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Re: Comments to Proposed Rulemaking – PRO 01/18 – Commercial
Financing Disclosures (SB 1235)

Rabo AgriFinance LLC (“RAF”) submits these comments to alert the Department of Financial Protection and Innovation (the “Department”) to the negative impacts that the proposed rules could have on California farmers and agricultural retailers and manufacturers. RAF is a subsidiary of Coöperatieve Rabobank U.A. (“Rabobank”), a Dutch multinational banking and financial services company headquartered in Utrecht, Netherlands. Rabobank is a global leader in food and agriculture financing and sustainability-oriented banking. It operates a branch in New York and is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978 (12 U.S.C. 3106). As discussed below, RAF is engaged in agricultural lending in California and licensed under the California Financing Law.

Farmers are unique. Each year, they confront a cycle of high upfront costs to plant their crops coupled with significant delays until crops are harvested and

revenues are realized.¹ At the same time, more than half of cropland is rented, not owner-operated.² As a result, many farmers have little to no pledge-eligible assets to qualify for financing under conventional lending models. And to make things even tougher, financing options for farmers are rapidly dwindling. In fact, according to a recent Reuters report, the farm-loan portfolios at the nation's top 30 banks declined 17.5% between December 2015 and March 2019.³

RAF provides a lifeline for many of these farmers through its innovative Input Finance Program, which provides an incremental line of credit that farmers can use to take advantage of early season discounts and align their crop year expenses to revenues to improve cash flow.

The program works as follows. RAF works with agricultural retailers and manufacturers to establish pre-negotiated product offerings, or “programs,” that often involve discounted prices, favorable interest rates, and repayment dates set after crops are harvested and revenues realized. Retailers and manufacturers are willing to offer these programs because they provide them with early purchase commitments and, as discussed below, certainty of payment. They also give retailers and manufacturers the ability to buy-down the interest rates for their customers in order to finance the sale of their products. This is similar to automobile lending where the manufacturer may offer incentives to the finance company to offer lower interest rates to the buyer in order to facilitate the sale of the vehicle.

Critical to these comments, the key terms applicable to the programs, including sales volume, interest rate, program start and end dates, payment due date and RAF fees, vary between each retailer and manufacturer. Indeed, each retailer and manufacturer itself has multiple programs with varying terms. As such, while RAF may know the specific terms offered under each program, those terms are not uniform.

Farmers access the programs by applying for an Input Finance Program account with RAF, which essentially works like a line of credit but with one big

¹ GAO, *Socially Disadvantaged Farmers*, GAO-19-539, 7 (July 11, 2019) (“Agricultural producers generally require financing to acquire, maintain, or expand their farms, ranches, or agribusinesses”).

² USDA, *Farmland Ownership and Tenure* (2014).

³ <https://www.reuters.com/article/us-usa-farmers-lending-insight/wall-street-banks-bailing-on-troubled-u-s-farm-sector-idUSKCN1U618F>.

difference. At the time that the RAF account is opened, none of the traditional financing terms are known other than the maximum available credit limit and uniform default and early payment terms. The RAF Input Finance Program contract does not set the interest rate or payment terms as those necessarily depend on the specific retailer/manufacturer program that the farmer ultimately chooses to access. RAF has no control over the farmer's choice and, in fact, is not even aware of any specific transaction until after it is consummated.

After a transaction is completed, a loan under the farmer's RAF account is created in the amount of the purchase price and on the terms offered by the applicable program, including whatever interest rate applies to that program (which could be as low as 0% in many cases when the supplier subsidizes the interest rate). RAF then pays the retailer/manufacturer the full amount owed by the farmer (minus their pre-negotiated RAF fee) within two business days of the transaction, and the farmer repays RAF on the payment due date applicable to the specific program, which is after the farmer has harvested his or her crops and realized revenues. There are no fees or penalties if the farmer wants to pay off the RAF account balance early.

