



## How Estimated APR is Computed for Merchant Cash Advances

Small business price transparency legislation asks merchant cash advances (or “MCAs”)<sup>1</sup> to disclose an *Estimated APR*, recognizing that the computation for MCAs includes an estimate of the business’s future revenues. That estimation is readily available and is often printed right in the financing contract. (See the example below, where the MCA company has labeled it “Average Monthly Sales”).

MCA companies rely on their estimate of a small business’s future revenue to decide whether to extend financing. They rely on this estimate to set the terms of the financing, and to establish their own estimate of what rate they expect to earn. If these revenue estimates can be relied on by the financing company on decisions that put their capital at risk, they can be relied on for price disclosures to the small business as well.

After all, the Estimated APR the business owner will pay is also the annualized rate the finance company expects to earn. Financing companies generally do not give out financing without an expectation of what rate they will earn. Merchant cash advance companies sometimes advertise their high estimated annualized rates to the hedge funds whose money they borrow and re-lend to small business owners. Surely the small business owner who is paying that rate deserves to know it as well.

### Real Example: Computing the Estimated APR of a Merchant Cash Advance Contract

To demonstrate how an Estimated APR is calculated, below is an excerpt from a typical merchant cash advance contract. As you can see, the Estimated APR is not disclosed. However, everything the financing company would need to compute the Estimated APR is printed in the contract.

<b>Purchase Price:</b> \$12,000.00	<b>Purchased Amount:</b> \$16,560.00	<b>Average Monthly Sales:</b> \$15,763.25
<b>Specified Percentage:</b> 13.1318%	<b>Initial Fees:</b> \$360.00	
<b>Net Amount to Seller:</b> \$11,640.00 (Purchase Price – Initial Fees)		
<b>Initial Weekly Amount:</b> \$517.50 (Average Monthly Sales x Specified Percentage / Average Business Days in a Calendar Month)		

Here how the Estimated APR for this transaction can be easily computed in software like Microsoft Excel, using numbers that already appear in this merchant cash advance financing contract:

	A	B	C
1	Funding Provided	\$11,640	This is the "Net Amount to Seller" in the contract excerpt above.
2	Total Repayment owed	-\$16,560	This is the "Purchased Amount" in the contract excerpt above.
3	Expected Payment Amount	-\$518	This is the "Initial Weekly Amount" in the contract. Charged weekly in this case.
4	Estimated Term Length	32	This is cell B2 ÷ cell B3. It's the expected number of weekly payments.
5			
6	<b>Estimated APR</b>	<b>119%</b>	This is computed by plugging in the numbers above to Microsoft Excel's "RATE" formula: =RATE(B4,B3,B1)*52 You plug in cell B4 (the number of payments), cell B3 (the payment amount), and cell B1 (the funding provided), and annualize using the number of weeks in a year (52). Different Excel formulas like "IRR" can also be used to the same result.

<sup>1</sup> Merchant cash advances, or MCAs, are also sometimes described as sales-based financing or revenue-based financing.