October 31, 2022
Department of Financial Services
George Bogdan
1 State St
New York, New York 10004
george.bogdan@dfs.ny.gov
VIA ELECTRONIC TRANSMISSION

RE: Proposed 23 NYCRR 600, Disclosure Requirements for Certain Providers of Commercial Financing Transactions

Dear Mr. Bogdan:

We, the undersigned coalition of 61 non-profit organizations and for-profit lending companies, thank the Department for publishing a strong proposed rule of the New York State Small Business Truth-in-Lending Act. We thank the New York State Department of Financial Services ("Department" or "DFS") for this critical step towards the final rule.

As background, in 2020 the New York State legislature passed the Small Business Truth in Lending Act (SB5470B, now Article 8 of the Financial Services Law), bringing sunshine to the commercial financing marketplace. On

October 20, 2021, the Department published a comprehensive draft rule that enables New York to set a strong standard for small business truth-in-lending disclosures. On September 24, 2022, DFS published another proposed rule incorporating thoughtful revisions from the comments received from the previous comment period.

We applaud the New York State Department of Financial Services for releasing the most thorough set of small business lending disclosures in the country. Congress and other state legislatures, recognizing the strength of this law, are looking to New York to harmonize their own small business truth-in-lending bills. In particular, we commend the proposed rule's clear directives on disclosure of the Annual Percentage Rate, broad application to borrowers AND financiers based in New York, as well as the high financing threshold to trigger disclosures: $2.5 million. DFS' regulations will empower entrepreneurs with the standardized, transparent disclosures they need to compare financing options and select the best product for their business.

We offer two recommendations to ensure the proposed rule is consistent with the statute and accomplishes its laudable goals for the people of New York:

> Recommendation 1: Reflect the statute's prohibition against quoting pricing in misleading ways
>
> Recommendation 2: Clarify that APR disclosures remains required after a specific financing offer is extended

Additionally, we urge the Department to release resources for lenders in order to streamline compliance and reduce ambiguity, once the final rule is released.

Recommendation #1: Reflect the statute's prohibition against quoting pricing in misleading ways

A central problem that the Small Business Truth in Lending Act set out to address is the widespread use of potentially misleading ways of describing prices. It is common for financing companies to quote prices using metrics that are easily mistaken by small business owners to be an annual interest rate or APR, when in fact the actual interest rate or APR is much higher.

As currently written, the proposed changes leave out and undermine a key provision of the statute that makes the New York State's Small Business Truth in Lending Act the strongest in the nation, as well as the model for other states and federal legislation. Specifically, Section 810 of the statute prohibits financing companies from the common practice of describing pricing using misleading metrics. These misleading metrics can lead a borrower to believe that the financing is much less expensive than it actually is. This provision of the statute is not currently reflected in the proposed rules and should be included. Later, we suggest two language changes to accomplish this recommendation.

Examples of these potentially misleading terms include "simple interest rate," "factor rate," "fee rate," and even simply the "rate." For example, financing described as having a "simple interest rate of 20%" may in fact have an interest rate of 66%.[1]

This problem has been studied by Federal Reserve researchers, who established that certain pricing metrics used by financing companies are easily misunderstood by borrowers to be the interest rate or APR, and so can have the effect of misguiding small businesses. This study explains that "non-standard terminology" used by some alternative

[1] In this example, financing with a fee of 20%, here called a "simple interest rate of 20%," is repaid over 6 months with monthly payments of equal amount. The resulting annual interest rate is 66%.

lenders "proved challenging for focus group participants trying to compare online offerings with traditional credit products."[2]

The following table published by the Federal Reserve illustrates the severity of this misleading practice. In the left column, the "non-standard terminology" for price is displayed. The price number presented on the left is markedly lower than the actual APR noted in the right column. For example, a "4% fee rate" may be understood to be a 4% rate, but represents an approximate APR of 45%.

