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USURY IN ARKANSAS—REVISITED, REVISED AND REAFFIRMED

James E. Mitchell* and W. Christopher Barrier**

I. A CONTINUING REVIEW

Usury in Arkansas, published several years ago,¹ attempted to do three things: (1) *Explain the operation of Arkansas' constitutional limitation on interest:*² Citing an "insatiable urge to categorize," the author divided "all of Arkansas' usury law into fifteen rules"³ some of which were stated unequivocally as being the law, while others were "proposed", "perceived" or "disputed." (2) *Examine the economic impact of the usury law:* The author found risk capital scarce, consumer credit tight, and economic growth stunted, findings based largely on interviews and an examination of financial, rather than legal, publications.⁴ (3) *Propose an alternative approach:* The author suggested removing the limitation as to loans to corporations and partnerships; establishing a public loan fund for the poor at 10%; and allowing merchants to charge a higher price, plus the interest, on credit sales.⁵

The activity—judicial, legislative, and economic—since 1972 warrants a new look at the rules, the economy and the Arkansas Constitution. Of the fifteen rules set forth in *Usury in Arkansas*, only nine were stated as being the law, without qualification. All nine of those rules have survived intact and are set forth in this article with citations to new cases, if any, which confirm them. Rule 5, on Commitment Fees, was labeled a "proposed rule." The Arkansas Supreme Court has recently made its own proposal with some precision in *Arkansas Savings & Loan Association v. Mack Trucks of Arkansas, Inc.*⁶ and Rule 5 must be revised in light of the court's work. Rule 7, on Computational Devices, was acknowledged to be "disputed" in part. Such devices have taken as many new forms as they had old ones, and the Rule must be reconsidered. Rules 6, 9,

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1. Mitchell, *Usury in Arkansas*, 26 *ARK. L. REV.* 263 (1972), [hereinafter *Usury in Ark.*].

2. *ARK. CONST.* art. 19, § 13.

3. *Usury in Ark.*, *supra* note 1, at 265.

4. *Id.* at 298-321.

5. *Id.* at 264.

6. 263 *Ark.* 264, 566 S.W.2d 128 (1978).

12, and 14 were said to have been "perceived." That weasel word has proved fifty percent accurate. Rules 9 (Consolidations and Re-workings) and 12 (Intent) must be reconsidered. Rules 6 (Compensating Balances) and 14 (Single Interest and Insurance) have proved resilient, though Rule 6 bears a new look.

Beyond these revisions, several entirely new areas have developed, requiring the review of questions not previously considered central to usury law. The rules, old and new, affirmed or revised, are set out in Section II of this article. Old rules which have been modified and new rules are printed in italics.

Recent developments which have amplified or clarified the original rules, including a number of procedural matters, are discussed in Section III of this article with new citations. Other developments which have necessitated changes in the original rules or which have required new rules are also discussed in Section III.

Section IV is a discussion of recent decisions in areas which were not covered by the original rules or which were not amenable to the "urge to categorize." These areas include leasing, federal legislation, federally-related loans, and federal constitutional questions.

The economic predictions of *Usury in Arkansas* have proved painfully accurate in the intervening seven years. As predicted, risk capital has become scarcer still, consumer credit has tightened, and even home mortgage money has been hard to come by. Indeed, these predictions have even been affirmed by the United States Congress. *Stephens Security Bank v. Eppivic Corp.*,⁷ dealt with the validity of the Brock Bill,⁸ which allowed federally-insured banks and savings and loan associations to charge a rate related to the cost of money in the federal reserve system on large business and agricultural loans.⁹ Under the Brock Bill the permissible rate hovered around thirteen percent on such loans in Arkansas during the life of the law, October 29, 1974, to July 1, 1977. The district court in *Stephens Security Bank* noted that the measure was remedial and was a conscious effort by Congress to deal with economic adversity.¹⁰

The 1979 Arkansas Constitutional Convention, whose handiwork will be considered by the electorate on November 4, 1980, has reviewed the constitutional limitation on interest. The fate of a new

7. 411 F. Supp. 61 (W.D. Ark. 1976), *aff'd*, 553 F.2d 102 (8th Cir. 1977).

8. 12 U.S.C. § 1831(a) (1976).

9. These lenders can negotiate their commercial paper through the system at less than par, *i.e.* "discount" it, to gain liquidity.

10. *Stephens Security Bank v. Eppivic Corp.*, 411 F. Supp. 61, 65 (W.D. Ark. 1976).

constitution may well depend on the Convention's ability to separate a revised usury article from the main document or to draft an acceptable compromise article which gives both the relief which is needed and some protection for which a need is perceived.

Section V of this article attempts to examine where we now stand legally and to propose a revised usury article for consideration by the Arkansas Constitutional Convention, when it reconvenes in 1980.

II. THE RULES—OLD AND NEW

Rule 1. CALCULATING ERRORS: MISTAKE AND FRAUD - An honest error of calculation or fraud on the part of an intermediary will not render a note usurious as between borrower and lender even though the rate called for by the document in question be in excess of 10%.

Rule 2. CALLING LOANS - A lender may call or accelerate a callable loan without fear that such action will render usurious a previously non-usurious loan. If the lender, upon accelerating payments due, fails to calculate a rebate or otherwise account for unearned interest, the borrower may refuse to pay that excess amount only, but he may not refuse to repay principal and earned interest.

Rule 3. COLLATERAL AGREEMENTS - In addition to signing a loan contract, a borrower and a lender may enter into other contracts which result in extra payments to the lender if the lender provides adequate independent consideration for the extra compensation.

Rule 4. COMMERCIAL PAPER: DISCOUNTING AND RECOURSE - (Seller): As a seller of commercial paper

1. You may sell the paper for any price without fear of a usury charge so long as the transaction is a *bona fide* sale of commercial paper. The sale may be with or without recourse. You may not agree with a finance company in advance that the company will buy your paper at, say, 90% of face value and then set your credit price and sell your merchandise for credit at 10% simple. The court views this as one transaction in which the real loan from the finance company to the credit buyer bears usurious interest

of roughly 20% and in which the sale price is set in contemplation of the promised discount, thereby implicating the seller in the usury. Neither the seller in a recourse arrangement nor the lender in a non-recourse arrangement can collect the debt or repossess the merchandise.

(Buyer): As a buyer of commercial paper

1. You may buy paper at a discount from a retail seller who can prove that he has only one price at which he sells his merchandise whether you buy his paper or not.

2. You may buy a usurious contract from a seller, but you will find you have bought a nullity since usurious paper is void upon being written. If you knowingly purchase such a usurious and therefore void contract, you may not recover your purchase price since the instrument cannot be sued upon in court nor otherwise enforced by you or the merchandise seller against the merchandise buyer who is the actual recipient of the benefit of your cash advance.

Rule 5. COMMITMENT FEES - (*Proposed*) - *A lender may require a potential borrower to buy the lender's commitment to lend money if the proposed loan transaction is sufficiently far off in time or is contingent upon the borrower's completion of interim matters. The lender requiring this fee may then still lend money at 10% or get someone else to lend it at 10% without fear of a usury charge.*

Rule 5. COMMITMENT FEES - (*Perceived Rule*) - *The Court will consider a fee for the reservation of funds to be part of the interest charged on the funds so reserved.*

Rule 6. COMPENSATING BALANCES - (*Perceived Rule*) - *A bank may refuse to lend to noncustomers when conditions require such a restriction, but it may not legally require a borrower to open a checking or savings account nor to buy a certificate of deposit as an express identifiable condition of getting a specific loan when the interest on the loan plus the value of the use of the deposited funds gives the bank an overall return on its loan in excess of 10%.*

Rule 7. COMPUTATIONAL DEVICES: DISCOUNTING, POINTS, ALLOCATING PAYMENTS - *A lender may withhold or discount the*

maximum legal interest on a note for a period of twelve months. That is, on a \$100.00 note, at 10%, for one year, a lender may legally refuse to forward more than \$90.00 even though that procedure raises the technical interest rate to 11.11%.

1. Disputed sub-rule: A lender may withhold the maximum legal interest or a portion thereof on a note for a period of thirty-six months or more.

2. Sub-rule: Lenders may apply payments received first to interest to the maximum amount of 10% per annum on the unpaid balance as of the time of receipt of payment and then to principal.

