FINAL STATEMENT OF REASONS

FOR THE PROPOSED ADOPTION OF REGULATIONS UNDER THE CALIFORNIA CONSUMER FINANCIAL PROTECTION LAW REGARDING COMMERCIAL FINANCIAL PRODUCTS AND SERVICES PRO 02-21

UPDATE OF INITIAL STATEMENT OF REASONS (§ 11346.9, subd. (a)(1))[1]

The text of these proposed regulations has changed from the text originally proposed. The Department of Financial Protection and Innovation modified the initial text and sought public comment on the modified text. This update of the information contained in the Initial Statement of Reasons (ISOR) describes all changes to the initial text and the purpose and necessity of each changed provision, as applicable. In proposing these regulations, the Department did not rely on any data or technical, theoretical, or empirical study, report, or similar document that was not previously identified or made available for public review. All references to regulations are to title 10 of the California Code of Regulations.

Nonsubstantive or Technical Changes

To account for subdivisions that were added or deleted, certain subdivisions have been renumbered. The purpose of this change is to provide regulations that are coherent and organized. Renumbering is necessary because properly numbered subdivisions are easily read and understood.

Section 1060. Definitions

Section 1060, subdivision (c). This subdivision was added to provide that "commercial financing transaction" means a consummated commercial financing transaction for which a disclosure is provided in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures regulations.[2] The purpose of this provision is to make the regulations more readable and easier for the public to understand. Using a defined term is necessary because it allows the regulations to avoid frequent repeating of a lengthy phrase. Another purpose of this provision is to provide clarity and guidance on the scope of the regulations. This definition is necessary because it narrows the scope of the data-reporting requirements to accommodate public comments that the proposed regulations should align with the Commercial Financing Disclosures law[3] and regulations, which minimizes additional regulatory burdens on covered providers who are also subject to that law and avoids imposing the burden of calculating annual percentage rates on persons that are not subject to that law.

[1] All further statutory references in the headings are to the Government Code.
[2] Cal. Code Regs., tit. 10, § 900 et seq.
[3] Fin. Code, § 22800 et seq.

Section 1060, subdivision (d)(1). This subdivision was formerly subdivision (c)(1) and was renumbered and modified to define "covered entity" rather than "covered consumer." The purpose of this change is to make the regulations more readable and easier for the public to understand. Using a defined term is necessary because it allows the regulations to avoid frequent repeating of a lengthy phrase. Changing the defined term to "covered entity" is necessary to avoid confusion that may arise if "consumer" is narrowly construed to refer to individuals rather than given its ordinary and common meaning, which is "one that consumes."

Section 1060, subdivision (e)(1). This subdivision was formerly subdivision (d) and was renumbered and modified to reflect the change of the defined term "covered consumers" to "covered entities."

Section 1060, subdivision (e)(2). This subdivision was added to provide that "covered provider" does not include any person exempted from the California Consumer Financial Protection Law (CCFPL) under Financial Code section 90002. The purpose of this provision is to define a term used in the regulations. This provision is necessary because it clarifies who is not subject to the regulations, by making explicit that the CCFPL's exemptions in Financial Code section 90002 apply to these regulations, which was a concern raised in public comments.

Section 1060, subdivision (f). This subdivision was formerly subdivision (e) and was renumbered.

Section 1060, subdivision (g). This subdivision was formerly subdivision (f) and was renumbered.

Section 1060, subdivision (h). This subdivision was formerly subdivision (g) and was renumbered.

Section 1060, subdivision (i). This subdivision was formerly subdivision (h) and was modified by deleting the definition referring to Code of Civil Procedure section 1028.5, subdivision (c), and adding a new definition. Under the new definition, "small business" means a business entity organized for profit with annual gross receipts of no more than $16,000,000 or the annual gross receipt level as biennially adjusted by the Department of General Services in accordance with Government Code section 14837, subdivision (d)(3), whichever is greater. The definition further provides that for the purpose of determining a business entity's annual gross receipts, a covered provider may rely on any relevant written representation by the business entity, including information provided in any application or agreement for commercial financing or other financial product or service.

The purpose of this provision is to define a term used in the regulations. The CCFPL does not define "small business." This modified definition is necessary because it addresses concerns in public comments that the original definition was too complex and difficult to apply. With simpler and fewer criteria, the modified definition minimizes the burden of determining whether one is a covered provider and what portion of a covered provider's business activity is subject to these regulations. Using a single receipts threshold is easier than using multiple industry-specific receipts thresholds and determining whether a business is independently owned and operated and not dominant in its field of operation. Annual gross receipts of $16 million is the current size

standard for small-business certification[4] under the Small Business Procurement and Contract Act,[5] which requires that a proportion of state agencies' purchases and contracts for goods and services be awarded to small businesses.[6] The Department of General Services is required to review and adjust the receipts threshold biennially to account for inflation.[7] The modified definition provides that the receipts threshold is the greater of $16 million or the biennially adjusted amount, which prevents the regulations from becoming outdated and ensures that they continue to further the purposes of the CCFPL as economic conditions change. To further reduce regulatory burden, the modified definition allows covered providers to use information they might already collect from customers for the purpose of determining their annual gross receipts.

Section 1060, subdivision (j). This subdivision was formerly subdivision (i) and was renumbered.

Section 1061. Unfair, Deceptive, and Abusive Acts and Practices

Section 1061, subdivision (a). This subdivision was modified by deleting "propose to engage" and adding "in connection with the offering or provision of commercial financing or another financial product or service to a covered entity." The purpose of this provision is to clarify when a covered provider is in violation of the law. The change is necessary because it avoids overbreadth, which was a concern raised in public comments.

Section 1061, subdivision (b)(1)(A). This subdivision was modified to reflect the change of the defined term "covered consumers" to "covered entities."

Section 1061, subdivision (b)(1)(B). This subdivision was modified to reflect the change of the defined term "covered consumers" to "covered entities."

Section 1061, subdivision (b)(1)(C). This subdivision was modified to reflect the change of the defined term "covered consumers" to "covered entities."

Section 1061, subdivision (b)(2). This subdivision was modified by changing "within the meaning of Business and Professions Code section 17200" to "in accordance with Business and Professions Code section 17200 and the case law thereunder." The purpose of this provision is to clarify the criteria used to determine when an act or practice is unfair. The change is necessary for the purpose of symmetry with subdivision (c)(2), the analogous provision that defines a deceptive act or practice. The change results in clearer, more understandable regulations.

Section 1061, subdivision (c)(1)(A). This subdivision was modified to reflect the change of the defined term "covered consumer" to "covered entity."

Section 1061, subdivision (c)(1)(B). This subdivision was modified to reflect the change of the

[4] Dept. of Gen. Services, Bulletin No. E-08-22: Announcing Biennial Review Adjustments to the Small Business Certification (SB) Size Standards: Gross Annual Receipts (GARs) (Aug. 16, 2022) <www.dgs.ca.gov/-/media/Divisions/PD/PTCS/Broadcast-Bulletins/2022/E-08-22-SB-cert-size-GARs.pdf>.

[5] Gov. Code, § 14835 et seq.

[6] Gov. Code, § 14836.

[7] Gov. Code, § 14837, subd. (d)(3).

defined term “covered consumer’s” to “covered entity’s.”