Table 3. Estimated APRs for select online products

Rate advertised on website	Product details	Estimated APR equivalent
1.15 factor rate	• Total repayment amount $59,000 • Fees: 2.5% set-up fee; $50/month administrative fee • Term: none (assume repaid in six months) • Daily payments (assume steady payments five days/week)	Approximately 70% APR
4% fee rate	• Total repayment amount $56,500 • Fee rate: 4% (months 1–2), 1.25% (months 3–6) • Fees: none • Monthly payments • Term: six-month term	Approximately 45% APR
9% simple interest	• Total repayment amount $54,500 • Fees: 3% origination fee • Weekly payments • Term: six-month term	Approximately 46% APR

Source: Authors' calculations, based on product descriptions on company websites.

Each of these "non-standard" metrics in the left column is a different name for the same metric. It is a financing charge expressed as a fraction of the financing amount. A more common term for this metric is a "fee." The first example in the table above, the "1.15 factor rate," is more commonly understood as a 15% fee. The second example, a "4% fee rate," would be more commonly understood as a 4% fee charged monthly. The third example, "9% simple interest" is a 9% fee, and bears little resemblance to the interest rate, which would be 34%. (Combining that 34% effective interest rate with the 3% origination fee produces the 46% APR).

An earlier Federal Reserve research study came to the same conclusion that certain pricing metrics are often confusing and can be effectively misleading. It found that small businesses in the study "most commonly conflated 'simple interest' with APR." On a separate disclosure using the metric "factor rate," the study found that "the term

[2] Lipman, Barbara and Wiersch, Anne Marie, Board of Governors of the Federal Reserve System, "Uncertain Terms: What Small Business Borrowers Fund When Browsing Online Lender Websites," Dec 2019. https://www.federalreserve.gov/publications/files/what-small-business-borrowers-find-when-browsing-online-lenderwebsites.pdf

'factor rate' was the main source of confusion for the majority of participants who stated that they had not heard it before."[3] It may not be a coincidence that the "simple interest" rate and "factor rate" is also often a lower number than the APR. This may be why financing companies use these metrics!

The problem of misleading pricing metrics is only partially addressed by the Small Business Truth in Lending Act's required disclosure form. That form is presented when a financing offer is extended or changed. While a one-time disclosure of the APR is helpful, it does not fully address the issue because potentially misleading pricing metrics may be used outside of the required disclosure, before and after a financing offer is extended or changed.

We should not overestimate the power of a one-time disclosure. If an applicant sees "simple interest rate of 9%" several times before the disclosure indicates a 46% APR, and then sees "simple interest rate of 9%" several times after, the lower number that is stated first and more often may be the one that applicants remember. Some applicants may simply not pay attention to the required disclosure form, or may focus on another detail disclosed in that form, such as the payment amount.

Fortunately, the drafters of the New York Small Business Truth in Lending Act included the following language, now Section 810 of the CFDL, specifically to address the use of misleading price metrics outside of the presentment of a specific offer of financing:

> "IF OTHER METRICS OF FINANCING COST ARE DISCLOSED OR USED IN THE APPLICATION PROCESS OF A COMMERCIAL FINANCING, THESE METRIC SHALL NOT BE PRESENTED AS A "RATE" IF THEY ARE NOT THE ANNUAL INTEREST RATE OR THE ANNUAL PERCENTAGE RATE. THE TERM "INTEREST", WHEN USED TO DESCRIBE A PERCENTAGE RATE, SHALL ONLY BE USED TO DESCRIBE ANNUALIZED PERCENTAGE RATES, SUCH AS THE ANNUAL INTEREST RATE."[4]

