(4)), and is related to section 2061(a)(6), discussed above. The Department determined that for products that do not require monthly payments, an additional disclosure of the average monthly cost is necessary so that small business owners can more easily compare disclosures from one offer to another.

Section 2061(a)(11): This section accounts for the possibility that a financier might offer a recipient multiple payment options. It is the Department’s understanding that this is a common industry practice. In order to accommodate that possibility while keeping the disclosure requirements in compliance with the legislative mandate, this section is necessary to ensure recipients understand that they are seeing disclosures that are based upon the minimum possible payment permitted under the contract, and not a potentially higher, alternative payment option.

Section 2062(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2062(a)(2): These sections describe what information must appear in the first row of the table. The first row of the table provides a space for the provider to state the basic underlying assumptions that a provider must make to present disclosures for open-end credit plans. Because some providers may offer multiple payment options, alternative explanatory language was needed to explain that calculations are based upon the minimum possible payment permitted under the contract. This section is necessary to ensure that recipients understand the key assumptions underlying every open-end credit plan disclosure.

Section 2062(a)(3): These sections describe what information must appear in the first row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount of funds provided.” (Financial Code section 22802(b)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although there are other methods of validly expressing the “amount of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2062(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total cost of financing expressed as an annualized rate.” (Financial Code section 22802(b)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers. Because of the variable components that may be included in the calculation of APR, the subparagraphs (a)-(d) are necessary to ensure the recipient understands the meaning of the specific disclosure being made to them. Without such clarifying statements, the risk of a recipient misunderstanding what the APR percentage represents would be significantly greater.

Section 2062(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost of the financing.” (Financial Code section 22802(b)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2062(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(b)(4).) Because of the general variability between commercial financing products, and variability even between products of the same type, provisions were included here to ensure clear reporting of each possible situation concerning how variable payments might occur. These provisions are necessary to avoid confusion as to how different payment situations should be disclosed.

Section 2062(a)(7): These sections describe what information must appear in the sixth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) For open-ended credit plans, the Department has interpreted this requirement to mean the length of time that it is anticipated will be necessary for the recipient to fulfill its obligations under the financing agreement with respect to a particular loan advance (section 2057(a)(25)(C)). This metric is required to be disclosed by section 2062(a)(8), discussed further below, however, the Department recognizes that with open-ended credit plans, there may also be a time period during which a recipient may make draws under the agreement. The purpose of this section is to help recipients better understand their commercial financing disclosures, by disclosing “draw period” separately from “term”. Without this disclosure, the recipient may misunderstand the disclosure required by Section 2062(a)(8) below.

Section 2062(a)(8): These sections describe what information must appear in the seventh row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2062(a)(9-11): These sections describe what information must appear in the eighth and ninth rows of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22802(b)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed financed charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2062(a)(12): These sections describe the situation where a periodic payment might be permitted that is not monthly and how to alter the table

accordingly. These sections are necessary to effect the legislative intent requiring disclosure of the “amount of payments”, (Financial Code section 22803(b)(4)), and are related to section 2061(a)(5), discussed above. The Department determined that for products that do not require monthly payments, an additional disclosure of the average monthly cost is necessary so that small business owners can more easily compare disclosures from one offer to another.

Section 2063(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2063(a)(2): These sections describe what information must appear in the first row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount of funds provided.” (Financial Code section 22802(b)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although there are other methods of validly expressing the “amount of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2063(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total cost of financing expressed as an annualized rate.” (Financial Code section 22802(b)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers.

Section 2063(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost of the financing.” (Financial Code section 22802(b)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2063(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.”

(Financial Code section 22803(b)(4).) Under true factoring transactions, the financier bears the risk of loss in the event that the account debtor fails to pay the legally enforceable claim when the claim becomes due and payable. In these circumstances, the recipient has no obligation to pay the financier. As such, this section directs the provider to disclose “NA” or “Not applicable” as the disclosed payment and include a description of why no payment amount is being disclosed. In this case, the Department determined that disclosing the payment amount could give the recipient the mistaken impression that they are obligated to remit payment to the financier on the date the legally enforceable claim becomes due and payable.

Section 2063(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2063(a)(7): These sections describe what information must appear in the sixth row of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22802(b)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed financed charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2064(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2064(a)(2): These sections describe what information must appear in the first row of the table. The first row of the table provides a space for the provider to state the basic underlying assumptions that a provider must make to present disclosures for general factoring agreements pursuant to Financial Code section 22803. Because some providers offer general factoring agreements with different finance charges, annual percentage rates, and terms for different types of legally enforceable claims, alternative explanatory language was needed to explain that calculations are based upon particular underlying assumptions relating to the type of legally enforceable claim assigned. This section is necessary to ensure that recipients under the key assumptions underlying every general factoring agreement disclosure.

Section 2064(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount financed.” (Financial Code section

22803(a)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although other methods of validly expressing the “amount of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2064(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of “the total cost of the financing expressed as an annualized rate.” (Financial Code section 22803(a)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers.

Section 2064(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost.” (Financial Code section 22803(a)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2064(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(a)(4).) Under true factoring transactions, the financier bears the risk of loss in the event that the account debtor fails to pay the legally enforceable claim when the claim becomes due and payable. In these circumstances, the recipient has no obligation to pay the financier. As such, this section directs the provider to disclose “NA” or “Not applicable” as the disclosed payment and include a description of why no payment amount is being disclosed. In this case, the Department determined that disclosing the payment amount could give the recipient the mistaken impression that they are obligated to remit payment to the financier on the date the legally enforceable claim becomes due and payable.

Section 2064(a)(7): These sections describe what information must appear in the sixth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term or estimated term.” (Financial Code

section 22803(a)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2064(a)(8): These sections describe what information must appear in the seventh row of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22803(a)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed finance charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2065(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2065(a)(2): These sections describe what information must appear in the first row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount of funds provided.” (Financial Code section 22802(b)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although there are other methods of validly expressing the “amount of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2065(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total cost of financing expressed as an annualized rate.” (Financial Code section 22802(b)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers.

Section 2065(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost of the financing.” (Financial Code section 22802(b)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with

the financing and would diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Many types of sales-based financing have a fixed finance charge that does not increase if the recipient takes longer than anticipated to pay off the financing. Subparagraph (C) allows providers to include this information in the explanation section of the finance charge. This section is necessary to prevent recipients from mistakenly assuming that additional charges will accrue (as is common for financial products that accrue interest charges) if their monthly income (and thus their payments) turns out to be lower than anticipated.

