

SENATE JUDICIARY COMMITTEE
Senator Thomas Umberg, Chair
2023-2024 Regular Session

SB 1286 (Min)
Version: March 18, 2024
Hearing Date: April 23, 2024
Fiscal: Yes
Urgency: No
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SUBJECT

Rosenthal Fair Debt Collection Practices Act: covered debt: small business debts

DIGEST

This bill extends the scope of the Rosenthal Fair Debt Collection Practices Act (“Rosenthal Act”) to cover the collection of “covered commercial debts,” as defined.¹

EXECUTIVE SUMMARY

The Rosenthal Act establishes a set of basic norms that debt collectors must adhere to when going about their work. Without excusing anyone from paying what they rightly owe, Rosenthal requires debt collectors to treat debtors civilly and honestly throughout the process. It prohibits things like threatening debtors, trying to trick them, humiliating them in front of others, or calling them up repeatedly in the middle of the night to demand payment.

Small business owners steeped in commercial debt are often faced with the same pressures and limitations as consumers are with consumer debt. However, the Rosenthal Act only covered consumer debt, meaning it was taken out primarily for personal, family, or household purposes.

This bill, as recently agreed to be amended, extends select portions of the Rosenthal Act to include “covered commercial debt.” This is defined as money, property, or their equivalent, due or owing or alleged to be due or owing from a natural person to a lender, a commercial financing provider, or a debt buyer by reason of a covered commercial credit transaction.

¹ This is an analysis of the bill as was agreed to be amended in the Senate Banking and Financial Institutions Committee. The amendments will be taken in this Committee.

The bill is co-sponsored by East Bay Community Law Center, the Consumer Federation of California, Small Business Majority, and the California Association for Micro Enterprise Opportunity (CAMEO). The bill is supported by various legal services and business organizations, including the San Juan Capistrano Chamber of Commerce and Bet Tzedek Legal Services. It is opposed by various industry associations, including the California Association of Collectors. This bill passed out of the Senate Banking and Financial Institutions Committee on a vote of 4 to 2.

PROPOSED CHANGES TO THE LAW

Existing law:

- 1) Prohibits debt collectors, pursuant to the Fair Debt Collection Practices Act (FDCPA), from using abusive, unfair, or deceptive practices. (15 U.S.C. § 1692 et seq.)
- 2) Defines a debt collector as a person who regularly collects, or attempts to collect, debts owed to another person. (15 U.S.C. § 1692a)
- 3) Establishes the Rosenthal Act to regulate the collection of consumer debt, generally prohibiting deceptive, dishonest, unfair, and unreasonable debt collection practices by debt collectors and regulates the form and content of communications by debt collectors to debtors and others. (Civ. Code §§ 1788 *et seq.*) The Rosenthal Act:
 - a) Defines “consumer debt” and “consumer credit” as money, property, or their equivalent, due or owing or alleged to be due or owing from a natural person by reason of a consumer credit transaction. The term “consumer debt” includes a mortgage debt. (Civ. Code § 1788.2.)
 - b) Defines “consumer credit transaction” as a transaction between a natural person and another person in which property, services, or money is acquired on credit by that natural person from the other person primarily for personal, family, or household purposes. (Civ. Code § 1788.2.)
 - c) Defines “debt collector” as any person who, in the ordinary course of business, regularly, on behalf of that person or others, engages in debt collection.
 - d) Prohibits a debt collector from the following conduct or practices, among others, when collecting or attempting to collect a consumer debt:
 - i. The use or threat of physical force or violence. (Civ. Code § 1788.10.)
 - ii. Threats and communications that rely on false representations. (Civ. Code §§ 1788.10 and 1788.13.)
 - iii. Using obscene or profane language. (Civ. Code § 1788.11.)

- iv. Communicating with the debtor with such frequency as to be unreasonable, and to constitute harassment of the debtor under the circumstances. (Civ. Code § 1788.11.)
- v. Communicating unnecessarily about the debtor's debt with the debtor's employer or extended family. (Civ. Code § 1788.12.)
- e) Requires a debt collector to provide its California debt collector license number to a consumer in specified circumstances. (Civ. Code § 1788.11.)
- f) Incorporates by reference specified provisions of the FDCPA into state law, but exempts original creditors and specified people collecting debts on their behalf from some of those incorporated provisions. (Civ. Code § 1788.17.)
- g) Provides remedies to a harmed debtor in an amount equal to any actual damages sustained by the debtor as a result of the violation, plus an amount of \$100 - \$1,000 if the violation was conducted willfully and knowingly by the debt collector. (Civ. Code § 1788.30.)
- h) Provides a release from liability to a debt collector who cures a violation, as specified, or who shows by a preponderance of evidence that the violation was not intentional and resulted notwithstanding the maintenance of procedures reasonably adapted to avoid any such violation. (Civ. Code § 1788.30.)

