***The Consumer Finance Podcast* x *Payments Pros* –** Point-of-Sale Finance Series: The New Regulatory Reality for Small Business Financing and Trade Credit
**Host:** Taylor Gess
**Guests:** Jason Cover, Caleb Rosenberg
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**Taylor Gess (00:05):**

Welcome to this special edition of *The Consumer Finance Podcast* and *Payments Pros*. I'm Taylor Gess, an associate in Troutman Pepper Locke's Consumer Financial Services Regulatory Practice, and I'll be your guest host for today's episode. Today, we're going to be giving you another installment of our special highlight series on point-of-sale finance, where we will discuss issues related to small business credit. But before we jump into that topic, let me remind you to visit and subscribe to our blogs, TroutmanFinancialServices.com and ConsumerFinancialServicesLawMonitor.com. And don't forget about all of our other podcasts. We have the *FCRA Focus*, all about credit reporting, the *Crypto Exchange* about crypto and digital assets. We have *Unauthorized Access*, which is our privacy and data security podcast, and of course, *Moving the Metal*, our auto finance podcast. All of those are available on all popular podcast platforms. Speaking of those platforms, if you like this podcast, let us know.

(00:58):

Leave us a review on your podcast platform of choice and tell us how we're doing. Now, as I said, today's episode is another in our special highlight series on point-of-sale finance. Here, I'm joined by my colleagues, Jason Cover and Caleb Rosenberg, to give us some insights into small business finance. Welcome to the podcast, Jason and Caleb.

**Caleb Rosenberg (01:15):**

Thanks, Taylor.

**Jason Cover (01:16):**

Thanks, Taylor.

**Taylor Gess (01:17):**

So Jason, we spent many of these episodes discussing consumer purpose transactions, but today's focus is on small business finance. How does the regulatory environment for small business transactions compare to the consumer space?

**Jason Cover (01:28):**

Taylor, I think much like what we've seen with home improvement products and general point-of-sale finance, I'd say over the last decade, and I know I've said this multiple times about multiple things, but there's been a real explosion in growth in small business lending or small business quasi-credit. And in conjunction with that, we've seen increased regulatory scrutiny, increased scrutiny at the legislature, increased scrutiny with plaintiffs, et cetera, over various types of small business lending as it's sort of moved from the traditional banking space to the fintech space and sort of permeated the landscape a bit more than it might have 10 or 15 years ago. So, with that, it's been both the states, the legislatures enacting various laws covering commercial lending transactions in the small business context or the FTC has weighed in, state AGs have weighed in. So, it's just one more area, particularly because of the growth of fintechs offering these types of products that there's been just increased awareness of them at the same time.

**Taylor Gess (02:28):**

Thanks, Jason. So, Caleb, where does this consumerization of small business finance arise for point-of-sale transactions in the B2B space?

**Caleb Rosenberg (02:36):**

Thanks, Taylor. So a lot of the same issues come up in B2B transactions that come up in the consumer space. So embedded finance offerings on the commercial side have increased in recent years. And even before that, as a starting point, sellers to business customers want to offer their customers flexibility on financing. Frequently, this has included offering trade credit where invoices is due 60 or 90 days after a sale. Those offerings don't tend to require a financing partner, but offering additional financing options such as multiple installments or longer terms is frequently where we see third-party financing begin to be offered. As Jason was talking about, this is frequently less burdensome in the consumer space from a regulatory perspective, but each of these arrangements can trigger regulations on disclosures, registration, rate caps, and fair lending requirements that should be considered. And so starting up these programs that I think a lot of our clients tend to think that the space is going to be almost unregulated.

(03:36):

And where that was true 10 years ago or 15 years ago, the focus on the space has really increased. And so even the simple disclosures that are required by some state laws do require some planning when offering in the point-of-sale context, especially when you're going to need customer signatures, when are you getting e-sign consents? A lot of the same requirements that we have to consider in the consumer space.

**Taylor Gess (03:57):**

Thanks, Caleb. That was really helpful. Jason, are there any recent updates on requirements for small business finance that you'd like to share with us today?