Section 2065(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(b)(4).) No reasonable alternatives could be identified for the presentation of payment amounts other than listing payment amounts as these sections require.

Section 2065(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(b)(4).) These sections provide additional space to provide explanation of certain features common to sales based financing products such as daily payments that only occur on certain days of the week, payments that vary in proportion to daily receipts, and set payments with a true-up mechanism. The Department determined that without these disclosures, recipients will be unlikely to understand key aspects of their contract relating to the method, frequency, and amount of their payments.

Section 2065(a)(7): These sections describe what information must appear in the sixth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2065(a)(8-10): These sections describe what information must appear in the sixth and seventh rows of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22802(b)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed finance charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2065(a)(11): These sections describe the situation where a periodic payment might be required that is not monthly and how to alter the table accordingly. These sections are necessary to effect the legislative intent requiring disclosure of the “amount of payments.” (Financial Code section 22803(b)(4)), and is related to section 2061(a)(5), discussed above. The Department determined that for products that do not require monthly payments, an additional disclosure of the average monthly cost is necessary so that small business owners can more easily compare disclosures from one offer to another.

Section 2066(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2066(a)(2): These sections describe what information must appear in the first row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount of funds provided.” (Financial Code section 22802(b)(1).) Unlike other forms of financing, lease financing would not typically involve funds being released directly to the recipient. As such, the “funding provided” that is disclosed in the first row is intended to reflect either the net cost to the financier to acquire the property to be leased or, if the financier selects, manufactures, or supplies the goods to be leased, the price that the financier would sell the goods for in a cash transaction, less any down payment or deposit to be paid by the recipient. The Department determined that these required metrics were the best approximation of the funding provided in a lease financing transaction.

Section 2066(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total cost of financing expressed as an annualized rate.” (Financial Code section 22802(b)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers.

Section 2066(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost of the financing.” (Financial Code section 22802(b)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and would diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2066(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22802(b)(4).) Because of the general variability between commercial financing products, and variability even between products of the same type, provisions were included here to ensure clear reporting of each possible situation concerning how variable payments might occur. These

provisions were necessary to avoid confusion as to how different payment situations should be disclosed.

Section 2066(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2066(a)(7-9): These sections describe what information must appear in the sixth and seventh rows of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22802(b)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed financed charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2066(a)(10): These sections describe the situation where a periodic payment might be permitted that is not monthly and how to alter the table accordingly. These sections are necessary to effect the legislative intent requiring disclosure of the “amount of payments.” (Financial Code section 22802(b)(4)), and is related to section 2061(a)(5), discussed above. The Department determined that for products that do not require monthly payments, an additional disclosure of the average monthly cost is necessary so that small business owners can more easily compare disclosures from one offer to another.

Section 2067(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2067(a)(2): These sections describe what information must appear in the first row of the table. The first row of the table provides a space for the provider to state the basic underlying assumptions that a provider must make to present disclosures for asset-based lending transactions. This section is necessary to ensure that recipients understand the key assumptions underlying every open-end credit plan disclosure.

Section 2067(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount financed.” (Financial Code section 22803(a)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although there are other methods of validly expressing the “amount

of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2067(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of “the total cost of the financing expressed as an annualized rate.” (Financial Code section 22803(a)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to ensure a clear and concise disclosure of APR for the recipient’s ability to quickly compare comparable rates and offers.

Section 2067(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost.” (Financial Code section 22803(a)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financer in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2067(a)(6): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(a)(4).) No reasonable alternatives could be identified for the presentation of payment amounts other than listing payment amounts as these sections require.

Section 2067(a)(7): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22803(a)(3).) For sales-based financing, the Department has interpreted this requirement to mean the length of time that it is anticipated will be necessary for the recipient to fulfill its obligations under the financing agreement with respect to a particular loan advance (section 2057(a)(25)(C)). This metric is required to be disclosed by section 2067(a)(8), discussed further below, however, the Department recognizes that with sales-based financing, there may also be a time period during which a recipient may make draws under the agreement. The purpose of this section is to help recipients better understand their commercial financing disclosures, by disclosing “draw period” separately from “term”. Without this disclosure, the recipient may misunderstand the disclosure required by Section 2067(a)(8) below.

Section 2067(a)(8): These sections describe what information must appear in the sixth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22803(a)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2067(a)(9-11): These sections describe what information must appear in the seventh and eighth rows of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22803(a)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed financed charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2067(a)(12): These sections describe the situation where a periodic payment might be required that is not monthly and how to alter the table accordingly. These sections are necessary to effect the legislative intent requiring disclosure of the “amount of payments.” (Financial Code section 22803(a)(4)), and is related to section 2067(a)(6), discussed above. The Department determined that for products that do not require monthly payments, an additional disclosure of the average monthly cost is necessary so that small business owners can more easily compare disclosures from one offer to another.

Section 2068(a)(1): See general explanation applicable to sections 2061-2068 above. This section is necessary to implement and ensure uniformity in the intended disclosure structure.

Section 2068(a)(2): These sections describe what information must appear in the first row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “amount of funds provided.” (Financial Code section 22802(b)(1).) It excludes deductions to the financing received in order to most accurately represent the sum being provided to the recipient, since including such information would be misleading and inaccurate in making this particular disclosure. Although there are other methods of validly expressing the “amount of funds provided”, the alternatives the Department considered would result in an increased risk of consumer confusion and a diminished ability for the recipient to effectively compare disclosures for one offer to another.

Section 2068(a)(3): These sections describe what information must appear in the second row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total cost of financing expressed as an annualized rate.” (Financial Code section 22802(b)(6).) In accordance with the requirements of section 3001 of the regulations, these sections were written to

ensure a clear and concise disclosure of APR for the recipient's ability to quickly compare comparable rates and offers.

Section 2068(a)(4): These sections describe what information must appear in the third row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “total dollar cost of the financing.” (Financial Code section 22802(b)(2).) As defined in section 2057(a)(10) of these regulations, this disclosure uses the term “Finance Charge” to summarize the calculation that must be conducted by the financier in accordance with section 3010 of these regulations. Although other methods of validly expressing the “total dollar cost of financing” exist, the alternatives the Department considered would less clearly communicate to the recipient the costs and charges associated with the financing and diminish the ability of the recipient to effectively compare disclosures from one offer to another.

