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Articles in reference to SB0825 - Consumer Credit - Commercial Financing Transactions

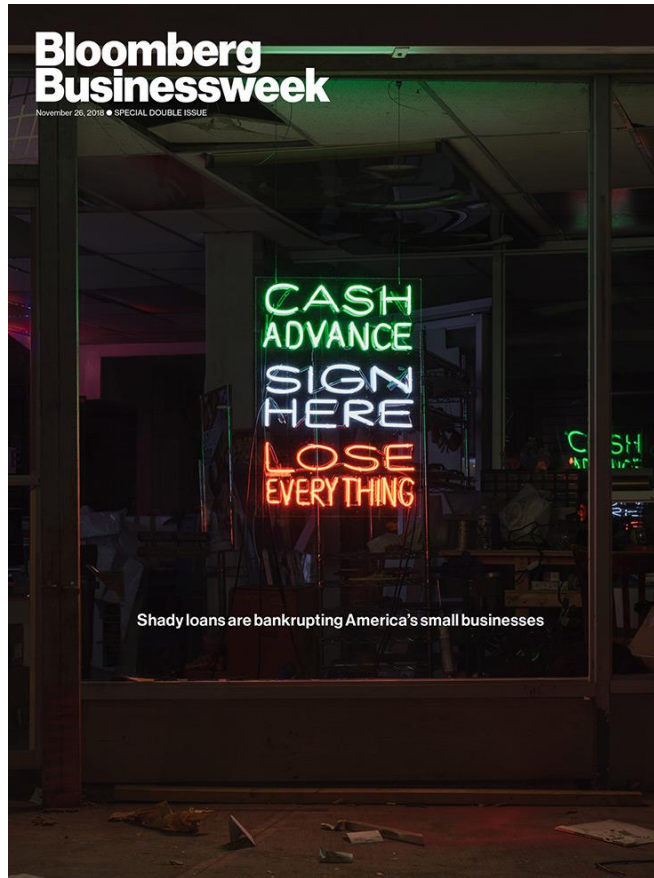
How an obscure legal document turned New York's court system into a debt-collection machine that's chewing up small businesses across America.

Story by [Zachary R. Mider](#) and [Zeke Faux](#)
Data analysis by [David Ingold](#) and [Demetrios Pogkas](#)
November 20, 2018

<https://www.bloomberg.com/graphics/2018-confessions-of-judgment/>

Look out, the stranger on the phone warned. They're coming for you.

The caller had Janelle Duncan's attention. Perpetually peppy at 53, with sparkly jewelry and a glittery manicure, Duncan was running a struggling Florida real estate agency with her husband, Doug. She began each day in prayer, a vanilla latte in her hand and her Maltese Shih Tzu, Coco, on her lap, asking God for business to pick up. She'd answered the phone that Friday morning in January hoping it would be a new client looking for a home in the Tampa suburbs.



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PHOTOGRAPHER: JAMIE CHUNG FOR BLOOMBERG BUSINESSWEEK

The man identified himself as a debt counselor. He described a bizarre legal proceeding that he said was targeting Duncan without her knowledge. A lender called ABC had filed a court judgment against her in the state of New York and was planning to seize her possessions. “I’m not sure if they already froze your bank accounts, but they are RIGHT NOW moving to do just that,” he’d written in an email earlier that day. He described the lender as “EXTREMELY AGGRESSIVE.” Her only hope, the man said, was to pull all her money out of the bank immediately.

His story sounded fishy to the Duncans. They *had* borrowed \$36,762 from a company called ABC Merchant Solutions LLC, but as far as they knew they were paying the money back on schedule. Doug dialed his contact there and was assured all was well. They checked with a lawyer; he was skeptical, too. What kind of legal system would allow all that to happen 1,000 miles away without notice or a hearing? They shrugged off the warning as a scam.

But the caller was who he said he was, and everything he predicted came true. The following Monday, Doug logged in at the office to discover he no longer had access to his bank accounts. A few days on, \$52,886.93 disappeared from one of them. The loss set off a chain of events that culminated a month later in financial ruin. Not long after her agency went bankrupt, Janelle collapsed and was rushed to the hospital, vomiting bile.

As the Duncans soon learned, tens of thousands of contractors, florists, and other small-business owners nationwide were being chewed up by the same legal process. Behind it all was a group of financiers who lend money at interest rates higher than

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those once demanded by Mafia loan sharks. Rather than breaking legs, these lenders have co-opted New York's court system and turned it into a high-speed debt-collection machine. Government officials enable the whole scheme. A few are even getting rich doing it.