**Jason Cover (04:04):**

Yeah, I guess just to follow up real quick on Caleb's point, I think sometimes things that are lost in small businesses, you never quite know who you're lending or financing. And Caleb and I were just talking about this with a client yesterday. You could have a consumer account as the payment mechanism for repayment. And Reg E would apply because it's a consumer account, even if it's a commercial purpose loan. So the federal rules are not necessarily out of play and you have to be careful with that. There's Reg B requirements. I think Caleb will talk about that in a second. And then to get to your point, Taylor, what we have seen is a rash of legislation at the state level. And much of that is in the disclosure regimes that are somewhat TILA similar, I suppose. Recently, for example, Louisiana passed a law that requires commercial financing transaction disclosures.

(04:52):

That's on the heels of California, Connecticut, Florida, Georgia, New York, Virginia, and Utah. And some of these, depending on your type of program, much like the other types of point-of-sale finance transactions we've been talking about, there's folks that do direct loans, license lending loans, loans under general usury statutes, bank programs. So some of these commercial disclosure regimes may have exemptions. If you're a bank, they may have exemptions for other things. So you need to be aware of that when you're entering into this market. And then I guess the most recent thing we've seen, or maybe the most disconcerting is a recent law in Texas that materially regulates merchant cash advance programs. And if you're in that industry, if you're in Texas, you really need to be aware of that because it really changes the lay of the land there. And most MCA programs probably won't work.

(05:43):

So we've been working with a number of clients on alternatives here, and we're sort of pausing to see if anything like that pops up in other states.

**Caleb Rosenberg (05:51):**

The other place where we've seen state level distinctions that go beyond just the disclosure laws, California on the heels of including small business transactions in the Rosenthal Act followed up by amending its disclosure and UDAAP law, both of which already applied to small business transactions to prohibit certain uses of the term “interest” or “rate,” finding them deceptive if they're being used to describe a rate that's non-annual. There are legislative findings in this law targeting practices like describing a factor rate, which significantly diverges from what the annual rate would be or describing a rate as simple interest when it's meant to refer to non-pre-computed interest as opposed to how most small business owners may expect simple interest to be described, which is describing a non-compounding rate. These probably are not significantly burdensome to comply with, except for maybe describing an APR anytime a pricing metric or financing amount is referenced after providing California's disclosures.

(06:58):

But the thing that I think is really interesting about it is that it's California coming back again to the same space, amending its laws after seeing some practices that the legislature disapproved of, and also just adding to the patchwork between states. So we're seeing the payment provision in the Texas law that is very burdensome for MCA providers and now we're seeing another somewhat unique provision coming out of California. And so considering states on a state-by-state basis like providers have to do in the consumer space is becoming a much more frequent consideration in the commercial space as well. And then on the federal piece, Jason touched on this. In the fair lending area, 1071 developments continue to roll out as they have from time to time over the last more than decade now. The latest from that is that the CFPB has accepted comments through December 15th on the latest 1071 proposal.

(07:50):

It's expected that they'll roll out an updated rule relatively quickly, but we've said that before for 1071, and we expect following the finalization of any rule that the CFPB does publish for there to be probably follow-on litigation from one group or another, possibly both from consumer side and from the industry side, potentially delaying this further. Some litigation remains pending, and so things are still up in the air, but we expect there to be further developments in the next few weeks to months.

**Jason Cover (08:21):**

Caleb, any bets on whether MCA will be in route?

**Caleb Rosenberg (08:24):**

I think they'll be out given the current proposal and just the commentary on that both for prior rules and in this latest turn, but we'll see if it stays out given the litigation space and some prior filed actions and how those came out, but I'm following it pretty closely.

**Taylor Gess (08:41):**

Thank you, Jason and Caleb, for being here with us today. We've done a great job highlighting some of the key issues for people in the small business finance space to consider. So let's leave this special series here for now, and we'll pick back up with another very interesting topic on our next special joint episode for *The Consumer Finance Podcast* and *Payments Pros*. In the meantime, thanks to our audience for listening today. And don't forget to visit and subscribe to our blogs, TroutmanFinancialServices.com and ConsumerFinancialServicesLawMonitor.com. While you're at it, why not visit us on the web at Troutman.com and add yourself to our Consumer Financial Services email list. That way we can send you copies of the alerts and advisories that we send out, as well as invitations to our industry-only webinars that we put on from time to time. And of course, stay tuned for a great new episode of this podcast every Thursday afternoon and look forward to the remainder of our series on point-of-sale finance coming soon to your podcast feed. Thank you all for listening.

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