



Commissioner of Financial Protection and
Innovation Attn: Sandra Sandoval, Regulations
Coordinator
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Via Electronic Mail to:
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**ILPA Comments on Proposed Rulemaking under the California Consumer Financial
Protection Law: Commercial Financing to Small Businesses, Nonprofits, And Family Farms
(PRO 02-21)**

Dear Ms. Sandoval,

The Innovative Lending Platform Association (ILPA)¹ appreciates the opportunity to provide comments on the California Department of Financial Protection and Innovation's (DFPI) proposed rulemaking regarding the California Consumer Financial Protection Law ("CCFPL"). ILPA applauds DFPI's goal of ensuring that small businesses are treated fairly by financing providers, and we look forward to engaging in a thoughtful, collaborative approach to promulgating these regulations.

While DFPI addressed several concerns raised in the initial proposed regulations, particularly regarding aligning California's unfair, deceptive, and abusive definitions with federal laws, ILPA still has some concerns that we hope can be addressed.

Confusing Terminology

As you know, consumer and commercial financing are vastly different products and markets. However, throughout the Proposed Regulations, the DFPI conflates consumer and commercial financing. In the Initial Statement of Reasons, the DFPI acknowledges that the legislature was focused on creating "[r]obust consumer protections" and asserts the anticipated benefits of the Proposed Regulations include "an increase in consumer welfare."

¹ ILPA is the leading trade organization for companies focused on online, small business financing services. Our member companies share a commitment to the health and success of our nation's small businesses. They are dedicated to advancing best practices and standards that promote responsible innovation and access to capital. Our member companies consist of A10 Capital, BFS Capital, Biz2Credit, BlueVine, Fundbox, Funding Circle, Kabbage/AMEX, Lendio, Mulligan Funding, OnDeck (Enova), Paynet/Equifax.

The Proposed Regulations try to connect consumer lending to commercial finance with claims that organizations are “managed and operated by individuals and consumers of financial products and services.” This assertion ignores the differences between commercial and consumer financing, both in terms of what funds are used for (i.e. consumer funds are used to cover expenses, commercial financing is often used as an investment in the business, to purchase inventory, hire staff, or carry a business through a particularly slow time, all with a hope of a return on that investment). It also skips over the legal and practical distinctions between businesses and the individuals who own those organizations.

In addition, the definitions of the proposed regulations use the term "covered consumers" to refer to small businesses, family farms, and nonprofits. The term "consumer," when dealing with a commercial transaction, is confusing and conflicts with the CCFPL's terminology, which defines "consumer financial products and services" as "any financial product or service that is delivered, offered, or provided for use by consumers primarily for personal, family, or household purposes."²

To avoid confusion and conflating consumer and commercial products, ILPA respectfully requests that DFPI update the proposed regulations to focus on the unique market that is commercial financing and change the term “covered consumer” to "covered entity" or another term that avoids consumer/commercial confusion. The definition, “a small business, family farm, or nonprofit whose activities are principally directed or managed from California” should stay the same.

Incomplete and Misleading Data Reporting

As ILPA shared in our last comments, the DFPI's annual reporting requirements, according to the CCFPL, fail to include the critical metrics necessary to gather a complete picture of the financing provided. The draft regulations require that commercial financing providers report the financing's minimum, maximum, average, and median total dollar cost at each interval. However, without the financing length, the data collected ignores the time value of capital, making certain products (those with shorter terms or open-ended products) seem disproportionately more expensive than others.

For example, two providers could provide a small business with \$10,000 in financing. They could both charge the same in simple interest. However, if one provider offers financing for a term of less than one year, the APR will be significantly higher than the other provider's. For this reason, DFPI must collect additional information; it is simply not enough to collect the number of transactions in particular principal intervals and the minimum, maximum, average, and median APR for each interval. Without the term, this data will be misleading and prejudice the data against short-term financing options, even if the total cost of these financing products in a dollar amount is less than those with longer terms.

The proposed regulations also require covered providers to report information that they may not currently collect from commercial customers, such as gross annual revenue, which is critical to determining what transactions are to be reported and how. The proposed regulations do not set forth a preferred protocol or safe harbor method as to how commercial finance companies should go about collecting and vetting the information required to determine whether a company meets, for example, the definition of a “small business.”

² Cal. Fin. Code § 90005

In addition, and more broadly, ILPA requests more clarity on why DFPI needs this data. The underlying statute grants DFPI the authority to “define unfair, deceptive, and abusive acts and practices in connection with the offering or provision of commercial financing, as defined in subdivision (d) of Section 22800, or other offering or provision of financial products and services to small business recipients, nonprofits, and family farms. The rulemaking may also include data collection and reporting on the provision of commercial financing or other financial products and services.”

It is unclear whether the data DFPI proposes to collect is in relation to defining “unfair, deceptive, and abusive acts and practices in connection with the offering or provision of commercial financing.” So it is unclear what the data will be used for and whether it will be released to the public. Given the complexities and added burden, the rule should clarify why DFPI needs this exact set of data as it relates to defining UDAAP, whether it will be released to the public, in what format, and whether it will be reported in aggregate or by the individual company (NOTE: CFL reporting is only done in the aggregate).

Definition of Small Business

In addition to the above concern over the term "covered consumer," the draft proposed regulations use the same definition for "small business" as defined under Code of Civil Procedure section 1028.5, subdivision (c). This definition, pulled from an unrelated section of the California code, utilizes information that ILPA members typically do not collect from their small business customers. For example, determining whether a business is "independently owned and operated" and "dominant in its field of operation" is problematic as these are undefined terms, entirely subjective, and not part of a typical financing application. In addition, the definition includes different revenue thresholds for different industries. It is difficult for providers to determine which of their customers' financing data is required to be submitted in the reports.

This subjective, overly broad definition creates significant burdens for providers to comply with data reporting requirements. As such, we request simplifying the definition of small business to remove undefined terms such as dominant and independently owned, create one revenue threshold standard, and give providers the flexibility to calculate gross receipts based on data collected during the underwriting process.

We hope DFPI will consider these thoughtful comments when revising the proposed regulations for PRO 02-21 and look forward to continuing to work with the DFPI on this critical rulemaking process. If you have any questions, please do not hesitate to contact me at [REDACTED].

Best regards,

Scott Stewart, CEO

Innovative Lending Platform Association