Janelle and Doug Duncan

“Somebody just comes in and rips everything out. It’s cannibalized our whole life”

The lenders’ weapon of choice is an arcane legal document called a confession of judgment. Before borrowers get a loan, they have to sign a statement giving up their right to defend themselves if the lender takes them to court. It’s like an arbitration agreement, except the borrower always loses. Armed with a confession, a lender can, without proof, accuse borrowers of not paying and legally seize their assets before they know what’s happened. Not surprisingly, some lenders have abused this power. In dozens of interviews and court pleadings, borrowers describe lenders who’ve forged documents, lied about how much they were owed, or fabricated defaults out of thin air.

“Somebody just comes in and rips everything out,” Doug said one evening in August, pulling up a stool at a Starbucks and recounting the events that killed the Duncans’ business. After a long day spent selling houses for another company, the name tag pinned to his shirt had flipped upside down like a distress signal. “It’s cannibalized our whole life.”

Confessions of judgment have been part of English common law since the Middle Ages, intended as a way to enforce debts without the fuss and expense of trial. Concerns about their potential abuse are almost as old. In Charles Dickens’s 1837 novel *The Pickwick Papers*, a landlady who’s tricked into signing one **ends up in debtors’ prison**. Some U.S.

states outlawed confessions in the middle of the 20th century, and federal regulators [banned them for consumer loans](#) in 1985. But New York still allows them for business loans.

For David Glass, they were the solution to a problem: People were stealing his money. Among the hustlers and con men who work the bottom rungs of Wall Street, Glass is a legend. Before he was 30, he'd inspired the stock-scam movie *Boiler Room*. Later busted by the FBI for insider trading, he avoided prison by recording incriminating tapes of his old colleagues. Even his enemies say Glass, who declined to comment for this story, is one of the sharpest operators they've ever dealt with.

In 2009, while still on probation, Glass and a friend named Isaac Stern started a company called Yellowstone Capital LLC. (ABC, the firm that wiped out the Duncans, is one of more than a dozen corporate names used by Yellowstone's sales force.) Operating out of a red-walled office above an Irish bar in New York's financial district, these salespeople phoned bodegas and pizzerias and pitched their owners on loans. The rates sometimes exceeded 400 percent a year, and daily payments were required, but borrowers were desperate.

A Confessions Boom

Judgments by confession in favor of merchant cash-advance companies in New York state

A Confessions Boom

Judgments by confession in favor of merchant cash-advance companies in New York state

Note: Totals by quarter

Source: Bloomberg News analysis of New York State Unified Court System documents

In the aftermath of the financial crisis, banks were cutting back on lending just when small businesses most needed cash. Companies such as Yellowstone stepped in. They got around lending regulations by calling what they did "merchant cash advances," not loans—a distinction [judges recognize](#) though there's little practical difference. The same people who'd pushed stock swindles in the 1990s and subprime mortgages a decade later started talking small businesses into taking on costly debt. The [profits were huge](#), and the industry grew. Last year it extended about \$15 billion in credit, [according to an estimate](#) by investment bank Bryant Park Capital.

Yellowstone would hire anyone who could sell. A nightclub bouncer sat next to ultra-Orthodox Jews fresh out of religious school. The best brokers earned tens of thousands of dollars a month, former employees say; others slept at the office, fought, sold loose cigarettes, and stole from each other. A [video posted on YouTube](#) shows Glass firing an employee. "Get the f--- out of my firm," he yells. "Why are you still sitting

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there, fat ass? Get out of my company!” To keep the troops focused, management would [stack a pile of cash](#) on a table and hold a drawing for closers.

Glass’s problem was that some borrowers took Yellowstone’s money with no intention of paying it back. Lawsuits against deadbeats proved pointless, dragging on for months or years. Then a lawyer who worked for Yellowstone and other cash-advance outfits came up with the idea of requiring borrowers to sign confessions of judgment before receiving their loans. That way, at the first sign of trouble, lenders could start seizing assets, catching borrowers unawares.

In May 2012, Yellowstone became what appears to be the first company in the industry to file a confession in court. Others copied the trick. The innovation didn’t just make collections easier; it upended the industry’s economics. Now, even if a borrower defaulted, a company stood a chance of making a full recovery. By tacking on extra fees, it might even make more money, and faster, than if the borrower had never missed a payment. In some cases, the collections process became a profit engine.

Confessions aren’t enforceable in Florida, where the Duncans signed theirs. But New York’s courts are especially friendly to confessions and will accept them from anywhere, so lenders require customers to sign documents allowing them to file there. That’s turned the state into the industry’s collections department. Cash-advance companies have secured more than 25,000 judgments in New York since 2012, mostly in the past two years, according to data on more than 350 lenders compiled by *Bloomberg Businessweek*. Those judgments are worth an estimated \$1.5 billion. The biggest filer by far, with a quarter of the cases: Yellowstone Capital.