To take an example, say a farmer opens an RAF Input Finance Program account with a \$100,000 credit line. At the time that contract is made, the only terms that are set are the maximum credit available to the farmer and certain uniform terms relating to default and early payment. The key interest rate and payment terms are not known and cannot be known at that time, as they depend on what program or programs the farm chooses to access. Assume the farmer decides to use the RAF account to purchase \$40,000.00 worth of seeds under Retailer X's Early Order Seed program, which offers an 8% discount and 0% interest if the purchase is made before November 15, 2020, and payment is made by December 15, 2021. The farmer thus purchases \$40,000 worth of seeds for the discounted price of \$36,800, re-payable on December 15, 2021 after his or her crops are harvested and sold. And Retailer X receives full payment for the farmer's purchase from RAF (less the pre-negotiated RAF fee applicable to the program) within two business days of the transaction.

As the above example demonstrates, RAF's Input Finance Program is a critical resource for agricultural retailers and manufacturers looking for early purchase commitments and certainty of payment, and farmers who need to finance their upfront costs, particularly those who do not own their farmland and do not have the collateral needed to access traditional financing sources. RAF's Input

Finance Program allows the farmer to fund crop production without collateral and the agricultural retailer/manufacturer to shift the risk of non-payment to RAF. This process is very similar to the arrangement between retailers and financing sources in other areas.

Our concern is that, as drafted, the proposed rules could jeopardize RAF's ability to offer its Input Finance Program to California farmers and other members of the agricultural community. RAF's program does not fit neatly into any of the categories of financing established under the proposed rules. It has elements of factoring in that the retailers and manufacturers are effectively selling their accounts receivables to RAF. It also has elements of an commercial open-end credit plan, in that farmers can at their discretion use their RAF account to buy seeds and other products.

If the Department were to regulate RAF's Input Finance Program as a commercial open-end credit plan, the proposed rules as drafted could prevent RAF from offering the program in California because RAF will not have the information needed to make the required disclosures at the time it extends the financing offer to farmers.

To illustrate, the proposed rules require the disclosure form to be presented to the borrower "at the time of extending a specific commercial financing offer," which in the case of RAF's Input Finance Program could be deemed to occur when a farmer opens his or her account with RAF. The proposed rules further require the first row of the disclosure form to state that the calculations assume the borrower will "pay off the draw entirely according to the agreed payment schedule" if the contract only allows for a single payment option, or that the borrower will "choose to make minimum payments" if the contract allows for multiple payment options. However, the payment terms associated with RAF's Input Finance Program are not set at the time that a farmer opens his or her RAF account. Those terms depend on the specific manufacturer/retailer program or programs that the farmer ultimately chooses to access. As such, RAF does not have the information needed to make this disclosure at the time it extends an offer to farmers.

The third and fourth rows present similar challenges. The third row requires the provider to disclose an annual percentage rate (APR) for either a fixed interest or adjustable interest rate loan. The fourth row requires disclosure of the estimated finance charges, including interest charges and origination fees. Again, however, in RAF's Input Finance Program, these terms are not set when the farmer opens a

RAF account; they necessarily depend on the specific retailer/manufacturer program or programs that the farmer chooses to access. At the time that the RAF account is opened, RAF does not know and cannot know what program(s) the farmer will choose and thus cannot know what the interest rate will ultimately be.

The fifth, sixth and seventh rows pose the same issue. The fifth row requires the provider to disclose the amount and frequency of periodic payments. The sixth and seventh rows require the provider to disclose the draw period and transaction term, respectively. Again, because the interest rate, draw periods and payment terms are set by whatever specific retailer/manufacturer program that the farmer ultimately chooses to access, this information is not known and cannot be known at the time that a farmer opens a RAF account.

Finally, the disclosure required for contracts that do not provide for monthly payments presents the same concern as the payment terms are set by the individual retailer/manufacturer program and are not known and cannot be known at the time that a farmer opens a RAF account.

In short, the RAF Input Finance Program cannot possibly comply with the required disclosures as drafted as most of the information to be disclosed is not known and cannot be known by RAF at the time that it offers a contract to a farmer. Unless the proposed rules are clarified or amended, RAF may have no choice but to cease providing access to its Input Finance Program to California farmers, which would remove a valuable market for agricultural retailers and manufacturers and put many farmers – particularly those who do not own their land – at serious financial risk.

