

New California Disclosure Rules Reduce Capital Available to Small Businesses

In a poll conducted by the Secured Finance Network (SFNet), since new CA disclosure rules were implemented in December 2022, 40% of respondents were found to be “no longer lending” to prospective borrowers who fall within the regulations’ threshold of less than \$500,000. SFNet is an 80-year-old nonprofit with members representing the \$4T U.S. secured finance industry. The new law, requiring sweeping financial disclosures, introduced by CA State Senator Steven M. Glazer in 2018, faced four years of strong opposition before being rolled out in December of 2022.

According to the poll, commercial finance companies would rather not lend to small businesses than comply with what they believe are “misguided and un-compliable” requirements. Mark Hafner, president and CEO of Celtic Capital Corporation, based in Calabasas, CA, said, “Unfortunately, we must now shy away from smaller deals (under the \$500k threshold) as the disclosure requirements are extremely complicated to figure out and would require getting our attorneys and CPAs involved to ensure compliance. It’s just not worth the costs involved to fund a small deal anymore. The statute is not user friendly and, frankly, not representative of the true costs as there are numerous assumptions that have to be made to calculate the APR based on the state’s requirements. I honestly don’t think it was designed to meet the stated goal of the statute.”

Robert Meyers, president of Republic Business Credit, which does business with many California-based businesses, explained, “While the fines and penalties are clear under the regulations, the state has been unwilling to confirm our compliance or anyone else’s compliance. That fear is what has stopped 40% of our non-banks from doing business in the state, thus reducing access to capital for small- and medium-sized businesses. I expect this number to increase as time goes on. If the goal of this law was to better inform, it is actually doing the opposite as APR just doesn’t apply to our products.”

SFNet reports that its member companies provide “tens of billions” of capital annually in California to small businesses for essential working capital that funds everything from inventory, to work in process to payroll.

“Forty percent of billions is a large number,” said SFNet CEO, Richard D. Gumbrecht. “In attempting to find a one-size-fits-all solution to financial transparency, the State has created a complex set of requirements that misrepresent the actual cost of borrowing. Lenders are saying it’s not worth the cost and risk of complying. If this sample of 50 lenders is indicative of what we can expect, clearly that was not the intent of the legislation. And considering the demise of Silicon Valley Bank, it’s more important than ever that capital is not restricted in California.” The trade association is working with State legislatures to revise the

statute. “Other states have found a simpler and more accurate way to protect small borrowers, and given the unintended consequences we are seeing, we are hopeful California will be receptive to these alternative approaches.”

To demonstrate how vital small businesses are to the U.S. economy, and the importance of not curtailing funding, consider these statistics: According to the U.S. Small Business Association (SBA), small businesses of 500 employees or fewer make up 99.9% of all U.S. businesses and 99.7% of firms with paid employees. Of the new jobs created between 1995 and 2020, small businesses accounted for 62%—12.7 million compared to 7.9 million by large enterprises. A 2019 SBA report found that small businesses accounted for 44% of U.S. economic activity.

About Secured Finance Network

Founded in 1944, the Secured Finance Network (formerly Commercial Finance Association) is an international trade association connecting the interests of companies and professionals who deliver and enable secured financing to businesses. With more than 1,000 member organizations throughout the U.S., Europe, Canada and around the world, SFNet brings together the people, data, knowledge, tools and insights that put capital to work. For more information, please visit [SFNet.com](https://www.sfnet.com).