This statutory requirement does not limit any particular metric from being used. Rather, it requires the metrics be formatted in a manner less likely to be misleading. For example, a "fee rate of 4%" is not permissible because the statute states that, "THESE METRIC SHALL NOT BE PRESENTED AS A 'RATE' IF THEY ARE NOT THE ANNUAL INTEREST RATE OR THE ANNUAL PERCENTAGE RATE." Instead, this same charge could be permissibly described as a "monthly fee of 4%." Similarly, a "factor rate of 15%" is not permissible, but a "factor charge of 1.15x" would be. Describing pricing as having "simple interest of 9%" would not be permissible because the statute states that, "THE TERM 'INTEREST', WHEN USED TO DESCRIBE A PERCENTAGE RATE, SHALL ONLY BE USED TO DESCRIBE ANNUALIZED PERCENTAGE RATES, SUCH AS THE ANNUAL INTEREST RATE." However, the same charge could be permissibly described as a "9% fee." We are hopeful these clarifications will reduce the use of confusing or misleading pricing terms.

As you can see in the text of Section 810 of the CFDL quoted above, this limitation on potentially misleading pricing metrics is not limited to the timing of presentation of a specific offer of financing. It applies *at any time* "in the application process."[5]

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[3] Lipman and Wiersch, Federal Reserve Board of Governors, "Browsing to Borrow: 'Mom & Pop" Small Business Perspectives on Online Lenders," June 2018. https://www.federalreserve.gov/publications/files/2018-small-businesslending.pdf

[4] Financial Services Law (FIS) CHAPTER 18-A, ARTICLE 8, § 810, "Additional Information." https://www.nysenate.gov/legislation/laws/FIS/810

[5] Financial Services Law (FIS) CHAPTER 18-A, ARTICLE 8, § 810, "Additional Information." https://www.nysenate.gov/legislation/laws/FIS/810

This concern about misleading pricing metrics does not appear to be addressed in the "Assessment of Public Comments for the Revised Proposed New Part 600 to 23 NYCRR." Of concern, changes made in the new version of the proposed rules worsen the problem. The new version of the proposed rule includes new language, intended to address a *different* provision within Section 810 of the statute, that undermines this statutory restriction of misleading financing metrics "in the application process."

The new language of the rule states that Section 810's requirements would apply only *after* a specific offer is made, although "the application process" described in Section 810 begins before a specific offer is made. The proposed rule's definition of "at the time of extending a specific offer" in 600.1(f) now reads: "The requirements pertaining to the statement of a rate of finance charge or a financing amount, as that term appears in Section 810 of the CFDL, shall be in effect only upon the quotation of a specific commercial financing offer."

The Assessment of Public Comments explains the rationale for this newly added language. It makes clear the new language was intended to address a *different* requirement within Section 810 of the CFDL related to APR disclosure.[6] The new language was intended to make clear that APR disclosure is not required until after a specific offer of financing has been extended, making APR easiest to calculate.

However, the provision of Section 810 that restricts the use of misleading rates does not require the calculation of APR and so should not be subject to this limitation. As such, we recommend two additions to the proposed rule.

First, we suggest that Part 600.01(f)(1) of the proposed rule, and all similar language, be amended to include underlined phrase below:

> "The requirements pertaining to the <u>re-statement of APR upon any</u> statement of a rate of finance charge or a financing amount, as that term appears in Section 810 of the CFDL, shall be in effect only upon the quotation of a specific commercial financing offer;"

This amendment would help clarify that the portion of Section 810 of the CFDL that prohibits certain potentially misleading pricing metrics applies when the "application process" begins, as described in the statute, rather than "only upon the quotation of a specific commercial financing offer."

Second, we suggest that language be added to the rule clarifying that the portion of Section 810 of CFDL quoted above does in fact apply. Although statute remains binding whether or not it is restated in regulation, most financing companies and lawyers may be relying on the Department's rules as the guide for requirements, without additionally consulting the statute for matters unaddressed in the rule. The degree of compliance with a portion of statute not reflected in the rule is likely to be lower.