There are two ways to address this concern. One is to issue a clarification that the proposed rules do not apply to RAF as an agricultural lender, or specifically RAF's Input Finance Program. As noted, RAF's program does not fit neatly into any of the defined categories covered by the proposed rule. Given the nature of agricultural lending and the terms of RAF's Input Finance Program, the protections of the proposed rule are unnecessary to protect the borrowers. This is consistent with the California Financing Law, which excludes various types of agricultural lending and lenders from the scope of the law. *See* Cal. Fin. Code § 22051. Moreover, from a fairness standpoint, Farm Credit System institutions are exempted by statute from the requirements altogether, even though they offer similar products and services to the same agricultural borrowers as RAF. Irrespective of the problems identified above, the application of the proposed rules

to RAF thus create an uneven playing field that could negatively impact the financing alternatives available to farmers and agricultural retailers. In order to preserve competitive equality, RAF should be afforded the same treatment as the Farm Credit System institutions and exempted from the rules as the organizations serve similar agricultural borrowers.

Alternatively, the proposed rules should be amended to accommodate innovative products like RAF's Input Finance Program and ensure that choice and competition thrive in the marketplace. Given that such products are arguably akin to factoring, one possibility is to allow them to utilize hypothetical terms, as section 2064 of the proposed rules allows for factoring. Specifically, section 2062 could be amended to allow for hypothetical interest rates and payment terms to be used when those terms are not set by the commercial open-end credit plan contract and it is not possible to set them in advance. We would suggest the following amendments to section 2062 of the proposed rule (the full text of section 2062 with our suggested changes is included as Exhibit A to this letter):

(1) Amend section (a)(2) to add the following subdivision (C)”

(C) If the contract does not provide payment options and it is not possible to set them in advance: “The calculations below are based upon an initial draw of your full Approved Credit Limit of [approved credit limit] and a hypothetical invoice which requires you to make [number of payments] payment[s], that you miss no payments, and that you do not re-draw on this line. Actual costs may differ substantially.”

(2) Amend section (a)(4)(A) to add the following subdivision (iii):

(iii) If the contract does not provide an interest rate and it is not possible to set an interest rate in advance, the following language: “Estimated Annual Percentage Rate (APR)”.

(3) Amend section (a)(4)(B) to read as follows:

(B) In the second column, the provider’s calculation of the annual percentage rate or the estimated annual percentage rate if the contract does not provide an interest rate and it is

not possible to calculate an interest rate in advance, calculated in accordance with section 3001 of these rules.

(4) Amend section (a)(4)(C) to add the following subdivision (iv):

(iv) If the contract does not provide an interest rate and it is not possible to calculate an interest rate in advance, the following language:

“This is the estimated cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make.

The contract does not preset these terms, so for the purpose of calculating this APR estimate, we assume you will draw your full Approved Credit Limit today at an interest rate of [estimated interest rate] and that you will repay the draw [payment terms].”

(5) Amend section (a)(5)(B) to read as follows:

(B) In the second column, the total finance charge or the estimated total finance charge if the contract does not provide finance charges and it is not possible to calculate finance charges in advance, calculated in accordance with section 3010 of the rules.

(6) Amend section (a)(5)(C) to read as follows:

(C) In the third column, an explanation of the provider’s calculation of the finance charge, with the amount and description (such as interest charges and origination fees) of each expense that is included in the finance charge. In addition, if the contract provides for an adjustable interest rate that changes over time, an explanation of how the initial interest rate was used to calculate interest charges. If the contract does not provide finance charges and it is not possible to calculate finance charges in advance, an

explanation of the provider's calculation of the estimated finance charge, with the amount and description (such as interest charges and origination fees) of each estimated expense that is included in the estimated finance charge.

(7) Amend section (a)(6) to add the following subdivision (F):

(F) If periodic payments during the term of the transaction vary and it is not possible to calculate all payment amounts in advance because the contract does not include the amount of the interest rate or the frequency of payments:

(i) In the second column, a periodic payment amount calculated using the estimated interest rate followed by the date and amount of any payments using an estimated frequency of payments.