Section 1061, subdivision (c)(2). This subdivision was modified by changing “within the meaning of Business and Professions Code section 17200” to “in accordance with Business and Professions Code section 17200 and the case law thereunder.” The purpose of this provision is to clarify the criteria used to determine when an act or practice is deceptive. The change is necessary because it avoids confusion by reflecting that although Business and Professions Code section 17200 prohibits “fraudulent,” not “deceptive,” business acts or practices, case law under section 17200 recognizes that the term “fraudulent” addresses deceptive conduct.

Section 1061, subdivision (d)(1). This subdivision was modified to reflect the change of the defined term “covered consumer” to “covered entity.”

Section 1061, subdivision (d)(2)(A). This subdivision was modified to reflect the change of the defined term “covered consumer” to “covered entity.”

Section 1061, subdivision (d)(2)(B). This subdivision was modified to reflect the change of the defined term “covered consumer” to “covered entity.”

Section 1061, subdivision (d)(2)(C). This subdivision was modified to reflect the change of the defined term “covered consumer” to “covered entity.”

Section 1062. Annual Report

Section 1062, subdivision (a). This subdivision was formerly subdivision (a)(1) and (a)(2) and was renumbered and modified to reflect the deletion of subdivision (a)(2) and the change of the defined term “covered consumers” to “covered entities.” The purpose of this provision is to clarify who is covered by the reporting requirement. Deleting subdivision (a)(2) is necessary because it is rendered superfluous by the expansion of the scope of the exemption in subdivision (a)(1) that results from the new defined term “commercial financing transaction” in section 1060, subdivision (c).

Section 1062, subdivision (b). This subdivision was added to provide that “type of commercial financing” refers to one of the types of commercial financing listed in section 917, subdivision (a), of the Commercial Financing Disclosures regulations or, if the commercial financing does not the meet the definition of any of the listed types, an “Other” type. The purpose of this provision is to define a term used in the regulations. This definition is necessary because it clarifies, in response to several public comments, what “type of commercial financing” means, by referring explicitly to the types identified in the Commercial Financing Disclosures regulations. This definition also clarifies how covered providers should identify types of commercial financing that do not meet the definition of any of the listed types.

Section 1062, subdivision (c). This subdivision was formerly subdivision (b) and was renumbered and modified by specifying 2025 as the first year that annual reports will be due, changing “each covered provider” to “any covered provider who offers commercial financing.” The purpose of this provision is to specify the procedures that covered providers must follow for the reporting of information about their provision of commercial financial products and services.

The 2025 date is necessary because it clarifies when the first annual report will be due, which was a concern raised in several public comments. Changing "each" to "any" is necessary because it promotes readability. Adding "who offers commercial financing" after "covered provider" is necessary because it helps covered providers more easily understand that if they do not offer commercial financing, they are not required to submit an annual report.

Section 1062, subdivision (c)(2). This subdivision was formerly subdivision (b)(2) and was renumbered and modified to reflect the change of the defined term "covered consumers" to "covered entities." It was also modified by deleting "or other financial product or service" and specifying "commercial financing transactions" instead of "transactions." The provision was also modified by adding that the "dollar amount" of a commercial-financing transaction is the "amount financed" as defined in section 900, subdivision (a)(1), of the Commercial Financing Disclosures regulations.

The purpose of this provision is to specify the information that covered providers must provide in the annual report. Deleting the reference to "other" financial products or services and specifying "commercial financing transactions" instead of "transactions" is necessary because the changes clarify, in response to several public comments, that only commercial-financing transactions are required to be reported. Defining "dollar amount" by referring to the definition of "amount financed" from the Commercial Financing Disclosures regulations is necessary because it clarifies how to determine the dollar amount of a transaction for each of the broadly different types of commercial financing.

Section 1062, subdivision (c)(3). This subdivision was formerly subdivision (b)(3) and was renumbered and modified to reflect the change of the defined term "covered consumers" to "covered entities." It was also modified by deleting "or other financial product or service" and specifying "commercial financing transactions" instead of "transactions." The provision was also modified to direct covered providers to use the definition of "amount financed" in section 900, subdivision (a)(1), of the Commercial Financing Disclosures regulations instead of "the regulations adopted under Financial Code section 22804." The provision was also modified by deleting the "over $500,000" interval.

The purpose of this provision is to specify the information that covered providers must provide in the annual report. Deleting the reference to "other" financial products or services and specifying "commercial financing transactions" instead of "transactions" is necessary because the changes clarify, in response to several public comments, that only commercial-financing transactions are required to be reported. In the guidance regarding "amount financed," changing the general reference to the Commercial Financing Disclosures regulations to a specific citation is necessary because a specific citation is clearer and more direct. Deleting the "over $500,000" interval is necessary because it accommodates public comments that the proposed regulations should align with the Commercial Financing Disclosures law and regulations.

Section 1062, subdivision (c)(4). This subdivision was formerly subdivision (b)(4) and was renumbered and modified by deleting "or other financial product or service" and changing the name of the required data from "total cost of financing expressed as an annualized rate" to "annual percentage rate" (APR). The provision was also modified by changing the guidance regarding calculating and reporting the required data so that covered providers need not

recalculate the APR of each transaction but instead may use already calculated APRs that were disclosed to customers in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures regulations. The provision was also modified by adding that for a given type of commercial financing and dollar-amount interval, if a covered provider was not required to calculate or disclose APRs, it must so indicate.

The purpose of this provision is to specify the information that covered providers must provide in the annual report. Deleting the reference to "other" financial products or services is necessary because it clarifies, in response to several public comments, that only commercial-financing transactions are required to be reported. Changing the name of the required data from "total cost of financing expressed as an annualized rate," which appears in Financial Code section 22804, to "annual percentage rate," which appears in the Commercial Financing Disclosures regulations, is necessary because the term more clearly indicates to covered providers the proposed regulations' alignment with the Commercial Financing Disclosures regulations. The modified guidance regarding calculating and reporting is necessary because it reduces the burden of complying with these regulations, especially for those who are also subject to the Commercial Financing Disclosures law and regulations, which was a concern raised in public comments. The requirement that covered providers explicitly indicate that they are not required to report certain information is necessary because it enables the Department to understand the reason for an absence of reported data.

Section 1062, subdivision (d). This subdivision was formerly subdivision (c) and was renumbered and modified. For covered providers who are licensed under the California Financing Law (CFL),[8] instead of requiring that they not report information that they report in their CFL annual report, this provision requires that they not report information for activity conducted under the authority of that CFL license.

The purpose of this provision is to specify the information that covered providers must provide in the annual report. The change is necessary because it clarifies, in response to public comments, that covered providers who are also CFL licensees should not report CFL activity in their annual reports under these regulations. The original provision was unclear about whether a covered provider would be required to submit a report under section 1062 if it reported all information on its CFL report instead.

SUMMARY OF AND RESPONSE TO COMMENTS SUBMITTED DURING INITIAL 45-DAY COMMENT PERIOD (JUNE 24 TO AUGUST 8, 2022)

The initial proposed regulations were made available for public review and comment from June 24 to August 8, 2022. The following persons submitted comments to the Department for this period:

1. Moorari K. Shah, Sheppard, Mullin, Richter & Hampton LLP, dated July 26, 2022.
2. Moorari K. Shah, Sheppard, Mullin, Richter & Hampton LLP, dated August 2, 2022.
3. Jeff DeVine, Director, California Community Banking Network, dated August 3, 2022.
4. Christina J. Grigorian, Katten Muchin Rosenman LLP, dated August 5, 2022.

[8] Fin. Code, § 22000 et seq.