Additionally, omitting key potions of the statute from the rule could undermine the use of these rules as the model for the nation. Other states such as Maryland have proposed small business truth legislation that would require the local state's department of financial regulation to adopt rules based on those promulgated by the New York Department of Financial Services. These laws of other states point to the Department's rules rather than New York State's statute, and so would not include topics addressed in the statute but omitted from the Department's rule. If

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[6] The Assessment of Public Comments explains the rationale for this new language is unrelated to this provision of Section 810 of the CFDL. It states, "The Department believes that FSL Section 810 requires disclosure of APR any time an interest rate is quoted as part of a specific offer of commercial financing, but does not believe it requires an APR disclosure any time a broker, salesperson, or covered individual mentions an interest rate or financing amount during the application process, because calculating APR correctly is complex and requires consideration of much information, some of which may not be knowable until more specifics of the transaction have been finalized. For clarity, the Department revised Part 600 to include the following language: "The requirements pertaining to the statement of a rate of finance charge or a financing amount, as that term appears in Section 810 of the CFDL, shall be in effect only upon the quotation of a specific commercial financing offer." Part 600.01(f)(1)." https://www.dfs.ny.gov/system/files/documents/2022/09/rp_23nycrr600_apc_20220914.pdf

this key topic is not addressed in the Department's rules, the rules may not serve as an appropriate model for other states.

This needed addition that Section 810's prohibition of misleading pricing metrics applies could be included in as a new section of the rule, perhaps entitled, "Other pricing disclosures during the application process." This new section could read,

> "(a) During an application process for commercial financing, if metrics of financing cost are disclosed or used:
>
> (1) These metric shall not be presented as a "rate" if they are not the annual interest rate or the annual percentage rate;
>
> (2) The term "interest", when used to describe a percentage rate, shall only be used to describe annualized percentage rates, such as the annual interest rate."

If the Department seeks to define "during an application process for commercial financing," we encourage the Department to use as broad a definition as possible. As discussed above, these requirements place no significant compliance burden on providers because in all cases the same pricing metric can continue to be disclosed, albeit using language that is less potentially misleading. An appropriate definition of "during an application process for commercial financing," may be "at any point in the sale of financing where a potential recipient could initiate an application or has already initiated an application."

Recommendation #2: Clarify that APR disclosures remains required *after* a specific financing offer is extended

We urge the Department to clarify that disclosure of APR is required any time price or amount is quoted to a small business applying for credit, *after* a specific financing offer has been extended. Below, we suggest additional language the Department could consider to provide this clarification.

Section 810 of the CFDL includes an important provision that requires APR to be disclosed alongside any other pricing metrics or financing amount metrics, during an application process. It reads:

> "WHEN A PROVIDER STATES A RATE OF FINANCE CHARGE OR A FINANCING AMOUNT TO A RECIPIENT DURING AN APPLICATION PROCESS FOR COMMERCIAL FINANCING, THE PROVIDER SHALL ALSO STATE THE RATE AS AN 'ANNUAL PERCENTAGE RATE', USING THAT TERM OR THE ABBREVIATION 'APR'."[7]

This provision was intended by the bill's author and the Responsible Business Lending Coalition, which supported the drafting of the bill to keep APR as part of the financing process between the provider and small business applicant.

The Department has added language to the proposed rule addressing this requirement, which we believe merits further clarification. The Assessment of Public Comments explains that new language has been added to the rule to clarify that Section 810 does not require that APR be disclosed *before* a specific offer has been extended. We believe

[7] Financial Services Law (FIS) CHAPTER 18-A, ARTICLE 8, § 810, "Additional Information." https://www.nysenate.gov/legislation/laws/FIS/810

the rule should be clarified to state that APR continues to be required *after* the specific offer has been extended. The Assessment of Public Comment explains:

> "The Department believes that FSL Section 810 requires disclosure of APR any time an interest rate is quoted as part of a specific offer of commercial financing, but does not believe it requires an APR disclosure any time a broker, salesperson, or covered individual mentions an interest rate or financing amount during the application process, because calculating APR correctly is complex and requires consideration of much information, some of which may not be knowable until more specifics of the transaction have been finalized. For clarity, the Department revised Part 600 to include the following language: "The requirements pertaining to the statement of a rate of finance charge or a financing amount, as that term appears in Section 810 of the CFDL, shall be in effect only upon the quotation of a specific commercial financing offer." Part 600.01(f)(1).[8]

While the Department has concluded that calculating an APR requires information that may not be knowable until terms of the transaction has been finalized, we believe the Department would agree that APR can continue to be calculated and presented *after* those terms have been finalized.

