

This column will examine the rules and regulations that govern closed-end commercial loans in California, New Jersey, New York and Connecticut, and I have recently learned that North Carolina has joined the disclosure club. On May 11, 2021, the “Small Business Truth in Lending Act” was introduced to cover business loans, merchant cash advances and factoring.

Here’s a link to the bill, which has a disclosure threshold of \$500,000.

<https://webservices.ncleg.gov/ViewBillDocument/2021/51680/0/DRH10488-MUf-27A> (2021)

Because it appears to be a bill that will become law, I will include it in our discussions.

A substantial portion of the recent modifications proposed by California relates to the *formatting* of the disclosures. I think it will be more efficient and helpful to the reader for me to discuss the substantive disclosure requirements. For one, when it comes time to modify your documents, you will want to do this once, and it is probably best to wait for the final word on font size, column formats, and other changes related to the form of the disclosure rather than the substance of it. Also, I am hopeful to continue to pursue our goal of presenting a unified disclosure list for these five states. Of course, that doesn’t mean you will be able to ignore the formatting requirement, but it will give you guidance as to what you will need to disclose and how you will need to do it.

CLOSED-END TRANSACTIONS DEFINED

Let’s start with a definition, this one from California. “A closed-end transaction” means:

. . . a transaction in which credit is extended only once over a specific term (including contracts that include an option in which the recipient may extend the term), and is repaid:

(A) in regular predetermined payments of a specified amount over a fixed period of time; or

(B) in the case of sales-based financing, in payments calculated as a percentage of sales or income but with a minimum requirement payment or payments such that the recipient is eventually required to repay the amount advanced regardless of the sales or income the recipient collects.

California Code of Regulations, Title 10, Chapter 3 §2057(a)(8). (2021)

Note that this is taken from the latest round of modifications and may not become law once the review process is concluded. It is, however, a reasonable definition, one that will probably survive the final review process, and should work for the purpose of this discussion.

Under New York’s S5470, “closed-end” transactions mean a closed-end extension of credit, secured or unsecured, including equipment financing that does not meet the definition of a lease under section 2-A-103 of the uniform commercial code, the proceeds of which the

recipient does not intend to use primarily for personal, family or household purposes. "Closed-end financing" includes financing with an established principal amount and duration.

New York Financial Services Law Article 8, Section 804. (2019)

On September 21, 2021, New York promulgated a set of regulations to supplement and clarify S5470. This is a 45-page set of definitions, formatting requirements, and substantive disclosure rules that strongly resemble the 53 pages of modifications now under review in California. The proposed rule is intended to provide small businesses with adequate information to make informed decisions about credit offers by implementing New York's Commercial Finance Disclosure. A key modification, one that came as no surprise, raised the finance threshold from \$500,000 to \$2.5 million, covering a much broader swath of financing transactions.

The new rules can be found at 23 NYCRR 600. Here is a link.

https://www.dfs.ny.gov/industry_guidance/regulations/fs_outreach/section600 (2021)

Connecticut defines "closed-end" financing as a closed-end extension of credit, secured or unsecured, including equipment financing that is not considered a lease, as defined in section 42a-2A-102 of the general statutes, the proceeds of which the recipient does not intend to use primarily for personal, family or household purposes. "Closed-end financing" includes financing with an established principal amount and duration. This is identical to New York, a parallel we will see repeatedly as the Connecticut disclosures law closely mirrors that of New York.

Connecticut Committee Bill No. 745, Section 1. (2021)

Finally, New Jersey does not define "closed-end" transactions. Instead, it uses the term "small business financing" to mean a loan, line of credit, or a factoring or asset-based transaction made for a business purpose with a principal amount or maximum credit limit of \$500,000 or less.

New Jersey Act S.233, Section 1. (2020)

North Carolina defines a "closed end transaction" as "a type of commercial financing consisting of a closed-end extension of credit, secured or unsecured, including equipment financing. This term includes commercial financing for a fixed principal amount and a fixed duration.