(ii) In the third column, a statement explaining that the periodic payment amount disclosed is based on an estimated interest rate and payment terms and that the actual rate and terms may vary.

(8) Amend section (a)(7)(B) to read as follows:

(B) In the second column, the draw period for the transaction, or an estimated draw period if the contract does not provide a draw period and it is not possible to identify the draw period in advance.

(9) Amend section (a)(8)(B) to read as follows:

(B) In the second column, the term of the transaction, or an estimated term if the contract does not provide a term and it is not possible to identify the term in advance.

(10) Amend section (a)(12) to read as follows:

(12) If the contract provides or could provide for periodic payments that are not monthly, the provider shall insert one

additional row below the fourth row, and the additional row shall include only the following information:

- (A) In the first column, the following language: “Average Monthly Cost” or, if the contract does not provide for payment terms and it is not possible to set payment terms in advance, “Estimated Average Monthly Cost.”
- (B) In the second column, the average monthly cost or average estimated monthly cost that the recipient will pay over the term of the transaction.
- (C) In the third column, language explaining that the recipient will or, if the contract does not provide for payment terms and it is not possible to set payment terms in advance, may not be required to make monthly payments and explaining how the provider has calculated the monthly cost.

In sum, although the intent of the proposed rules is noble, as drafted they could reduce the financing alternatives available to California farmers, which could, in turn, lead to serious negative impacts for farmers and the agricultural retailers and manufacturers that serve them. While we ultimately believe that the rules should set a level-playing field and treat agricultural financing offered by Farm Credit System institutions the same as credit offered by companies like RAF, at the very least the rules should be amended to permit estimated disclosures for RAF’s Input Finance Program and similar arrangements where the terms are not known at the time the credit application is approved.

We appreciate your consideration of these comments.

Very truly yours,

Greg Hoover

EXHIBIT A (Proposed Amended Text of Section 2062)

§ 2062. Commercial Open-End Credit Plan Disclosure Formatting.

(a) Disclosures for commercial open-end credit plans, provided in accordance with section 22802 of the Code, shall comply with the following requirements:

(1) The provider shall present the disclosures in a table consisting of nine rows and three columns.

(2) In the first row, the first, second and third columns shall be combined, and the resulting cell shall have only the following language, in italics:

(A) If the contract allows only for a single payment option: “The calculations below are based on an initial draw of your full Approved Credit Limit of [approved credit limit] and assume that you will pay off the draw entirely according to the agreed payment schedule, that you miss no payments, and that you do not redraw on this line. Actual costs may differ substantially.”

(B) If the contract allows for multiple payment options: “The calculations below are based on an initial draw of your full Approved Credit Limit of [approved credit limit] and assume that you will choose to make minimum payments, that you miss no payments, and that you do not re-draw on this line. Actual costs may differ substantially.” If the amount borrowed is payable on demand, the provider shall disclose that amounts borrowed are payable on demand and that the estimate assumes a term of one year. If an alternate maturity date is stated in the legal obligation between the parties, then the provider shall state that the disclosure is based upon that maturity date.

(C) If the contract does not provide payment options and it is not possible to set them in advance: “The calculations below are based upon on an initial draw of your full Approved Credit Limit of [approved credit limit] and a hypothetical invoice which requires you to make [number of payments] payments, that you miss no payments, and that you do not re-draw on this line. Actual costs may differ substantially.”