3. Sub-rule: A lender may not devise any other collection technique or computational device which will increase his actual return above 10% per annum simple.

Rule 8. CONFLICT OF LAWS - The law of the state in which the contract is made will usually govern unless the parties agree that the law of some other place should govern and they have a reasonable and *bona fide* basis for making the agreement. When the place of contract is in question, the court will count contacts between the parties, the contract, and competing jurisdictions. Place of payment of the loan does not determine the issue.

Rule 9. CONSOLIDATING LOANS AND REMAKING CONTRACTS - (Perceived Rule) - A finance company that refinances and consolidates its own old notes for a borrower must give the borrower full rebate credit for unearned interest and unused insurance premium payments or else run the risk of losing the entire principal amount of the new loan because the unrebated sums become part of the interest charges on the new loan. This rule applies to any loan called prematurely and to any circumstance which forces the borrower involuntarily to pay the loan company more than 10%. Interest would be on the actual authorized principal outstanding as opposed to some hypothetical or manipulated principal amount.

Sub-rule: A borrower and lender may agree to cancel a usurious contract and replace it with a legal one. When the borrower makes the new contract voluntar-

ily it is binding.

Sub-rule: If a contract is not usurious to begin with, a usurious extension agreement will not void the original contract, but only the extension thereof.

Rule 10. CONTINGENCIES AND PARTICIPATIONS - Lenders may participate in profits in addition to receiving interest on loans only if the profits depend on a contingency which involves a legitimate commensurate risk of capital and is within reasonable control of the debtor. Any other arrangement to participate in profits may be usurious even though the excess profit never materializes.

Rule 11. CONTINUOUS ACCOUNTS AND PENALTIES - When a seller and buyer enter into a long-term contract for services, buyer to pay for services periodically as consumed, the seller may charge a penalty for any and all overdue payments, which charge may exceed 10% annual interest on the outstanding balance of payments due.

Rule 12. CONTRACT LIMITATIONS AND INTENT - (Perceived Rule) - Except in cases of clear violation on the face of a contract or of mistaken ideas about the law or legal limit, intent to extract a usurious interest charge is a primary element of the offense of usury. A recitation in the contract itself of intent to charge no more than a legally computed 10% rate will negate less probative evidence of evil or unlawful intent.

Rule 12 - CONTRACT LIMITATIONS AND INTENT - (*New Perceived Rule*) - *While the intent of the lender, when ascertainable, is one element to be considered in determining whether a contract is usurious, good faith efforts to comply with the law will not excuse carelessness or mistake resulting in a usurious rate being charged or collected. Although a disclaimer of illegal intent will be considered, statements of intent are less important than actual results. Intent to collect more than 10% interest alone may be sufficient evidence to find a lender guilty of usury, even without any agreement by the borrower to pay it, especially if there is a strong likelihood that the excess, in the ordinary course of events, would have in fact been collected.*

New Perceived Sub-rule: "Intent to collect" may be established by previously established or used procedures; or computer programs in existence at the time of the loan; or bills sent, calling for the excessive interest.

Rule 13. COST OF BUSINESS AND EXCESS CHARGES - A lender may charge a borrower, in addition to 10% interest, for all services or fees which benefit the borrower and do not fall within normal business expenses of lenders even if such charges also partially benefit lender. Any charge to the borrower for services which benefit only the lender or parallel his normal business expenses constitutes interest and must be added to the recited contract interest to determine the actual effective interest rate on the questioned loan. Payment by the lender of a collected fee to a third party will partially negate any inference that the fee is of benefit to the lender.

Sub-rule: If the lender fails to specify what excess charges are for, the court will assume they are interest charges unless the lender can prove otherwise.

Rule 14. CREDIT INSURANCE - (Perceived Rule) - Lenders may require that a borrower insure his loan or his credit purchase. As agents for third party insurance companies, they may sell insurance. They may buy it for the borrower. But they may not require that he buy insurance through them, nor may they participate in kickbacks, as distinguished from *bona fide* agent's fees from insurers which add to their lending profits. If lenders collect premiums for credit or credit-related property insurance out of the money they lend to borrowers, they must pay these premiums to third parties and insure that the borrower actually benefits or is given the opportunity to benefit from the insurance coverage for which they withheld the premium. Collecting the premium with professed intent to pay it out at some future time will not satisfy the court that the collector is not using the collection and supposed intent to pay it out as a cloak for usury.

Rule 15. CREDIT PRICE: THE TIME-PRICE DIFFERENTIAL - A seller may sell any item for credit at a credit price which is higher than the cash

price so long as he does not set the credit price on a cash price estimate and use the difference in fact to add to his interest charges.

Added Rule 16. *DISBURSEMENT - A lender may charge interest from the day of closing at a full 10% even if funds are actually disbursed after the day of closing, provided the discrepancy involves no bad faith and relates to legitimate commercial problems of borrower and lender.*

Added Rule 17. *UNCERTAIN RATES - A non-usurious contract which calls for an uncertain or variable rate of interest, or which calls for specified applications of funds going to the lender under specified circumstances, may become usurious as a result of occurrences taking place after the contract is executed, even if those circumstances were not within the contemplation of either party to the contract.*

III. RECENT DEVELOPMENTS

RULE 1 (CALCULATING ERRORS: MISTAKE AND FRAUD)

While Rule 1 has not changed, the use of fraud as a counter to the defense of usury gained some strength with the decision in *Turney v. Roberts*.¹¹ In *Turney*, the borrower defrauded the lender in a host of ways. The borrower over-valued collateral, misrepresented the actions of third parties, and assured the lender that the loan arrangement was legal when in fact the borrower had not checked with a lawyer about the loan's legality. The loan documents as signed, taking all the circumstances of the transaction into account, called for an interest rate substantially in excess of ten percent. The lender knew he would get more than ten percent but had been tricked into believing this to be legal. The chancellor had reluctantly voided the contract for usury while censuring the borrower.¹² The Arkansas Supreme Court merely reformed the contract and noted, "We perceive no valid rationale why a usurious contract is immune to reformation. Our usury law is not so ironclad nor designed to provide an impenetrable shield so as to prevent absolutely an action for reformation of a written instrument."¹³ In

11. 255 Ark. 503, 501 S.W.2d 601 (1973).

12. *Id.* at 508, 501 S.W.2d at 605.

13. *Id.* at 509, 501 S.W.2d at 606.

Turney the court must have viewed the borrower's palpable fraud as worse than the lender's usury. Since the lender clearly intended to receive more than ten percent, any other reading would make *Turney* inconsistent with such cases as *First National Bank of Memphis v. Thompson*¹⁴ and *Ford Motor Credit Co. v. Catalani*.¹⁵

Because *Turney* involved a naive individual lender, it may not help professional lenders. It is highly unlikely that a commercial lender will manufacture a case in which it allows itself to be defrauded to test this rule, but if such circumstances arise, the *Turney* reasoning should be exploited.

While fraud has gained new strength as a counter to the defense of usury, recent cases have further eroded the use of honest mistakes as a shield against usury defenses. Lenders blamed "computer error" for overcharges in three cases, *Redbarn Chemicals, Inc. v. Bradshaw*,¹⁶ *Cagle v. Boyle Mortgage Co.*,¹⁷ and *Southland Mobile Home Corp. v. Webster*.¹⁸ Each case was decided against the lender. In *Redbarn* there was evidence contradicting the claim that the computer had been programmed incorrectly. Nevertheless, in all three cases the result seemed to be based at least in part on the assumption that anyone sophisticated enough to use a computer had better be sophisticated enough to program it correctly. It may be almost a rule of law that a computer cannot make a good faith mistake in calculating interest.¹⁹

RULE 3 (COLLATERAL AGREEMENTS)

Rule 3 was recently reaffirmed in *Key v. Worthen Bank & Trust Co., N.A.*,²⁰ wherein the Arkansas Supreme Court found the annual membership fees charged by banks on bank cards to be fees for "a convenience" and not interest,²¹ "although their effect may be to

14. 249 Ark. 972, 463 S.W.2d 87 (1971). In *Thompson* the court found no evidence of fraud or mistake and no evidence of excusable error in calculation. The defense of usury was upheld on the basis that any mistake by the lender lay in its belief that the charge was lawful, which amounted to a mistake of law from which the lender could not be relieved. *Id.* at 977, 463 S.W.2d at 89.