North Carolina Small Business Truth in Financing Act Section 53-441(2)

Now that we have established our definitions, let's discuss the disclosure requirements for closed-end transactions.

TIMING OF DISCLOSURES:

California: Disclosures must be made “at the time of extending a specific commercial financing offer and shall obtain the recipient’s signature on such a disclosure before consummating the commercial financing transaction.” *Ca. Financial Code Section 22802.* (2020) According to the most recent modifications, this means:

(A) Any time a specific (i) periodic payment or amount, irregular payment amount, or financing amount, and (ii) any rate, price, or price, cost of financing (including, without limitation, any total repayment amount), in connection with a commercial financing, is quoted in writing to a recipient, based upon information from, or about, the recipient.

The recent modification also includes this language:

However, if a provider simultaneously presents multiple periodic payment amounts, irregular payment amounts, or financing amounts, and rates, prices, or costs of financing (including, without limitation, any total repayment amounts) to the recipient, representing different financing offers and allows the recipient to select from among those options, then “at time of extending a specific commercial financing offer” occurs at the time that the recipient selects a preferred option. Information “about the recipient”

includes information about the recipient that informs the provider’s quote to the recipient, such as the recipient’s financial or credit information, but not the recipient’s name, address, or general interest in financing.

Additionally, disclosure must be made:

(B) Any subsequent time when the terms of an existing consummated commercial financing contract are amended, supplemented, or changed, prior to the recipient agreeing to the changes, if the resulting changes to the contract would result in an increase to the finance charge or annual percentage rate, regardless of whether those terms were previously disclosed to the recipient. The requirement of this subparagraph does not apply to changes made to resolve a recipient’s default on a financing contract.

California Code of Regulations, Title 10, Chapter 3 §2057(a)(4). (2021)

As you will see, this is a rule that applies across the board.

New York: Under *S5470 Section 804* (2019), the disclosures must be made “at the time of extending a specific offer for closed-end financing according to formatting prescribed by the superintendent.” The new regulations go further:

“At the time of extending a specific offer for financing under the CFDL means:

(i) any time a specific periodic payment or irregular payment amount, rate or price, in connection with a commercial financing, is quoted in writing to a recipient, based upon information from, or about, the recipient; and

(ii) any subsequent time when the terms of an existing consummated commercial financing contract are changed, prior to the recipient agreeing to the changes, if the resulting changes to the contract would result in an increase to the finance charge.

(iii) notwithstanding subparagraphs (i) and (ii) of this paragraph, at the time a specific periodic payment or irregular payment amount, rate or price is quoted to a recipient in writing based upon information from, or about, the recipient, and before the draw or purchase occurs, in connection with each draw on an open-end credit plan if:

(a) draws occur at the time that a recipient purchases products or services from a retailer or supplier; and

(b) the rate or price varies based upon the retailer or supplier the recipient selects, or the products or services the recipient purchases; or

(iv) notwithstanding subparagraphs (i) through (iii) of this paragraph, where a provider allows a recipient to select from multiple offer options or customize a financing offer, a provider must only provide the disclosure(s) for the specific offer that the recipient elects to pursue.”

That definition is similar to the one in California.

Connecticut: *A provider subject to the provisions of sections 1 to 10, inclusive, of this act shall provide to a recipient at the time of extending a specific offer for closed end financing the following disclosures in a format prescribed by the Banking Commissioner:*

Connecticut Bill No. 745 Section 4 (2021)

New Jersey: *Notwithstanding any other law to the contrary, a provider that extends small business financing to a small business concern located in this State shall, **at the time the contract is offered**, provide the following disclosures to the small business concern, as applicable:*

a. (1) for a closed-end loan, the total dollar costs to be charged to a borrower, assuming the borrower pays the loan according to its original payment schedule, plus all required fees and charges that cannot be avoided by the borrower, including any fees deducted or amounts withheld at disbursement.

New Jersey S.233 Section 2(a)(1) (2021)

North Carolina: *A covered lender shall provide all of the following disclosures to a borrower in a format prescribed by the Commissioner at the time of extending a specific offer of closed-end financing:*

North Carolina Small Business Truth in Financing Act Section 53-444.