Section 2068(a)(5): These sections describe what information must appear in the fourth row of the table. The sections are necessary to effect the legislative intent requiring disclosure of the “method, frequency and amount of payments.” (Financial Code section 22803(b)(4).) Because of the general variability between commercial financing products, and variability even between products of the same type, provisions were included here to ensure clear reporting of each possible situation concerning how variable payments might occur. These provisions were necessary to avoid confusion as to how different payment situations should be disclosed.

Section 2068(a)(6): These sections describe what information must appear in the fifth row of the table. The sections are necessary to effect the legislative intent of requiring disclosure of the “term.” (Financial Code section 22802(b)(3).) “Term” is more particularly defined in section 2057(a)(25) of the regulations, and necessarily differs depending on the type of transaction for which it is disclosed.

Section 2068(a)(7-9): These sections describe what information must appear in the sixth and seventh rows of the table. The sections are necessary to effect the legislative intent of requiring a “description of prepayment policies” as a part of the disclosure. (Financial Code section 22802(b)(5).) Although other methods of expressing this disclosure exist, the Department was not able to identify alternative methods that would clearly communicate to recipients when fixed financed charges limit the benefits of prepayment and when prepayment would result in additional charges not included in the finance charge.

Section 2068(a)(10): These sections describe the situation where a periodic payment might be permitted that is not monthly and how to alter the table accordingly. These sections are necessary to effect the legislative intent requiring disclosure of the “amount of payments.” (Financial Code section 22803(b)(4)), and is related to section 2061(a)(6), discussed above. The Department

determined that for products that do not require monthly payments, an additional disclosure of the average monthly cost is necessary so that small business owners can more easily compare disclosures from one offer to another.

Section 2068(a)(11): This section accounts for the possibility that a financier might offer a recipient multiple payment options. It is the Department's understanding that this is a common industry practice. In order to accommodate that possibility while keeping the disclosure requirements in compliance with the legislative mandate, this section is necessary to ensure recipients understand that they are seeing disclosures that are based upon the minimum possible payment permitted under the contract, and not a potentially higher, alternative payment option.

Section 2070: Financial Code sections 22802 and 22803 require a provider to obtain a copy of the signed disclosures required by those sections before consummating the commercial financing transaction for which the disclosures were provided. Subdivision (a) of section 2070 makes clear that, in addition to the provider obtaining the recipient's signature, the financier must secure a copy of the signed disclosures prior to consummating a commercial financing transaction. It further clarifies that, in the case of a non-natural person entity being the recipient, a non-natural person may "sign" for receipt of the disclosures via its authorized natural person so long as that individual is not a broker. This section also allows for the transmission of associated documents and disclosures electronically regardless of how documents may be provided in the future. This section is necessary to account for situations where a non-natural person entity is the recipient as well as situations where the provider (the person extending the offer of commercial financing) is not necessarily the same entity that is providing the actual financing for the transaction (see 2057(a)(11)). Since it is the provider's duty (regardless of who the financier is) to obtain the recipient's signature prior to consummating the transaction, it ensures that a financier won't consummate the transaction before the provider has complied with its duty to obtain the recipient's signature. The section is further necessary to permit the electronic transmission of documents in that situation without regard to how future, supplemental documents might be transferred.

Subdivision (b) of section 2070 clarifies the signature requirement, discussed above, may be obtained electronically or by facsimile by the provider. This section is necessary since the disclosure formatting requirements contemplate electronic transmission and a regulation was necessary to expressly authorize that possibility.

Section 2071(a): This section is necessary to clarify how the \$500,000 threshold should be calculated and determined for the different types of transactions (and how those transactions are operated) contained within the definition of "commercial financing".

Section 2071(a)(1): This section clarifies that, for an open-ended credit transaction, the \$500,000 threshold should be determined using the approved credit limit (as defined in section 2057, subdivision (2) of the regulations). This is necessary to avoid confusion on which transactions are subject to the disclosure requirements.

Section 2071(a)(2): This section clarifies that, for asset-based lending transactions meeting certain conditions, the \$500,000 threshold should be determined using the approved credit limit (as defined in section 2057, subdivision (2) of the regulations).

Subparagraphs (a)(2)(A)(i)-(iii) set forth the requirements to use the “approved credit limit” as the evaluation of whether a particular asset-based lending transaction exceeds the \$500,000 threshold (in which case disclosures would not be required). If an asset-based lending transaction meets fewer than all three requirements, then disclosures are required for that transaction. If an asset-based lending transaction meets all three requirements, then the approved credit limit should be calculated and, if the approved credit limit exceeds \$500,000, no disclosures are required for that transaction. This section is necessary to both (1) take into account unique aspects of asset-based lending transactions, and (2) clarify when providers must provide disclosures for those transactions.

Section 2071(a)(3): This section clarifies that, for factoring transactions meeting certain conditions, the \$500,000 threshold should be determined using the approved advance limit (as defined in section 2057, subdivision (1) of the regulations).

Subparagraphs (a)(3)(A)(i)-(iii) set forth the requirements to use the “approved advance limit” as the evaluation of whether a particular factoring transaction exceeds the \$500,000 threshold (in which case disclosures would not be required). If a factoring transaction meets fewer than all three requirements, then disclosures are required for that transaction. If a factoring transaction meets all three requirements, then the approved advance limit should be calculated and, if the approved advance limit exceeds \$500,000, no disclosures are required for that transaction. This section is necessary to both (1) take into account unique aspects of certain factoring transactions, and (2) clarify when providers must provide disclosures for those transactions.

Section 2071(a)(4): This section clarifies that, for lease financing transactions, the \$500,000 threshold should be determined using the net cost to acquire the property to be leased if the financier does not select, manufacture, or supply the goods to be lease, or the price the financier would sell the goods in a cash

transaction, less any down payment or deposit paid by the recipient, if the financier selects, manufactures, or supplies to good to be lease.

This section is necessary to both (1) take into account unique aspects of lease financing transactions, and (2) clarify when providers must provide disclosures for these transactions.

Section 2071(a)(5): This section clarifies that, for all transactions other than open-end credit plans, asset-based lending transactions, and factoring transactions, the \$500,000 threshold should be determined by calculating all funds provided by the provider directly to the recipient or on behalf of the recipient in connection with the commercial financing. This is necessary to avoid confusion on which transactions are subject to the disclosure requirements.

