LAW OFFICES OF PAUL SOTER
149 SAN FELIPE AVENUE
SAN FRANCISCO, CALIFORNIA 94127
WWW.LAWOFFICESOFPAULSOTER.COM
TEL. (415) 867-9484
E-MAIL: PSOTER@SONIC.NET

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Commissioner of Financial Protection and Innovation
Attn: Sandra Sandoval, Regulations Coordinator
300 South Spring Street, 15th Floor
Los Angeles, CA 90013

By e-mail to regulations@dfpi.ca.gov

Re: Comments on Proposed Rulemaking Under the California Financing Law (PRO 01/18): Proposed Commercial Financing Disclosure Regulations

Dear Ms. Sandoval,

This letter is submitted on behalf of my clients to in response to the Notice of Third Modifications to Proposed Regulations (the "Proposal") under the California Financing Law (the "CF Law") issued by the Department of Financial Protection and Innovation (the "Department") on November 18, 2020, as part of its anticipated proposed revisions to its CF Law regulations implementing Senate Bill 1235. I am an attorney practicing in the area of consumer and commercial finance in the California market. I represent or advise nearly 100 corporate entities operating in that space. This client base consists primarily of commercial lenders, many of which are most active in the so-called small commercial finance space: financing in amounts ranging from $50,000 to $2,000,000. The clients' commercial lending activities include financing that is unsecured, secured by personal property, and secured by real property. I do not currently represent any mortgage lenders, as that term is defined in the CF Law. Approximately 70 of those entities currently hold one or more California Finance Lender ("CFL") licenses. Three or four of those entities currently have active applications for CFL licenses pending. Ten or twelve of those entities have recently surrendered some or all of their CFL licenses and either left the California market or pivoted their business models away from CF Law-regulated activities. As this letter is submitted in the collective interests of those clients, it will use the first person plural to set forth our comments to the Proposal.

The Time Frame for Comment on Significant Issues Is Unreasonably Short

No substantive comment is provided here on the bulk of the Proposal, for the simple reason that the turnaround time is too short. In the middle of summer, in the first year in two years in which many businesses and families are able to do so, a huge proportion of my client base is on vacation or otherwise unavailable during the 14-day period provided for comment. This alone makes the 14-day comment period unreasonable.

Further, 14 days is not sufficient comment time for several other reasons. Therefore, while we are able to provide skeletal comments on one portion of the Proposal, we submit this letter as a general objection to the Department's proceeding to implement *any* rule on in this timeframe. I note that the Department has had the most recent version of the comments to this Proposal since April: a good four months. Now, with this Proposal, the Department is requiring the public to respond to its most recent issuance within 14 days. The Department cannot truly expect intelligent and thoughtful responses in 14 days to what it took the Department four months to formulate, and that after nearly three years since the enactment of SB 1235. So, it is difficult to discern any need for this rush now. Further, as will be discussed below, a major portion of this proposal seeks to quiet an issue, on 14 day's notice, that has been pending since 1909.

We further note that this a common practice by the Department, and we object to that practice. We refer to the practice of the Department taking months and months to review an issue, and then demanding an essentially immediate response from a regulated entity or an allegedly regulated. The Department engages in this conduct across all of its activities: examination responses, rulemaking, subpoena responses, etc. This is not a practice consistent with the operation of a government agency in a liberal democracy, and the Department should cease, desist, and refrain from this conduct. It can start to do so by extending the comment period for this Proposal to at least 60 days.

Finally in this regard, senior staff of the Department have expressed to us a concern with compliance by regulated and potentially regulated persons with the spirit as well as the letter of the laws the Department and forces. We suggest that the Department should follow this same guidance in its own action actions here, and adhere to the spirit of the California Administrative Procedures Act, which is to ensure a reasonable opportunity for a full public comment on all proposed regulations. Accordingly, the Department is urged to extend the comment period on this proposal to at least 60 days, and the Office of Administrative Law is urged not to permit regulation to take affect following short comment.

The Proposed New Definition of "Broker"

Brief comments are provided on this issue. There is a lot more to be discussed here, further comment time permitting.