The Duncans’ ordeal began in November 2017 with an unsolicited fax from a broker promising term loans of as much as \$1 million at a cheap rate. The couple had owned their agency, a Re/Max franchise, for three years and now had 50 employees, but they still weren’t turning a profit. A planned entry into the mortgage business was proving more expensive than expected. Doing some quick math, Doug figured he could borrow \$800,000 to fund the expansion, pay off some debt, and come out with a lower monthly payment. The spam fax felt like a gift from God.

On the phone, the broker said that to qualify for a big loan, Doug would first have to accept a smaller amount and make a few payments as a tryout. He sent over the paperwork for a cash advance, not a term loan—and included confessions for both Doug and Janelle to sign. Without talking to a lawyer, they did. Why not? Doug thought. They intended to pay the money back on time.

The advance turned out to be for \$36,762, repaid in \$800 daily debits from their bank account starting the day after they got the money. This would continue for about three months, until they’d repaid \$59,960, amounting to an annualized interest rate of

more than 350 percent. A small price to pay, Doug figured—soon he'd have all the money he needed in cheaper, longer-term debt. But when he followed up the next month to inquire about the status of the bigger loan, he got no response. The trouble started soon after.

How Confessions of Judgment Work

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Small Business

Wants a loan

The Confession

Borrower signs a confession of judgment as part of the application, agreeing to lose any dispute

Lender

Sends money to borrower

The Dispute

Borrower misses a payment, or so the lender claims

County Clerk

Lender sends confession to clerk,
who rubber-stamps it

New York City Marshal

Demands money from borrower's bank

Bank

Hands money over to lender

Lender

Gets money back, with interest and fees tacked on

A few hours after learning that their bank accounts had been frozen, the Duncans met with a local attorney, Jeffrey Dowd, in a law office squeezed between a nail salon and a transmission shop. Their bank, SunTrust, refused to tell them who was behind the freeze. It wasn't clear why Yellowstone would target them. Their contact there was still pleading ignorance; the lender had collected its \$800 payment as recently as the previous business day. Janelle was on the verge of tears.

A broad-shouldered man with a white goatee, Dowd handles everything from wills to lawsuits for small-business owners in the Tampa suburbs. After assuring the Duncans he'd get to the bottom of it, he logged on to his computer. He soon found a legal website showing that [Yellowstone had won a judgment](#) against the Duncans a few hours after Janelle received the warning phone call. The lender had gone to a court in the village of Goshen, 60 miles north of New York City.

"I hereby confess judgment," read the documents Doug and Janelle had signed. Attached was a statement signed by the same person at Yellowstone who'd assured Doug everything was fine. It said the Duncans had stopped making payments.

That wasn't true. The Duncans' bank records show that Yellowstone had continued to get its daily \$800 even after going to court. The company's sworn statement also inflated the size of the couple's debt. But by the time Dowd found the case, it was already over. A clerk had approved the judgment less than a day after Yellowstone's lawyer asked for it. No proof was demanded, no judge was involved, and the Duncans didn't have a chance to present their side in court.

Beau Phillips, a Yellowstone spokesman, said in an email to *Businessweek* that the company was within its rights, because the Duncans had blocked one payment and never made up for it. The Duncans respond that if a block had taken place, it must have been a computer error. Why stop paying and then resume the next day?

The court papers revealed the name of Yellowstone's lawyer, and on a whim, Dowd searched for her other cases and found more than 1,500 results. The Duncans' predicament was no aberration. "It was like a rabbit hole," Dowd says. He dove in, clicking on case after case after case.

