April 23, 2021

Commissioner of Financial Protection
and Innovation
Attn: Sandra Sandoval
Regulations Coordinator
300 S. Spring Street
15th floor
Los Angeles, Ca. 90013
by email: regulations@dfpi.ca.gov

Re: April 7, 2021 Modifications to Proposed Regulations for SB 1235

Dear Ms. Sandoval

These comments are provided by both Camel Financial, Inc. and State Financial Corporation. Separately each of us commented on earlier drafts of the regulations and described our 87 years of combined experience as asset based lenders. Our respective portfolios are made up of many accounts borrowing less than $500,000. Following are our comments to this draft:

First some technical matters:

1. We suggest §2057(a)(3)(i) use the term "account debtors." "Account debtor" is defined in the California Uniform Commercial Code, the law which governs all transactions in which lenders obtain security interests in personal property. All asset based lenders make loans subject to the Commercial Code. The paragraph would then read: "in which a recipient and the financier create an account in which account debtors deposit payments."

See also §2057(a)(29)(A). This section defines account debtor differently than the Commerical Code; which again is the law which governs all secured loans. We see no reason to use the same term defined by the Commercial Code if a different meaning is intended. If a different meaning is intended, we suggest using a different term.

2. §2057(b). Average means mean. While both mathematical concepts, their meaning are different.

This section is unintelligible when applied to asset based loans. Interest on asset based loans are calculated on the average daily balance of the loan.

Most important, this section can create real confusion. See for instance §3026(c). We expect that here the term "average" meant average not mean. We suggest using "average" throughout the regulations when the DFPI means average and "mean" when the DFPI means mean.

3. §3021(a). The reference in the first line should be to section 2067 not 2062.

Substantive issues:

1. §2057(a)(4)(C). One should keep in mind that the purpose of the statute is to allow borrowers to compare costs. It is less relevant when a borrower is under contract, and even less so if the borrower is in default of its loan agreement. At the least, consideration be given to limiting the effect for this section to changes made while the borrower is in compliance with the terms of its agreement with the lender. If the borrower is in default this provision should not be applicable.

Similarly, temporary accommodations to the borrower should also be excluded. In our experience temporary accommodations are not documented. As prior comments describe, asset based loans typically consist of frequent transactions, often daily, of sales, collections and advances. Communication between borrowers and lenders also often occurs daily. Accommodations to borrowers are often made on the fly. The regulation is not amenable to this constant flow. Thus, we suggest this section be applicable to changes with are meant to remain in force for more than 30 days.

2. §2057(a)(31) Recipient funds and §2067 (a)(3)(A) Funding you will be provided. Asset based lenders commonly charge a loan fee upon initiation. Ordinarily, this fee is deducted from the initial advance. Assume a $100,000 line of credit and a 1% loan fee deducted upon closing. It is not clear if under the proposed regulations the funding to be provided is $100,000 or $99,000. The borrower owes the lender $1,000. Is $100,000 being provided and the deduction is merely a matter of accounting or is the funding $99,000? To our reading the proposed regulations are not clear as to what should be disclosed, $99,000 or $100,000.

3. §2067 (a)(5)(C). We strongly suggest that the language "with the amount and description of each expense" be reinstated. Without this language hidden fees will remain hidden. A prime motivation for the statute is to provide disclosure. The omitted language provides disclosure. Without it Borrowers are left to guess how the cost is calculated.

Currently, some lenders fail to tell borrowers about some of their fees. The omitted language cured that problem. In order for a borrower to fairly compare dollars they should be able to see the cents that have added up.

The borrower must also see the assumptions that went into the calculation. We can easily reduce the projected cost of our loans with unrealistic assumptions. Often, some lenders also try to get a leg up by doing just that.

Finally

4. §3026. These provisions are too tight.

First, given most asset-based lenders use an adjustable benchmark rate plus margin to calculate an interest rate, if the reference rate increases by more than 1/8 of one percent the safe harbor provided by §3026(a)1 disappears. If a lender is charging 10% per annum a .25% change in the reference rate will increase the annual percentage rate by 2.5% wiping out the protection provided by of §3026(a)2 A.

The flexibility apparently given by 2067(a)5(C)ii, disclosing that the estimated finance charge is subject to an adjustable benchmark, does not salvage the ineffectiveness of §3026.

Second, different forms of financing require different rules under §3026. Different forms of financing all require calculation of "Estimated Finance Charge" for Open Ended Financing (§2062(a)5), "Finance Charge" for Sales Based Financing (2065(a)4) and Estimated Finance Charge for Asset Based Financing (§2067(a)5), but each of these types of financing are very different. Most importantly the inputs necessary to make the calculation for asset based lending are the most variable, and require a larger safe harbor.

Thus, these tolerances are too tight. We suggest the DBO, as borrowers should, and these regulations provide, first look at dollars, and then percentages.

Putting dollars to the tolerance of §3026(a)1 1/8 of one percent against a $500,000 loan is only $625. For a business borrowing $500,000 $625 is nothing. Against a $100,000 loan $125 is meaningless. Either amount could easily consist of charges outside of the lender's control, such as bank charges passed through.

If a lender were to disclose an APR of 15% and the actual rate was 15.5% that difference would fall outside of the 2.5% tolerance given by §3026(a)2. In dollars against at $500,000 ½ of one percent is $2,500. Not a lot when the annual interest at 15% on $500,000 is $75,000.

A $25,000 error on a $500,000 loan when so much is left to assumptions would be more realistic.

Thank you for the opportunity to comment.

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