15. 238 Ark. 561, 383 S.W.2d 99 (1964). In *Catalani* the contract was held usurious as a mistake of law when the lender thought his method of charging interest was lawful. *Id.* at 564, 383 S.W.2d at 101.

16. 254 Ark. 557, 494 S.W.2d 720 (1973).

17. 261 Ark. 437, 549 S.W.2d 474 (1977).

18. 263 Ark. 100, 563 S.W.2d 430 (1978).

19. See also the discussion under Rule 12, p. 328 *infra*.

20. 260 Ark. 725, 543 S.W.2d 496 (1976).

21. *Id.* at 730, 543 S.W.2d at 498.

increase the sum payable from the borrower to the lender."²² The court in *Key* cited *Leavitt v. Marathon Oil Co.*²³ in which the borrower was also required to lease certain property from the lender as a condition to obtaining the loan.²⁴ *Key*, however, may serve to clarify Rule 3 and qualify *Leavitt*. The court noted, "Mrs. Key was not a necessitous borrower who as a prerequisite to a loan was forced to buy something which she did not want."²⁵ The cost of the collateral agreement must relate to its actual value *to the borrower*, not simply in absolute terms.

**RULE 5 (COMMITMENT FEES) and RULE 7
(COMPUTATIONAL DEVICES: DISCOUNTING, POINTS,
ALLOCATING PAYMENTS)**

Rule 5 was only a "proposed rule," there being no fixed law on the subject at the time of the prior article. *Arkansas Savings & Loan Association v. Mack Trucks of Arkansas, Inc.*²⁶ does not change the proposal offered in Rule 5 nor the substance of Rule 7, but the rules must be narrowed somewhat in view of that case.

In *Mack Trucks*, over the filed protests of the major portion of Arkansas' financial community, the court found a "service charge" or "commitment fee" to be interest, without distinguishing the two terms. The lender collected a one percent fee on a construction loan in addition to interest at nine percent. Because the one percent was collected in advance on the full amount, while disbursements were made periodically, the overall return exceeded ten percent. We question whether *Mack Trucks* is really a "service charge" case. A "service charge" is ordinarily a flat periodic fee for extending credit, such as a "carrying charge" on a charge account, or the "membership fees" on credit card plans, as in *Key v. Worthen Bank & Trust Co., N.A.*²⁷ (which appears to us to be a genuine "service charge" case). Because the "commitment fee" in *Mack Trucks* was charged not in advance of closing to reserve funds entirely at a future time, but rather at closing, the case may not be a true "commitment fee" case either.

To contrast a nominal commitment fee with a genuine commit-

22. *Id.* at 730, 543 S.W.2d at 499.

23. 186 Ark. 1077, 57 S.W.2d 814 (1933).

24. *Id.* at 1079-80, 57 S.W.2d at 815.

25. *Key v. Worthen Bank & Trust Co., N.A.*, 260 Ark. 725, 730, 543 S.W.2d 496, 498 (1976).

26. 263 Ark. 264, 566 S.W.2d 128 (1978).

27. 260 Ark. 725, 543 S.W.2d 496 (1976).

ment fee, it may be useful to compare *Mack Trucks* and *Paley v. Barton Savings & Loan Association*.²⁸ In *Paley* a New Jersey court noted that there was "no loan of money" at the time of the payment of the fee,²⁹ and reasoned that if there is no loan, there is no interest, and the fee must necessarily be something else. In *Mack Trucks*, even though all of the money was not disbursed at closing, there was a note and other attendant loan documents—a "loan of money." The Arkansas Supreme Court's language in *Mack Trucks* does not recognize the *Paley* distinction and is otherwise so broad that Proposed Rule 5 has been changed to a Perceived Rule and rewritten.

This rule, as rewritten, is consistent with the "admission" in *Sosebee v. Boswell*,³⁰ over which the proposed rule had glossed. In *Sosebee*, a one percent "commitment fee" and a one percent "service charge" were "admittedly . . . chargeable as interest,"³¹ an "admission" certainly *not* made in *Mack Trucks*. That this perceived rule may defy economic reality is immaterial.³²

The Arkansas Supreme Court also considered whether the fee in *Mack Trucks* was a permissible discount, as discussed in Rule 7 (Computational Devices: Discounting, Points, Allocating Pay-

28. 82 N.J. Super. 75, 196 A.2d 682 (1964).

29. *Id.* at 81, 196 A.2d at 685.

30. 242 Ark. 396, 414 S.W.2d 380, *cert. denied*, 389 U.S. 953 (1967).

31. *Id.* at 398, 414 S.W.2d at 381.

32. A true commitment fee serves a true purpose. It pins the availability of a given amount of money at a certain rate. It is a speculative purchase of a promise. If the rates go up, the fee was well spent. If the rates go down, it was wasted.

A true commitment fee is analogous to a call option. To say that the fee is nothing more than extra interest to the bound lender is as logically inaccurate as to say that the price of a call option is nothing more than extra dividends to the seller of the option. The commitment fee is extra income to the lender just as call option proceeds are extra income to the holder of the optioned shares, but all income is not interest to a lender any more than all income is dividends to a holder of stock.

A true commitment fee is paid *before* money is loaned. There may never be a loan of money. If the money were never loaned, what would the rate of interest be if the fee is interest?

In *Mack Trucks* the fee was not a true commitment fee, even though the court said it was. (Although the decision itself is unanimous, in his concurring opinion on rehearing, Mr. Chief Justice Harris seems to be suggesting that the court withhold judgment on "true" commitment fees.) The case, however, must be read as though *all* commitment fees were tainted, and the financial community remains, to that degree, further hamstrung by the usury law, which has wreaked enough havoc without this.

As a possible way out, we propose a test case. Set up a true commitment fee, paid in advance of the loan, exclusively to pin the price and availability of money. Set it up in parallel with two borrowers. One will decide to borrow the money and one will decide not to borrow. Have the rate in both cases be 10% on the money to be borrowed. Have both sue for a declaratory judgment voiding the deal on the basis of usury. If the court affirms the *Mack Trucks* language, no one will be any worse off than now. Forced by circumstances to deal with economic reality, the court may reinterpret *Mack Trucks*. It is worth a try.

ments). The answer was no. The court characterized the fee as "no more than a discount"³³ and found it to be interest. But we would also question whether *Mack Trucks* is a true "discount" case, in the sense that that term is ordinarily used in mortgage lending. Specifically, a mortgage banker may agree to make a loan, after receiving a commitment from a permanent lender (probably a quasi-governmental entity, such as the Federal National Mortgage Association), at a specific rate—perhaps nine percent. The mortgage banker closes the loan and immediately assigns it to, in this example, FNMA, which funds it. But how does the mortgage banker make any money? On such loans, the mortgage banker charges a "discount" or "points," the maximum amount of which is ordinarily set by the federal government. (The borrower may also end up paying a "commitment fee" and a "service fee" as well, which do not need to be considered for purposes of this illustration.) In today's money market, the numerical value of the discount, when added to the nominal percentage rate, is almost invariably in excess of ten percent, bringing such loans within the prohibition of the third sub-rule under original Rule 7 which disapproves collection techniques which increase the lender's actual return above ten percent per annum and echoes the "admission" in *Sosebee v. Boswell*.³⁴

Questions of federal pre-emption aside, more recently lawyers for lenders have disregarded *Sosebee* and have privately rationalized this apparent transgression in one of two ways. The first argument would spread the dollar amount of the discount over the life of the loan, adding it to the actual interest. This seems artificial and, in the light of the court's skepticism in *Mack Trucks*, wholly unsupported.³⁵

The second argument is more sophisticated. It would deduct the discount from the face amount of the loan and ignore the stated interest rate. The effective interest rate is then calculated by looking at this new face amount and the monthly payments. The results can be somewhat startling. Computed actuarially, a twenty-five year loan with a stated interest rate of nine and three-quarters percent per annum will support a discount of almost two "points"—a numerical

33. *Ark. Sav. & Loan Ass'n v. Mack Trucks of Ark., Inc.*, 263 Ark. 264, 268, 566 S.W.2d 128, 131 (1978). By commenting gratuitously on ARK. STAT. ANN. § 68-604 (Cum. Supp. 1977) (as amended 1961) which permits discounting in advance for 36 months, the court added further dispute to the "disputed sub-rule" set out under Rule 7 in the original article, which recognized this 36-month statutory exception.