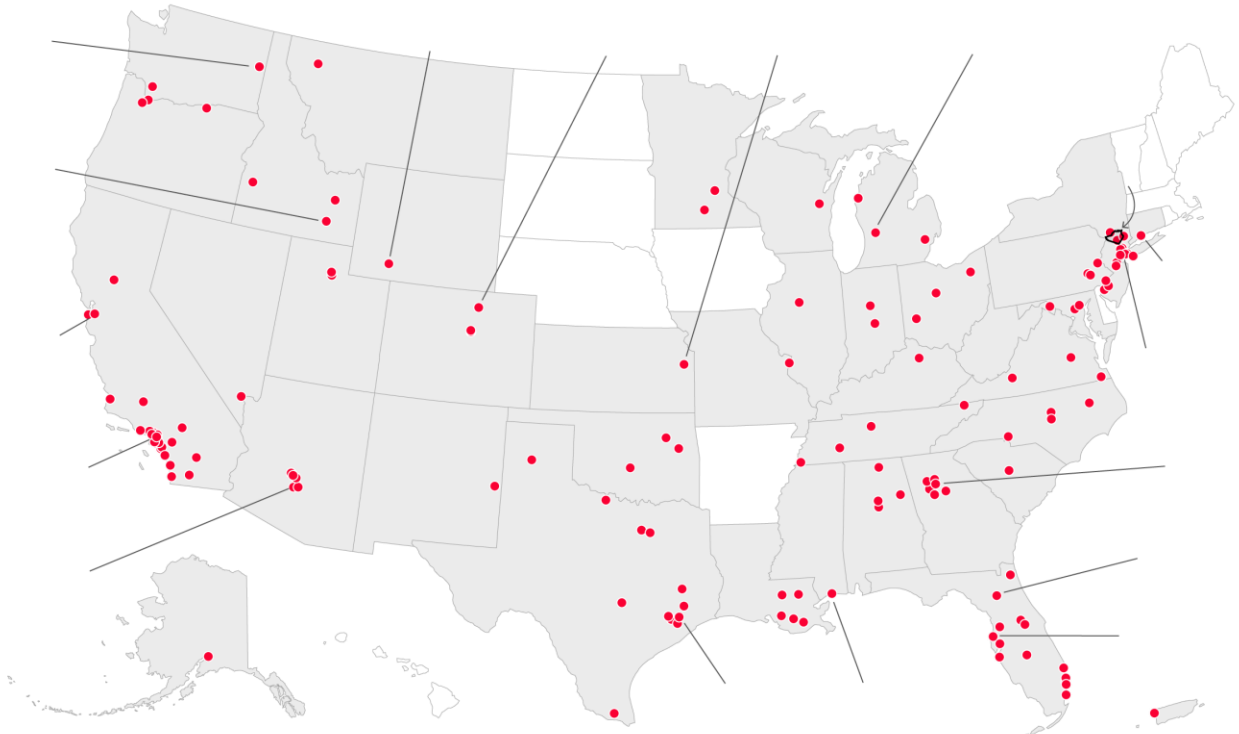
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The Long Reach of a Rubber Stamp

In one month, a single clerk's office in Orange County, New York, issued 176 judgments against small businesses in 38 states and Puerto Rico



Wholesale florist
Spokane, Wash.

\$211,727

Tire and automotive shop
Rock Springs, Wyo.

\$9,562

Prosthetics services
Greeley, Colo.

\$217,070

Roofing company
Wellsville, Kan.

\$44,225

Auto accessories retailer
Grand Rapids, Mich.

\$33,936

Assisted-living center
Pocatello, Idaho

\$46,827

Orange County, N.Y.

Insurance agency

Milford, Conn.
\$33,206
 Moving company
 San Leandro, Calif.
\$9,163
 Child care center
 Irvington, N.J.
\$30,067
 BBQ restaurant
 Atlanta
\$11,974
 Dental laboratory
 Monterey Park, Calif.
\$248,615
 Brewing company
 Gainesville, Fla.
\$40,215
 Building contractor
 Gilbert, Ariz.
\$13,813
 Bowling alley
 New Port Richey, Fla.
\$85,475
 Janitorial services
 Houston
\$45,469
 Furniture store
 Gulfport, Miss.
\$18,153

Note: Judgments issued based on merchant cash-advance filings in Orange County in July 2018

Source: Bloomberg News analysis of New York State Unified Court System documents
 Goshen, N.Y., is a bucolic stop on the harness-racing circuit, just west of the Hudson River. Not far from the track, in the Orange County Clerk's office, women with ID lanyards around their necks sit behind Plexiglas windows, processing pistol permits and recording deeds. One clerk prints out proposed judgments sent electronically by cash-advance companies and makes them official with three rubber stamps.

Orange is one of a handful of counties in upstate New York that together handle an outsize share of the nation's cash-advance collections. Industry lawyers pick offices known to sign judgments quickly; there's no need for the borrower or lender to have a connection to the area. In even smaller Ontario County, cash-advance filings make up about three-quarters of the civil caseload. No matter how abusive the confessions might be, clerks have no choice but to continue processing them, says Kelly Eskew, a deputy clerk in Orange County.

To obtain a judgment, a lawyer for a cash-advance company must send in the confession along with a sworn affidavit explaining the default and how much is still owed. The clerk accepts the statement as fact and enters a judgment without additional review. Once signed, this judgment is almost impossible to overturn. Borrowers rarely

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try. Few lawyers will take on a client whose money is already gone, and getting a ruling can take months—too long to save a desperate business. It's a trap with no escape.

Clicking around a database of New York state court records, Dowd did find some cases in which cash-advance borrowers had sought to overturn judgments. They'd almost always failed. New York judges took the view that debtors waived their rights when they signed the papers. Dowd concluded it would probably cost the Duncans \$5,000 to retain a lawyer to travel to Orange County. He advised them not to bother.

It's possible that if the Duncans had tried to overturn the judgment, they would have discovered that the confessions they'd signed were later altered. The signed originals contain an apparent drafting error, failing to identify the Duncans' company as subject to the judgment, a flaw that might have prevented Yellowstone from seizing their money. In the [version filed in court](#), someone had replaced the first two pages of each confession with the mistake corrected. Asked by *Businessweek* about the discrepancy, Phillips didn't provide an explanation.