This bill:

- 1) Adds "covered commercial debt" to the scope of the Rosenthal Act. Makes clear that a "debtor" with relation to such debts includes a natural person who guarantees an obligation related to a covered commercial credit transaction but does not include a corporation or limited liability company.
- 2) Defines the following terms:
 - a) "Covered debt" means a consumer debt or a covered commercial debt.
 - b) "Covered credit" means consumer credit or covered commercial credit.
 - c) "Covered commercial debt" and "covered commercial credit" mean money, property, or their equivalent, due or owing or alleged to be due or owing from a natural person to a lender, a commercial financing provider, or a debt buyer, by reason of a covered commercial credit transaction.
 - d) "Covered commercial credit transaction" means a transaction between a person and another person in which property, services, or money of a total value of no more than \$500,000 is acquired on credit by that person from the other person for use primarily for other than personal, family, or household purposes.
- 3) Replaces "consumer debt" with "covered debt" throughout much of the Rosenthal Act, except for certain provisions, including those related to consumer

debt originated by a hospital, provisions prohibiting calling a debtor's employer, and the section incorporating by reference the FDCPA.

- 4) Applies the provisions of Section 1788.14.5 to delinquent covered commercial debt sold or assigned on or after July 1, 2025.

COMMENTS

1. Stated intent of the bill

According to the author:

Small businesses face many barriers in accessing capital, especially minority-owned businesses. Since the economic crash and Great Recession in 2008, many lenders have moved to require small business owners to personally guarantee their business debt. While lenders are within their right to require co-signatories, this goes against the purpose of entity formation. Although the individual is borrowing for their business, the personal guarantee exposes the individual to abusive, deceptive, or unfair debt collection practices. SB 1286 will extend the debt collection protections provided under the Rosenthal Act to individuals who have a personal guarantee on their business debt.

2. The Rosenthal Fair Debt Collection Practices Act

Since 1977, the Rosenthal Act has protected debtors against the most egregious tactics that creditors might otherwise be tempted to utilize while pursuing their money. The Rosenthal Act prohibits creditors from engaging in deceptive, harassing, humiliating, threatening, or otherwise unreasonable conduct while seeking payment. For example, under the Rosenthal Act, a creditor cannot try to extract payments by waking the debtor up in the middle of the night with repeated phone calls; trying to embarrass the debtor in front of family members or their employer; threatening to have the debtor sent to jail, cursing at the debtor, or telling the debtor that the creditor will drop the matter in exchange for a payment when the creditor has no actual intention of doing so. Nothing in the Rosenthal Act excuses a debtor from having to pay, but the Rosenthal Act does demand that creditors treat the people who owe them money with honesty and civility.

The Rosenthal Act applies to "consumer debt," which is defined as "money, property, or their equivalent, due or owing or alleged to be due or owing from a natural person by reason of a consumer credit transaction." (Civ. Code § 1788.2(f).) "Consumer credit transaction" is defined as "a transaction between a natural person and another person in which property, services or money is acquired on credit by that natural person from such other person primarily for personal, family, or household purposes." (Civ. Code § 1788.2(e).)

3. Extending the protections of the Rosenthal Act to commercial debt

This bill extends the modest protections of the Rosenthal Act to “covered commercial debts,” defined as money, property, or their equivalent, due or owing or alleged to be due or owing from a natural person to a lender, a commercial financing provider, or a debt buyer by reason of a covered commercial credit transaction. The term “covered commercial credit transaction” means a transaction between a person and another person in which property, services, or money of a total value no more than \$500,000 is acquired on credit by that person from the other person for use primarily for other than personal, family, or household purposes.

The bill makes clear that a “debtor” for the purposes of covered commercial debts includes natural persons who guarantee an obligation related to a covered commercial credit transaction but does not include a corporation or limited liability company. In response to opposition concerns, the bill has taken amendments to narrow its scope. The bill changes references in many provisions of the Rosenthal Act from consumer debt to covered debt, which includes both consumer and covered commercial debt, but does not extend this change to provisions governing collection of consumer debt originated with a hospital, provisions prohibiting communicating with a debtor’s employer, and the section incorporating by reference the FDCPA.