The Proposal seeks to implement, for the first time, a definition of the term "broker." While such a definition is long overdue in regulations interpreting the CF Law, this is an inopportune time and place to introduce such a definition. First, such a definition is significant to many areas of licensees' operations under the CF Law, well beyond the scope of the SB 1235 disclosures. It should therefore be implemented following the publication of a full explanation by the Department of its reasoning behind the such a regulatory definition; an appropriate notice and comment period; full discussion by the Department

in consultation with stakeholders; and a full deliberation of all input received by the Department. Second, the definition of the term "broker" is not necessary to promulgate in a regulation implementing SB 1235.

Problematic Nature of the Proposed Definition: CFL's have been urging the Department to adopt a reasonable and useful definition of the term "broker" for decades. It has for years been highly problematic for both the CFL industry and the Department that this key definition, in a statute that dates back to 1909, has never been clarified from the circular and unhelpful definition in the CF Law.

The short comment period precludes a full discussion of the issues pertaining to the definition of "broker" in any meaningful manner. However, we do point out that the last three of the six portions of the definition – which are merely clerical or ministerial functions – are contrary to the contents of the most complete and therefore best standard for source of a definition of "broker:" the Department of Real Estate (the "DRE regulation") at 10 California Code of Regulations § 2841. By fully defining what the Real Estate Law means by "negotiation," that DRE regulation sets forth clear, complete, practical, and workable, and standards for loan brokers' activities for which compliance is easily examinable by the DRE.

There is, of course, no requirement of law that the Department conform its regulatory definition of the term "broker" to that of the DRE. However, since the DRE's regulatory definition has been in effect since 2000, and seems to have served the DRE and its licensees well, we believe that any regulatory proposal that seeks to impose a significantly different definition applicable to the CF Law should be fully explained by the Department and provide a sufficient comment period and outreach by the Department before it is adopted. The definition of "broker" in the Proposal, and the inappropriately short comment period, do not do this, and so this definition is accordingly inappropriate for adoption.

Unnecessary and Thus Inappropriate Nature of the Definition in This Regulation: Next, again only briefly due to time constraints addition, we must point out that a definition of "broker" is completely unnecessary to the implementation of the SB 1235 regulations. The word "broker" does not appear in SB 1235. Therefore, to the extent that the Department's aim is, appropriately, to ensure that all financing transactions covered by SB 1235 are by the Regulation, there are several potential approaches that are less disruptive and less likely to have for seeable side effects that will cause additional and unnecessary conflict between the Department and stakeholders.

Our suggestion in this regard is that, rather than singling out "brokers" unnecessarily for a poor definition and SB 1235 coverage, the Department should instead promulgate a list of covered intermediary entities and allow existing law to define what those entities are. As one example, the regulation could provide that its provisions apply to

"brokers, finders, channel partners, agents, co-venturers, or other intermediaries that refer loans and other financing transactions to persons covered by SB 1235." This would fully apply SB 1235 to all persons whom the Legislature intended to be covered, without the unnecessary and foreseeable potential for mischief that promulgation of an inappropriate definition of "broker" will cause. As another example, the SB 1235 regulation could borrow the broad language of Financial Code §§ 23001(d) and 23005(a) and apply the SB 1235 rules to persons who "offer, originate, or make a [covered] transaction, arrange a [covered] transaction for a [covered] originator, act as an agent for a [covered] originator, or assist a [covered] originator in the origination of a [covered] transaction. This approach would stabilize the situation and make the coverage determination in any particular transaction a factual, rather than legal issue.

Other Significant Issues

For the reasons set forth above, time precludes a discussion of the other significant issues raised by the Proposal. Those include, but may not be limited to the following:

- Numerous technical operational issues, which need a thorough review by operators, for which time is not provided; and
- The deletion of the previous draft provision that an entity would not be deemed to have engaged in lending simply because it used the terms set forth in the regulation in a disclosure. This is clearly contrary to analogous federal disclosure law, and thus deserves full explanation and discussion.

As time is too short, we must content ourselves at this point to a general objection to the implementation of the Proposal.

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On behalf of my clients and myself, I reiterate our appreciation for the consideration of these comments by the Department, and look forward to a more meaningful opportunity to fully analyze and comment upon the contents of this important Proposal.

Sincerely,

/s/ *R. P. Soter, Jr.*

R. Paul Soter, Jr.

cc: [redacted]*@dfpi.ca.gov*
[redacted]*@dfpi.ca.gov.*