PRIVILEGED AND CONFIDENTIAL

M E M O R A N D U M

March 18, 2020

TO: SECURED FINANCE NETWORK, INC.

FROM: CO-GENERAL COUNSEL

RE: SUMMARY OF PROPOSED LEGISLATION (NEW JERSEY) DISCLOSURE / LICENSING FOR FACTORS AND ABL

Please be advised that New Jersey state Senator Nellie Pou (D-Paterson) has submitted to the New Jersey Senate and General Assembly legislation which, if enacted, would require certain factors and asset based lenders who lend to New Jersey borrowers to be licensed and comply with a very detailed and onerous set of disclosures prior to entering into a financing or factoring relationships with its borrowers/clients. This proposed legislation requires your immediate attention and, hopefully, your cooperation in working with SFNet and its professionals to try to change this outcome.

1. Basis of the proposed Legislation:

The proposed legislation has as its basis, the perceived lending abuses and predatory lending engaged in by merchant cash advance firms who are unregulated at present on either the state or federal level and who are referred to in the proposed legislation as Non-Bank Financers who engage in Alternative Lending. However, the proposed legislation is expansive in it definitions and also defines factors and asset based lenders as Alternative Lenders and Non-Bank Financers.

2. Who is Affected

Factors and asset based lenders who are not currently regulated by the state or federal government (banks being excluded) and who wish to extend credit to New Jersey borrowers either by making a loan, extending a line of credit, factoring, an asset based transaction or merchant cash advance in amount not to exceed $500,000 and which facility contains one or more of the following characteristics:

(a.) a term to maturity of less than 2 years or

(b.) payment frequency of greater than bi weekly or

(c.) credit approval without reliance on tax returns or financial and related traditional underwriting metrics or

(d) an interest rate, or a disclosed internal rate of return in the case of a merchant cash advance, in excess of 25 percent;

the proceeds of which are used for business purposes.

3. <u>Who is to regulate and license?</u>

New Jersey Department of Banking and Insurance.

4. <u>Lending Licenses for Non-Bank Financers engaged in Alternative Lending</u>

a. This license will be issued by the Department of Banking and Insurance

b. There will be a net worth requirement for the Non-Bank Financer who engages in Alternative Lending equal to the annual volume of Alternative Lending transactions the Non-Bank Financer "closes". If the volume is $10,000,000 or less the net worth requirement is $250,000. If the volume is between $10,000,000.and $20,000,000 then the net worth requirement is $500,000. And if greater than $20,000,000, the net worth requirement would then be $1,000,000. Clearly, this will be an extremely difficult calculation for our factoring and asset based lenders.

c. A bond from a New Jersey surety will be required in favor of the State of New Jersey for the benefit of any person injured by the wrongful act, default, fraud or misrepresentation of the Non-Bank Financer engaged in Alternative Lending and its employees and agents. As with the net worth requirement the bonding requirement is based upon the annual volume of Alternative Lending transactions "closed"by the Non-Bank Financer. If the annual volume is $10,000,000.or less the bond will be $250,000. If the annual volume is above $10,000,000 but below $20,000,000.the bond will be in the amount of $500,000. And for annual transaction volume above $20,000,000. the bond will be $1,000,000. Same questions above apply? Again, this will be an extremely difficult calculation for our factoring and asset based lenders.

d. All officers, directors or employees of the Non-Bank Financer engaged in Alternative Financings shall disclose basic background information(including providing fingerprinting) and any record of criminal history as no person shall serve as an officer, director or employee of a Non-Bank Financer engaged in Alternative Lending if the person is convicted of any crime involving dishonesty or breach of trust or other crime determined by the Commissioner to disqualify a person from serving in those roles.

e. Any employee of a Non-Bank Financer engaged in Alternative Lending shall complete at least 10 hours of continuing education each calendar year two of which shall cover business ethics. There is no rationale given for this requirement and will be difficult to enforce.

Obtaining such a license exempts the Non-Bank Financer engaged Alternative Financings from New Jersey's usury laws;

5. <u>Disclosures by Non-Bank Financer Making Alternative Financing</u>

(i) The disclosures set forth below are made to the borrower in writing not more than 10 days and not less than 24 hours before the "closing" of the Alternative Lending transaction and are as follows:

a. Total amount financed.
b. Payment Schedule.
c. Term to maturity.
d. Annual interest rate before considering financer's charges, assuming all payments are made under the contract as anticipated.
e. Annual percentage rate after considering financer's charges, assuming all payments are made under the contract as anticipated.
f. Interest cost per dollar borrowed.
g. Total repayment amount to maturity.
h. Any right to prepay and the applicability and calculation of any prepayment charges.
i. Collateral requirements;
j. An itemized list of all possible fees and costs and charges;
k. A representation that the Non-Bank Financer is providing borrower with the most favorable terms offered by the Non-Bank Financer for the particular Alternative Lending transaction which the borrower qualifies.
l. If the Alternative Financing is being offered to a borrower to whom the Non-Bank Financer has previously extended Alternative Financing, and the proceeds of the new Alternative Financing are being used to pay off the existing financing the Alternative Lender must disclose the original annual percentage rate to the existing financing, the increase in the annual percentage rate to the existing financing and what the annual percentage rate of the existing financing will be after it is refinanced under the second Alternative Financing.

(ii) In addition to the foregoing any Non-Bank Financer engaged in Alternative Lending must demonstrate to the borrower that the economic benefit of the facility offers one of the following:

a. Lower payments through the payoff of outstanding debt balances;
b. Funding the purchase of equipment or inventory;

c. Payoff of tax liens or judgments adversely impacting business operations, or limiting access to collateral to support funding.
d. Funding of business expansion, acquisition, or combination that is projected to generate revenue growth and future profitability;
e. Funding of working capital to support continued business operations or
f. Completion of construction.

We realized that while these requirements may be attainable by a term loan lender, they are virtually impossible for a factor or asset based lender.

(iii) The proposed legislation requires that the Non-Bank Financer engaged in Alternative Financings to maintain a staff dedicated to addressing complaints; clear disclosure of the contact for complaint resolution; and maintain a separate file for each complaint that identifies each complainant and the nature and disposition of that complaint. Again, this is MCAs only

(iv) If the Non-Bank Financer engaged in Alternative Financings make a materially false or misleading statement or representation to a borrower about the terms or conditions of an Alternative Financing or advertises, prints, displays, publishes, distributes or broadcasts or cause to permit to be advertised printed displayed published distributed or broadcast in any manner any statement or representation with regard to any Alternative Financing that is false or misleading or deceptive or omits material information then as determined by a court of competent jurisdiction the Alternative Lender may be liable to the extent of a civil penalty of not more than $10,000 per occurrence which action may only be brought by the Department of Banking and Insurance.

6. <u>Conclusion</u>

SFNet is advancing the positions, among others, that its factoring and asset based lending members should not in the first place be defined as Alternative Lenders and that factors and asset based lenders are already and adequately regulated by the NJ UCC (this argument worked for the equipment finance folks who are exempted from the proposed legislation). Furthermore,that many of the disclosure items are not capable of being complied with as they do not represent the manner in which our factoring and asset based clients conduct their business and, finally, that there is not a “safe harbor” provision for members who use their best efforts in making disclosure, but have still not complied with the disclosure requirements in the opinion of the Commissioner of the New Jersey Department of Banking.

<u>We need your help.</u>