34. 242 Ark. 396, 398, 414 S.W.2d 380, 381 (1967).

35. In this regard, see also *Ryder Truck Rental, Inc. v. Kramer*, 263 Ark. 169, 563 S.W.2d 451 (1978), discussed p. 347 *infra* with respect to added Rule 17.

total of nearly eleven and three-quarters percent. However, a thirty year loan with a stated interest rate of nine percent per annum will support a discount of over eight points—a numerical total of over seventeen percent!³⁶

Despite the size of these numbers, the borrower still pays ten percent or less on the money he actually gets, if one looks at the *substance* of the transaction, as the law says we should.³⁷ Additionally, the device provides a means for compensating mortgage bankers for originating loans and, hence, stimulates production of housing. Finally, the size of the discount fluctuates with the money market, varying the amount of cash borrowers must produce on the front end—something which also occurs with conventional loans as to down payments.

The underlying policy of the Arkansas Supreme Court's decisions as well as economic realities would dictate to us the acceptance both of true commitment fees and of an actuarial approach to discounts. Nevertheless, the language of *Mack Trucks*—although written in very broad terms by a special justice—falls clearly within the trend of the majority's thinking and must be taken at face value in condemning both commitment fees and discounts.

RULE 6 (COMPENSATING BALANCES)

The Arkansas court has yet to consider this perceived rule. In *McAdoo v. Union National Bank*,³⁸ the Eighth Circuit Court of Appeals faced the issue noting the lack of Arkansas Supreme Court precedent. In *McAdoo* the lender clearly required the borrower to purchase a \$300,000 certificate of deposit from a broker and place it in the lending bank in order to secure a \$500,000 loan. The jury found no usury. The court of appeals stated:

36. The following figures were provided by a consulting actuary. The first column is the duration of the loan. The headings on the next four columns indicate the stated interest rate. The figures below each of these rates indicate the maximum discounts (as a percent) which may be applied to loans at those stated rates, for those durations, to produce an effective interest rate of slightly less than ten percent per annum:

| Years | 9% | 9.25% | 9.50% | 9.75% |
|-------|----------|----------|----------|----------|
| 20 | 6.76624% | 5.09364% | 3.40826% | 1.71030% |
| 25 | 7.64873% | 5.75752% | 3.85207% | 1.93276% |
| 30 | 8.31259% | 6.25546% | 4.18397% | 2.09865% |

37. *Ragge v. Bryan*, 249 Ark. 164, 458 S.W.2d 403 (1970).

38. 535 F.2d 1050 (8th Cir. 1976).

[W]e think that the requirement with which we are concerned is suspect, and we do not give carte blanche legal approval to the requirement or to others comparable to it. On the other hand, we are not prepared to say that such a requirement automatically or as a matter of Arkansas law makes the affected obligation usurious simply because the lender may derive more money from the overall transaction than he would have received had he made the loan at the maximum legal rate of interest with no strings attached.³⁹

Thus, the law of the Eighth Circuit clearly is that the law of Arkansas on this issue is unclear.

Despite *McAdoo*, any careful lawyer will still rely on Perceived Rule 6 when advising a lender. Compensating balances are dangerous until proven otherwise. It is one thing to *prefer* customers who *already* have substantial balances, still another to dictate the deposit of specific minimums as a precondition of a loan. The Arkansas Supreme Court's reasoning in *Key v. Worthen Bank & Trust Co., N.A.*⁴⁰ may have some bearing here. A pre-existing account would presumably meet some need of the borrower. A new account, however, may be positively undesirable—if, for example, a high checking account balance were required, causing a complete loss of interest, or a deposit in a savings account bearing interest at a rate lower than would otherwise be available to the borrower was required.

In *McAdoo* the court of appeals noted specifically that the loan was fully disbursed before the certificate of deposit was purchased.⁴¹ Time of disbursement may be critical in compensating-balances cases if the Arkansas Supreme Court follows the Eighth Circuit's reasoning in *McAdoo*. If the law flows in another direction, we can only say that the significance of time of disbursement is as yet unknown.⁴²

RULE 9 (CONSOLIDATING LOANS AND REMAKING CONTRACTS)

A new sub-rule, helpful to lenders in some instances, has been added to Rule 9 (Consolidating Loans and Remaking Contracts). In

39. *Id.* at 1057.

40. 260 Ark. 725, 543 S.W.2d 496 (1976).

41. *McAdoo v. Union Nat'l Bank*, 535 F.2d 1050, 1055 (8th Cir. 1976).

42. In this regard, consider the discussion with reference to Added Rule 16 (Disbursement). Even if compensating balances may be required, the *McAdoo* decision does not condone mere failure to disburse as a means of maintaining them. In that way, it follows the spirit of the Arkansas decisions.

Hayes v. First National Bank,⁴³ the Arkansas Supreme Court held that when payment of the unpaid balance of a nonusurious loan is extended at a usurious rate, only the extension is usurious.⁴⁴ However, this sub-rule may be of significance to national banks only. If a borrower *pays* a usurious loan, he may only recoup the excessive interest.⁴⁵ But, if the lender is a national bank, under federal law, it may have to refund *twice* the amount of the interest already paid.⁴⁶ (This sub-rule is dictum in *Hayes*, but is apparently well-considered.)

RULE 10 (CONTINGENCIES AND PARTICIPATIONS)

Rule 10 still applies to contingent *profits*. Added Rule 17 (Uncertain Rates) is required to consider contingent *interest rates*.⁴⁷

RULE 11 (CONTINUOUS ACCOUNTS AND PENALTIES)

*Hayes v. First National Bank*⁴⁸ also extends the doctrine of Rule 11 (Continuous Accounts and Penalties) beyond utility cases. *Hayes* supports a broad application of the rule that true penalty charges are not interest.⁴⁹

RULE 12 (CONTRACT LIMITATIONS AND INTENT)

The law with reference to intent, as enunciated in Rule 12, seemed relatively clear when the rule was written. In *Southland Mobile Home Corp. v. Webster*,⁵⁰ however, Justice Smith adopted virtually Chinese inscrutability to effect a subtle change in Arkansas' substantive law of usury:

We have often said, in upholding contracts assailed as usurious, that for a charge to constitute usury the lender must have intended to take more than the maximum rate of interest. *Brown v. Central Ark. Production Credit Ass'n* That statement, needless to say, cannot be taken literally in every situation. A lender can no more purge a loan of usury by saying that he did not intend to charge more than 10% interest than a borrower can contaminate his debt by saying that he meant to pay more than 10%. Our

43. 256 Ark. 328, 507 S.W.2d 701 (1974).

44. *Id.* at 332, 507 S.W.2d at 703-04.

45. *Harris v. McCann*, 229 Ark. 972, 319 S.W.2d 832 (1959).

46. 18 U.S.C. § 86 (1976).

47. See discussion of Rule 17 p. 347-49, *infra*.

48. 256 Ark. 328, 507 S.W.2d 701 (1974).

49. *Id.* at 331, 507 S.W.2d at 703.

50. 263 Ark. 100, 563 S.W.2d 430 (1978).

decisions have never implied that usury does not exist unless the parties, upon concluding their agreement, have shaken hands and congratulated each other upon having arrived at a contract calling for only 12% interest.⁵¹

The last sentence we must take as dictum. The case at bar involved a computer mistake overcharging a total of between five and twenty-five dollars over a six year period on a loan in excess of \$5,000.00 made by a mobile home dealer. The dealer had actually submitted computer print-outs to a law firm in advance to be certain the calculated interest rates were legal.⁵²

The court will undoubtedly continue to say, on occasion, that the intent required is the intent to charge a certain amount and that if that amount happened to exceed ten percent, there was an intent to charge a usurious rate of interest. But that gets us nowhere, especially when dealing with computers. The reality may be, as in *Webster* or *Cagle*, that the lender knows little about the operation of computers or has a party some distance removed from the transaction do the calculations or the billing, or both. When we were dealing with manual pre-calculated interest tables⁵³ (which tables, by the way, themselves disagree with each other) the court excused obvious good faith errors. No more.

