

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

SB 666 (Min)
Version: April 10, 2023
Hearing Date: May 2, 2023
Fiscal: No
Urgency: No
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SUBJECT

Small business: commercial financing transactions

DIGEST

This bill prohibits certain fees in connection with commercial financing that is provided to small businesses, as defined.

EXECUTIVE SUMMARY

The issue of “junk” fees and other pricing schemes gained more prominence nationally when President Joe Biden took aim at them in his State of the Union address in February 2023. When merchants include hidden or “junk” fees in the purchase price of goods and services, their customers are not able to make fully informed decisions. There are various types of pricing schemes generally deemed unfair or unlawful business practices, but this bill specifically targets transparency in commercial financing transactions.

Just as with consumers, small businesses can be hit hard by hidden fees and other unknown costs related to financing transactions. Existing law requires disclosures of specific information in connection with commercial financing of less than \$500,000. However, certain junk fees in this context are not covered by those transparency measures. This bill seeks to address this gap by prohibiting certain fees from being charged to small businesses, as defined, in connection with this type of commercial financing, this includes fees in addition to an origination fee that do not have a clear corresponding service provided for the fee.

This bill is co-sponsored by the California Association for Micro Enterprise Opportunity (CAMEO) and the Consumer Federation of California. It is supported by the Consumer Attorneys of California and the Small Business Majority. There is no known opposition. The bill passed out of the Senate Banking and Financial Institutions 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.)

This bill:

- 1) 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 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 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 90 days; and
 - 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.
- 2) 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 \$15,000,000 or less over the previous three years.
- 3) Defines “commercial financing” to have the same meaning as Section 22800 of the Financial Code, related to commercial financing disclosures.
- 4) Defines “recipient” as a person who is presented a specific commercial financing offer by a provider that is equal to or less than \$500,000.
- 5) Exempts the following from the provisions of the bill:

- a) a provider that is a depository institution;
 - b) a provider that is a lender regulated under the federal Farm Credit Act;
 - c) a commercial financing transaction secured by real property; and
 - d) 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
- 6) 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.
- 7) 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.

COMMENTS

1. Pricing transparency

In his prepared speech for his State of the Union address, President Biden took aim at so-called "junk fees":

My administration is also taking on "junk" fees, those hidden surcharges too many businesses use to make you pay more. For example, we're making airlines show you the full ticket price upfront and refund your money if your flight is cancelled or delayed. We've reduced exorbitant bank overdraft fees, saving consumers more than \$1 billion a year. We're cutting credit card late fees by 75%, from \$30 to \$8. Junk fees may not matter to the very wealthy, but they matter to most folks in homes like the one I grew up in. They add up to hundreds of dollars a month. They make it harder for you to pay the bills or afford that family trip.

I know how unfair it feels when a company overcharges you and gets away with it. Not anymore. We've written a bill to stop all that. It's called the Junk Fee Prevention Act. We'll ban surprise "resort fees" that hotels tack on to your bill. These fees can cost you up to \$90 a night at hotels that aren't even resorts. We'll make cable internet and cellphone companies stop charging you up to \$200 or more when you decide to switch to another provider. We'll cap service fees on tickets to concerts and sporting events and make companies disclose all fees upfront. And we'll prohibit airlines from charging up to \$50 roundtrip for families just to sit together.

Baggage fees are bad enough – they can't just treat your child like a piece of luggage.

Americans are tired of being played for suckers.¹

As part of its rulemaking, the FTC has made the case for why government action in response to these widespread and growing practices is critical to protecting consumers: “Junk fees are especially likely to cause consumer harm when they arise ‘without real notice, unconnected to any additional service, in an industry where advertising is essential.’ . . . Junk fees impose substantial economic harms on consumers and impede the dissemination of important market information.”²

While the Biden Administration has clearly declared war with hidden fees at the federal level, a host of bills have been introduced in the California Legislature this year to combat these deceptive practices at the state level. This bill targets fees that face small businesses in 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.³ 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.⁴

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 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.⁵ The bill's disclosure requirements are intended to help small

¹ Remarks of President Joe Biden – State of the Union Address as Prepared for Delivery (February 7, 2023) The White House Briefing Room, <https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/02/07/remarks-of-president-joe-biden-state-of-the-union-address-as-prepared-for-delivery/>. All internet citations are current as of March 22, 2023.

² Federal Register, *Unfair or Deceptive Fees Trade Regulation Rule Commission Matter No. R207011* (November 8, 2022) FTC, <https://www.govinfo.gov/content/pkg/FR-2022-11-08/pdf/2022-24326.pdf>.