- (3) The second row of the table shall include only the following information:
- (A) In the first column, the following language: “Funding You Will Receive”.
 - (B) In the second column, the maximum credit amount, minus any deductions such as origination charges and amounts used to pay off other financings.
 - (C) In the third column, a description of how the amount in the second column was calculated, including a disclosure of the amount owed and the amounts and descriptions of any deductions excluded from (3)(B) above.
- (4) The third row of the table shall include the following information:
- (A) In the first column:
 - (i) If the contract provides for a fixed interest rate or rates that are predetermined by the contract, the following language: “Annual Percentage Rate (APR)”.
 - (ii) If the contract provides for an adjustable interest rate and it is not possible to calculate the interest rates throughout the term of the transaction in advance, the following language: “Initial Annual Percentage Rate (APR)”.
 - (iii) If the contract does not provide an interest rate and it is not possible to set an interest rate in advance, the following language: “Estimated Annual Percentage Rate (APR)”.
 - (B) In the second column, the provider’s calculation of the annual percentage rate or the estimated annual percentage rate if the contract does not provide an interest rate and it is not possible to calculate an interest rate in advance, calculated in accordance with section 3001 of these rules.
 - (C) In the third column:

- (i) If the contract provides for a single, fixed interest rate, the following language:

“APR is the cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make.

APR is not an interest rate. Your interest rate is [interest rate]. Your APR may be higher than your interest rate because APR incorporates interest costs and other finance charges.”

- (ii) If the contract provides for multiple pre-determined interest rates that change over time, the following language:

“APR is the cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make.

Your APR is not an interest rate. Your initial interest rate is [initial interest rate]. Your APR may be higher than your interest rate because APR incorporates interest costs and other finance charges.”

- (iii) If the contract provides for an adjustable interest rate and it is not possible to calculate the interest rates throughout the term of the transaction in advance, the following language:

“APR is the cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make.

APR is not an interest rate. Your initial interest rate is [initial interest rate]. Although your interest rate will adjust over time, for the purposes of calculating this APR estimate, we have used the initial interest rate for future periods where the interest rate is not preset by the contract. Your APR may be higher than your interest rate because APR incorporates interest costs and other finance charges.”

(iv) If the contract does not provide an interest rate and it is not possible to calculate an interest rate in advance, the following language:

“This is the estimated cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make.

The contract does not preset these terms, so for the purpose of calculating this APR estimate, we assume you will draw your full Approved Credit Limit today at an interest rate of [estimated interest rate] and that you will repay the draw [payment terms].”

(5) The fourth row of the table shall include only the following information:

- (A) In the first column the following language: “Estimated Finance Charge”.
- (B) In the second column, the total finance charge or the estimated total finance charge if the contract does not provide finance charges and it is not possible to calculate finance charges in advance, calculated in accordance with section 3010 of these rules.
- (C) In the third column, an explanation of the provider’s calculation of the finance charge, with the amount and description (such as interest charges and origination fees) of each expense that is included in the finance charge. In addition, if the contract provides for an adjustable interest rate that changes over time, an explanation of how the initial interest rate was used to calculate interest charges. If the contract does not provide finance charges and it is not possible to calculate finance charges in advance, an explanation of the provider’s calculation of the estimated finance charge, with the amount and description (such as interest charges and origination fees) of each estimated expense that is included in the estimated finance charge.

(6) The fifth row of the table shall include only the following information:

- (A) In the first column “Estimated Payment”.

- (B) If periodic payments during the term of the transaction will not vary:
- (i) In the second column, the amount of each periodic payment followed by a forward slash (/) and the frequency of each periodic payment followed by the date and amount of any irregular payments listed in chronological order.
 - (ii) In the third column, a short explanation of the payment frequency and any irregular payments. The provider may also include a short statement describing when each payment will become due.
- (C) If periodic payments during the term of the transaction vary and it is possible to calculate the payment amounts in advance, the second and third columns in the fifth row shall be combined and the provider shall list the periodic payment amounts with a description of when each amount will become due followed by the date and amount of any irregular payments in listed chronological order and any assumptions made when calculating the payment amounts. For example:
- Months 1-12: \$600/month
Months 13-24: \$1200/month
- Maintenance Fee Due 2/1/2021: \$500.
Maintenance Fee Due 8/1/2022: \$300.
- (D) If periodic payments during the term of the transaction vary and it is not possible to calculate all payment amounts in advance because the transaction has an adjustable interest rate that cannot be calculated in advance:
- (i) In the second column, a periodic payment amount calculated using the initial interest rate followed by the date and amount of any reasonably anticipated irregular payments listed in chronological order.
 - (ii) In the third column, a statement explaining that the periodic payment amount disclosed is based upon the initial interest rate,

and that the actual rate may change over time and an explanation of any irregular payments. The provider may also include a statement describing when the payment will adjust and how it will be calculated.