Section 2089(a): Financial Code section 22802, subdivision (b)(4) and section 22803, subdivision (a)(4) require one of the disclosures made to recipients by a provider be “amount of payments.” In conjunction with the requirement set forth in section 2061(a)(11) of the regulations, this section is necessary to address the situation where a provider offers a recipient multiple payment options for a particular commercial financing transaction. In that situation, the disclosures should be based upon the minimum possible payment permitted under the contract. The Department determined that this is necessary to avoid potentially confusing or misleading disclosures, and to ensure the best information is being provided to the recipient for purposes of making comparisons between offers and disclosures.

Section 2089(b): Following similar requirements applicable to closed-end credit consumer financing (see 12 C.F.R. § 1026.17(c)(5)), this section requires that providers assume a term of one year if a transaction provides for a balance that is payable on demand. Without this requirement, an advance that is payable on demand may have no defined term that providers can use to provide required disclosures. This section is necessary to provide guidance to providers and promote consistency among disclosures where the amount due is payable on demand.

Section 2091(a): Sales-based financing transactions, which are a subset of asset-based lending transactions (defined in section 2057(a)(22)), require the provider to make certain calculations that are unique to sales-based financing before the provider can provide the disclosures mandated by Financial Code section 22802. This section establishes the parameters in performing those calculations and is necessary to ensure uniformity and consistency in making such calculations.

Section 2091(b): This section provides instruction on how a provider should calculate a recipient’s “estimated monthly sales, income, or receipts projection” in

order to make the required disclosures. This section is necessary in order to ensure there is no confusion on the provider's part on how to calculate the necessary information to make the proper disclosures to the recipient.

This section also contains the details on calculating the "estimated monthly sales, income or receipts projection" described in subsection (b) of section 2091, above. Subparagraph (1) requires the calculation to be made based on the recipient's historical average sales volume or income, with respect to the particular payment channel or mechanism (see that defined term in section 2057(a)(17)). This section is necessary to explain the basis for the calculation to be made. Subparagraph (2) establishes the parameters for evaluating the historical average sales volume or income, limiting both the minimum and maximum possible number of months to be used in the calculation. This section is necessary to prevent providers from making the calculation in a manner that would be unfairly short (or long), leading potentially to misleading disclosures or unreasonable payment terms. Subparagraph (3), in the same vein as subparagraph (2), is necessary because it ensures the provider will be consistent in its calculation to avoid any chance of a disclosure being misleading. Subparagraph (4) addresses the situation where a recipient may not have historical volume or income going back far enough to properly make the calculations. This section is necessary to avoid a situation where a provider cannot meaningfully make a disclosure to a recipient that is too new.

Section 2091(c): This section addresses the possibility of a provider needing to make additional estimates or assumptions in a sales-based financing transaction other than monthly sales, income, or receipt projections. Since such situations could arise under a variety of circumstances, this section is necessary to provide guidance to the provider on how to deal with such a situation and further ensure that any disclosures provided to the recipient based on such circumstances are clearly set forth as estimates based on the best information reasonably available to the provider at the time.

Section 2092(a): Sales-based financing transactions, which are a subset of asset-based lending transactions (defined in section 2057(a)(22)), require the provider to make certain calculations that are unique to sales-based financing before the provider can provide the disclosures mandated by Financial Code section 22802. This section establishes the parameters in performing those calculations, as an alternative to the calculations described in section 2091, and is necessary to ensure uniformity and consistency in making such calculations.

Section 2092(a)(1): This section identifies section 2092 as an alternative to the method used in section 2091. The Department determined it was necessary in order to accommodate issues raised by stakeholders concerned that the method in section 2091 could, in some cases, be less accurate than the method permitted here.

Section 2092(a)(2): This section provides instruction on how a provider should calculate a recipient's "internal estimated monthly sales, income, or receipts projection" in order to make the required disclosures. This section is necessary in order to ensure there is no confusion on the provider's part on how to calculate the necessary information to make the proper disclosures to the recipient.

Section 2092(a)(3): This section contains the details on calculating the "internal estimated monthly sales, income, or receipts projection" described in subsection (a)(2) of section 2092, above. This alternative calculation is intended to permit a provider to use the best information available to it at the time of the projection, rather than relying only upon historical information as set forth in section 2091. The Department determined this option was necessary in order to accommodate a variety of issues raised by stakeholders, including that a purely historical calculation could lead to less accurate projections that would ultimately be detrimental to the recipient.

Section 2092(a)(4): This section is intended to function as a check on providers choosing to use the "internal estimated monthly sales, income, or receipts projection". Because of the potential for "gaming" the numbers in order to make a particular disclosure deceptively appealing to a recipient, this provision is necessary to ensure that providers use only the best information available at the time of projection. In order to accomplish that, this section requires providers choosing to use this method to perform a self-audit of certain data points every 4 months. Subdivision (A) identifies the information that the audit should cover. It is necessary to ensure the overall scope of the audit is not too large but sufficiently covers relevant financings. Subdivision (B) identifies what information that was part of each financing included in the audit must be reviewed and calculated as part of the audit. It is necessary to further narrow the scope of the audit so it is not overbroad. Subdivisions (C) and (D) require a basic calculation to establish data points that are used elsewhere. They are necessary to ensure a meaningful result is generated by the audit process.

Section 2092(a)(5): This section specifies what providers choosing to use the "internal estimated monthly sales, income, or receipts projection" should do with the data points generated in the self-audit. It requires the provider to calculate the weighted average of numbers generated in the previous section for the last three audits and last five audits, with an exception made if a provider has not yet conducted sufficient audits to calculate that weighted average. Subdivision (A) establishes the maximum weighted average across three audits that a provider may not exceed, or be unable to use the "internal estimated monthly sales, income or receipts project" for a period of 24 months (and shall instead employ the method described in section 2091) in making its disclosures. The Department determined this section was necessary in order to ensure that a provider's use of the "internal estimated monthly sales, income or receipts projection" is fair and

less likely to be “gamed” in a way that would be detrimental to a recipient. Subdivision (B) establishes the maximum weighted average across five audits that a provider may not exceed or be unable to use the “internal estimated monthly sales, income or receipts projection” for a period of 24 months. Again, the Department determined this was necessary to ensure that a provider’s use of the “internal estimated monthly sales, income or receipts projection” is fair and less likely to be “gamed” in a way that would be detrimental to a recipient.