In *Cagle v. Boyle Mortgage Co.*,⁵⁴ the contract documents called for a ten percent rate of interest. This should have been far stronger evidence of a lack of intent to charge a usurious rate than any sort of disclaimer clause saying that no more than the legal rate would be charged. The *Cagle* lender, using a contract valid on its face, availed itself of a modestly generous interest rate calculated by a computer located and programmed in its Memphis, Tennessee, office. Billing on a daily interest calculation, based on a 360 day year, resulted in a rate slightly in excess of ten percent per annum. Interest was also compounded. The true annual interest came to 10.6235296 percent, as billed. The Arkansas Supreme Court apparently did not believe the assertion that the calculations were simply mistakes.

But *Cagle* does more than indicate the court's disbelief in the assertion of mistake, because when the lender discovered its error (concurrently with the beginning of litigation), it dropped the excess

51. *Id.* at 105, 563 S.W.2d at 432.

52. *Id.* at 104, 563 S.W.2d at 432.

53. *Davidson v. Commercial Credit Equip. Corp.*, 255 Ark. 127, 499 S.W.2d 68 (1973); *Sammons-Pennington Co. v. Norton*, 241 Ark. 341, 408 S.W.2d 487 (1966).

54. 261 Ark. 437, 549 S.W.2d 474 (1977).

charge. The charge furthermore, would *not* have been permissible under the contract signed. There was clearly no "contract" to take usurious interest as required by the Constitution,⁵⁵ no "agreement" as required by prior cases,⁵⁶ and no such interest was "reserved, taken or secured."⁵⁷ No such interest was reserved, taken or secured in *Cagle*, because no payment was made.⁵⁸ There was nothing which would previously, under case, constitutional or statutory law, have constituted usury except the intent, inferred from billing statements, to collect a certain amount of money, in excess of either the legal or the contract rate.

It would appear, therefore, from *Cagle* that the intent to *collect* alone—without contractual consent or consummation—may constitute usury. The case also seems to say that the intent to *avoid* usury is insufficient, if one in fact has collected a payment. Based upon the facts in *Cagle* the following elements should render a loan usurious: 1) a note not usurious on its face, but 2) a computer which uses a 360 day year, 3) and compounds interest at intervals of less than a year, with 4) the actual interest billed-for exceeding ten percent per annum, even though no payment is collected. But will such a fact situation always result in a usurious loan?

In *First American National Bank of Nashville, Tennessee v. McClure Construction Co.*,⁵⁹ a Nashville bank bought three mortgage loans on Arkansas real estate from its Memphis subsidiary under circumstances similar to those above. The Arkansas Supreme Court conceded that these facts made the case "similar" to *Cagle*.⁶⁰ The chancellor had found usury, but the Arkansas Supreme Court disagreed and proceeded to note certain dissimilarities.

In *Cagle*, the lender had an Arkansas office and did business regularly in Arkansas, while First American of Nashville and its assignor neither had offices in Arkansas nor regularly transacted business in the state.⁶¹ The point of making this distinction, however, is certainly unclear, as the court was not deciding a conflict of law question, as contemplated by Rule 8.

The *Cagle* computer used a 360 day year for all loans; the Arkansas manager brushed off complaints of excessive interest; and "[m]ost significantly," the *Cagle* lender had actually collected ex-

55. ARK. CONST. art. 19, § 13.

56. See, e.g., *Briggs v. Steele*, 91 Ark. 458, 461-62, 121 S.W. 754, 755 (1909).

57. *Id.* at 462, 121 S.W. at 755.

58. *Cagle v. Boyle Mortgage Co.*, 261 Ark. 437, 439, 549 S.W.2d 474, 475 (1977).

59. 265 Ark. 792, 581 S.W.2d 550 (1979).

60. *Id.* at 794-95, 581 S.W.2d at 551.

61. *Id.* at 795, 581 S.W.2d at 551.

cessive interest in a companion transaction.⁶² There is nothing in the *McClure* opinion, however, to indicate that the Nashville bank would *not* have collected the excess interest, had the loans been paid according to their terms, instead of being foreclosed. What if, for instance, one were paid, and then the other two were foreclosed? Would this occurrence provide a usury defense to the foreclosures?

There was no evidence in *McClure*, according to the court, that the computer was programmed to compute all loans on a 360 day year, but one would assume from *Cagle* that the burden of proof in this regard would be on the lender to prove affirmatively that it *did* have an appropriate program that was not used. The *McClure* opinion does not even mention the compounding problem.

What it does mention is intent, and a "distinction, . . . sometimes a fine one, between a mistake of fact and one of law."⁶³ As for intent, the chancellor did not "make a specific finding of intent to make an unlawful charge," but simply found *Cagle* controlling.⁶⁴ This apparently was not enough. By way of making this distinction the court cited *Brooks v. Burgess*⁶⁵ and *Ford Motor Company v. Catalani*.⁶⁶ If these cites mean anything, the formulation has to be something like this: If you *know* how interest is going to be calculated, but think the method is acceptable, you had better be right. If you *don't* know how it is going to be calculated, but hope it is done within the law, you may be safe.

The bank in *McClure*, however, did not send off for an interest table. It used its own computer. The only distinction would seem to be that in *McClure* the *officer* supposedly knew he couldn't use a 360 day year and one was used anyway, while in *Cagle* the computer would calculate *every* loan that way, regardless of the officer's intent.

In the final analysis, we must profess some affinity for Justice Purtle's opinion in *McClure*, which concurs in the result but not the method: "I cannot distinguish the facts in the present case from those in *Cagle* As it stands, the lawyers and the courts will just have to guess at which case we may decide to follow."⁶⁷ *Cagle* made the new rule on intent somewhat fuzzier than the old one. *McClure* now makes the rule almost metaphysical.

Before *Webster*, *Cagle*, and *McClure* a careful analysis of intent

62. *Id.*

63. *Id.* at 796, 581 S.W.2d at 552.

64. *Id.* at 795, 581 S.W.2d at 551-52.

65. 228 Ark. 150, 306 S.W.2d 104 (1957).

66. 238 Ark. 561, 383 S.W.2d 99 (1964), also discussed at footnote 15.

67. 265 Ark. 792, 796-97, 581 S.W.2d 550, 552 (1979).

would have relied on *Garvin v. Linton*,⁶⁸ confirmed and quoted as recently as 1973 in *Davidson v. Commercial Credit Equipment Corp.*⁶⁹ Both of these latter cases are cited in *McClure*.⁷⁰ The *Davidson* case reviews a few other aspects of the law of intent and deserves some attention. A quote sets the stage:

We agree with appellant that one cannot purge a usurious contract by a retroactive correction or a subsequent disclaimer. We also agree that the validity of a contract attacked for usury does not turn upon the question of whether the alleged usurer has a specific intent to violate the usury laws. The intent required is an intent to receive or reserve a rate of interest that proves to be usurious. Still, we have long recognized that an honest error of calculation will not render a contract usurious.⁷¹

The *Davidson* court upheld a chancellor's finding of no usury, even though the lender received under the contract an extra three or four dollars on a \$20,000 loan, because the overcharge had been made by error.⁷²

Even before *Webster* and *Cagle*, all mistakes did not suffice to excuse usury. If the mistake were one of law, and not one of fact, there could be no avoidance of usury.⁷³ This rule did not appear to hold when the lender's mistake of law was induced by fraud on the part of the borrower.⁷⁴

It is important to note that, under earlier cases, the intent required was not necessarily the intent to violate the law, but rather the intent to take an amount of money as interest or for the forbearance of collecting a debt which, if calculated properly, amounted to more than ten percent per annum. A clear judicial statement of this distinction appears in *Perry v. Shelby*:⁷⁵ "While it is not necessary that both parties be cognizant of the fact or facts constituting usury, it is necessary that the lender have an intention to charge a usurious

68. 62 Ark. 370, 35 S.W. 430 (1896).

69. 255 Ark. 127, 499 S.W.2d 68 (1973).

70. *First American Nat'l Bank of Nashville, Tenn. v. McClure Const. Co.*, 265 Ark. 792, 795, 581 S.W.2d 550, 552 (1979).