5. Scott Riehl, Vice President, State Government Relations, Equipment Leasing and Finance Association, dated August 8, 2022.
6. Michael Jesse Carlson, Senior Vice President and General Counsel, Strategic Funding Source, Inc., doing business as Kapitus, dated August 8, 2022.
7. Deveron Gibbons, Executive Director, Revenue Based Finance Coalition, received August 8, 2022.
8. Thomas L. Dresslar, dated August 8, 2022.
9. Joseph D. Looney, General Counsel, Small Business Financial Solutions, LLC, doing business as RapidAdvance, dated August 8, 2022.
10. Matthew Kownacki, Director, State Research and Policy, American Financial Services Association, dated August 8, 2022.
11. Responsible Business Lending Coalition et al., dated August 8, 2022.
12. Tom R. Normandin, Prenovost, Normandin, Dawe & Rocha, A Professional Corporation, dated August 8, 2022.
13. Matt Tremblay, Senior Manager, State Government Relations, Electronic Transactions Association, dated August 8, 2022.
14. Scott Stewart, Chief Executive Officer, Innovative Lending Platform Association, dated August 8, 2022.
15. Robert C. Fellmeth, Executive Director, Centers for Public Interest Law, University of San Diego School of Law, dated August 9, 2022.

Comment letter 1.1 – Moorari K. Shah, Sheppard, Mullin, Richter & Hampton LLP ("Sheppard Mullin") (dated July 26, 2022)

Comment 1.1: Sheppard Mullin notes that the proposed regulations require annual reporting of information by "type of commercial financing or other financial product or service" but that some of the required information is incompatible with certain "other" financial products or services as defined by the proposed regulations. Sheppard Mullin recommends several ways to address this issue.

Response to comment 1.1: The Department amended section 1062, subdivision (b)(2), (b)(3), and (b)(4) (since renumbered as subdivision (c)(2), (c)(3), and (c)(4)), by deleting "or other financial product or service" and deleting subdivision (a)(2) to clarify that only commercial-financing transactions are required to be reported.

Comment letter 1.2 – Moorari K. Shah, Sheppard, Mullin, Richter & Hampton LLP ("Sheppard Mullin") (dated August 2, 2022)

Comment 1.2: Sheppard Mullin recommends that the proposed regulations clarify that subsidiaries of banks are exempt from the CCFPL. Sheppard Mullin acknowledges that although the CCFPL exempts banks and bank holding companies,[9] it does not exempt bank subsidiaries. Sheppard Mullin notes that bank subsidiaries engaging only in commercial lending are not licensed under the California Financing Law (CFL)[10] and therefore would not qualify for the

[9] Fin. Code, § 90002, subd. (c).
[10] Fin. Code, § 22000 et seq.

exemption from data reporting for CFL licensees in section 1062, subdivision (c).

Response to comment 1.2: The Department did not make any changes in response to this comment. The proposed regulations are not intended to exempt from any requirement persons or activities that are not exempted by the CCFPL. The recommended change would result in a regulation that improperly impairs the scope of the CCFPL. The data-reporting requirement is intended to cover commercial financing that is not subject to the CFL.

Comment letter 1.3 – Jeff DeVine, Director, California Community Banking Network (CCBN)

Comment 1.3: CCBN recommends that the definition of "covered provider" not include state-chartered banks, which are exempted from the CCFPL.

Response to comment 1.3: The Department amended the definition of "covered provider" to clarify that the CCFPL's exemptions in Financial Code section 90002 apply.

Comment letter 1.4 – Christina J. Grigorian, Katten Muchin Rosenman LLP ("Katten")

Comment 1.4: Katten recommends that the data-reporting requirements exempt third-party finance companies that provide trade credit to small businesses in connection with retail installment sales at an annual percentage rate of less than 36%. Alternatively, Katten recommends that such providers be excluded from the definition of "covered provider."

Response to comment 1.4: The Department narrowed the scope of the data-reporting requirements by adding a new definition of "commercial financing transaction" that captures only consummated commercial-financing transactions for which disclosures were provided in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures regulations.[11] This change results in the requested outcome: if the financial product described in the comment is not "commercial financing" as defined in Financial Code section 22800, subdivision (d), it would not be subject to the data-reporting requirements of the proposed regulations. The Department declined to adopt the alternative recommendation because doing so would exempt the described providers from the proposed regulations entirely rather than from only the data-reporting requirements.

Comment letter 1.5 – Scott Riehl, Vice President, State Government Relations, Equipment Leasing and Finance Association (ELFA)

Comment 1.5.1: ELFA recommends that the proposed regulations specify when data collection must start and when the first annual report will be due. Specifically, ELFA recommends that data collection begin no sooner than January 1, 2024, with the first report due no sooner than March 15, 2025.

Response to comment 1.5.1: The Department amended the proposed regulations to specify that the first report is due in 2025.

[11] Cal. Code Regs., tit. 10, § 900 et seq.

Comment 1.5.2: ELFA recommends that the definitions of small business, nonprofit, and family farm be simplified.

Response to comment 1.5.2: The Department did not make any changes in response to this comment. The comment did not describe with sufficient specificity how the regulations should be changed. In any event, in response to other comments on the definition of "small business," the Department substantially amended that definition with the overall effect of simplifying it.

Comment 1.5.3: ELFA recommends that the proposed regulations allow covered providers to rely on a customer's representation that it is a small business, nonprofit, or family farm.

Response to comment 1.5.3: The Department did not make any changes in response to this comment. Allowing covered providers to rely on customers' self-representations could lead to misidentifications of their status as a small business, nonprofit, or family farm, which would frustrate the purposes and intent of the CCFPL. In response to other comments, however, the Department amended the definition of "small business" to allow covered providers to rely on any relevant written representation by the business for the purpose of determining its annual gross receipts.

Comment 1.5.4: ELFA recommends that the definition of "covered provider" conform to the CCFPL's definition of "covered person" and incorporate by reference the exemptions in Financial Code section 90002.

Response to comment 1.5.4: The Department amended the definition of "covered provider" to clarify that the CCFPL's exemptions in Financial Code section 90002 apply. The Department declined to conform the definition to the CCFPL's definition of "covered person" in section 90005, subdivision (f), because that definition is overbroad for the purpose of these regulations, which govern financial products and services to a specific group of recipients, namely, small businesses, nonprofits, and family farms.

Comment 1.5.5: ELFA recommends that the proposed regulations' language be consistent with the Commercial Financing Disclosures regulations.[12]

Response to comment 1.5.5: The Department amended the proposed regulations as recommended, including by changing "total cost of financing expressed as an annualized rate" to "annual percentage rate" and defining that term and others, such as "type of commercial financing" and "amount financed," by referring to specific provisions in the Commercial Financing Disclosures regulations.

Comment 1.5.6: ELFA recommends that commercial-financing transactions that are exempt from the Commercial Financing Disclosures regulations should also be exempt from the proposed regulations' data-reporting requirements—for example, transactions over $500,000, transactions secured by real property, and car-dealer-inventory financing transactions.

Response to comment 1.5.6: The Department amended the data-reporting requirements by removing the "over $500,000" interval and added a new definition of "commercial financing

[12] Cal. Code Regs., tit. 10, § 900 et seq.

transaction" that captures only consummated commercial-financing transactions for which disclosures were provided in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures regulations.

Comment 1.5.7: ELFA recommends that section 1062, subdivision (c), provide that a licensed finance lender's or broker's compliance with annual-reporting requirements under Financial Code section 22159 of the California Financing Law (CFL) constitutes compliance with the annual-reporting requirements under the proposed regulations.

