

## **The Rosenthal Act and Covered Commercial Debt**

### **What Good Faith Debt Collectors Need to Know**

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Commercial creditors and collection professionals already operate with established processes and a clear understanding that how an account is handled matters. The issue raised by California's Rosenthal Fair Debt Collection Practices Act, particularly as it applies to covered commercial debt, is not one of correcting conduct.

It is the reality of a strict liability statute that turns on technical distinctions and statutory definitions rather than intent or demeanor. Even careful, professional collection activity can fall within coverage unexpectedly. Once that occurs, ordinary commercial practices are evaluated under a different set of rules. That is where risk emerges, and why attention to nuance matters even for experienced, well-run organizations.

### **This Is a Populist Expansion, Not a Moral Judgment**

SB 1286 did not pass because the legislature believed commercial collectors were behaving improperly. It passed in response to a broader populist concern regarding small business owners who personally guarantee loans and then become subject to commercial collection processes that were never designed with natural persons in mind.

The author's statement makes this explicit. Traditional bank lending has long been inaccessible to many entrepreneurs, particularly entrepreneurs of color and women entrepreneurs. Alternative lenders filled that gap and often required personal guarantees. That practice is lawful, rational, and commercially necessary.

Once a natural person is personally obligated, however, the legislature determined that the manner in which collection occurs should more closely resemble consumer collection than traditional commercial enforcement. That change introduces compliance obligations that do not naturally align with established commercial collection processes.

SB 1286, passed in 2024 and effective for debts created or assigned on or after July 1, 2025, was intended to accomplish that shift. It expanded the definition of "debt" to include "covered commercial debt," defined as obligations incurred for a commercial purpose, in amounts under \$500,000, and owed by a natural person. On paper, the contours appeared straightforward. In practice, the expansion was unsettling. The breadth of the definition, combined with Rosenthal's strict liability framework, raised immediate questions about

how far coverage might extend and how many ordinary commercial collection activities could suddenly fall within scope.

### **AB 1520 and the Legislature's Course Correction**

Following SB 1286, there was understandable concern that the scope of covered commercial debt could extend well beyond its intended target. AB 1520 responded by clarifying and narrowing coverage.

AB 1520 made clear that not all obligations involving a business and a natural person guarantor are covered. In particular, it excluded obligations arising from trade credit, and, for the first time, actually defined "trade credit." This clarification was significant. It confirmed that ordinary trade credit was never the target. Covered commercial debt is focused on lending transactions, not routine extensions of trade credit such as net 30 invoices, supplier accounts, service contracts, or open book accounts arising from day-to-day commerce.

Without that clarification, any unpaid invoice supported by a personal guaranty risked Rosenthal treatment. AB 1520 restored balance by drawing a clearer line between financing and commerce. That distinction matters operationally, economically, and legally. Its passage was met with relief across the credit and collections industry.

Rosenthal's expansion is about lending. It is not about every commercial dispute involving an individual.

### **Why the Narrowing Still Requires Care**

The narrowing accomplished by AB 1520 is meaningful. First, it provides real statutory boundaries. Second, it confirms that coverage is transaction driven, not simply person driven. The presence of a natural person does not, by itself, invoke Rosenthal protections.

Third, it allows debt collectors to design intake and classification processes that are defensible, rather than overly conservative to the point of operational paralysis.

At the same time, exclusion remains something that must be established, not assumed. AB 1520 provides better tools. It does not eliminate the need for careful analysis.

### **Covered Commercial Debt Is About Lending, But Coverage Is Litigated as a Defense**

The statute is clear about its focus. It regulates commercial lending transactions where a natural person guarantees repayment. It is not directed at payment defaults arising from ordinary trade credit relationships or routine commercial disputes.

That said, whether a debt qualifies as covered commercial debt is ultimately a defense, not a shield. By the time coverage is being argued, the collector is already in a posture it would prefer to avoid.

From a risk management standpoint, coverage cannot be treated as an academic question. If a court later determines that a debt was covered, every communication, report, and workflow decision leading up to that point is examined under Rosenthal's strict liability framework.

The more useful question is not whether coverage seems unlikely, but what the consequences would be if someone later asserts that it applies.

### **The Real Operational Risk Is Misalignment, Not Misconduct**

The most persistent misconception surrounding Rosenthal's expansion is that it requires debt collectors to change who they are.

It does not.

What it requires is alignment between traditional commercial collection systems and consumer style statutory triggers.

Historically, commercial collection systems were built around efficiency, including standardized intake, automated reporting, uniform demand letters, flexible dispute handling, and significant reliance on vendors. None of those practices are inherently improper. When a natural person guarantor is involved, however, those same systems can produce technical violations without any abusive intent.

Examples include a courteous demand letter that lacks a required disclosure or is sent in the wrong language, credit reporting that occurs while a dispute is under review, or failing to bring a legal action in the debtor's jurisdiction (or business jurisdiction), as opposed to following the venue clause. No one is being harassed. No one is acting aggressively. And yet - Liability can still attach.

Compliance under Rosenthal is therefore less about tone and more about process architecture.

## **Vendor Risk and Oversight**

One of the most significant and often underestimated implications of Rosenthal is the affirmative duty of monitoring vendors. Even careful debt collectors can find themselves exposed through vendor activity.

This commonly occurs when vendors use outdated templates, apply consumer rules inconsistently, or treat disputes as informal communications rather than statutory triggers. The issue is not poor intent. It is the continued use of legacy commercial assumptions in a legal environment that has changed.

Debt collectors are not disengaging from vendors. They are reviewing processes, tightening oversight, and ensuring that vendor practices align with current compliance expectations. It is not always fun, but it is basic risk management.

## **Final Thoughts**

California is the first jurisdiction to extend consumer style debt collection protections into the commercial lending space in this manner, but it is unlikely to be the last. Other states are watching closely, and similar proposals are already being discussed elsewhere. Debt collectors who treat Rosenthal as a California specific anomaly risk missing the larger trend. Awareness, preparation, and thoughtful process design now will be far easier than reactive adjustments later.