I think it is safe to conclude that all of the states we’re discussing require that the disclosures be generated before or at the time the offer is extended. Be careful, though, if you

are renewing or rewriting a loan, particularly one that consolidates a previous loan, as it may require an entirely new set of disclosures.

DISCLOSURES IN CLOSED-END TRANSACTIONS

California: We begin with the statute, SB235 which, thankfully is not very long. Financial Code Section 22802 requires that the following disclosures be provided to the recipient at the time of extending an offer on a separate document and which must be signed by the recipient prior to consummating the transaction. The disclosures required by law are followed by some of the definitions contained in the modifications:

Except as provided in Section 22803, a provider subject to this division shall disclose all of the following:

(1) The total amount of funds provided. *Note: No definitions in the regulations but there are charts which serve as examples. For this I commend to you the proposed modifications at Pages 52-53.*

<https://dfpi.ca.gov/wp-content/uploads/sites/337/2021/08/2021-08-09-Commercial-Financing-Disclosures-Second-Modified-Text.pdf> (2021)

(2) The total dollar cost of the financing. *“Amount financed” means, with respect to a closed-end transaction, the principal amount, plus any other amounts that are financed by the financier and are not part of the finance charge, minus any prepaid finance charge. “Finance charge” means the amount of any and all costs of the financing, represented as a dollar amount, as more specifically described in section 3010 of these rules.*

(3) The term or estimated term. *With respect to closed-end transactions, the contracted length of time necessary for the recipient to fulfill its obligations under the financing agreement with respect to a particular loan advance*

If the term or estimated term of a transaction is:

(A) One year or less, the term or estimated term shall be disclosed in days;

(B) Greater than one year, the term or estimated term shall be disclosed in units of years and months, with any remaining days expressed as a portion of a month to the nearest two decimal points. For the purposes of these disclosures, a provider shall assume that there are 30 days in every month and 360 days in a year. For example, a term of 400 days would be disclosed as “1 year, 1.33 months”.

(4) The method, frequency, and number of payments.

Frequency: *If, assuming the recipient makes minimum required payments under the contract, it is possible to calculate with certainty, the total payments the recipient will make during the contract’s term, disclose the total payments. If, assuming the recipient makes minimum required payments under the contract, it is not possible to calculate with certainty the total payments the recipient will make during the contract’s term, disclose the estimated total payments.*

Amount: *The total dollar amount of payments or total estimated dollar amount of payments the recipient will make during the term of the contract if the recipient makes minimum required payments.*

(5) A description of prepayment policies. *There is nothing in the regs about this as to closed-end transactions, but the regs do address this issue as it pertains to lease financing:*

A) If, at any time during the term of the transaction, prepayment of the outstanding balance due will require the recipient to pay finance charges other than interest accrued since the recipient's last payment, the following statement: "If you pay off the financing before the end of the Term, you will be required to pay all or a portion of the finance charge other than accrued and unpaid interest, up to \$[maximum non-interest finance charge]."

(B) In all other cases, the following statement: "If you pay off the financing before the end of the Term, you will not be required to pay any portion of the finance charge other than unpaid interest accrued."

And:

(A) If, at any time during the term of the transaction, prepayment of the outstanding balance due will require the recipient to pay additional fees and charges not included in the finance charge, the following statement: "If you pay off the financing before the end of the term, you must pay additional fees or charges, including" followed by a description of any prepayment charges.

(B) In all other cases, the following statement: "If you pay off the financing before the end of the term, you will not be required to pay additional fees or charges."

(6) The total cost of the financing expressed as an annualized rate. *APR: If the contract provides for a fixed interest rate or rates that are predetermined by the contract, or no interest rate, the following language: "Annual Percentage Rate (APR)".*

(ii) If the contract provides for an adjustable interest rate or rates that are not predetermined by the contract, the following language: "Estimated Annual Percentage Rate (APR)."