³ Fin. Code, div. 9, §§ 22000 et seq.

⁴ *Id.*, § 22001.

⁵ Sen. Comm. on Banking & Financial Institutions on Sen. Bill No. 1235 (2017-2018 Reg. Sess.) Aug. 31, 2018, p. 7; Fin. Code, § 228801.

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 do not include all the fees that may be, and often are, charged to small businesses in connection with financing. Especially with the economic impact of the COVID-19 pandemic for such businesses, the author argues that these hidden and exorbitant fees are particularly egregious.

This bill seeks to fill this void by prohibiting certain “junk fees” in the commercial financing space for small businesses. This includes fees imposed for accepting or processing a payment required by the financing contract as an automated clearing house debit; fees for providing a payoff or statement letter; fees imposed for monitoring collateral, except as specified; and fees imposed in addition to an origination fee with no clear, corresponding service provided.

Small businesses can enforce violations and seek actual damages, including the amount of fees charged in violation, statutory damages of \$500 to \$2,5000, fees and costs, and other relief the court deems proper. If the claim is found to be brought in bad faith, the prevailing defendant may be awarded reasonable attorneys’ fees.

According to the author:

“Junk fees” have become an all too common addition to the goods and services Californians buy every day, most notably with concert tickets, hotel bookings, and rental cars. Small businesses are also subject to these types of junk fees, specifically when taking out loans with commercial lenders or financing companies. With many of California’s small businesses still struggling to recover from the COVID-19 pandemic, it is imperative to provide proper consumer protections and transparency measures for small businesses in the lending process.

SB 666 will allow the financing process to be more equitable and transparent for small businesses here in California. This bill identifies fees charged by lenders or MCA providers that are either exorbitant, hidden, or provide no service to the customer. These fees include: fees imposed for the lender collecting payment via automated clearing house; fees for statement and pay-off letters; fees charged in addition to an origination fee without a clear, corresponding service; and collateral monitoring fees outside of a collections scenario. This measure would also prohibit a lender from charging a small business a UCC lien filing or termination fee that is not just or reasonable.

The Consumer Federation of California and CAMEO, the co-sponsors of the bill, write jointly with the Small Business Majority:

SB 666 is part of a multi-bill package sponsored by CFC and a wide range of consumer and small business organizations to crack down on so-called “junk fees.” The pernicious nature of these fees and the negative impact they have on consumers and their pocketbooks and small businesses’ bottom lines is widely recognized and driving important public policy changes. Approximately 85% of Americans have direct experience with hidden or junk fees. These fees can be predatory and unnecessary. That’s why President Biden and some leading Republicans agree that reigning in junk fees is important.

With the decline of traditional small business bank lending and lack of scale from most microlenders and CDFIs, online lending is filling the access to capital gap with little to no oversight. It’s never been faster or easier for small businesses to fill out an application and receive the money, often with no regard on whether or not they can pay it back. With a couple of clicks, borrowers can submit an application for financing and receive an answer within days, if not minutes. Because they lack traditional banking relationships, African American and Hispanic-owned employer firms apply to online lenders at higher rates than White-owned firms.

While not all online lending is predatory, if a deal sounds too good to be true, it often is. It is not uncommon to find small business financing with interest rates of higher than 50 percent – some even reaching 350 percent – without these rates being disclosed to the borrower. Often, high fees are wrapped up in these high APRs. Unregulated commercial lenders often charge large sums to small businesses as duplicate fees or fees that do not provide a clear, corresponding service.

SUPPORT

California Association for Micro Enterprise Opportunity (co-sponsor)
Consumer Federation of California (co-sponsor)
Consumer Attorneys of California
Small Business Majority

OPPOSITION

None known

RELATED LEGISLATION

Pending Legislation:

SB 33 (Glazer, 2023) removes the sunset date that applies to the requirement that providers of commercial financing disclose the total cost of financing expressed as an annualized rate. SB 33 is pending in the Senate Appropriations Committee.

SB 869 (Glazer, 2023) requires a person who provides commercial brokerage services to a borrower in a commercial loan transaction by soliciting lenders or otherwise negotiating a commercial loan, to be licensed by the Commissioner of the DFPI and would impose a fiduciary responsibility to the borrower upon a person who provides commercial brokerage services in a commercial loan transaction by soliciting lenders or otherwise negotiating a commercial loan, as specified. SB 869 is pending before the Senate Banking and Financial Institutions Committee.

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

PRIOR VOTES:

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