Altered Documents

The confession of judgment signed by the Duncans (left) and the one filed by Yellowstone in court

1) I am a principal, owner, and an officer of STAR PERFORMANCE REALTY INC. d/b/a REMAX SOUTH SHORE REALTY, a Corporation located at 10445 GIBSENTON DR, RIVERVIEW, FL 33578 in the County of PASCO, and as such, I have the authority to act on behalf of STAR PERFORMANCE REALTY INC. d/b/a REMAX SOUTH SHORE REALTY, and have been authorized to execute this affidavit of confession of judgment. (DOUGLAS W DUNCAN, and JANELLE M DUNCAN are collectively referred to as "Merchant Defendant".)

1) I am a principal, owner, and an officer of STAR PERFORMANCE REALTY INC. d/b/a REMAX SOUTH SHORE REALTY, a Corporation located at 10445 GIBSENTON DR, RIVERVIEW, FL 33578 in the County of PASCO, and as such, I have the authority to act on behalf of STAR PERFORMANCE REALTY INC. d/b/a REMAX SOUTH SHORE REALTY, and have been authorized to execute this affidavit of confession of judgment. (STAR PERFORMANCE REALTY INC. d/b/a REMAX SOUTH SHORE REALTY is referred to as "Merchant Defendant".)

Borrowers have accused Yellowstone of forgery before. Just in the past year, a Georgia contractor [presented evidence in court](#) that a confession used against him was a complete fabrication, and a Maryland trucker complained to Yellowstone that a key term in his confession had been changed after the fact, as had happened with the Duncans. The company backed off from those borrowers but faced no further consequences. Phillips declined to comment on the accusations.

While Dowd didn't challenge the ruling against the Duncans in court, he did think he could get SunTrust to help them. He told the bank that one of the couple's accounts

held funds that didn't belong to them because it was used to collect rent on behalf of landlords. Dowd says a banker at the local branch wanted to help but was overruled by higher-ups. The account remained frozen. A spokesman for SunTrust declined to comment.

When Dowd finally reached Yellowstone's lawyer, she referred him to a marshal who she said was handling the case. Dowd was confused. Why would a U.S. marshal be involved? His clients weren't fugitives. He called the phone number, and somebody with a Russian accent answered.

The person on the phone wasn't a federal official. Dowd had reached the Brooklyn office of Vadim Barbarovich, who holds the title of New York City marshal. He'd stumbled onto an arcane feature of the city's government that's become another powerful tool for cash-advance companies.

New York's 35 marshals are government officers, appointed by the mayor, who collect private debts. They evict tenants and tow cars, city badges dangling from their necks. When they recover money, they get a fee of 5 percent. The office dates to Dutch colonial days, formed by a [decree of Peter Stuyvesant's council](#). Fees for the biggest jobs were initially set at a dozen stivers, less than one-tenth the price of a beaver pelt.

Barbarovich's office is in the immigrant enclave of Sheepshead Bay. Before he was appointed in 2013, he'd tracked inventory at a Brooklyn hospital and volunteered as a Russian translator. He's now the go-to marshal for the cash-advance business and has gotten rich in the process. Last year, city records show, he cleared \$1.7 million after expenses.

As soon as Yellowstone had obtained its judgment against the Duncans, it had sent a copy to Barbarovich, who issued legal orders demanding money from Atlanta-based SunTrust and another bank in Alabama where the couple kept their personal funds. By law, New York marshals' authority is limited to the city's five boroughs, but a loophole vastly extends their reach: They're allowed to demand out-of-state funds as long as the bank has an office in the city, as SunTrust does. A few big banks refuse to comply with the orders, but most just hand over their customers' money.

SunTrust proved accommodating. Three days after freezing the Duncans' accounts, it took \$52,886.93 and mailed a check to Barbarovich, enough to satisfy the judgment plus the 5 percent marshal's fee. Almost all of it was rent money the Duncans were holding for landlords, not their own funds. Barbarovich didn't respond to questions about the couple's case but said in an email that he follows the rules when issuing a demand for money. Phillips, the Yellowstone spokesman, said no one told the company that the money belonged to third parties until seven weeks after it was seized. Even then, Yellowstone refused to return it.

The Duncans scrambled to make up the shortfall. Doug got another, larger cash advance from a different company to keep afloat. The daily payments on that loan were too much for them to handle, though, and they were soon short of cash again. Sensing trouble, employees fled.

One evening, Janelle thought she was having a heart attack. Her pulse raced, her limbs went numb, and she grew nauseous. An ambulance rushed her to the hospital. Her heart was fine. Her insurance claim was denied.

Unlike the Duncans, most of the dozens of borrowers interviewed by *Businessweek* really did fall behind on their debt payments. Their experiences were no less wrenching. They spoke of divorce, of lost friendships, of unpaid medical bills.