71. 255 Ark. 127, 129, 499 S.W.2d 68, 69 (1973).

72. *Id.* at 132, 499 S.W.2d at 71.

73. *First Nat'l Bank v. Thompson*, 249 Ark. 972, 977, 463 S.W.2d 87, 89 (1971) (citing *Ford Motor Credit Co. v. Catalani*, 238 Ark. 561, 383 S.W.2d 99 (1964); *Holland v. C. T. Doan Buick Co.*, 228 Ark. 340, 307 S.W.2d 538 (1957); *Brooks v. Burgess*, 228 Ark. 150, 306 S.W.2d 104 (1957)).

74. *Turney v. Roberts*, 255 Ark. 503, 501 S.W.2d 601 (1973); *Perry v. Shelby*, 196 Ark. 541, 118 S.W.2d 849 (1938).

75. 196 Ark. 541, 118 S.W.2d 849 (1938).

rate of interest or be cognizant of the fact or facts which constitute usury."⁷⁶

In ferreting out intent, previous cases appear to rely heavily on the following:

(1) the level of sophistication of the parties involved;⁷⁷

(2) the obviousness of overcharges, as in *Wilson v. Whitworth*,⁷⁸ in which the court, commenting on an effective seventy percent rate of interest disguised as a charge for insurance, quoted Lord Mansfield: "[I]t is impossible to wink so hard as not to see;"⁷⁹

(3) the care with which documents are drawn. Blank contracts are very dangerous for lenders to use.⁸⁰ It is equally dangerous for a lender to fail to explain the purpose of extra charges.⁸¹ This rule is so strong that it stands as a minor exception to the general rule that "[U]sury will not be presumed, imputed or inferred where an opposite result can be reached."⁸² The exception provides that any such unexplained extra charges will be presumed to be interest until proved to be something else;

(4) the involvement of the borrower in creating the deal and the voluntariness of his actions;⁸³

(5) the credibility of the witnesses, especially with respect to whether the lender tried to comply with the law;⁸⁴

(6) the weight and clarity of evidence;⁸⁵ and

(7) the general circumstances of the loan.⁸⁶

76. *Id.* at 546, 118 S.W.2d at 851 (emphasis added).

77. *Turney v. Roberts*, 255 Ark. 503, 501 S.W.2d 601 (1973); *Ragge v. Bryan*, 249 Ark. 164, 458 S.W.2d 403 (1970); *Perry v. Shelby*, 196 Ark. 541, 118 S.W.2d 849 (1938).

78. 197 Ark. 675, 125 S.W.2d 112 (1939).

79. *Id.* at 679, 125 S.W.2d at 114.

80. *Universal C.I.T. Corp. v. Hudgens*, 234 Ark. 1127, 356 S.W.2d 658 (1962); *Clem v. Nelson*, 230 Ark. 296, 322 S.W.2d 448 (1959); *Thompson v. Murdock Acceptance Corp.*, 223 Ark. 483, 267 S.W.2d 11 (1954).

81. *United-Bilt Homes, Inc. v. Teague*, 245 Ark. 132, 432 S.W.2d 1 (1968).

82. *Hayes v. First National Bank of Memphis*, 256 Ark. 328, 331, 507 S.W.2d 701, 703 (1974).

83. *Turney v. Roberts*, 255 Ark. 503, 501 S.W.2d 601 (1973); *Green v. Mid-State Homes, Inc.*, 245 Ark. 866, 435 S.W.2d 436 (1968); *Perry v. Shelby*, 196 Ark. 541, 118 S.W.2d 849 (1938).

84. *Brown v. Central Ark. Prod. Credit Ass'n*, 256 Ark. 804, 510 S.W.2d 571 (1974); *Davidson v. Commercial Credit Equip. Corp.*, 255 Ark. 127, 499 S.W.2d 68 (1973); *Redbarn Chemicals, Inc. v. Bradshaw*, 254 Ark. 557, 494 S.W.2d 720 (1973).

85. *Davidson v. Commercial Credit Equip. Corp.*, 255 Ark. 127, 499 S.W.2d 68 (1973). See also *Brown v. Central Ark. Prod. Credit Ass'n*, 256 Ark. 804, 808, 510 S.W.2d 571, 574 (1974), where the court noted that "[w]hen the questioned instrument is not usurious on its face, this intent must be clearly shown;" and *Sosebee v. Boswell*, 242 Ark. 396, 402-12, 414 S.W.2d 380, 384-89 (1967) (Harris, C.J. and Fogleman, J., dissenting).

86. *Brown v. Central Ark. Prod. Credit Ass'n*, 256 Ark. 804, 510 S.W.2d 571 (1974);

We can hope that *Webster*, *Cagle*, and *McClure* do not render this analysis meaningless, but we must admit that they cause us concern. The court will have to revert to careful rather than clever language before we can be sure.

RULE 14 (CREDIT INSURANCE)

*Poole v. Bates*⁸⁷ confirms Rule 14, as perceived, explicitly. *Robinson v. Rebsamen Ford, Inc.*,⁸⁸ confirms the rule but with cautionary teachings. In *Poole* the lender was also the insurance agent. The lender, as agent, received the premium payment for a credit life insurance policy. He paid sixty-five percent of that premium to the insurance carrier, but he either kept or received back thirty-five percent of it as his commission. Since the entire cost of the premium was included in the loan, borrower contended that the interest (here ten percent) on the thirty-five percent of the premium retained by the lender was interest on money which never left the lender's control and, when added to ten percent on the rest of the money, rendered the contract usurious. The Arkansas Supreme Court disagreed for three reasons: First, the borrower requested the insurance; Second, the insurance transaction was *bona fide*, in that the charge for the insurance was not excessive and the benefit that the borrower desired to purchase was received (echoes of *Key v. Worthen Bank*); and Last, there was "no element of fraud, nor duress or compulsion."⁸⁹ "In other words," said the court, "no unlawful charge or profit is involved."⁹⁰ The interest on lawful profit was lawful.

In *Robinson v. Rebsamen Ford, Inc.*,⁹¹ the Arkansas Supreme Court overturned a summary judgment in favor of an installment seller who had also sold credit life insurance to a buyer. The buyer had voluntarily elected to buy the insurance from the seller. The seller received the same thirty-five percent premium commission approved in *Poole*. In *Robinson*, however, the buyer alleged in an affidavit that he could have purchased the insurance for less from any one of eight other insurance companies, and that the seller knew of this fact and failed to tell the buyer. The buyer further alleged that the insurance he bought from the seller was more expensive,

Ragge v. Bryan, 249 Ark. 164, 458 S.W.2d 403 (1970); Textron, Inc. v. Whitener, 249 Ark. 57, 458 S.W.2d 367 (1970); Nineteen Corp. v. Guaranty Financial Corp., 246 Ark. 400, 438 S.W.2d 685 (1969).

87. 257 Ark. 764, 520 S.W.2d 273 (1975).

88. 258 Ark. 935, 530 S.W.2d 660 (1975).

89. *Poole v. Bates*, 257 Ark. 764, 767, 520 S.W.2d 273, 275 (1975).

90. *Id.*

91. 258 Ark. 935, 530 S.W.2d 660 (1975).

by about the value of the seller's thirty-five percent commission, than the insurance he could and would have bought had he known of it. The court said this raised a triable issue of whether "the collateral transaction was a cloak for usury" and cited an Arkansas statute requiring life insurance salesmen to exercise discretion and good faith.⁹²

In view of the earlier decision in *Poole*, the theory seemed to be that the *difference* between the *reasonable* cost of the insurance and the seller's *inflated* cost was interest, not that the commission itself was necessarily interest. The decision in *Robinson*, however, contains the opposite inference.⁹³ Essentially identical fact situations in *Poole* and *Robinson*, even down to the borrower's requesting the insurance, were distinguished by the lender's intent and good faith; by the relationship of extraneous facts to the facts of the case; and by differing approaches to commissions which are difficult to reconcile objectively.

