

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

SB 1521 (Committee on Banking and Financial Institutions)

Version: March 11, 2024

Hearing Date: April 23, 2024

Fiscal: Yes

Urgency: No

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**SUBJECT**

Commercial financing transactions: fees

**DIGEST**

This bill allows for collateral monitoring fees to be charged in connection with non-delinquent commercial financing transactions involving small businesses, as specified.

**EXECUTIVE SUMMARY**

Last year, SB 666 (Min, Ch. 881, Stats. 2023) responded to concerns regarding junk fees charged in connection with financing transactions involving small businesses. The bill prohibited certain fees from being charged to small businesses in commercial financing involving \$500,000 or less. This included fees for accepting or processing a payment and fees for providing businesses with specified documentation.

Relevant here, the bill also prohibited charging a fee for monitoring the small business's collateral, unless the underlying commercial financing transaction is delinquent for more than 60 days. Concerns were raised late in the legislative process that collateral monitoring fees should not be prohibited except where repayment is delinquent, or at least should be treated differently, as they were not "junk fees" as the term was understood.

This bill effectuates an agreement made by the author and sponsors of SB 666 that such fees should in fact be treated differently. This bill allows for such fees to be charged, even where the loan is not delinquent, for asset-based loans or factoring, where the fee is intended to compensate the lender for actions taken to validate the collateral with the intended purpose of maximizing the amount of financing provided to the small business; or where the fee is expressed as a dollar amount or a percentage of an identifiable base, and the fee is deemed a finance charge, as provided. No support or opposition has been received by the Committee. This is a Senate Banking and Financial Institutions Committee bill, and it passed out of that committee on a 7 to 0 vote.

**PROPOSED CHANGES TO THE LAW**

Existing law:

- 1) Establishes the California Financing Law (CFL), which regulates specified finance lenders and brokers making certain types of commercial loans. (Fin. Code § 22000 et seq.)
- 2) Establishes, separate from the CFL, disclosure requirements for certain small commercial loans, subject to specified terms and exemptions. (Fin. Code § 22800 et seq.)
- 3) Requires a commercial financing provider to disclose specified information to a loan recipient, at the time the provider extends a specific commercial financing offer to that recipient, and to obtain the recipient's signature on such disclosure before consummating the commercial financing transaction. The information to be disclosed is as follows:
  - a) the total amount of funds provided; the total dollar cost of the financing; the term or estimated term; the method, frequency, and amount of payments; a description of prepayment policies; and the total cost of financing expressed as an annualized rate. (Fin. Code § 22802(a), (b).)
  - b) if the provider of commercial financing offers commercial financing that is factoring or asset-based lending and that offers the recipient an agreement that describes the general terms and conditions of the commercial financing transaction that will occur under the agreement, the provider may disclose the following in lieu of 3)(a): an amount financed; the total dollar cost; the term or estimated term; the method, frequency, and amount of payments; a description of prepayment policies; and the total cost of the financing expressed as an annualized rate. (Fin. Code § 22803(a).)
- 4) Provides that, after the final regulations have become effective, any provider required to make the above disclosures shall be subject to examination and enforcement by the Commissioner of the California Department of Financial Protection and Innovation (DFPI) pursuant to provisions under the California Financing Law. (Fin. Code § 22805.)
- 5) Exempts from the disclosure requirement above all of the following:
  - a) depository institutions;
  - b) lenders regulated under the federal Farm Credit Act (12 U.S.C. §§ 2001 et seq.);
  - c) a commercial financing transaction secured by real property;
  - d) a commercial financing transaction in which the recipient is a dealer or a vehicle rental company, as specified, pursuant to a specific commercial financing offer or commercial open-end credit plan of at least \$50,000,

- including any commercial loan made pursuant to such a commercial financing transaction; and
- e) any person who makes no more than one commercial financing transaction in California in a 12-month period or any person who makes five or fewer commercial financing transactions in California in a 12-month period that are incidental to the business of the person relying upon the exemption. (Fin. Code, § 22801.)
- 6) Defines “recipient” to mean a person who is presented a specific financing offer by a provider that is equal to or less than \$500,000. (Fin. Code § 22800.)
- 7) Prohibits the following fees from being charged to a small business in connection with a commercial financing transaction:
- a) A fee for accepting or processing a payment required by the terms of the financing contract as an automated clearinghouse transfer debit.
  - b) A fee for providing a small business with documentation prepared by the financing provider that contains a statement of the amount due to satisfy the remaining amount owed, including, but not limited to, interest accrued to the date the statement is prepared and a means of calculating per diem interest accruing thereafter.
  - c) A fee in addition to an origination fee that does not have a clear corresponding service provided for the fee, including, but not limited to, a risk assessment, due diligence, or platform fee.
  - d) A fee for monitoring the small business’s collateral, unless the underlying financing transaction is delinquent for more than 60 days.
  - e) A fee for filing or terminating a lien filed in accordance with the provisions of the Uniform Commercial Code against the business’s assets that exceeds 150 percent of the cost of the filing or termination. (Civ. Code § 1799.302.)
- 8) Defines “small business” as an independently owned and operated business that is not dominant in its field of operation, the principal office of which is located in California, the officers of which are domiciled in California, and that, together with affiliates, has 100 or fewer employees and average annual gross receipts of \$15 million or less over the previous three years. (Civ. Code § 1799.300(j).)
- 9) Authorizes a recipient to bring a claim against an entity in violation for actual damages, statutory damages between \$500 and \$2,500, injunctive relief, and attorneys’ fees and costs. A prevailing defendant may be awarded fees if the recipient is found to have brought the action in bad faith. (Civ. Code § 1799.303(a).)