Section 2092(a)(6): This section establishes the criteria for a provider, who has been restricted from using the “internal estimated monthly sales, income or receipts projection”, may start using it again after the 24 month period described in subdivision (a)(5) of section 2092, above. This section was necessary to avoid confusion as to when or how a provider may perform the “internal estimated monthly sales, income or receipts projection” again.

Section 2092(a)(7): This section addresses the possibility of a provider needing to make additional estimates or assumptions in a sales-based financing transaction other than a monthly sales, income or receipts projection. Since such situations could arise under a variety of circumstances, this section is necessary to provide guidance to the provider on how to deal with such a situation and further ensure that any disclosures provided to the recipient based on such circumstances are clearly set forth as estimates based on the best information reasonably available to the provider at the time.

Section 3000(a): Financial Code sections 22802 and 22803 require one the disclosures made to a recipient of a commercial financing offer be the total cost of financing expressed as an annualized rate. Section 3000 establishes that the annualized rate shall be the annual percentage rate (APR). The APR, including how to calculate it, is further discussed in section 3001 of the regulations. This section is necessary in order to comply with the legislative mandate contained in Financial Code section 22804(b) that the Department establish regulations concerning the annualized rate disclosure, including a determination of the appropriate method to express the annualized rate.

Section 3001: This section establishes the method for calculating APR. It is necessary to comply with the legislative mandate contained in Financial Code section 22804(b) to establish regulations concerning the calculation of the annualized rate as well as the fees and charges to be included in that calculation.

Section 3001(a): This section briefly explains what information comprises APR. It also specifies how the rate shall be calculated. Because the calculation of APR is fairly complex to express on paper, and because it has already been expressed in the cited federal regulation, this section incorporates the relevant federal regulation to the extent necessary to explain how APR should be

calculated. This section is necessary for several reasons: (1) to simplify the regulations rather than reprinting numerous pages of mathematical formulae to show how APR is calculated, (2) to ensure that providers calculate APR in the same manner that they would for a financing covered by the applicable federal rule, and (3) avoids confusion by implementing a known and widely used calculation of the cost of financing rather than introducing a brand new metric that could not be used to comparison shop outside of California or among other types of financing. By making sure APR calculations are performed in the same manner as the federal rule (and including substantially the same types of charges/fees, though the federal rule permits certain costs, fees, etc. to be excluded – see subdivision (e), below), this section maximizes the likelihood recipients will understand the rate disclosure provided to them and ensures the ability to comparison shop, even between types of financings or outside of California.

Section 3001(b): Multiple commenters requested calculation tolerances for disclosed APRs similar to those required for open-end credit under the Truth in Lending Act (TILA) The Department decided to adopt the same tolerances permitted under TILA (12 C.F.R. § 1026.14, subd. (a)). This section is necessary to ensure that minor APR discrepancies that would not ordinarily impact a recipient’s decision to pursue financing do not result in liability for providers.

Section 3001(c): This section makes clear that all finance charges (as defined in section 3010) must be included in the APR calculation set forth in subdivision (a) of section 3001. To avoid confusion and ensure compliance with the legislative mandate to disclose the cost of financing expressed as an annualized rate, this section is necessary because it highlights a difference from the federal rule for open-end credit in that no charges or fees may be excluded from the annual percentage rate calculation for any type of commercial financing. While the APR calculation method remains the same as the federal rule, this rule requires all finance charges be incorporated into the calculation regardless of the type of commercial financing provided.

Section 3001(d): This section provides simplifying assumptions that providers can use when calculating the annual percentage rate. Where possible, the Department endeavored to minimize the potential economic impact of the regulations. The Department determined that this section is necessary to reduce costs and liabilities for providers by allowing providers to ignore days when they might not be able to collect a payment.

Section 3001(e): This section addresses calculating APR under open-ended credit plans. The nature of open-ended credit financing means that APR is difficult to calculate without knowing how the recipient intends to borrow under

the agreement. This section is necessary to give providers guidance on what assumptions to make when disclosing APR for open-ended financing offers. This helps to avoid each provider assuming different information in making its disclosures which could lead to widely different APRs.

Section 3002(a): This section addresses how a provider, seeking to comply with Financial Code section 22802 in making a disclosure of APR for an offer of factoring, should treat the payment of a legally enforceable claim in calculation of APR for the particular transaction. This section is necessary to make clear how to calculate APR since factoring transactions are unique compared to other types of commercial financing addressed by these regulations in that the APR is dependent on when a legally enforceable claim is actually paid to the provider.

Section 3002(b): This section addresses how a provider, seeking to comply with Financial Code section 22803 in making a disclosure of the annualized rate for an offer of factoring using an example transaction, should treat the payment of an example legally enforceable claim in calculation of APR for the example transaction. This section is necessary to make clear how to calculate APR since factoring transactions are unique compared to other types of commercial financing addressed by these regulations in that APR is dependent on when a legally enforceable claim is actually paid to the provider.

Section 3003(a): This section addresses how a sales-based financing provider shall calculate estimated payments (see subdivision (a)(5)(B)(i) of section 2065) and reasonably anticipated true-ups (see subdivision (a)(5)(B)(iii) of section 2065). It requires a provider to use its chosen projection (from either subdivision (a)(2) of section 2091 or subdivision (a)(3) of section 2092) and account for specified variables. This section is necessary to provide guidance for providers of sales-based financing transactions in calculating certain provisions necessary to make an accurate disclosure to the recipient.

Section 3003(b): This section addresses how a sales-based financing provider shall calculate estimated monthly cost (see subdivision (a)(10)(B) of section 2065), the finance charge (see subdivision (a)(4)(B) of section 2065), term (see subdivision (a)(7)(B) of section 2065) and APR (see subdivision (a)(3)(B) of section 2065). It requires a provider to use its chosen projection (from either subdivision (a)(2) of section 2091 or subdivision (a)(3) of section 2092) and account for specified variables, including any reasonably anticipated true-ups calculated in accordance with subdivision (a) of section 3003. This section is necessary to provide guidance for providers of sales-based financing transactions in calculating certain provisions necessary to make an accurate disclosure to the recipient.

Section 3010(a): This section defines what charges are considered part of the finance charge that must be disclosed to recipients and incorporated into the annualized rate calculation. The purpose of this section is to make effective Financial Code sections 22802, subdivision (b)(2) and 22802, subdivision (a)(2) (“total dollar cost of the financing” and “total dollar cost,” respectively). The Department determined that a specific definition of finance charge was necessary to ensure that provider’s disclosures uniformly incorporate the costs of financing.

