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Connecticut Broadens Scope of Small Loan Act

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In June 2023, the Connecticut legislature passed amendments to the Small Loan Lending and Related Activities Act (the "Act"). On September 11, 2023, the Connecticut Department of Banking (the "Department") subsequently issued related guidance (the "Guidance") on the scope of the amended Act and its requirements. The amendments to the Act, which became effective October 1, 2023, have potentially significant implications for a wide range of financial services providers.

In addition to requiring the calculation of the annual percentage rate ("APR") in accordance with the method prescribed by Military Lending Act, instead of by the method prescribed by federal Truth-in-Lending Act as had previously been done, the amendments broadened the scope of the Act in a number of ways. First, the amendments raised the dollar threshold for application of the Act from $15,000 to $50,000. The amendments also expressly imposed licensing requirements on persons acting as an agent, service provider or in another capacity for persons who are exempt from licensure (such as a bank) under certain circumstances. Finally, the amendments simplified the definition of "small loan" in a manner that is arguably more inclusive.

The Guidance confirms that imposing licensing on certain agents of exempt entities was designed to "codif[y] existing common law true lender principles to require licensure of partners to banks when the following conditions are met":

- Such person holds, acquires, or maintains, directly or indirectly, the predominant economic interest in a small loan; or
- Such person markets, brokers, arranges, or facilitates the loan and holds the right, requirement or right of first refusal to purchase the small loans, receivables, or interests in the small loans; or
- The totality of the circumstances indicates that such person is the lender and the transaction is structured to evade the licensing requirements.

Inclusion of the predominant economic interest standard, consistent with similar recent legislation in other states, including Illinois, Maine, and New Mexico, may require the licensing of many fintech providers. The Guidance also confirms that the Department will consider the true lender factors set forth above, in addition to caselaw precedent construing such factors, to determine whether loans made on and after October 1, 2023,

must comply with the provisions of the Act as amended, including its APR limitations. Additionally, those who service loans made by a bank pursuant to a "true lender" arrangement on and after October 1, 2023, will need to obtain licensure.

The amendments also changed the definition of a covered "small loan" to "any loan of money or extension of credit, or the purchase of, or an advance of money on, a borrower's future potential source of money, including, but not limited to, future pay, salary, pension income or a tax refund" that was within the amount (now $50,000) and rate (12% APR) thresholds under the Act. The Act previously defined a "covered "small loan" as "any loan of money or extension of credit, or the purchase of, or an advance of money on, a borrower's future income" that was within the amount and rate thresholds under the Act. The Act also previously defined "future income" to mean "any future potential source of money, and expressly includes, but is not limited to, a future pay or salary, pension or tax refund."

The Guidance provides examples of non-traditional loan products that are generally covered by the Act as amended, when within the Act's amount and rate thresholds, including but not limited to, lawsuit settlement advances, inheritance advances, earned wage access advances, and income share agreements. While the Guidance concedes that applicability of the Act must be evaluated on a case-by-case basis, the Guidance also notes "that an advance of money on an individual's future potential source of money of $50,000 or less with an APR greater than 12% will likely be covered by the Small Loan and Related Activities Act." The Guidance further explains that an earned wage product, or an advance of money on future wages or salary that have been earned but not yet paid, will generally be covered by the Act as amended when the amount is $50,000 or less and the APR exceeds 12% when considering any finance charges.

Notably, the Guidance states that "[i]n substance, the revised definition remains the same as the previous iteration concerning the types of transactions considered [covered small loans]" and simply "streamline[d] the small loan definition by removing this intermediary definition [future income]." Accordingly, although the new definition of covered "small loans," which is not limited by the term "future income", may appear broader than the prior iteration, the Department's position appears to be that the non-loan products identified in the Guidance as subject to the Act, were also potentially subject to the Act before the amendments. The Guidance provides a form of potential relief in the form of the No-Action Position expressed in the Guidance. This position states that the Department will not take enforcement action alleging unlicensed activity, against a person that *newly* requires licensure for small loan activities under the Act as amended, but only if the person filed an application for licensure by October 1, 2023.

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7037 Ridge Road, Suite 300, Hanover, Maryland 21076
410.684.3200

hudsoncook.com