Response to comment 1.5.7: The Department declined to amend section 1062, subdivision (c), as recommended but did amend the provision to provide that covered providers that are also CFL licensees should not report CFL activity in annual reports submitted under the proposed regulations. This change clarifies that the intent of the data-reporting requirement is to capture commercial financing that is done outside the authority of the CFL license.

Comment letter 1.6 – Michael Jesse Carlson, Senior Vice President and General Counsel, Strategic Funding Source, Inc., doing business as Kapitus

Comment 1.6.1: Kapitus recommends changing "covered consumer" to "covered entity" throughout the regulations.

Response to comment 1.6.1: The Department amended the proposed regulations as recommended.

Comment 1.6.2: Kapitus recommends that the definition of "covered provider" clarify that the CCFPL's exemptions in Financial Code section 90002 apply.

Response to comment 1.6.2: The Department amended the proposed regulations as recommended.

Comment 1.6.3: Kapitus recommends changes to the definition of "financial product or service" in section 1060, subdivision (f) (since renumbered to subdivision (g)). Kapitus recommends changing the "consumer" portion of the definition so that instead of providing that "consumer" also includes any organization or entity as enumerated nonexhaustively, the definition should provide that "consumer" is replaced with "covered entity." Kapitus also recommends deleting the definition's treatment of "consumer financial product or service."

Response to comment 1.6.3: The Department did not make any changes in response to this comment. Although the recommendation as to "consumer" may be an acceptable alternative to the "consumer" portion of the definition, the definition's treatment of "consumer financial product or service" is necessary to clarify that a person engaged in the business of offering or providing to a small business, nonprofit, or family farm any financial product or service listed in Financial Code section 90005, subdivision (k), is a covered provider under the proposed regulations even if the product or service is intended primarily for commercial purposes.

Comment letter 1.7 – Deveron Gibbons, Executive Director, Revenue Based Finance Coalition (RBFC)

Comment 1.7: RBFC recommends that the requirement to report total cost of financing be deleted because requiring such data is not reasonably necessary to carry out the purpose of the CCFPL. The purpose of the enabling statute is to protect small businesses by eliminating unfair, deceptive, and abusive acts and practices (UDAAP) and requiring reporting of data on the total cost of financing does not help the Department achieve this goal. Regulating the cost of commercial financing is not a purpose of the CCFPL. By adopting the proposed UDAAP definitions, the Department has already achieved its stated goal of improving accountability and transparency in California's financial marketplace and to protect residents from abuses. Information on the total cost of financing does not serve the purpose of detecting and assessing risks to small businesses as authorized in Financial Code section 90010, subdivision (b).

Response to comment 1.7: The Department did not make any changes in response to this comment. Financial Code section 90009, subdivision (e), authorizes rulemaking not only on UDAAP but also on data collection and reporting on the provision of commercial financing. Regulating the cost of commercial financing is indeed not a purpose of the CCFPL, but as the comment acknowledges, increasing accountability and transparency in the marketplace is a purpose. Only defining UDAAP in the commercial-financing context does not carry out this purpose. The goal of increasing accountability and transparency in California's financial marketplace requires that the Department collect data about that marketplace, including information about the availability and cost of credit to small businesses, nonprofits, and family farms. The comment's discussion of the purpose of detecting and assessing risks to small businesses in Financial Code section 90010, subdivision (b), is not relevant because the proposed regulations are based on a different provision of the CCFPL—section 90009, subdivision (e).

Comment letter 1.8 – Thomas L. Dresslar

Comment 1.8.1: Dresslar approves of the proposed definitions of unfair, deceptive, and abusive acts or practices as sound and workable, noting that the definitions avoid problems of overbreadth and vagueness that were present in earlier versions.

Response to comment 1.8.1: The Department appreciates this comment of support. No change was made in response to this comment because it concurred with the proposed regulations.

Comment 1.8.2: Dresslar recommends that "small business" be defined as businesses that are independently owned and operated and that obtain commercial financing or other financial products or services valued at $500,000 or less. Regarding the definition of "small business" in Code of Civil Procedure section 1028.5, Dresslar notes that section 1028.5 was enacted to allow small businesses that sue state regulatory agencies to collect litigation costs if they prevail and questions whether using section 1028.5's definition is appropriate given its legislative context. Dresslar objects to industry-specific receipts thresholds. Dresslar notes that under the federal small-business regulatory regime, on which section 1028.5 is based, the Small Business Administration reviews receipts caps every five years, and if inflation has significantly eroded a cap's value, it proposes a rule to increase the cap amount. Dresslar notes that the proposed regulations do not clearly address whether the Department plans to follow that course.

Response to comment 1.8.2: The Department substantially amended the definition of "small business" in section 1060, subdivision (h) (since renumbered to subdivision (i)), to accommodate this recommendation. The definition no longer uses industry-specific receipts thresholds and instead uses a single threshold of the greater of $16 million annual gross receipts or the annual gross receipt level as biennially adjusted by the Department of General Services. The Department declined to include "independently owned and operated" in the definition to minimize the burden of determining whether a person or transaction is subject to the proposed regulations.

Comment 1.8.3: Dresslar notes that the second and third categories of required data refer to "amount financed" and that it is unclear how that term applies to "other financial product or service."

Response to comment 1.8.3: Although this comment is an observation rather than a specific recommendation, the Department deleted "or other financial product or service" from section 1062, subdivision (b)(2) and (b)(3) (since renumbered as subdivision (c)(2) and (c)(3)).

Comment 1.8.4: Dresslar notes that the requirement to report data regarding the "total cost of financing expressed as an annualized rate" refers to the 2018 commercial financing disclosure law and further notes that that law's requirement to disclose the total cost of financing expressed as an annualized rate expires at the end of 2023 unless extended by legislation. Dresslar notes that this circumstance should be kept in mind as the rulemaking process continues.

Response to comment 1.8.4: The Department acknowledges the note. The Department did not make any changes in response to this comment because it is an observation rather than a recommendation to change the regulation.

Comment 1.8.5: Dresslar recommends that section 1062 be amended to specify that covered providers' annual reports "shall be made available to the public for inspection."

Response to comment 1.8.5: The Department did not make any changes in response to this comment. The authorizing statute for the proposed regulations, Financial Code section 90009, subdivision (e), does not mandate that the data or reports received by the Department be made available to the public.

Comment 1.8.6: Dresslar recommends that section 1062 be amended to require that the Department publish an annual composite report based on covered providers' individual reports.

Response to comment 1.8.6: The Department did not make any changes in response to this comment. The authorizing statute for the proposed regulations, Financial Code section 90009, subdivision (e), does not mandate that the data or reports received by the Department be aggregated into a composite report that is made available to the public.

Comment 1.8.7: Dresslar recommends that section 1062 be amended to give the Department discretion to augment the reporting requirements with "relevant information the Commissioner reasonably requires concerning the business and operations" of covered providers.

Response to comment 1.8.7: The Department did not make any changes in response to this

comment. A supplement to or revision of any standard of general application intended to implement the CCFPL is a regulation that must be adopted in accordance with the Administrative Procedure Act (APA).[13] The proposed language is not consistent with the Department's obligations under the APA.