Section 3010(a)(1): This section incorporates by reference items that are finance charges under the Truth in Lending Act under 12 Code of Federal Regulations part 1026.4. This section also clarifies that charges that would be finance charges under that section are finance charges for the purposes of these regulations even though the commercial financing transaction is not a consumer credit transaction and the financier may not be considered a creditor under federal law. The purpose of this section is to make effective Financial Code sections 22802, subdivision (b)(2) and 22802, subdivision (a)(2) (“total dollar cost of the financing” and “total dollar cost,” respectively). This section is necessary to ensure uniformity and completeness with respect to the items that are included in the disclosed finance charge and used to calculate other disclosure items.

Section 3010(a)(2): This section clarifies that in any accounts receivable purchase transaction other than a factoring transaction, the finance charge includes any discount taken on the face value of the accounts receivable purchased. The purpose of this section is to make effective Financial Code sections 22802, subdivision (b)(2) and 22802, subdivision (a)(2) (“total dollar cost of the financing” and “total dollar cost,” respectively). For a merchant cash advance (one example of an accounts receivable purchase transaction), the financier purports to purchase a set amount of a recipient’s future receivables for less than the value of the receivables. For example, the financier may pay a “purchase price” of \$3,000 to the recipient for \$4,000 in future receivables. The difference between the purchase price and the value of future receivables is sometimes described as a discount. Although 12 Code of Federal Regulations parts 1026.4(b)(1) and (9), which are incorporated by reference, include “any amount payable under [a]... discount system” and “discounts,” in the definition of finance charge, the Department determined that this section was necessary to remove any ambiguity, and to ensure uniformity and completeness with respect to the items that are included in the disclosed finance charge and used to calculate other disclosure items.

Section 3010(a)(3): This section clarifies that in a factoring transaction, the difference between face value of the invoice and the amount paid to the recipient for the invoice is part of the finance charge. The section also clarifies the circumstances in which a reserve amount may be excluded from the finance charge. The purpose of this section is to make effective Financial Code sections

22802, subdivision (b)(2) and 22802, subdivision (a)(2) (“total dollar cost of the financing” and “total dollar cost,” respectively). For a factoring transaction, a financier might pay a recipient \$800 for an invoice with a face value of \$1,000. The agreement might state that the purchase price for the invoice is \$950, but only \$800 is paid to the recipient up front while \$150 is held in reserve to secure the financier in the event that the invoice is not paid. Even after the invoice is paid in full, a financier might hold the reserve amount to secure itself against non-payment on other invoices that the recipient has assigned or may assign to the financier. This section is necessary to ensure that reserve amounts are excluded from the finance charge only in cases where financiers treat the reserve as the recipient’s property used to secure unpaid invoices and return the reserve amounts to the recipient at the appropriate times. This section is also necessary to ensure uniformity and completeness with respect to the items that are included in the disclosed finance charge and used to calculate other disclosure items.

Section 3010(a)(4): This section explains that for lease financing transactions, the finance charge includes the sum of the lease payments and the purchase price, less the amount disclosed to the recipient as the “Funding Provided” pursuant to Section 2066(b)(2). The purpose of this section is to make effective Financial Code sections 22802, subdivision (b)(2) and 22802, subdivision (a)(2) (“total dollar cost of the financing” and “total dollar cost,” respectively). This section is necessary to ensure uniformity and completeness with respect to the items that are included in the disclosed finance charge and used to calculate other disclosure items for lease financing transactions.

Section 3010(b): This section clarifies that for interest-based finance charges where the interest charge adjusts over time and it is not possible to calculate the charge in advance, the provider should calculate the interest charges for the life of the loan based upon the rate in effect at the time of disclosure, taking into account any contractual requirements that would cause the rate to deviate from that rate. The purpose of this section is to make effective Financial Code sections 22802, subdivision (b)(2) and 22802, subdivision (a)(2) (“total dollar cost of the financing” and “total dollar cost,” respectively). This section is necessary to ensure uniformity and completeness with respect to the items that are included in the disclosed finance charge and used to calculate other disclosure items for lease financing transactions.

Section 3021(a)(1): This section helps to clarify how the example transaction permitted under Financial Code section 22803 (as an alternative to making disclosures pursuant to Financial Code section 22802) should be made with respect to eligible asset-based lending transactions.

Section 3021(a)(2): This section addresses the situation where the agreement between a financier and recipient specifies a maximum draw amount and how to make the disclosures in an example transaction given that information. It is

necessary to ensure that disclosures are made with the same requirements across providers (without this provision, a provider could potentially make an example transaction using figures that are unrealistic or unrelated to the recipient's actual financing needs, raising the potential for misleading disclosures). The Department determined that, based on feedback from stakeholders, when a maximum draw amount is specified in the agreement, half of the maximum draw amount is a reasonable number to use in providing a recipient with realistic disclosures based on an example transaction.

Section 3021(a)(3): This section addresses the situation where the agreement between a financier and recipient does not specify a maximum draw amount and how to make the disclosures in an example transaction without that information. As with subsection (a) of section 3021, this is necessary to ensure that the same requirements apply to all transactions of the same type. The Department determined that, based on feedback from stakeholders, when the agreement does not specify a maximum draw amount, \$10,000 is a reasonable number to use in providing a recipient with realistic disclosures based on an example transaction.

Section 3022(a): This section clarifies that providers of factoring commercial financing transactions who are providing disclosures to a recipient based upon an example transaction under Financial Code section 22803 must give a recipient a separate disclosure (pursuant to section 2064) for each type of legally enforceable claim if the finance charge, APR or term varies based on the type of legally enforceable claim. This is necessary to ensure that the varying terms, depending on the type of legally enforceable claim, are accurately disclosed to the recipient.

Section 3022(b): This section clarifies how to make disclosures based on an example transaction where a factoring agreement between a financier and recipient permits an advance of funds up to and including a maximum aggregate price for legally enforceable claims that have not yet been paid by the account debtor. It is necessary to ensure that disclosures are made with the same requirements across providers (without this provision, a provider could potentially make an example transaction using figures that are unrealistic or unrelated to the recipient's actual financing needs, raising the potential for misleading disclosures). The Department determined that, based on feedback from stakeholders, where such an agreement exists, half of the maximum aggregate purchase price is a reasonable number to use in disclosures based on an example transaction.