- 10) Provides that a court may award a provider or broker that is the prevailing party in an action brought pursuant to this section reasonable attorney's fees upon a finding that the recipient brought the action in bad faith. (Civ. Code § 1799.303(b).)

This bill prohibits a fee for monitoring a small business' collateral except where the commercial financing transaction is an asset-based loan or factoring, and the fee is intended to compensate the covered entity for actions taken to validate the collateral with the intended purpose of maximizing the amount of financing provided to the small business or small business owner under the financing contract pursuant to which the fee is charged; or where the fee is expressed as a dollar amount or a percentage of an identifiable base, and the fee is deemed a finance charge, as specified.

### COMMENTS

#### 1. Stated intent of the bill

According to the author:

SB 1521 is clean-up legislation related to SB 666 (Min, Chapter 881, Statutes of 2023), which passed the Legislature with zero "no" votes. The law enacted by SB 666 proscribes the charging of specified fees on commercial financing transactions. Senator Min and the sponsors of SB 666 approved the amendments to that law that are contained in SB 1521. The amendments allow for collateral monitoring fees to be charged in specified circumstances related to commercial financing transactions.

#### 2. Pricing in small business financing

Consumer protection in the banking and finance sector is a particular priority for this state. The California Financing Law (CFL) sets forth a comprehensive regulatory framework for consumer and commercial loans issued by specified financial institutions.<sup>1</sup> The CFL's goals include permitting and encouraging the development of economically sound lending practices and protecting borrowers against unfair practices by some lenders, and its provisions should be liberally construed to promote its purposes and policies.<sup>2</sup>

With the advent of different types of commercial financing, however, not all commercial lending entities are covered by the CFL. This left a gap in the CFL's protective framework for commercial lending. In response, the Legislature enacted SB 1235 (Glazer, Ch. 1011, Stats. 2018), which established disclosure requirements for specified entities extending commercial financing offers of less than \$500,000. SB 1235

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<sup>1</sup> Fin. Code, div. 9, §§ 22000 et seq.

<sup>2</sup> *Id.*, § 22001.

deliberately placed its disclosure requirements outside of the CFL to ensure that it covered all commercial lenders, except those already covered by other specified disclosure laws.<sup>3</sup> The bill's disclosure requirements are intended to help small businesses understand the terms of commercial financing being offered to them and the total dollar cost of financing.

However, SB 1235 has limitations. The required financing disclosures did not include all the fees that may be, and often are, charged to small businesses in connection with financing. In response, SB 666 (Min, Ch. 881, Stats. 2023) sought to fill that void by prohibiting certain "junk fees" in the commercial financing space for small businesses. This included fees imposed for accepting or processing a payment required by the financing contract as an automated clearing house transfer debit; fees for providing a payoff or statement letter; and fees imposed in addition to an origination fee with no clear, corresponding service provided.

Relevant here, SB 666 also prohibited fees imposed for monitoring collateral, except where the underlying commercial financing transaction was delinquent for more than 60 days.

### 3. Rethinking collateral monitoring fees

According to the author, the Secured Finance Network (SFN), a trade association for providers of secured commercial financing, voiced concerns late in the legislative process in 2023 that collateral monitoring fees should not be covered by SB 666 or should be addressed differently. SB 666 was intended to target "junk fees," defined as those fees that are "either exorbitant, hidden, or provide no service to the customer." SFN argued that collateral monitoring fees were a necessary component of the pricing of factoring transactions, and that the fees were tied to a "service to the customer."

After the law was enacted, SFN worked with the author and sponsors of SB 666 to agree on the language now contained in this bill. The bill continues to allow for such fees when the transaction is more than 60 days delinquent but also allows them regardless of delinquency in two situations:

- The commercial financing transaction is an asset-based loan or factoring, and the fee is intended to compensate the covered entity for actions taken to validate the collateral with the intended purpose of maximizing the amount of financing provided to the small business or small business owner under the financing contract pursuant to which the fee is charged.
- The fee is expressed as a dollar amount or a percentage of an identifiable base, and the fee is deemed a finance charge, as described in Section 943 of Subchapter 3 of Chapter 3 of Title 10 of the California Code of Regulations.

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<sup>3</sup> Sen. Comm. on Banking & Financial Institutions on Sen. Bill No. 1235 (2017-2018 Reg. Sess.) Aug. 31, 2018, p. 7; Fin. Code, § 228801.

The author and supporters of the bill argue that collateral monitoring expenses are incurred by the lender even if the borrower is not delinquent. Those costs relate to the ongoing reconciliation of eligible collateral that determines how much the borrower may draw. For accounts that are current, these costs can vary if the reports show changing characteristics that require increased frequency of monitoring, if the profile of collateral changes due to shifting business conditions, or due to special funding requests by the borrower that require analysis. If a lender was unable to recover collateral monitoring costs on a variable basis, the lender would charge a higher interest rate to all borrowers to cover the aggregate collateral monitoring activities that the lender expected to undertake for a pool of borrowers.

**SUPPORT**

None received

**OPPOSITION**

None received

**RELATED LEGISLATION**

Pending Legislation: None known.

Prior Legislation:

SB 666 (Min, Ch. 881, Stats. 2023) *See* Executive Summary and Comment 2.

SB 1235 (Glazer, Ch. 1011, Stats. 2018) *See* Comment 2.

**PRIOR VOTES:**

Senate Banking and Financial Institutions Committee (Ayes 7, Noes 0)

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