A wide coalition of groups, including the East Bay Community Law Center, several small business advocacy organizations, and various consumer groups, write in support:

Since the 2008 Great Recession, many lenders started requiring business owners to personally sign for their business debt. Lenders are within their right to require co-signatories, however a personal guarantee defeats the purpose of an LLC, and is antithetical to the purpose of entity formation.

These requirements only hurt minority entrepreneurship. Disparities in access to capital for minority-owned small businesses are well-documented, even if you control for factors like revenue. For instance, a study from Stanford found Latino-owned businesses had lower approval rates than white-owned businesses for loans of over \$50,000, despite having larger revenues, similar credit scores, and less debt. . . .

Given the lack of access to traditional business funding and the current trend of requiring personal guarantees, the need for dignified debt collection practices for individuals who incur debt for their business is necessary as small businesses do not have the same protections as consumers in the collection of a business debt.

This bill is narrowly tailored to solve the specific issue—and only applies to individual people who incur a business debt. The rationale behind the

Rosenthal Act is applicable to small business owners (the people behind the business): decency and informed debt collection practices. *No abuse should be allowed in the collection of a small business debt.*

Writing in opposition, the California Association of Collectors argues:

SB 1286 seeks to extend the coverage of the Rosenthal Act to include "small business" debts, thereby subjecting commercial transactions to regulations originally designed to protect individual consumers. While we understand the intention behind this bill, we believe it is fundamentally flawed and impractical for several reasons. . . .

Moreover, the provisions of the Rosenthal Act are ill-suited for commercial debt collection. For instance, while individual consumers have the right to demand that creditors cease contact, it is unclear under SB 1286 to whom a creditor or collector may reach out to, in the case of a small business. This ambiguity raises concerns about potential violations of privacy and confidentiality, particularly regarding the disclosure of debt details to employees handling accounts payable.

Lastly the bill as currently written, will require all commercial debt collection companies to be licensed. Commercial debt collection requires a tailored approach that accounts for the unique dynamics of business transactions, rather than applying regulations intended for individual consumers.

SUPPORT

Cameo - California Association for Micro Enterprise Opportunity (sponsor)

Consumer Federation of California (sponsor)

East Bay Community Law Center (sponsor)

Small Business Majority (sponsor)

Berkeley Law & Organizing Collective

Bet Tzedek Legal Services

California Coalition for Community Investment

California Low-income Consumer Federation

Consumer Attorneys of California

Decosimo Law

Housing and Economic Rights Advocates (HERA)

ICA

La Cocina

Microenterprise Collaborative of Inland Southern California

Public Law Center

Renaissance Entrepreneurship Center

San Juan Capistrano Chamber of Commerce
Sonya Yruel Photography
The Lisa B Company
25 Individuals

OPPOSITION

American Financial Services Association
California Association of Collectors, Inc.
California Bankers Association
California Chamber of Commerce
California Community Banking Network
California Credit Union League
California Creditors Bar Association
California Financial Services Association
California Mortgage Bankers Association

RELATED LEGISLATION

Pending Legislation: SB 1482 (Glazer, 2024) expands the California Financing Law (CFL) to include all types of commercial financing offered to small businesses; and adds new requirements for commercial financing providers and commercial financing brokers in commercial financing transactions with small businesses, as defined. These provisions will take effect January 1, 2026. SB 1482 is currently in this Committee.

Prior Legislation:

SB 908 (Wieckowski, Ch. 163, Stats. 2020) established the Debt Collection Licensing Act, which provides for licensure, regulation, and oversight of debt collectors by the Department of Financial Protection and Innovation.

SB 187 (Wieckowski, Ch. 545, Stats. 2019) added mortgage debt to the definition of consumer debt covered by the Rosenthal Act and removed the exception for an attorney or counselor at law from the definition of debt collector under the Rosenthal Act.

AB 969 (Papan, Ch. 319, Stats. 1999) incorporated some components of the federal Fair Debt Collection Practices Act, including its remedies provisions, into the Rosenthal Act, with specified exceptions.

SB 237 (Robbins, Ch. 907, Stats. 1977) enacted the Rosenthal Fair Debt Collection Practices Act.

PRIOR VOTES:

Senate Banking and Financial Institutions Committee (Ayes 4, Noes 2)