Comment letter 1.9 – Joseph D. Looney, General Counsel, Small Business Financial Solutions, LLC, doing business as RapidAdvance

Comment 1.9.1: RapidAdvance states that the proposed regulations alter the definitions of "covered consumer" and "financial product or service" to include commercial financing and commercial-financing providers. The proposed regulations inappropriately expand the scope and authority of the CCFPL to include commercial financing and providers even though they were not included in AB 1864, the bill that created the CCFPL. The proposed regulations should be "removed" because they violate the consistency and necessity standards of the Administrative Procedure Act (APA) and alter or amend the governing statute and enlarge or impair its scope.

Response to comment 1.9.1: The Department did not make any changes in response to this comment. Section 90009, subdivision (e), of the CCFPL explicitly authorizes rulemaking on the offering and provision of commercial financing to small businesses, nonprofits, and family farms. As described in the ISOR and this Final Statement of Reasons, the proposed regulations must include certain definitional provisions to harmonize the CCFPL's clear grant of rulemaking authority over commercial financing with the CCFPL's definitions of "financial product or service" and related terms, which generally focus on noncommercial transactions. The definitional provisions of the proposed regulations apply only to the regulations and serve to eliminate any interpretive ambiguities that might arise if the regulations merely incorporated the CCFPL's definitions wholesale. Thus, the proposed regulations do not alter or amend the governing statute or enlarge or impair its scope.

Comment 1.9.2: RapidAdvance recommends changing the definition of "covered consumer" to more accurately reflect the CCFPL's statutory language.

Response to comment 1.9.2: The Department changed "covered consumer" to "covered entity" throughout the regulations.

Comment 1.9.3: RapidAdvance recommends changing the definition of "covered provider" to explicitly include brokers.

Response to comment 1.9.3: The Department did not make any changes in response to this comment. "Covered provider" includes, in addition to providers of commercial financing, providers of another "financial product or service," which includes brokering extensions of credit.[14]

Comment 1.9.4: RapidAdvance seeks additional guidance and clarity regarding the definition of an unfair act or practice in section 1061, subdivision (b)(1). According to RapidAdvance, the proposed regulations provide no definition, examples, or guidance as to what would constitute an

[13] Gov. Code, §§ 11340.5, subd. (a), 11342.600.
[14] Fin. Code, § 90005, subd. (k)(1).

injury.

Response to comment 1.9.4: The Department did not make any changes in response to this comment. The proposed regulations provide general guidance through longstanding standards that are familiar to the regulated community. Further guidance interpreting these standards, including what constitutes substantial injury, is provided in state and federal case law.

Comment 1.9.5: RapidAdvance seeks additional clarity regarding the definition of an abusive act or practice in section 1061, subdivision (d)(1). What constitutes interference with a small business's ability to understand a financing term or condition? Is a small business's own ignorance of a term or condition considered interference? If a covered provider does not simplify the language of financing contracts sufficiently but does the best it can, does that constitute interference? If a covered provider provides an APR and the small business does not understand the concept of APR, is there liability?

Response to comment 1.9.5: The Department did not make any changes in response to this comment. The proposed regulations provide general guidance through established standards that are familiar to the regulated community and are intended to apply to a wide range of factual circumstances. This comment raises specific legal questions about whether the proposed regulations apply to specific facts.

Comment 1.9.6: RapidAdvance seeks additional guidance and clarity regarding the definition of an abusive act or practice in section 1061, subdivision (d)(2). According to RapidAdvance, the prohibition against taking unreasonable advantage of a small business is broad and vague and does not provide definitions, examples, or specifics. If a covered provider asks a small business if it understands the costs and conditions of the financing and it says yes when it actually did not understand, is the covered provider still liable? What does it mean to take unreasonable advantage of a small business's inability to protect its interests in selecting or using commercial financing? Is a covered provider liable if a third party, such as a broker, engaged in conduct that made a small business unreasonably rely on terms and costs that were not actually the terms and costs of the financing?

Response to comment 1.9.6: The Department did not make any changes in response to this comment. Section 1061, subdivision (d)(2), provides that one form of abusive conduct is taking unreasonable advantage of a covered entity and specifies three examples in subdivision (d)(2)(A), (d)(2)(B), and (d)(2)(C). The proposed regulations provide general guidance through established standards that are familiar to the regulated community and are intended to apply to a wide range of factual circumstances. This comment raises specific legal questions about whether the proposed regulations apply to specific facts.

Comment 1.9.7: RapidAdvance recommends that the annual report required under the CFL be changed to include non-CFL products, so that providers subject to the proposed regulations who also have CFL licenses can submit one report. Alternatively, RapidAdvance recommends that the annual report required under the proposed regulations be changed so that it is similar to the CFL annual report. RapidAdvance currently provides data about merchant cash advances on its CFL annual report and asks whether it need not also report such data under the proposed regulations.

Response to comment 1.9.7: The Department declined to change the CFL annual report because it is not authorized to do so by the enabling statute for the proposed regulations. The Department declined to make the changes recommended in the alternative, which were construed to mean that the annual report required under the proposed regulations ("CCFPL annual report") should allow reporting of both CCFPL and non-CCFPL products, in the same way that the CFL annual report allows reporting of both CFL and non-CFL products. Instead, the Department amended section 1062, subdivision (c) (since renumbered to subdivision (d)), to require that covered providers who are also CFL licensees should not report CFL activity in their CCFPL annual report. In other words, only CCFPL products should be reported on the CCFPL annual report.

Comment 1.9.8: RapidAdvance recommends that the CFL annual report and CCFPL annual report be made consistent regarding the sorting of transaction data by dollar-amount intervals. For example, because the CFL annual report does not sort by dollar-amount intervals, neither should the CCFPL annual report. RapidAdvance asks whether the Department's intent is to avoid having covered providers report duplicative information on both reports.

Response to comment 1.9.8: The Department declined to remove the dollar-amount intervals from the data-reporting requirements but amended section 1062, subdivision (c) (since renumbered to subdivision (d)), to more clearly define how to report data that might be provided on both the CCFPL and CFL annual reports.

Comment 1.9.9: RapidAdvance recommends that the CFL annual report be changed so that the cost of financing expressed as an annualized rate is reported there in the same manner as in the CCFPL annual report. The CFL annual report uses annualized-rate intervals for sorting data, while the CCFPL annual report does not, and the "method for disclosure" of annualized rates is different for each report.

Response to comment 1.9.9: The Department declined to change the CFL annual report because it is not authorized to do so by the enabling statute for the proposed regulations. Instead, the Department amended section 1062, subdivision (c) (since renumbered to subdivision (d)), to more clearly define how to report data that might be provided on both the CCFPL and CFL annual reports. The Department also amended section 1062, subdivision (b)(4) (since renumbered to subdivision (c)(4)), so that it more clearly defines the total cost of financing expressed as an annualized rate, since renamed to "annual percentage rate," by referring to specific provisions in the Commercial Financing Disclosures regulations.[15]

Comment letter 1.10 – Matthew Kownacki, Director, State Research and Policy, American Financial Services Association (AFSA)

Comment 1.10.1: AFSA recommends that the proposed regulations clarify that any entity exempt from the CCFPL is also exempt from the proposed regulations.

Response to comment 1.10.1: The Department amended the definition of "covered provider" to clarify that the CCFPL's exemptions in Financial Code section 90002 apply.

Comment 1.10.2: AFSA notes that car-dealer-inventory financing (also called floorplan

[15] Cal. Code Regs., tit. 10, § 900 et seq.

financing) transactions are exempt from the Commercial Financing Disclosures law.[16] This and other exemptions indicate the Legislature's recognition that the commercial financing disclosure requirements may not be a fit for certain types of transactions. Thus, the proposed regulations are not a fit for floorplan financing and other financing to car dealers and do not make clear which entities may be subject to their requirements.