Section 3022(c): This section clarifies how to make disclosures based on an example transaction where the factoring agreement between a financier and recipient does not specify a maximum aggregate price for legally enforceable

claims that have not yet been paid by the account debtor. As with subsection (a) of section 3022, this is necessary to ensure that the same requirements apply to all transactions of the same type. The Department determined that, based on feedback from stakeholders, where such an agreement exists, \$10,000 is a reasonable number to use in disclosures based on an example transaction.

Section 3023(a): This section describes the duties that financiers and brokers have in the context of the disclosure requirements imposed by Financial Code section 22802, subdivision (a). This section aids the statutory objective that recipients receive timely and accurate disclosures. This section is necessary to clarify what disclosure obligations apply to financiers and brokers and to ensure consistency within the market as to who drafts and delivers disclosures.

Section 3023(a)(1): This section requires a financier to provide a copy of compliance disclosures to a broker whenever the financier provides a financing amount, rate, or price quote to the broker. This section aids the statutory objective that recipients receive timely and accurate disclosures. The Department recognizes that in many situations, a financier will be in a better position to provide reliable disclosure than the broker who directly communicates a specific commercial financing offer to a recipient. As such, the Department determined that it would be appropriate to require the financier to provide brokers with compliant disclosures at the time that they communicate a financing amount, rate or price quote to the broker (which the Department has determined meets the definition of a “specific commercial financing offer”, see Section 2057(a)(4). This section is necessary to clarify what disclosure obligations apply to financiers and brokers and to ensure consistency within the market as to who drafts and delivers disclosures.

Section 3023(a)(2): This section requires financiers to maintain copies of disclosures for a period of four years following the date that the disclosure is presented to the recipient or provided to a broker. This section aids the statutory objective that recipients receive timely and accurate disclosures. The Department notes that the statute of limitations for a contract claim in California is four years. (Cal. Code Civ. Proc. § 337.) Because the Department does not have jurisdiction over some of the products that require disclosures (e.g. true factoring transactions), the Department believes that in some cases, only private litigants will be able to enforce the required disclosure requirements. Requiring financiers to hold a copy of the disclosures for four years ensures that in the event of litigation, copies of the disclosures will be available to recipients. This is necessary to ensure that providers have an incentive to provide timely and accurate disclosures.

Section 3023(a)(3): This section requires financiers to maintain of evidence of transmission of disclosures provided by a broker in compliance with subdivision (b) for a period of four years following the date that the disclosure is presented to the recipient. This section aids the statutory objective that recipients receive timely and accurate disclosures. The Department notes that the statute of limitations for contract claim in California is four years. (Cal. Code Civ. Proc. § 337.) Because the Department does not have jurisdiction over some of the products that require disclosures (e.g. true factoring transactions), the Department believes that in some cases, only private litigants will be able to enforce the required disclosure requirements. Requiring financiers to hold a copy of the evidence of transmission ensures that in the event of litigation, copies of the relevant evidence will be available to recipients. This is necessary to ensure that providers have an incentive to provide timely and accurate disclosures.

Section 3023(a)(4): This section requires providers to develop procedures reasonably designed to ensure that recipients receive timely disclosures when the provider provides those disclosures to a broker. This section aids the statutory objective that recipients receive timely and accurate disclosures. This section is necessary to clarify what obligations financiers have to ensure that they work only with brokers that provide timely and accurate disclosures to recipients.

Section 3023(b): This section prohibits a broker from providing a quote to a recipient (which the Department has determines meets the definition of a “specific commercial financing offer” pursuant to Section 2057(a)) until the broker transmits the disclosures required by Section 3023(a)(1) to the recipient. The section further requires that the broker provide evidence of transmission to the financier. This section aids the statutory objective that recipients receive timely and accurate disclosures. This section is necessary to clarify that a broker is obliged to communicate disclosures and helps financiers ensure that their broker-partners are timely providing disclosures.

Section 3023(c)(1): This subparagraph clarifies what a broker is not required by the section to evaluate the accuracy of disclosures provided by the financier pursuant to subparagraph (a)(1) of the same section. This section aids the statutory objective that recipients receive timely and accurate disclosures. This section is necessary because without this provision, a broker may be reluctant to communicate financier-provided disclosures to a recipient.

Section 3023(c)(2): This subparagraph clarifies when a broker is not liable if disclosures provided by the financier pursuant to subparagraph (a)(1) do not comply with the law. This section aids the statutory objective that recipients receive timely and accurate disclosures. This section is necessary because

without this provision, a broker may be reluctant to communicate financier-provided disclosures to a recipient.

Section 3023(c)(2): This subparagraph clarifies that the section does not limit a broker's liability when the broker makes representations concerning a commercial financing. This section aids the statutory objective that recipients understand the nature of their commercial financing offers. This section is necessary because without this provision, a broker might believe that he or she can make misleading statements about the commercial financing as long as the broker transmits the disclosures required by subparagraph (b) of the same section.

Section 3024: This section clarifies that none of the new rules established in this rulemaking are intended to make any clarifications or interpretations on existing California law with regard to the definitions of loan, sale, or lease, as those terms may be used within these rules. This section further clarifies that the rulemaking is not intended to impact the Department's authority to regulate any person or transaction under other laws within its jurisdiction, except as permitted by Financial Code section 22805. This section is necessary to prevent any confusion stemming from provisions in this rulemaking, which are intended to apply only as specifically used herein without any wider reaching ramifications.

Section 3025: This section is intended to clarify that only recipients whose business is principally directed or managed from California are required to receive the disclosures mandated by Financial Code section 22802(a). This section is necessary to ensure that there is no confusion about to whom disclosures must be made.

Underlying Data / Studies Relied Upon

The Department did not rely upon any outside studies in drafting the regulations.

The Department has relied upon information provided by interested parties and parties who would be subject to the proposed regulations obtained during public discussions regarding the proposed regulations. (Gov. Code, § 11346.45.)