After the full disclosure form is presented upon the quotation of a specific financing offer, the financing company will continue to refer to the financing. For example, a later state of the application process that follows the initial disclosure form might state, "For your advance of $50,000 with a factor of 1.15, upload your documents here…" To comply with the statute, Section 810, this page of the application process would need to state, "For your advance of $50,000 with a factor of 1.15 *and estimated APR of 70%*, upload your documents here…"

As described above, we believe that the influence of a single disclosure page should not be overestimated. Applicants may in some cases scan the page, focus on some aspects more than others, or be influenced by a financing company's repetitive use of other pricing metrics. These patterns of behaviors are why we, as a coalition, worked with the author of the bill to include Section 810 of the CFDL.

To provide the needed clarification, we suggest adding a clarifying provision to the rule, "Section 600.3 Annual percentage rate disclosure." This section describes that APR disclosure takes place "at the time of extending the specific offer of commercial financing." It appears to not reflect the statutory requirement that APR disclosure continue to take place after this stage. We are concerned that, while the statute remains binding, a lack of clarity in the rules themselves will likely lead to lower rates of compliance. We thus suggest adding an additional sub-section reflecting the statutory requirement that, after a specific offer has been extended, the APR disclosure requirement remains in place. The following underlined language could be used:

> "(b) When a provider states a rate of finance charge or a financing amount to a recipient during an application process for commercial financing and after the quotation of a specific commercial financing offer, the provider shall also state the rate as an 'annual percentage rate,' using that term or the abbreviation 'APR.'"

Without this clarification, the proposed rules do not reflect the requirements of statute and may not result in the level of compliance, and benefit to New York's small businesses and economy, that the Department intends.

Secondary Recommendation: Simplify "double dipping disclosure"

We offer a secondary recommendation that we believe would simplify the disclosure form, increasing its readability and effectiveness. The proposed rules include an important and laudable section requiring disclosures related to the

[8] Page 6-7 https://www.dfs.ny.gov/system/files/documents/2022/09/rp_23nycrr600_apc_20220914.pdf

practice of double dipping.[9] We suggest that this subsection require disclosure of double dipping practices *if* double dipping is occurring, but *not if* double dipping is not occurring.

When double dipping is occurring, that disclosure is very valuable information. Double dipping is a confusing way to effectively double-charge a borrower. If the practice is not explained, it often goes unnoticed. However, if double dipping is *not* occurring, a discussion of this confusing practice presents unnecessary and potentially confusing text, potentially reducing the effectiveness of the disclosure overall.

We suggest the following underlined language be added in subsection 600.6(b)(3)(v) and similar subsections within Sections 600.10, 600.11, 600.12, 600.14, and 600.15:

> "(v) If any portion of the amount financed will be used to satisfy obligations under another financing with the provider, in the third column, in a second paragraph: 'Does the renewal financing include any amount that is used to pay unpaid finance charges or fees, also known as double dipping?' {Yes, enter amount}. If the amount is zero, the answer would be No.[2] If the amount is zero, this paragraph need not be included in the disclosure. If the financing being satisfied featured a fixed finance fee that did not vary based on the repayment period, the provider shall consider the amount that is used to pay unpaid finance charges or fees to be the pro rata portion of such finance fee based upon the fraction of the original total amount financed of the previous financing already repaid by the recipient."

