



## ANNUAL PERCENTAGE RATE (APR)

### → A CRITICAL COMPONENT OF SMALL BUSINESS FINANCING TRANSPARENCY

Small business owners have come to expect standard information to understand the cost of financing, including Annual Percentage Rate (APR), since this information has been required for consumer products like credit cards and home loans for more than 50 years. But because small business financing products aren't covered by the federal Truth in Lending Act, finance providers can legally mislead business owners to take on debt with hidden fees and APRs as high as 350%, without ever disclosing these rates to the borrower.<sup>1</sup> Business owners are being trapped in cycles of harmful debt that devastate their finances, and in many cases, force them to close their doors.

### → APR HELPS BUSINESS OWNERS COMPARE PRODUCTS

APR is the only pricing metric that enables business owners to accurately compare various finance products, regardless of the amount, term length, payment period, or combination of interest and fees. Research from the Federal Reserve suggests that in the absence of required disclosures, business owners confuse commonly used terms such as “simple interest” and “factor rate” with an APR and mistakenly select costlier products based on this information.<sup>2</sup>

The examples below from the Federal Reserve report illustrate the range of terms and rates promoted on alternative finance providers' websites. While the finance companies in the study did not disclose APR, the report authors calculated the estimated APR for these examples—showcasing just how misleading these lenders/products can be.<sup>3</sup>

Federal Reserve Report: Illustration of Terms for \$50,000 Repaid in 6 Months		
Rate advertised on website	Product details	Estimated APR
1.15 Factor Rate	<ul style="list-style-type: none"> <li>Total repayment amount \$59,000</li> <li>Fees: 2.5% set-up fee; \$50/month administrative fee</li> <li>Term: none (assume repaid in six months)</li> <li>Daily payments (assume steady payments five days/week)</li> </ul>	70% APR ( <i>not disclosed</i> )
4% fee rate	<ul style="list-style-type: none"> <li>Total repayment amount \$56,500</li> <li>Fee rate: 4% (months 1–2), 1.25% (months 3–6)</li> <li>Fees: none</li> <li>Monthly payments</li> <li>Term: 6 months</li> </ul>	45% APR ( <i>not disclosed</i> )
9% simple interest	<ul style="list-style-type: none"> <li>Total repayment amount \$54,500</li> <li>Fees: 3% origination fee</li> <li>Weekly payments</li> <li>Term: 6 months</li> </ul>	46% APR ( <i>not disclosed</i> )



## APR CAN BE CALCULATED FOR ANY FINANCING PRODUCT

APR can be calculated for a range of financing products regardless of their structure, fees, or term length. That’s why companies offering a range of innovative consumer financing products have been disclosing APR or estimated APR for decades as required under the federal Truth in Lending Act. Many commercial financing providers across the country, including members of the Responsible Business Lending Coalition and signatories of the Small Business Borrowers’ Bill of Rights, already disclose APR for various types of small business financing.

Finance providers have access to all the information they need to calculate the APR or estimated APR for business financing products. **In fact, many of the same financing providers that claim they can’t disclose APRs to their small business borrowers already disclose annualized yields (essentially the same metric) to their financing investors.** Small business owners deserve the same transparency.

## SMALL BUSINESS OWNERS NEED AND EXPECT TRANSPARENCY, INCLUDING APR DISCLOSURE, TO COMPARE FINANCE PRODUCTS

Research from the Federal Reserve demonstrates that business owners want clearly stated price disclosures to better compare financing options—including interest rates expressed as APR.<sup>4</sup>

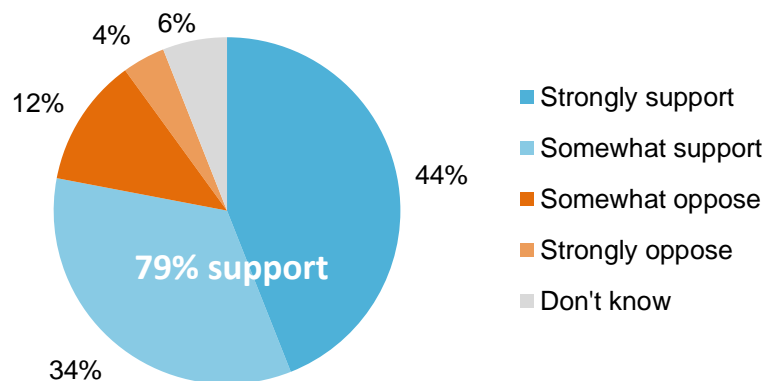
*“They don’t like to use the word ‘interest,’ and they dress it up in other ways to conceal the real cost of the loan.”*

*“Full disclosure, like on credit cards or mortgages... is what is necessary. They need to state the actual APR.”*

- Business owner quotes from the Federal Reserve’s online focus group research

**Scientific opinion polling commissioned by Small Business Majority reveals that nearly 8 in 10 small business owners support legislation that would require disclosure of APR and other key terms.<sup>5</sup>**

*Would you support or oppose a law to require certain disclosures for small business loan products, including Annual Percentage Rate (APR), total cost of capital, and all fees and prepayment penalties, in a uniform standard?*



### Endnotes

1. Accion Opportunity Fund. Unaffordable and Unsustainable: The New Business Lending. 2016 <https://aofund.org/news/unaffordable-and-unsustainable-new-business-lending/>
2. Federal Reserve Bank of Cleveland, “Uncertain Terms: What Small Business Borrowers Find When Browsing Online Lender Websites,” December 2019 <https://www.clevelandfed.org/publications/cd-reports/2019/sr-20191219-uncertain-terms>
3. Ibid.
4. Board of Governors of the Federal Reserve System, “Uncertain Terms: What Small Business Borrowers Find When Browsing Online Lender Websites,” December 2019. <https://www.federalreserve.gov/publications/files/what-small-business-borrowers-find-when-browsing-online-lender-websites.pdf>
5. Small Business Majority. “State Opinion Polls: Small business owners say government doesn’t understand their concerns, need help with healthcare costs and other challenges.” Poll conducted by Chesapeake Beach Consulting for August 13, 2019. <https://smallbusinessmajority.org/our-research/entrepreneurship-freelance-economy/small-business-owners-say-government-doesn-t-understand-their-concerns-need-help-healthcare-costs-and-other-challenges>