Information from interested parties include e-mails and/or letters from the following individuals, organizations and coalitions:

Affirm, Inc.
American Financial Services Association
Anchor Loans
ApplePie Capital, Inc.
Archie Julian

Balboa Capital Corporation
California Bankers Association
California Mortgage Association
California Reinvestment Coalition
Camel Financial, Inc.
CAN Capital, Inc.
CDC Small Business Finance
Channel Islands Leasing and Loan
Commercial Finance Association
Commercial Finance Coalition
Data Sales of California
Electronic Transactions Association
Elevate Funding
Equipment Leasing and Finance Association
F.I.T. Leasing
Fora Financial West, LLC
Halo Business Finance Corp.
Innovative Lease Services, Inc.
Innovative Lending Platform Association
International Factoring Association
Kapitus, Inc.
Katten Munchin Rosenmann LLP
Moore & VanAllen
On Deck Capital, Inc.
Paypal, Inc.
Protiviti
Quadra and Coll, LLP
Rapid Finance
Responsible Business Lending Coalition
Riviera Finance
Secured Finance Network
Senate Committee on Banking and Financial Institutions
Senator Steven M. Glazer
Small Business Finance Association
Small Business Financial Services, LLC
State Financial Corporation
Sunset Financial Group, LLC
Square Capital, LLC
Wells Fargo Bank, N.A.
Wolters Kluwer
Woodstock Institute

ECONOMIC IMPACT ASSESSMENT

In accordance with Government Code Section 11346.3(b), the Department has made the following assessments regarding the proposed regulation:

Creation or Elimination of Jobs Within the State

The Department has assessed whether this rulemaking action will create or eliminate jobs in California. The Department has determined that this regulatory proposal will not have an impact on job creation. The Department has determined that this regulatory proposal may have an impact on job elimination. Because the new disclosure requirements of this rulemaking will assist small business consumers in comparing commercial financing offers and making more informed financing decisions, certain providers of certain types of commercial financing may see a decrease in utilization. Furthermore, some commercial financiers who will be affected by this rulemaking have reported that this rulemaking may result in an increased risk of litigation (since failure to comply with the disclosure requirements is arguably a cause of action) for failing to lawfully make the disclosures required by this rulemaking. As a result, some commercial financiers may choose to cease doing business in California which could potentially lead to a loss of jobs.

Creation of New or Elimination of Existing Businesses Within the State

The Department has assessed whether this rulemaking action will create new businesses or eliminate existing businesses. This rulemaking action will not result in the creation of new businesses. This rulemaking action could result in the elimination of businesses if a business is unwilling or unable to comply with the provisions of the rulemaking action. Failure to comply with the provisions of this rulemaking action could subject a business to litigation, making doing business in California unprofitable or risky. However, this rulemaking action balances the regulatory requirements against the benefits of public protection and based on the Department's assessment the action does not burden business to the extent of eliminating businesses.

Expansion of Businesses Currently Doing Business Within the State

The Department has assessed whether this rulemaking action will result in the expansion of business currently doing business within the state. The Department has determined that this rulemaking action may result in the expansion of business currently doing business within the state. The regulatory requirements on commercial financing companies will initially require the minor reallocation of resources for a business to achieve compliance with the new regulatory requirements. In the long term, this rulemaking action may positively impact the commercial financing marketplace by increasing public confidence in the market, decreasing the likelihood of borrowers obtaining financing they are unable to

afford, and increasing consumer protection from predatory practices. Consequently, future expansion of business in the State is possible.

Benefits of the Regulations

The Department anticipates the proposed regulations will help protect the welfare of California commercial financing consumers. The specific nonmonetary benefits include: enhanced awareness about the costs of financing a variety of available commercial financing products, the ability for commercial financing consumers to more effectively comparison shop commercial financing products, the prevention of commercial financing consumers borrowing more than they can afford to pay, and increased effectiveness of the Department's examinations and regulatory oversight with respect to licensees that offer commercial financing products covered by the regulations.

The Department anticipates the proposed regulations will have nonmonetary benefits to providers of commercial financing as well. Specifically, providers of commercial financing products will have certainty with respect to what information must be disclosed to those seeking the provider's affected commercial financing products, when and how to disclose that information, enhanced confidence that a particular commercial financing product meets the customer's specific needs thereby increasing the likelihood of timely payments, and the opportunity to participate in adopting balanced regulations and comment on the rulemaking the Department is proposing, including the practicality of the proposed disclosures and associated requirements.

Significant Statewide Adverse Economic Impact Directly Affecting Businesses, including the Ability of California Businesses to Compete with Businesses in Other States

The proposed rulemaking will not have a significant statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states. The Department has determined that this regulatory action will not make existing businesses more competitive. The proposed regulations will require providers of commercial financing to disclose information to consumers seeking their commercial financing products. The Department anticipates the costs to comply with the proposed regulations to be minimal because the information necessary to be disclosed should be readily available or able to be calculated from the provider's own records and underwriting data. While some of the disclosures may include information a provider has not chosen to calculate or disclose in the past, the mechanisms for doing so are well established and may be conducted using freely available spreadsheet software. While there may be some new costs to the providers associated with these proposed regulations to train staff on the new required

procedures, these costs are likely to be minimal and offset by the benefits of the regulations.

Evidence Supporting Initial Determination Regarding Adverse Impact on Small Business

The Department relies on information provided by interested parties in letters provided to the Department in anticipation of rulemaking, including parties who would be subject to the proposed regulations, to support an initial determination that the action will not have a significant adverse economic impact on business. These letters are identified above.

Specific Technologies or Equipment

This regulation does not mandate the use of specific technologies or equipment.

Consideration of Alternatives

No reasonable alternatives to the regulations have been identified or brought to the Department's attention that would be: more effective in carrying out the purpose for which the action is proposed; as effective and less burdensome to affected consumers and providers; or more cost-effective to affected consumers and providers yet be equally effective in implementing the regulations required by Financial Code section 22800 *et seq.* than the proposed regulations described in this Initial Statement of Reasons.

No reasonable alternatives considered by the Department, or that have otherwise been identified and brought to the attention of the Department, would be as effective and less burdensome to affected small businesses, or would lessen any adverse impact on small businesses.

The regulations prescribe, minimally, the use of specific actions and procedures in making the disclosures. Specifically, they prescribe the formatting for how the disclosures must be made to recipients (a table with a particular format and clear readability requirements). Despite this prescribed formatting, providers are free to customize the look and feel of the disclosure document to match its preferred styling, company colors, etc. The alternative to this prescribed procedure would be to permit providers to make the disclosures in a completely unprescribed format. The Department determined that such an alternative could lead to significant confusion among recipients given the high probability that each provider would prepare its own version of the disclosures. Such variability would almost certainly impair the legislative intent of making sure recipients receive clear, complete and meaningful disclosures for purposes of making informed business decisions and comparison shopping.

Non-Duplication Standard

The proposed regulations do not duplicate any state statutes.