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“You can’t defend yourself,” says Richard Schilg, the owner of a human resources company in Ohio who borrowed hundreds of thousands of dollars with at least six advances. “As long as you still have a business, as long you have a personal checking account, they’re going to hound you. Your life is ruined by their contract.” Schilg says he always tried to honor his debts. But his access to money has been so restricted by cash-advance judgments that he’s had to sell furniture to buy food.

He’s one of many borrowers who’ve received nasty threats from debt collectors. “I will make this my personal business to f--- you,” a Yellowstone executive named Steve Davis told Schilg on a voicemail heard by *Businessweek*. Davis texted another: “I will watch you crash and burn.” Asked about the messages, Davis says, “People defraud us. When that happens we have to do what’s best for us.”

Jerry Bush, who ran a plumbing business with his father in Roanoke, Va., signed confessions for at least six cash advances from companies including Yellowstone, taking one loan after another as his payments mounted to \$18,000 a day. In January, Davis called him while he was accompanying his wife to a chemotherapy appointment and threatened him with the confession in a dispute over payment terms. Davis denies menacing Bush, but according to Bush’s account of their conversation, Davis said he would pursue Bush until his death and take all of his money, leaving nothing to pay for his wife’s treatment. Bush also says Davis then offered to send flowers to Bush’s wife.



Jerry Bush

“I wake up every morning afraid what else they will take. And every morning I throw up blood”

In August, Bush closed his business, laid off his 20 employees, and stopped making payments on his loans. Yellowstone never filed its signed confession in court, but other lenders went after him over theirs. One sunny day that month, he walked to a wooded area near his home, swallowed a bottle of an oxycodone painkiller, and began streaming video to Facebook. To anyone who might have been watching, he explained that he'd taken out cash advances in a failed attempt to save his business. Now the lenders had seized his accounts, Bush said, his voice wavering. One had even grabbed his father's retirement money.

“I signed 'em, I take the blame for it,” he said. “This will be my last video. I am taking this on me.” He asked his friends to take care of his family, then sobbed as he told his wife and teenage son he loved them.

Someone who saw the video alerted the police. They found Bush unconscious in the woods a few hours later—he credits them with saving his life. But the pressure from his confessions of judgment hasn't relented. “I wake up every morning afraid what else they will take,” he says. “And every morning I throw up blood.”

Bush's contracts with Yellowstone show that the company advanced him a total of about \$250,000 and that he paid them back more than \$600,000. Davis, who parted ways with Yellowstone in August, says he didn't mistreat Bush or other borrowers and always followed the company's protocols. “You know why people put the blame on me is because I'm successful,” he says. “It's just haters.”

As for the Duncans, each morning at their house still begins with a prayer and a Bible verse. Their retirement savings evaporated with their agency, but they've been able to keep their house. They continue to believe God has a plan for every one of his children, but they've learned to trust some of those children less. “If we don't have peace from God, and we live in outrage, it destroys us,” Janelle says. “So I'm choosing to have hope to start again, and we're relying on the Lord to replace what the enemy has stolen and turn it around for good.”

By seizing their bank deposits, Yellowstone had managed to collect its money ahead of schedule and tack on \$9,990 in extra legal fees, payable to a law firm in which it owns a stake. In about three months, the company and its affiliates almost doubled their money. At that rate of return, one dollar could be turned into 10 in less than a year.

Everyone else involved in the collection process got a slice, too. SunTrust got a \$100 processing fee. Barbarovich's office got approximately \$2,700, with about \$120 of that passed along to the city. The Orange County Clerk's office got \$41 for its rubber stamps. The New York state court system got \$184.

To date, no state or federal regulator has tried to police the merchant-cash-advance industry. Its lawyers designed it to avoid scrutiny, sidestepping usury laws and state licensing requirements by keeping the word “loan” out of paperwork and describing the deals as cash advances against future revenue. And because the customers are technically businesses, not individuals, consumer protection laws don't apply, either.

With regulators sidelined and lawmakers oblivious, Yellowstone and its peers keep growing. After Glass stepped back a couple of years ago from day-to-day operations—his criminal record was making it harder to find investors—Wall Street investment bankers arranged a **\$120 million line of credit** to finance more advances. In 2016 the company moved from its grimy downtown Manhattan offices to a shiny building in Jersey

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City, [pocketing \\$3 million in state tax incentives](#). On Instagram, a [top salesman](#) shows off flights on private jets, a diamond-encrusted watch, and a Lamborghini. Yellowstone advanced \$553 million last year, its highest total ever.



A stack of cash about to be raffled off to a lucky Yellowstone employee.

SOURCE: FACEBOOK

In April, on the same day Janelle Duncan was selling the last of her office furniture, Yellowstone executives marked the company's ninth anniversary with a luncheon in Jersey City. In a [celebratory email](#) marking the occasion, Stern, the co-founder, wrote, "I am continually blown away at the success and achievements we continue to have."