Ford Motor Credit Co. v. N. B. Yarbrough,⁹⁴ requires that the earlier case of *Foster v. Universal C.I.T. Corp.*,⁹⁵ cited in *Usury in Arkansas*, be re-examined and greater significance attached to its teachings. The "seeds of usury" doctrine set forth in *Foster* has been applied primarily in credit insurance cases.⁹⁶ In both *Foster* and *Yarbrough* the lenders sold insurance as part of a single transaction, to insure that all money was advanced at a single time under a single contract. The financing contracts, under which both auto sales and purchases of insurance were financed, provided that any refund of insurance premiums would be applied to the *last-maturing* installment. When the refunds occurred, according to the court, they should have been applied to the *then-outstanding* principal, with interest adjusted accordingly. To hold the refunds until the final payment, while charging interest on the full amount originally disbursed, resulted in actual interest exceeding ten percent. The refund of the insurance premium, oddly enough, caused the seeds of usury to ripen into illegality.

If *Foster* did not, *Yarbrough* should finally end the practice of financing a sale and an insurance premium together, unless the insurance premium is irrevocably paid to a third party without chance of refund into the dealer's hands. Apparently it would be

92. *Id.* at 939, 530 S.W.2d at 662 (citing ARK. STAT. ANN. § 66-3029 (Supp. 1973)).

93. *Id.* at 938, 530 S.W.2d at 662.

94. 263 Ark. 610, 567 S.W.2d 96 (1978).

95. 231 Ark. 230, 330 S.W.2d 288 (1959).

96. A contract contains the "seeds of usury" when, by its terms, it includes a contingency the happening of which will render the contract usurious.

safer to handle the sale and the insurance policy at separate desks with separate financing contracts. The customer could be told that the sale would be completed upon his purchase of insurance either at the second desk or any other place of his choosing. The risk of usury is far greater than the risk that many customers would either walk out or buy their insurance elsewhere.

ADDED RULE 16 (DISBURSEMENT)

This rule rests on two old cases, *Matthews v. Georgia State Savings Association*⁹⁷ and *McDougall v. Hachmeister*.⁹⁸ In *Matthews* the borrower executed a bond and mortgage on May 21, 1915, with the bond calling for interest from that day. The borrower, however, did not receive his funds from the lender until June 9, 1915. The Arkansas Supreme Court found the transaction free of usury, citing, among other reasons, the following:

[T]he circumstances of the loan show good faith on the part of the association. It is evident that the delay was unavoidably incident to the completion of the transaction and that there was no intent on the part of the association to charge usurious rate of interest.[sic] This is shown by the circumstances attending the consummation of the loan.⁹⁹

The *Matthews* court also found that, by calculating the payments a certain way, the lender could in effect avoid charging more than ten percent interest.¹⁰⁰ This reasoning is not persuasive because the instrument sued upon specified the method of calculation, stating how much of each payment was to be apportioned to interest. Under the terms of the instrument itself more than ten percent was collected.

*McDougall v. Hachmeister*¹⁰¹ contained no finding that the interest could have been calculated to reduce it below ten percent. In *McDougall* the court clearly allowed interest to be charged from May 23, 1921, even though a major portion of the money was not disbursed until July 1, 1921, (a small portion had been disbursed earlier on June 3, 1921). The court dismissed this problem, citing *Matthews* as follows:

(1) There was a delay in paying the money to appellants after the execution of the instruments, but it was caused by a defect in the

97. 132 Ark. 219, 200 S.W. 130 (1918).

98. 184 Ark. 28, 41 S.W.2d 1088 (1931).

99. *Matthews v. Georgia State Sav. Ass'n*, 132 Ark. 219, 226, 200 S.W. 130, 132 (1918).

100. *Id.* at 227, 200 S.W. at 132.

101. 184 Ark. 28, 41 S.W.2d 1088 (1931).

abstract of title to the land, which appellants agreed to furnish. The delay after the defects were corrected was not unreasonable, but, on the contrary, the transaction was wound up expeditiously. There is nothing in the record to indicate that the delay was a subterfuge resorted to in order to obtain more than 10 per cent per annum for the use of the money. This court said in the case of *Matthews v. Georgia State Building & Loan Assn.*, 132 Ark. 220, 200 S.W. 130, 21 A.L.R. 789, that "a contract is not usurious when the parties acted in good faith, where 10 per cent interest is charged, where the agreement was dated May 21, 1915, but was not closed and the money delivered until June 9, 1915." As the delay was not occasioned by the fault or bad faith on the part of appellees, the principal must be regarded as received by appellants on the date of the contract in determining whether same is usurious.¹⁰²

The *Matthews-McDougall* rule is Arkansas law.

It is interesting to note that if a loan has not been entirely disbursed, this does not necessarily create usury problems for lenders charging ten percent. Additionally, when a loan has been fully disbursed, this does assist lenders trying to fend off usury allegations based on collateral agreements.¹⁰³

Reliance on these two cases requires careful analysis. *Matthews* was partially overruled on other grounds by the Arkansas Supreme Court in *Winston v. Personal Finance Company*.¹⁰⁴ Later, however, the court clearly implied that both *Matthews* and *McDougall* remain good law by distinguishing them in *First National Bank v. Thompson*.¹⁰⁵ *McDougall* has been cited often in later cases.

The recent case of *McCoy Farms, Inc. v. J & M McKee*,¹⁰⁶ may also support this rule, although the case mentioned neither *Matthews* nor *McDougall*. *McCoy Farms* may not be a usury case at all, but rather a procedural case explaining the meaning of specific performance and the effect of settlements. In *McCoy Farms*, as a result of a trial settlement, a note dated February 1, 1976, was executed August 30, 1976. The note was due February 1, 1977, at eight and one-half percent interest. If the interest due on February 1, 1977, had been collected on money outstanding only since August 30, 1977, the return would have been usurious. The Arkansas Supreme Court found that the circumstances of settlement showed

102. *Id.* at 32, 41 S.W.2d at 1090.

103. See discussion with reference to Rule 7 (Computational Devices: Discounting, Points, Allocating Payments), p. 326-27 *supra*.

104. 220 Ark. 580, 249 S.W.2d 315 (1952).

105. 249 Ark. 972, 463 S.W.2d 87 (1971).

106. 263 Ark. 20, 563 S.W.2d 409 (1978).

clearly that the note should be construed to have been outstanding since February 1, 1976. The facts are highly unusual, but the sentiments, based primarily on cases from other jurisdictions, conform entirely to the rule of *Matthews* and *McDougall*.

ADDED RULE 17 (UNCERTAIN RATES)

Foster v. Universal C.I.T. Corp.,¹⁰⁷ discussed with reference to Rule 14 in this article, held the seeds of Added Rule 17. The doctrine did not fructify, however, until 1978 with the decision in *Ryder Truck Rental v. Kramer*.¹⁰⁸ In *Kramer*, the contract set a variable rate, one and three-quarters percent above Boston prime.¹⁰⁹ At the time of the contract's execution, the effective rate was well below ten percent. In a few months the Boston prime rate rocketed to more than ten percent and the obligation became usurious in Arkansas. The Arkansas Supreme Court affirmed summary judgment for defendant borrower. The court disregarded (over disclaimers to the contrary) intent of the parties and brushed aside a sophisticated theory calling for an analysis of return only over the entire life of the loan. The overall return on the loan could have been lower than ten percent if Boston prime had decreased before the final due date of the loan but after the filing of the complaint. If the variable rate contract had called for interest at one and three-quarters percent above Boston prime but not more than ten percent per annum in any given month or over the life of the loan, it apparently would have worked. The decision in *Kramer* requires both a life-of-the-loan and a periodic ceiling to avoid usury. In that way, *Kramer* is consistent with *Redbarn Chemicals, Inc. v. Bradshaw*,¹¹⁰ in which a single month's excessive interest rendered void a continuing contractual relationship.

Both *Kramer* and *Redbarn Chemicals, Inc.* elicited extensive dissenting opinions. The dissents demonstrate that the Arkansas Supreme Court is not immune to the emotional divisiveness the usury question tends to cause generally in Arkansas, but they do not give lenders much on which to rely. Despite such dissents the law has been relatively consistent since 1952. If the terms of the contract agreed to by the parties call for a usurious rate of interest, or if the

107. 231 Ark. 230, 330 S.W.2d 288 (1959).

108. 263 Ark. 169, 563 S.W.2d 451 (1978).