We trust that this change is consistent with legislative intent. In fact, this coalition had a role in drafting the bill's text. However, we believe an improperly placed quotation mark has implied that more disclosure is required than necessary. The end quote that follows "If the amount is zero, the answer would be No," may have been intended to fall earlier in the paragraph, at the end of the question, "Does the renewal financing include any amount that is used to pay unpaid finance charges or fees, also known as double dipping?"

Reducing this disclosure, where unnecessary, would simplify the disclosure for small businesses reading the disclosure form, and increase the disclosure's effectiveness.

Release Guidance to Streamline Compliance with the Final Rule

We recognize that the law is not meant to cause undue burden to lenders. Once the final rule is released, we urge DFS to release a Frequently Asked Questions document, convene an informational webinar, offer sample disclosure forms, a formal vehicle to engage the Department should implementation questions arise, and any other resources that would be helpful for lenders to understand the regulation. These resources will reduce ambiguity and streamline implementation, which is especially helpful for smaller lenders that do not have immediate access to an attorney.

Conclusion

As New York's hard-working entrepreneurs begin to emerge from the shadows of the COVID-19 crisis, they are seeking financing to adapt their products and services, hire employees, and expand their businesses. Entrepreneurs need clear information about rates and terms to avoid cycles of debt and unaffordable financing. The RBLC has upheld the New York legislation as a model, cross-sector consensus bill and look forward to working with you to

[9] See Section 600.6(b)(3)(v) and similar subsections within Sections 600.10, 600.11, 600.12, 600.14, and 600.15.

ensure that there's a clear path to implementation. We ask DFS to finalize and implement the regulations as soon as possible.

Sincerely,

1. Responsible Business Lending Coalition
   Members include: Accion Opportunity Fund, Camino Financial, Community Investment Management, Funding Circle, LendingClub, National Association for Latino Community Asset Builders, Opportunity Finance Network, Small Business Majority, and the Aspen Institute
2. 3Es Consulting Group
3. Accion Opportunity Fund
4. American Fintech Council
5. Anchor Financial Services
6. The Blackwall Street Corporation
7. Bluez Oils Inc
8. Business Outreach Center Capital
9. Business Outreach Center Network
10. Business Center for New Americans
11. The Business Council of Westchester
12. CAMEO Network
13. Capital CFO
14. CBR Improvement Strategies, LLC
15. Center for NYC Neighborhoods
16. CMR Communications
17. Community Capital New York
18. Community Development Venture Capital Alliance
19. Community Investment Management
20. Community Loan Fund of the Capital Region
21. The Dutch Pot LLC
22. Endorphin Advisors LLC
23. Fresh Neighborhood Market
24. Funding Circle
25. Greater Jamaica Development Corp
26. Guilderland Chamber of Commerce
27. Habitat for Humanity NYC Community Fund
28. The Hair Hive
29. Harlem Entrepreneurial Fund
30. Head Heart Hands Consulting LLC
31. Hill & Markes
32. Hot Bread Kitchen
33. Human Scale Business
34. Jefferson Economic Development Institute
35. Justine PETERSEN
36. La Fuerza Unida CDC

37. LendingClub
38. Leviticus Fund
39. Lighter Capital
40. Lockdown Security Services
41. Michael Roach Creative
42. MultiFunding
43. National Urban League
44. New York State CDFI Coalition
45. NextStreet
46. Opportunity Finance Network
47. Oswego County Federal Credit Union
48. PathStone Enterprise Center
49. Pursuit
50. Small Biz Silver Lining
51. Small Business Majority
52. SMB Intelligence
53. Spring Bank
54. StreetShares
55. Tech Valley Shuttle
56. This Week in Fintech
57. TruFund Financial Services, Inc.
58. United Way of the Greater Capital Region
59. Upstate Minority Economic Alliance (UMEA)
60. UpState New York Black Chamber of Commerce
61. Woodstock Institute