Response to comment 1.10.2: The Department did not make any changes in response to this comment. The comment did not describe with sufficient specificity how the regulations should be changed to accommodate its objection. In any event, the Department narrowed the scope of the data-reporting requirements by adding a new definition of "commercial financing transaction" that captures only consummated commercial-financing transactions for which disclosures were provided in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures regulations.

Comment 1.10.3: AFSA recommends that the "consumer" portion of the "financial product or service" definition, which nonexhaustively lists examples of types of entities, be revised to include only entities that "truly meet" the "small business" definition—namely, businesses that are independently owned and operated, are not dominant in their field of operation, and are of a smaller industry size according to annual receipts.

Response to comment 1.10.3: The Department did not make any changes in response to this comment. The comment did not specify which types of entities "truly meet" the definition of "small business," and, in any event, no one type of entity necessarily is or is not a small business as defined by the proposed regulations. The definition simply lists examples of types of organizations or entities.

Comment 1.10.4: AFSA recommends that the proposed regulations apply only to commercial financing of $250,000 or less. AFSA states that the Legislature's goal with the proposed regulations is to protect small businesses and that financing for these customers tends to be smaller.

Response to comment 1.10.4: The Department did not make any changes in response to this comment. The comment did not adequately explain why the threshold amount in the proposed regulations should be lower than the threshold amount specified by the Legislature in the Commercial Financing Disclosures law, $500,000.[17]

Comment 1.10.5: AFSA recommends that floorplan financing be exempted from data reporting because the information required to be reported is unworkable with the nature of the product and would result in a significant compliance burden.

Response to comment 1.10.5: The Department narrowed the scope of the data-reporting requirements by adding a new definition of "commercial financing transaction" that captures only consummated commercial-financing transactions for which disclosures were provided in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures

[16] Fin. Code, § 22800 et seq.
[17] Fin. Code, § 22800, subd. (n).

regulations.

Comment 1.10.6: AFSA states that it is not clear whether "type of commercial financing or other financial product or service" in section 1062, subdivision (b) (since renumbered to subdivision (c)), refers to the categories of covered consumers (small business, nonprofit, family farm).

Response to comment 1.10.6: The Department added a new definition of "type of commercial financing" in section 1062 that refers to the types of commercial financing listed in section 917, subdivision (a), of the Commercial Financing Disclosures regulations.

Comment letter 1.11 – Responsible Business Lending Coalition et al. (collectively, "RBLC")

Comment 1.11.1: RBLC strongly supports the promulgation of the Department's proposed definitions for unfair, deceptive, and abusive acts and practices (UDAAP) in the provision of commercial financing to small businesses, nonprofits, and family farms.

Response to comment 1.11.1: The Department appreciates the comment of support regarding the proposed UDAAP definitions. No change was made in response to this comment because it concurred with the proposed regulations.

Comment 1.11.2: RBLC recommends clarifying the Department's ability to bring cases in superior court, which will help deter unlawful conduct and provide redress when such conduct occurs.

Response to comment 1.11.2: The Department did not make any changes in response to this comment. Section 90013 of the CCFPL clearly authorizes the Department to bring a civil action in the superior court to enforce compliance with the CCFPL, including any rule or order.

Comment 1.11.3: RBLC recommends changes to the definition in section 1061, subdivision (c)(2), of a deceptive act or practice that refers to Business and Professions Code section 17200 so that the definition accurately reflects the language of section 17200 and related case law. For purposes of symmetry, RBLC recommends making the same changes to the analogous provision in section 1061, subdivision (b)(2), that defines an unfair act or practice.

Response to comment 1.11.3: The Department amended section 1061, subdivisions (b)(2) and (c)(2) as recommended.

Comment 1.11.4: RBLC applauds the Department for collecting data on the cost of small-business financing in the form of APR rather than dollar cost.

Response to comment 1.11.4: The Department appreciates this comment of support. No change was made in response to this comment because it concurred with the proposed regulations.

Comment 1.11.5: RBLC recommends that the regulations recognize the importance of data reporting to enable the Department to regulate the financing market (1) to encourage responsible innovation grounded in competition to provide better-priced, better-quality products, (2) to curb predatory practices, and (3) to ensure that members of the public and stakeholders can monitor trends and issues along with the Department.

Response to comment 1.11.5: The Department did not make any changes in response to this comment. The comment did not describe with sufficient specificity how the regulations should be changed to "recognize the importance of data reporting" in achieving the three identified purposes. In any event, the proposed regulations already recognized the importance of data reporting. As stated in the ISOR, the data collected under these regulations will enable the Department to compare covered providers and their products, as well as to identify and monitor market attributes such as size, growth, segmentation, anomalies, trends, and the availability and cost of credit. The data will also aid the Department in preparing its statutorily required annual reports to the public and to the Legislature under sections 90018 and 90009.5, subdivision (d), respectively. To the extent the comment recommends that the regulations be changed to make the data and reports available to the public, the Department declines to do so because the authorizing statute does not so mandate.

Comment 1.11.6: RBLC recommends that merchant-cash-advance (MCA) providers that use the underwriting method to calculate APRs in accordance with section 931 of the Commercial Financing Disclosures regulations be required to report data for actual retrospective APRs in addition to data for disclosed APRs. RBLC states that requiring MCA providers to report retrospective-APR data will ensure that they are held accountable for conducting accurate internal audits. Requiring this additional data would also help the Department assess whether the accuracy-tolerance thresholds specified in the Commercial Financing Disclosures rules are too restrictive or permissive.

Response to comment 1.11.6: The Department did not make any changes in response to this comment. The proposed regulations carry out the purposes and intent of the CCFPL by yielding useful data for market monitoring while imposing uniform compliance requirements on covered providers. Although the proposed regulations are related to the Commercial Financing Disclosure law, ensuring compliance with that law is not a purpose of the CCFPL. The Department agrees that it should consider various alternatives for ensuring compliance with the Commercial Financing Disclosure regulations, but such consideration is beyond the scope of this rulemaking.

Comment letter 1.12 – Tom R. Normandin, Prenovost, Normandin, Dawe & Rocha, A Professional Corporation ("Normandin")

Comment 1.12.1: Normandin recommends that the proposed regulations specifically exempt finance lenders licensed under the California Financing Law (CFL)[18] by adding the following language to California Code of Regulations, title 10, chapter 3, subchapter 4: "This subchapter shall not apply to any person licensed as a finance lender under Division 9 (commencing with Section 22000) of the Financial Code."

Response to comment 1.12.1: The Department amended the definition of "covered provider" to clarify that the CCFPL's exemptions in Financial Code section 90002 apply. This change clarifies that all the exemptions in section 90002 apply, not only the exemption for CFL-licensed lenders. The change also more appropriately places this clarification in subchapter 4, article 4, where the proposed regulations reside, rather than in subchapter 4.

[18] Fin. Code, § 22000 et seq.

Comment 1.12.2: Normandin recommends that to the extent that the proposed regulations are being promulgated under the Commercial Financing Disclosures law,[19] they should clarify that that law's exemption for car-dealer-inventory financing (also called floorplan financing) transactions applies. Normandin proposes that language substantially similar to Financial Code section 22801, subdivision (d), be added to California Code of Regulations, title 10, chapter 3, subchapter 4.