You must also include the following language if the contract provides for a single, fixed interest rate:

*"APR is the cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make. **Your APR is not an interest rate.** Your interest rate is [interest rate]. Your APR may be higher than your interest rate because APR incorporates interest costs and other finance charges."*

The following language, if the contract provides for a multiple pre-determined interest rate, that change over time:

*"APR is the cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make. **Your APR is not an interest rate.** Your initial interest rate is [initial interest rate]. Your APR may be higher than your interest rate because APR incorporates*

interest costs and other finance charges.”

The following language, if the contract provides for an adjustable interest rate or rates that are not predetermined by the contract.

“APR is the cost of your financing expressed as a yearly rate. APR includes the amount and timing of the funding you receive, interest and fees you pay and the payments you make.

***APR is not an interest rate.** Your initial interest rate is [initial interest rate]. Although your interest rate will adjust over time, for the purposes of calculating this APR estimate, we have used the initial interest rate for future periods where the interest rate is not preset by the contract. Your APR may be higher than your interest rate because APR incorporates interest costs and other finance charges.”*

The annual percentage rate shall be expressed to the nearest ten basis points.

Section 22803 deals with factoring or asset-based lending, which I will discuss at a later date.

New York: Again, we begin with the statute, the fairly straightforward SB5470. Then we need to look to the recent modifications to see how they may supplement or change the law.

Closed-end commercial financing disclosure requirements.

A provider, subject to this article, shall provide the following disclosures: (a) The total amount of the commercial financing, and the disbursement amount, if different from the financing amount, after any fees deducted or withheld at disbursement. Amount financed *means, with respect to:*

*(i) a closed-end transaction or sales-based financing, the amount of funds to be provided by the financier to the recipient or on the recipient’s behalf. This also applies to lease financing. **This disclosure also requires advising the recipient of deductions including broker fees.***

(b) The finance charge. (1) for all commercial financing transactions, all charges that would be included in the finance charge under the federal Truth in Lending Act, Regulation Z, 12 C.F.R. section 1026.4 (effective April 1, 2019), and only such charges, if the transaction were a consumer credit transaction and the financier were a creditor according to the definition set forth in 15 U.S.C. section 1602(g). (2) in any lease financing transaction, the sum of lease payments (including any regular periodic payments and irregular payments) and price of the purchase option that the lessee may pay to acquire the leased goods at the end of the lease, less the amount of funds provided that is disclosed to the recipient in accordance with section 600.15(b)(2) of this Part.

(c) The annual percentage rate, using only the words annual percentage rate or the abbreviation "APR", expressed as a yearly rate, inclusive of any fees and finance charges that cannot be avoided by a recipient, and calculated in accordance with the federal Truth in Lending Act, Regulation Z, 12 C.F.R. § 1026.22. The annual percentage rate is a measure of the cost of credit, expressed as a yearly rate, that relates the amount and timing of value received by the recipient to the amount and timing of payments made to the provider. For purposes of this section, the annual percentage rate shall be determined in accordance with either the United States Rule method or the actuarial method, as both are set forth in Appendix J, 12 C.F.R. Part 1026 (effective December 30, 2011). The annual percentage rate calculation shall include all finance charges.

The verbiage that must be included regarding the APR is almost identical to that of California (see above).

(d) The total repayment amount, which is the disbursement amount plus the finance charge. (i) *If, assuming the recipient makes minimum required payments under the contract, it is possible to calculate with certainty the total payments the recipient will make during the contract's term: "Total Payments.";* or (ii) *if, assuming the recipient makes minimum required payments under the contract, it is not possible to calculate with certainty the total payments the recipient will make during the contract's term: "Estimated Total Payments.";*

(e) The term of the financing. *The contracted length of time necessary for the recipient to fulfill its obligations under the financing agreement with respect to a particular financing advance. If, assuming the recipient makes minimum required payments under the contract, it is possible to calculate with certainty the total payments the recipient will make during the term of the contract: "This is the total amount of payments you will make during the term of the contract.";* or (ii) *if, assuming the recipient makes minimum required payments under the contract, it is not possible to calculate with certainty the total payments the recipient will make during the term of the contract: "This is our estimate of the total amount of payments you will make during the term of the contract."*

(f) The payment amounts: (i) *for payment amounts that are fixed, the payment amounts and frequency (e.g., daily, weekly, monthly), and, if the term is longer than one month, the average monthly payment amount;* or

ii) for payment amounts that are variable, a full payment schedule or a description of the method used to calculate the amounts and frequency of payments, and, if the term is longer than one month, the estimated average monthly payment amount.