Here's One Way to Help Small Businesses Survive

By The Editors | Bloomberg

August 18, 2020

Let them bake. (Photographer: Rodin Eckenroth/Getty Images/Getty Images North America) The coronavirus pandemic has thrust millions of American small businesses into crisis mode, as they scramble for the cash they need to get through to more normal times. One way Congress can help: Protect them from predators looking to take their money and leave them bankrupt.

Bloomberg News has reported extensively on the “merchant cash advance” companies that prey on plumbers, pizzerias, nail salons and other small businesses across the country. They skirt lending laws by structuring their products as advances against future revenue. They employ bucket-shop marketing tactics, offering seemingly sweet deals that obscure outrageous fees and interest rates sometimes exceeding 400%. Their collection practices border on extortion, ranging from draining bank accounts without business owners’ knowledge to surprise visits from a guy named Gino.

Now, entrepreneurs are particularly vulnerable, as lockdowns slam the economy and federal aid fails to reach many of those most in need. As Federal Trade Commissioner Rohit Chopra put it, “this is opening the door to even more predatory actors looking to profit from the pain of small business owners.”

After the Bloomberg News investigation, officials addressed some specific cases and practices. The FTC, the Securities and Exchange Commission and New York’s attorney general sued a number of companies — run by people including a convicted real-estate scammer and a former drug trafficker — for transgressions ranging from threatening kidnapping to overcollecting on debts. And New York legislators shut down a legal loophole that allowed cash-advance companies to use the state’s courts to seize the assets of small businesses nationwide, with no notice or hearing.

Yet the predatory behavior will keep coming back in new forms until Congress corrects a major omission: the lack of any consistent rules for lending to small businesses, akin to those that already exist for consumers. These should include clear disclosure of terms and interest rates, accountability for the brokers who sell the loans, and federal constraints on contracts that allow creditors to seize assets unilaterally. Legislators should also designate a federal agency to enforce the rules wherever they should apply. Congresswoman Nydia M. Velázquez, the chairwoman of the House Small Business Committee, has introduced legislation that would do what’s needed and put the Consumer Financial Protection Bureau in charge. Her colleagues across the aisle, who

often express admiration for small business, should offer their support. Entrepreneurs should be able to focus on getting through this crisis and doing what they do best, not trying to anticipate the myriad ways in which unscrupulous lenders might deceive them and destroy what they've built.

Feb 2, 2022,09:00am EST|917 views

Why Lending Transparency Matters For Small Businesses

Luz Urrutia

Forbes Councils Member

Forbes Finance Council

COUNCIL POST| Membership (Fee-Based)

[Money](#)

Luz leads [Accion Opportunity Fund](#), the nation's leading nonprofit providing small businesses with access to capital, networks, and coaching.



GETTY

It's no secret that small businesses — especially those owned by people of color, women and immigrants — face an uphill battle in accessing responsible and affordable capital. Before Covid-19 upended the nation's economy, the

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market gap for small-business loans was estimated to be \$87 billion per year, according to Next Street, and small-business owners looking for affordable, responsible financing had limited options.

The pandemic, of course, has made a difficult situation even worse. Covid-19 has been devastating for small businesses, with [disproportionate impacts](#) on Black, Latinx and Asian business owners, according to the Federal Reserve. These groups — as well as women entrepreneurs, who only made up [5%](#) of federal Paycheck Protection Program applicants (among businesses that indicated their owner’s gender) — struggled the most to keep their businesses afloat. Unfortunately, when businesses like these are poorly served by the financial sector, bad actors often fill the gap with predatory financial products.

As the nation works toward economic recovery to rebuild its Main Streets, it must ensure that lending institutions are more transparent, equitable and accountable, especially for small businesses. One critical step in this direction is for Congress to pass the [Small Business Lending Disclosure Act of 2021](#), introduced in November by House Small Business Committee chair Rep. Nydia Velázquez (D-NY) and Sen. Bob Menendez (D-NJ), senior member of the Senate Banking Committee.

This monumental legislation would expand disclosure requirements under the 1968 [Truth in Lending Act](#) (TILA) to provide small-business borrowers with the protections they need. The TILA protects individual consumers by requiring transparent disclosure of loan terms, fees and annual percentage rates (APRs) for consumer credit cards, loans and other lending products.

However, small businesses are not covered by this existing law, leaving them vulnerable to misleading or irresponsible lending practices.

We protect individuals from predatory lending practices — why not small businesses too?

BY JOYCE KLEIN, OPINION CONTRIBUTOR — 02/16/22 07:00 PM EST
THE VIEWS EXPRESSED BY CONTRIBUTORS ARE THEIR OWN AND NOT THE VIEW OF THE HILL

Despite the extraordinarily difficult two years our nation's small businesses have been through, we are seeing signs of resilience and optimism — with most firms reopening after temporary shutdowns and an unprecedented rate of new business formation. The latter, though, may be partly due to workers seeking alternatives to the lack of good options in the markets for wage labor.