Response to comment 1.12.2: The Department narrowed the scope of the data-reporting requirements by adding a new definition of "commercial financing transaction" that captures only consummated commercial-financing transactions for which disclosures were provided in accordance with section 920, subdivision (a), of the Commercial Financing Disclosures regulations. The change also more appropriately places this clarification in subchapter 4, article 4, where the proposed regulations reside, rather than in subchapter 4.

Comment letter 1.13 – Matt Tremblay, Senior Manager, State Government Relations, Electronic Transactions Association (ETA)

Comment 1.13.1: ETA objects to the proposed regulations because they "apply consumer regulations to commercial entities" and, without justification, conflate lending to individual consumers with lending to commercial borrowers, who "are, by definition, more sophisticated and distinct from the average consumer borrower."

Response to comment 1.13.1: The Department did not make any changes in response to this comment, which was construed as an objection to section 1061's prohibition against unfair, deceptive, or abusive acts and practices (UDAAP) in connection with the offering or provision of commercial financing to small businesses, nonprofits, and family farms. The comment did not describe with sufficient specificity how the regulations should be changed to accommodate its objection. The Department does not concede that small-business borrowers "are, by definition, more sophisticated . . . [than] the average consumer borrower." However, even if this were true, ETA does not explain why protecting small-business borrowers from unfair, deceptive, and abusive acts and practices is inappropriate. To the extent that the comment recommended eliminating the UDAAP prohibition altogether, it objected to the underlying statute, Financial Code section 90009, subdivision (e), rather than to the way the Department proposed to implement it.

Comment 1.13.2: ETA states that in describing the anticipated benefits of the proposed regulations in the ISOR, the Department provided no evidence or research to show discriminatory access or unfair competition as a result of UDAAP in the provision of commercial financing.

Response to comment 1.13.2: The Department did not make any changes in response to this comment. The comment did not describe with sufficient specificity how the regulations should be changed to accommodate its objection. In accordance with the APA, the ISOR and FSOR describe the purpose and necessity of each provision and the information relied on by the Department to propose the regulations, including comments from interested parties, studies, and

[19] Fin. Code, § 22800 et seq.

reports.

Comment 1.13.3: ETA recommends that "propose to engage in" be deleted from section 1061's prohibition against UDAAP.

Response to comment 1.13.3: The Department amended section 1061, subdivision (a), by deleting "or propose to engage in" and adding "in connection with the offering or provision of commercial financing or another financial product or service to a covered entity."

Comment 1.13.4: ETA recommends that the proposed regulations allow covered providers to rely on a customer's specific representation that its activities are principally directed or managed from California.

Response to comment 1.13.4: The Department did not make any changes in response to this comment. The proposed regulations already provided what ETA sought: section 1060, subdivision (d)(2), allows covered providers to rely on "any relevant written representation" by a customer.

Comment 1.13.5: ETA states that the proposed regulations' data-reporting requirements do not make sense for certain "other" financial products or services as defined by the proposed regulations.

Response to comment 1.13.5: This comment was construed as an observation rather than a specific recommendation to change the regulations. In any event, the Department amended section 1062, subdivision (b)(2), (b)(3), and (b)(4) (since renumbered as subdivision (c)(2), (c)(3), and (c)(4)), by deleting "or other financial product or service" and deleting subdivision (a)(2) to clarify that only commercial-financing transactions are required to be reported.

Comment 1.13.6: ETA states that the proposed regulations do not indicate why the Department needs such a broad data set or whether that data could be released to the public.

Response to comment 1.13.6: The Department did not make any changes in response to this comment. In accordance with the APA, the ISOR and FSOR describe the purpose and necessity of each provision. The authorizing statute for the proposed regulations, Financial Code section 90009, subdivision (e), does not mandate that the Department set forth in these regulations whether data or reports received by the Department will be made available to the public.

Comment 1.13.7: ETA states that the requested commercial-financing data must be further defined before covered providers can comply and report useful information. ETA recommends that the data-reporting requirement not go into effect until the Department finalizes a reporting form with associated definitions for the requested commercial financing data.

Response to comment 1.13.7: The Department substantially amended section 1062 so that it requires only commercial-financing transactions to be reported and more clearly defines the dollar amount of a transaction, amount financed, and total cost of financing, since renamed to "annual percentage rate." Because of these changes, the Department declined to delay effectiveness of the proposed regulations.

Comment 1.13.8: ETA states that the UDAAP definitions were copied from the Dodd-Frank Act, which was drafted for consumers, not commercial entities. ETA states that forcing commercial borrowers into the Dodd-Frank Act's definitions and framework "ignores the purpose of UDAAP."

Response to comment 1.13.8: The Department did not make any changes in response to this comment. The comment did not describe with sufficient specificity how the regulations should be changed to accommodate its objection. In addition, ETA does not explain why protecting small-business borrowers from unfair, deceptive, and abusive acts and practices is inappropriate.

Comment 1.13.9: ETA recommends expanding the de minimis exemption in section 1062, subdivision (a)(1), to five transactions.

Response to comment 1.13.9: The Department deleted the provision discussed in this comment, and the comment is therefore now moot.

Comment 1.13.10: ETA recommends changing "covered consumer" to "covered entity" throughout the regulations.

Response to comment 1.13.10: The Department amended the proposed regulations as recommended.

Comment 1.13.11: ETA recommends changes to the definition of "financial product or service" in section 1060, subdivision (f) (since renumbered to subdivision (g)). ETA recommends changing the "consumer" portion of the definition so that instead of providing that "consumer" also includes any organization or entity as enumerated nonexhaustively, the definition should provide that "consumer" is replaced with "covered entity." ETA also recommends deleting the definition's treatment of "consumer financial product or service."

Response to comment 1.13.11: The Department did not make any changes in response to this comment. Although the recommendation as to "consumer" may be an acceptable alternative to the "consumer" portion of the definition, the definition's treatment of "consumer financial product or service" is necessary to clarify that a person engaged in the business of offering or providing to a small business, nonprofit, or family farm any financial product or service listed in Financial Code section 90005, subdivision (k), is a covered provider under the proposed regulations even if the product or service is intended primarily for commercial purposes.

Comment 1.13.12: ETA recommends that the "small business" definition be changed to (1) remove the "not dominant in its field of operation" and "independently owned and operated" criteria, (2) use a single receipts threshold instead of industry-specific receipts thresholds, and (3) provide an option to calculate receipts using income data for the customer that the covered provider may use in its underwriting. ETA also recommends adding a "fallback" option that permits covered providers to report transactions in addition to those technically required to be reported.

Response to comment 1.13.12: The Department substantially amended the definition of "small business" in section 1060, subdivision (h) (since renumbered to subdivision (i)), to accommodate

this recommendation. The definition no longer uses industry-specific receipts thresholds and instead uses a single threshold of the greater of $16 million gross annual receipts or the annual gross receipt level as biennially adjusted by the Department of General Services. A covered provider may rely on any relevant written representation by the business for the purpose of determining its annual gross receipts, including information provided in any financing application or agreement. Because the amended definition is easier for covered providers to apply, the Department declined to provide the requested fallback option.

Comment 1.13.13: ETA recommends that the proposed regulations clarify that the exemptions in Financial Code section 90002 apply to these regulations and, in particular, that such exemptions include nonbank subsidiaries of banks.

Response to comment 1.13.13: The Department amended the definition of "covered provider" to clarify that "covered provider" does not include any person exempted from the CCFPL under Financial Code section 90002. The Department declined to clarify that the exemptions include nonbank subsidiaries of banks. The proposed regulations are not intended to exempt from any requirement persons or activities that are not exempted by the CCFPL. The recommended change would result in a regulation that improperly impairs the scope of the CCFPL.