(g) *A description of all other potential fees and charges that can be avoided by the recipient, including, but not limited to, late payment fees and returned payment fees.*

(h) *Were the recipient to elect to pay off or refinance the commercial financing prior to full repayment, the provider must disclose: If, at any time during the term of the transaction, prepayment of the outstanding balance due will require the recipient to pay charges other than interest accrued and unpaid since the recipient's last payment, the following statement: "If you pay off the financing early you will still need to pay all or portion of the finance charge, up to \$[maximum non-interest finance charge]."; and (2) in all other cases, "If you pay off the financing early, you will not need to pay any portion of the finance charge other than unpaid interest accrued."*

(i) whether the recipient would be required to pay any finance charges other than interest accrued since their last payment. If so, disclosure of the percentage of any unpaid portion of the finance charge and maximum dollar amount the recipient could be required to pay; and

(ii) whether the recipient would be required to pay any additional fees not already included in the finance charge.

(i) *A description of collateral requirements or security interests, if any. A description of the collateral requirements or security interests of the transaction, if any.*

Note that the modification contains a separate group of rules for lease transactions. They can be found via the following link at Pages 32-35.

https://www.dfs.ny.gov/system/files/documents/2021/09/pre_proposed_fs_sect600.pdf

It should be apparent that, despite the different verbiage, these disclosures are quite similar to the ones required by New York.

Connecticut:

Thankfully things get easier now that we've move away from the coastal states and their somewhat abstruse modifications. Connecticut's disclosure law requires that the provider disclose to the recipient:

1. *The total amount of the commercial financing and the disbursement amount, if different from the financing amount, after any fees are deducted or withheld at disbursement.*
2. *The finance charge.*
3. *The annual percentage rate, using only the words "annual percentage rate" or the abbreviation "APR," expressed as a yearly rate, inclusive of any fees and finance charges that cannot be avoided by a recipient, and calculated in accordance with the federal Truth in Lending Act, Regulation Z, 12 CFR 1026.22, as amended from time to time.*
4. *The total repayment amount, which is the disbursement amount plus the finance charge.*
5. *The term of the financing.*
6. *The payment amounts as follows: (A) For payment amounts that are fixed, the payment amounts and frequency, and, if the term is longer than one month, the average monthly payment amount; or (B) for payment amounts that are variable, a full payment schedule or a description of the method used to calculate the amounts and frequency of payments, and, if the term is longer than one month, the estimated average monthly payment amount.*
7. *A description of all other potential fees and charges that can be avoided by the recipient, including, but not limited to, late payment fees and returned payment fees.*
8. *Were the recipient to elect to pay off or refinance the commercial financing prior to full repayment, the provider must disclose whether the recipient would be required to pay: (A) Any finance charges other than interest accrued since the recipient's last payment and, if so, disclosure of the percentage of any unpaid portion of the finance charge and maximum dollar amount the recipient could be required to pay; and (B) any additional fees not already included in the finance charge.*

9. *A description of collateral requirements or security interests, if any.*

There are no other regulations or modifications yet, so this is all we have for Connecticut at the moment.

New Jersey: Also, pretty straightforward and, to date, without any modifications we've seen.