- (E) If periodic payments of principal during the term of the transaction do not vary but periodic payments of interest during the term of the transaction vary, and it is not possible to calculate all interest payment amounts in advance, because the transaction has an adjustable interest rate that cannot be calculated in advance:
- (i) In the second column, the phrase “Initial Interest Payment:” followed by an interest payment amount calculated using the initial interest rate, followed by a forward slash (/) and the frequency of each periodic interest payment.
 - (ii) In the second column, beneath the disclosure required by subdivision (6)(E)(i), the phrase “Principal Payment Amount:” followed by the amount of each periodic principal payment, followed by a forward slash (/) and the frequency of each periodic principal payment.
 - (iii) In the third column, a statement explaining that the Initial Interest Payment Amount disclosed is based upon the initial interest rate, and that the actual rate may change over time.
 - (iv) In the third column, beneath the statement explaining the Initial Interest Payment Amount and at the same height as the disclosure required under subdivision (6)(E)(iii), a short explanation of the principal payment amount and frequency.
- (F) If periodic payments during the term of the transaction vary and it is not possible to calculate all payment amounts in advance because the contract does not include the amount of the interest rate or the frequency of payments:
- (i) In the second column, a periodic payment amount calculated using the estimated interest rate followed by the date and amount of any payments using an estimated frequency of payments.

(ii) In the third column, a statement explaining that the periodic payment amount disclosed is based on an estimated interest rate and payment terms and that the actual rate and terms may vary.

- (7) The sixth row of the table shall include only the following information:
- (A) In the first column, the following language: “Draw Period.”
 - (B) In the second column, the draw period for the transaction, or an estimated draw period if the contract does not provide a draw period and it is not possible to identify the draw period in advance.
 - (C) In the third column, an explanation of the draw period for the transaction.
- (8) The seventh row of the table shall include only the following information:
- (A) In the first column, the following language: “Term.”
 - (B) In the second column, the term of the transaction, or an estimated term if the contract does not provide a term and it is not possible to identify the term in advance.
 - (C) In the third column, an explanation describing the term.
- (9) In the first column, the eighth and ninth rows shall be combined and shall include only the following language: “Prepayment.”
- (10) In the eighth row, the second and third columns shall be combined and shall include only:
- (A) If, at any time during the term of the transaction, prepayment of the outstanding balance due will require the recipient to pay finance charges other than interest accrued since the recipient’s last payment, the following statement: “If you pay off the financing early you will need pay all or portion of the finance charge, up to \$[maximum non-interest finance charge].”

(B) In all other cases, “If you pay off the financing early, you will not need to pay any portion of the finance charge other than interest accrued since your last payment.”

(11) In the ninth row, the second and third columns shall be combined and shall include only:

(A) If, at any time during the term of the transaction, prepayment of the outstanding balance due will require the recipient to pay additional fees and charges not included in the finance charge, the following statement: “If you pay off the financing early you must also pay additional fees not already included in the finance charge” followed by the amounts and descriptions of the additional fees and charges.

(B) In all other cases, the following statement, “If you pay off the financing early you will not pay additional fees not already included in the finance charge.”

(12) If the contract provides or could provide for periodic payments that are not monthly, the provider shall insert one additional row below the fourth row, and the additional row shall include only the following information:

(A) In the first column, the following language: “Average Monthly Cost” or, if the contract does not provide for payment terms and it is not possible to set payment terms in advance, “Estimated Average Monthly Cost.”

(B) In the second column, the average monthly cost or average estimated monthly cost that the recipient will pay over the term of the transaction.

(C) In the third column, language explaining that the recipient will or, if the contract does not provide for payment terms and it is not possible to set payment terms in advance, may not be required to make monthly payments and explaining how the provider has calculated the monthly cost.