Comment letter 1.14 – Scott Stewart, Chief Executive Officer, Innovative Lending Platform Association (ILPA)

Comment 1.14.1: ILPA recommends changing "covered consumer" to "covered entity" throughout the regulations. ILPA states that the term "consumer," when dealing with a commercial transaction, is confusing and conflicts with the CCFPL's terminology.

Response to comment 1.14.1: The Department amended the proposed regulations as recommended but not because the term "consumer" conflicts with the CCFPL's terminology. The CCFPL itself includes a commercial financial product or service in its definition of "consumer financial product or service."[20]

Comment 1.14.2: ILPA recommends that the proposed regulations require reporting of data on financing term lengths. Without that information, the data collected ignores the time value of capital, making certain products, such as shorter-term or open-ended products, seem disproportionately more expensive than others.

Response to comment 1.14.2: The Department did not make any changes in response to this comment. In response to other comments, however, the Department substantially amended section 1062 so that it more clearly defines the dollar amount of a transaction, amount financed, and total cost of financing, since renamed to "annual percentage rate" (APR), by referring to specific provisions in the Commercial Financing Disclosures regulations.[21] The APR incorporates the time value of money and provides a useful single metric that enables like-for-like comparison of different financial products.

Comment 1.14.3: ILPA states that the proposed regulations require covered providers to report

[20] Fin. Code, § 90005, subd. (e)(2).
[21] Cal. Code Regs., tit. 10, § 900 et seq.

information they may not currently collect from customers, such as gross annual revenue.

Response to comment 1.14.3: The Department did not make any changes in response to this comment because it is an observation rather than a recommendation to change the regulation. The comment mistakenly asserts that covered providers would be required to report customer information such as gross annual revenue. The proposed regulations require reporting of information on commercial-financing transactions, not commercial-financing customers.

Comment 1.14.4: ILPA states that the proposed regulations do not set forth a preferred protocol or safe-harbor method for collecting and vetting the information required to determine whether a customer meets the definition of a small business.

Response to comment 1.14.4: The Department did not make any changes in response to this comment because it is an observation rather than a recommendation to change the regulation. In any event, in response to other comments on the definition of "small business," the Department substantially amended that definition with the effect of addressing some of the comment's observations.

Comment 1.14.5: ILPA requests more clarity on why the Department needs the data specified in the proposed regulations, what it will be used for, whether it will be released to the public, and whether it will be reported on an aggregate or individual basis. In particular, it is unclear whether the data to be collected is related to defining unfair, deceptive, and abusive acts and practices in commercial financing.

Response to comment 1.14.5: The Department did not make any changes in response to this comment. In accordance with the APA, the ISOR and FSOR describe the purpose and necessity of each provision. The authorizing statute for the proposed regulations, Financial Code section 90009, subdivision (e), does not mandate that the data or reports received by the Department be made available to the public. As a general matter, documents received by the Department are subject to public disclosure unless exempt under specific provisions of the California Public Records Act.

Comment 1.14.6: ILPA recommends simplifying the "small business" definition by (1) removing the "not dominant in its field of operation" and "independently owned and operated" criteria, (2) using a single revenue threshold, and (3) providing an option to calculate gross receipts using data collected during the underwriting process.

Response to comment 1.14.6: The Department substantially amended the definition of "small business" in section 1060, subdivision (h) (since renumbered to subdivision (i)), to accommodate this recommendation. The definition no longer uses industry-specific receipts thresholds and instead uses a single threshold of the greater of $16 million gross annual receipts or the annual gross receipt level as biennially adjusted by the Department of General Services. A covered provider may rely on any relevant written representation by the business for the purpose of determining its annual gross receipts, including information provided in any financing application or agreement.

Comment letter 1.15 – Robert C. Fellmeth, Executive Director, Centers for Public Interest Law, University of San Diego School of Law

Comment 1.15: Fellmeth joins in the comments submitted by Thomas Dresslar (comment letter 1.8).

Response to comment 1.15: This comment was not timely submitted within the comment period. In any event, see responses to comment letter 1.8.

SUMMARY OF AND RESPONSE TO COMMENTS SUBMITTED DURING 15-DAY COMMENT PERIOD (FEBRUARY 24 TO MARCH 13, 2023)

The modified proposed regulations were made available for public review and comment from February 24 to March 13, 2023. The following persons submitted comments to the Department for this period:

1. Cole Harmonson, President, American Factoring Association, dated March 12, 2023.
2. Responsible Business Lending Coalition et al., dated March 13, 2023.

Comment letter 2.1 – Cole Harmonson, President, American Factoring Association (AFA)

Comment 2.1.1: AFA objects to the Commercial Financing Disclosures regulations'[22] methods of calculating annual percentage rates (APRs) for factoring transactions. AFA states that the factoring-specific assumptions required for APR calculations will result in inaccurate, overstated APRs and make apples-to-apples comparisons of financial products impossible for small businesses. AFA asks that the Department consider these concerns for this proposed regulatory action.

Response to comment 2.1.1: No response is required because this comment is not specifically directed to a change to the text that was made available to the public during this comment period.[23]

Comment 2.1.2: AFA states that any new reporting requirements impose a material burden on factors. AFA recommends that factors be exempted from reporting interval-sorted transaction data and APR data and be required to report only the total number and dollar amount of transactions, to minimize compliance costs.

Response to comment 2.1.2: The Department did not make any changes in response to this comment. The proposed regulations carry out the purposes and intent of the CCFPL by yielding useful data for market monitoring while imposing uniform compliance burdens on covered providers.

[22] Cal. Code Regs., tit. 10, § 900 et seq.
[23] Gov. Code, § 11346.8, subd. (c).

Comment letter 2.2 – Responsible Business Lending Coalition et al.

Comment 2.2: This comment is substantially similar to comment 1.11.4.

Response to comment 2.2: See response to comment 1.11.4.

ALTERNATIVES DETERMINATIONS

Alternatives Generally (§ 11346.9, subd. (a)(4))

The Department considered alternatives to various aspects of the initial proposed regulations, including alternatives identified and recommended by the public. The Department rejected or accepted and incorporated recommended alternatives as explained in the sections above. Accepted alternatives were less burdensome and equally effective in achieving the purposes of the regulations. The Department's chosen approach balanced the interests of both providers and recipients of commercial financial products or services and the purposes of the CCFPL. No remaining reasonable alternative to the current proposed regulations would be more effective in carrying out the purpose for which these regulations were proposed, as effective and less burdensome to affected private persons, or more cost-effective to affected private persons and equally effective in implementing the policy of the CCFPL.

Alternatives Relating to Small Business (§ 11346.9, subd. (a)(5))

As an initial matter, commercial financing providers that would be subject to the proposed regulations and any associated burdens are not "small businesses" within the meaning of the APA because "commercial finance companies" are excluded from the definition of "small business."[24] To the extent the proposed regulations would have an adverse economic impact on small businesses that receive commercial financing, the Department considered alternatives that would lessen such adverse economic impact and accepted some and rejected others. When the Department rejected an alternative, it did so because the alternative would not be as effective in achieving the purposes of the CCFPL, some of which are to improve accountability and transparency in California's financial marketplace and to protect California residents from abuses in that marketplace.

LOCAL MANDATES (§ 11346.9, subd. (a)(2))

The proposed regulations do not impose any mandate on local agencies or school districts.

[24] Gov. Code, § 11342.610, subd. (b)(1).