Notwithstanding any other law to the contrary, a provider that extends small business financing to a small business concern located in this State shall, at the time the contract is offered, provide the following disclosures to the small business concern, as applicable:

1. *The total dollar costs to be charged to a borrower, assuming the borrower pays the loan according to its original payment schedule, plus all required fees and charges that cannot be avoided by the borrower, including any fees deducted or amounts withheld at disbursement;*
2. *The annual percentage rate, expressed as a nominal yearly rate, inclusive of any fees and finance charges;*
3. *The amount financed, which shall mean the total loan amount less any prepaid finance charges for the closed-end loan, including any fees deducted or amounts withheld at disbursement;*
4. *If the contract with the provider requires the small business concern to pay or be liable to pay a fee directly to any broker or other third party with respect to the small business financing, a description of that fee;*
5. *A description of the prepayment policies, including any fees, expenses or charges due when the small business financing is paid in full;*
6. *If not otherwise provided in writing to the small business concern, notice that the provider has acquired or will acquire a security interest in the collateral and a description of the collateral; and*
7. *A description of any other fees or charges that can be avoided by the small business concern, including, but not limited to, draw fees, late payment fees, and returned payment fees.*

Also worth noting:

Notwithstanding any other law to the contrary, a broker shall provide a written disclosure to the small business concern and to the provider stating the total dollar amount of fees charged to the small business concern by the broker in connection with a small business financing. The broker must provide this disclosure in a document separate from the provider's contract with the small business concern prior to the consummation of the small business financing transaction.

One more thing: *The commissioner shall promulgate regulations pursuant to the "Administrative Procedure Act," P.L.1968, c.410 (C.52:14B-1 et seq.) to provide that, in addition to the disclosures required to be provided to a small business concern pursuant to section 2 of this act.*

So, it may be clear now, but who knows what tomorrow will bring?

North Carolina: The new kid on the block. The disclosure mandate threshold amount is \$500,000, and the law specifically excludes true/operating leases. For other closed-end transactions, these are the required disclosures.

1. *The total amount of the commercial financing.*
2. *The disbursement amount, if different from the total amount of the commercial financing. This amount does not include any fees deducted at the time of disbursement.*
3. *The finance charge.*
4. *The annual percentage rate, using the words "annual percentage rate" or the abbreviation "APR," inclusive of the finance charge and any fees and calculated in accordance with 12 C.F.R. § 1026.22.*
5. *The total repayment amount, or the disbursement amount plus the finance charge.*
6. *The term of repayment.*
7. *The payment amounts as follows:*
 - a. *For payment amounts that are fixed, all of the following:*
 - b. *The payment amounts and frequency.*
 - c. *If the payment frequency is other than monthly, the amount of the average projected payment per month.*
8. *For payment amounts that are variable, all of the following:*
 1. *A payment schedule or a description of the method used to calculate the amounts and frequency of the payments.*
 2. *The amount of the average projected payment per month.*
9. *A description of all other potential fees not included in the finance charge including draw fees, late payment fees, and returned payment fees.*
10. *The following information relating to a borrower's election to pay off or refinance the commercial refinancing prior to full repayment:*
 - a. *Whether the borrower upon this election would be required to pay a percentage of the unpaid portion of the finance charge, other than interest accrued since the borrower's last payment. If so, the covered lender shall disclose this percentage, as well as the maximum dollar amount the borrower could be required to pay.*
 - b. *Whether the borrower upon this election would be required to pay any fees not already included in the finance charge.*
11. *A description of any collateral requirements or security interests.*

There are also disclosure requirements for renewal financing at Section 53-448.
<https://webservices.ncleg.gov/ViewBillDocument/2021/51680/0/DRH10488-MUf-27A>

Also noteworthy:

A covered lender operating in this State shall register with the Commissioner in a format prescribed by the Commissioner and shall submit a registration fee, as required by this section. A covered lender shall comply with all provisions of this Article. It's not quite a license state, but it's close.

Finally:

The Commissioner may adopt rules to enforce this Article, including rules to calculate metrics required to be disclosed under this Article.

Nothing is easy!

Keep in mind that this is a necessarily truncated synopsis of the rules and regulations governing closed-end disclosures. It is intended to provide an overview of what the new disclosure laws require, but it is by no means complete, as it would be nearly impossible to condense 150 pages or so into something readable and helpful. But this should get you started. Still, you will want the assistance of a professional to revamp your contracts in a manner that complies with the various formatting, column, font and other technical requirements.