At some point, these new and recovering firms will need new injections of financing. The question is whether they will be able to access that capital, and whether the types of capital they are able to tap will support their growth and recovery or hinder it.

Commercial bank lending is falling, which is not unusual after a recession or an economic shock. Commercial lenders looking at the financial statements of small businesses for 2020 and 2021 would be hard pressed to determine whether a firm is ready and able to grow and thrive. But it's not just a question of the pandemic. Banks have always been reluctant to lend to firms that are less than two years old. And small business lending in amounts of less than

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\$250,000 had been falling for decades, largely because these loans generate little to no profit for banks.

The lenders that step into this credit void are nonbank lenders. These take multiple forms — fintech firms; mission-led community development financial institutions; large payment or e-commerce firms; and commercial lenders offering products such as factoring or merchant cash advances. To assess whether these lenders are aiding small businesses as they seek to recover and grow, the most important factor is not the type of institution they are, but the products they offer and the practices they use.

Predatory small business lending has a long history in the United States, often in the guise of “helping” those on the margins (it’s a motif in films like “It’s a Wonderful Life” and “The Godfather”). Predatory lenders, particularly in the digital age, aren’t as easy to recognize as they are in films. Prior to the pandemic there was rapid growth in “new” lenders offering products with annual percentage rates in the high double or triple digits, with monthly payments often double what the business could afford to pay, and sometimes using high-pressure collections tactics when borrowers fell behind on their products. The Responsible Business Lending Coalition — of which the Aspen Institute is a founding member — has been tracking these practices and working to identify and advocate for policies that help ensure that small businesses access financing that is fair and responsible.

These lenders seem to have disproportionately targeted business owners of color — which is not surprising given those are the small businesses who have always had the hardest time accessing capital. Why are small businesses in general and entrepreneurs of color a target for predatory lenders? Because currently small businesses are not afforded protections from predatory lending that consumers are now used to, such as transparency and reporting requirements that inform fair lending.

There are some simple steps that could expand access to capital while protecting small businesses. This Thursday, the Subcommittee on Consumer Protection and Financial Institutions of the U.S. House’s Committee on Financial Services is hosting a hearing on Small Businesses, Big Impact: Ensuring Small and Minority-Owned Businesses Share in the Economic Recovery. The hearing will likely cover two policy efforts that could play an

essential role in ensuring that small businesses — including those owned by business owners of color — are able to access fair and responsible credit.

One policy involves implementation of an existing law: Section 1071 of Dodd-Frank. Currently, there is no comprehensive information anywhere about how much small business lending is happening, who is being served, or at what terms. Section 1071 calls on the CFPB to collect data on small business credit, and the agency is close to formalizing its rules and process for doing so. The RBLC is strongly supportive of the CFPB's approach to date — which we believe is pro-innovation. But we strongly recommend that the agency include the collection of data on annual percentage rates APR among the pricing metrics it requires, and that the reporting requirements include all types of business financing, including factoring.

The second step involves passage of the Small Business Lending Disclosure Act of 2021, introduced in November by House Small Business Committee Chairwoman Nydia Velázquez (D-N.Y.) and Sen. [Bob Menendez](#) (D-N.J.), senior member of the Senate Banking Committee. It's surprising to many that commercial (or small business loans) are not subject to the same truth-in-lending requirements as consumer loans, mortgages and credit cards. The bill would require standard disclosures of rates, fees and annual percentage rates (APRs) for small commercial financing products, and provide the Consumer Financial Protection Bureau with expanded ability to oversee small business lending.

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Some opponents of the bill claim that because they offer shorter-term products (e.g., less than a year), that disclosing APR doesn't make sense or isn't feasible. But we already require disclosure of APRs on credit cards, which are often used for short-term financing (and credit card lending has grown significantly since the CFPB introduced new disclosure requirements a decade ago). The bill would not prohibit lenders from sharing other pricing metrics that small businesses might find useful. But it would ensure that all financing offers include the one metric that allows small businesses to make apples-to-apples comparisons on price. In the end, having this information will allow business owners to make the most informed choices among the credit offers they receive.

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Our economy and communities will recover more strongly from the pandemic if new and small firms are able to access the financing they need to adapt, rebuild, and grow. But not all financing is the same — some can spur growth and help business owners to manage volatility, while some can hollow out cash flow and strip wealth. Small businesses are critical to local, state and national economies. They deserve the same basic standards of transparency and fairness, and protection from bad actors, that American consumers now have. Let's put in place the policies small businesses need to get access to capital that will help them recover, not bury them deeper.

Joyce Klein is the director of the Business Ownership Initiative at the Aspen Institute and Chair of the Executive Committee of the Responsible Business Lending Coalition.