109. *Id.* at 172, 563 S.W.2d at 453. "Boston prime" means that rate which the major banks in Boston are charging on loans to their best customers, which rate rises and falls at irregular intervals.

110. 254 Ark. 557, 494 S.W.2d 720 (1973).

lender willingly receives what proves to be in fact a usurious rate, the contract will be voided. In deciding whether either has happened, the court will be conservative and will be intentionally blind to the economic impact of the law on the state's economy and on the parties litigant. As much and as strenuously as the authors of this article disagree with the policy of the law, they cannot and do not disagree with the Arkansas Supreme Court majority's decision to apply the law as it reads, so long as the law reads as it does.

Procedural matters

Most procedural matters relative to usury cases remain unchanged over the last seven years.¹¹¹ The burden of proof, namely the burden of going forward with the evidence in the first instance, rests with the party alleging usury.¹¹² Proof of usury must be clear and convincing. A mere preponderance of the evidence is insufficient because the intention to charge a usurious rate of interest will never be presumed, imputed, or inferred where an opposite result can be reached.¹¹³ This rule, however, does not help a careless lender who leaves loan documents blank. The borrower and the court may presume that unidentified extra charges are really interest.¹¹⁴ In matters of interpretation, a court will consider all attendant circumstances to determine the meaning of an allegedly usurious contract.¹¹⁵

Drafting errors which make a contract usurious on its face when it is not usurious in fact do not amount to usury. In *Parks v. E.N. Beard Hardwood Lumber, Inc.*,¹¹⁶ the seller under an open account calling for an annual interest of twelve percent, over a period of time, consistently billed and collected less than ten percent annual interest. The court found no usury, agreeing with the trial court that the interest charged as a matter of practice and not the interest called for was the critical focus under the usury law. This case, however, adds to the questions analyzed under the restatement of Rule 12.¹¹⁷

111. *Usury in Ark.*, *supra* note 1, at 265 nn.6(1) and 6(2), 266 nn.6(3)-6(11).

112. *Key v. Worthen Bank & Trust Co., N.A.*, 260 Ark. 725, 543 S.W.2d 496 (1976); *Poole v. Bates*, 257 Ark. 764, 520 S.W.2d 273 (1975); *Brown v. Central Ark. Prod. Credit Ass'n*, 256 Ark. 804, 510 S.W.2d 571 (1974); *Hayes v. First Nat'l Bank of Memphis*, 256 Ark. 328, 507 S.W.2d 701 (1974).

113. *Brown v. Central Ark. Prod. Credit Ass'n*, 256 Ark. 804, 510 S.W.2d 571 (1974).

114. *Usury in Ark.*, *supra* note 1 at 265, n.6(2).

115. *Brown v. Central Ark. Prod. Credit Ass'n*, 256 Ark. 804, 510 S.W.2d 571 (1974); *Redbarn Chemicals, Inc. v. Bradshaw*, 254 Ark. 557, 494 S.W.2d 720 (1973).

116. 263 Ark. 501, 565 S.W.2d 615 (1978).

117. See discussion of Rule 12 *supra* at 337.

In usury cases, the Arkansas courts will admit parol evidence. *Usury in Arkansas* indicated that this rule extended only to parol evidence tending to show usury.¹¹⁸ A careful analysis of the dictum in *Textron, Inc. v. Whitener*,¹¹⁹ shows that such evidence is admissible for broader purposes. The trial court in *Textron* had admitted parol evidence to show that a contract usurious on its face was not actually a violation of the usury law. Although the courts, both trial and appellate, found usury in *Textron*, the Arkansas Supreme Court said of the parol evidence question: "We cannot say that the trial court ignored that [parol] evidence simply because he ultimately found in his memorandum opinion that the promissory note sued upon was usurious."¹²⁰ Appellant alleged that the trial court had erred in failing to admit parol evidence. The Arkansas Supreme Court found that such parol evidence had been admitted and therefore refused to reverse on the alleged error.

IV. NEW AREAS

A. Are Leases Loans?

Usury in Arkansas suggested leases might be loans, not because of any usury cases, but because of *Sawyer v. Pioneer Leasing Corp.*,¹²¹ a warranty case holding an abandonment lease "analogous to a sale."¹²² In *Sawyer* the Arkansas Supreme Court's warning is clear:

[A]greements of this nature will be examined closely by this court. It is possible that similar agreements could be used to cloak usurious charges, i.e., a transaction which was actually a sale could be set up as a lease in order to enable charges to be made that would, under a credit sale, constitute usury.¹²³

The original article suggested that no careful leasing company should risk operating in Arkansas with abandonment leases calling for more than a ten percent return. Itek Leasing Corporation, apparently of Rochester, New York, neither heeded the warning nor took that advice. It should have. In *Bell v. Itek Leasing Corp.*,¹²⁴ the Arkansas Supreme Court overturned the trial court's ruling that a

118. *Usury in Ark.*, *supra* note 1, at 266.

119. 249 Ark. 57, 458 S.W.2d 367 (1970).

120. *Id.* at 59, 458 S.W.2d at 368. See also *Standard Leasing Corp. v. Schmidt Aviation, Inc.*, 264 Ark. 851, 576 S.W.2d 181 (1979).

121. 244 Ark. 943, 428 S.W.2d 46 (1968).

122. *Id.* at 954, 428 S.W.2d at 52; *supra* note 2 at 307-08.

123. *Sawyer v. Pioneer Leasing Corp.*, 244 Ark. 943, 958, 428 S.W.2d 46, 54 (1968).

124. 262 Ark. 22, 555 S.W.2d 1 (1977).

lease was not a credit sale. The court found the lease to be a sale due to "five important points:"¹²⁵ (1) Defendant was a finance company, not a manufacturer of the leased equipment; (2) All risk of loss was on lessee; (3) Default provisions made the lease like a conditional sale; (4) The lease called for a UCC financing statement, and one was signed; and (5) The lease called for purchase upon termination of the lease at ten percent of the original contract price.

The case leaves many questions unanswered. Would a change in one, two, or more of the above provisions make any difference? Can the presence of any one of the provisions render a lease a loan? A simple majority? Are some of the factors more important than others? We don't know. Given the history of litigants' imagination under Arkansas' usury law and the occasional carelessness of lenders in this area, we probably will find out over the next few years. The only prudent course in any lease with an option-to-buy arrangement, either explicit or implicit,¹²⁶ is to insure that the overall return to the lessor does not exceed the stated original cash price plus ten percent per annum on the outstanding balance of the total unpaid purchase price. The court, however, gave no real guidance to the lessor in making such calculations.

B. Federal Diversions.

When state law doesn't work, or when it works too well, lawyers routinely try to find a federal solution. With Arkansas usury law, four distinct federal diversions must be noted.

i. National Banks

National banks have been subject, from time to time, to the state imposed ceiling on interest rates, but never to the state penalties. This anomalous situation grows from title 12, sections 85 and 86 of the United States Code. Section 85 provides an interest ceiling equivalent to the state ceiling *or* one percent higher than the federal discount rate,¹²⁷ or, for business and agricultural loans in excess of \$25,000.00, five percent above the federal discount rate, whichever is higher. Section 86 then prescribes the penalty for violation of section 85. The penalty is generally loss of interest only.

125. *Id.* at 24-26, 555 S.W.2d at 2-3.

126. *Standard Leasing Corp. v. Schmidt Aviation, Inc.*, 264 Ark. 851, 854-55, 576 S.W.2d 181, 183-84 (1979).

127. *See* note 9, *supra*.

National banks in Arkansas, relying on title 12, section 86 of the United States Code and faced with the staggeringly high discount rates of 1978 and 1979, have charged rates in excess of ten percent, generally ten and one-half percent. To a degree, this has ameliorated the economic effects of Arkansas' usury law.

ii. *The "Brock Bill" and its Arkansas step-child*

For a brief time, the usury limit for FDIC-insured state banks also exceeded ten percent. The "Brock Bill"¹²⁸ allowed such institutions to charge five percent above the federal discount rate. The law was in effect from October 29, 1974, until it expired on July 1, 1977. It was considered a temporary emergency measure and applied in practice to only three states. For business or agricultural loans in excess of \$25,000.00 processed during this period, the law's effect was monumental, allowing loans to be made at thirteen percent.

During the life of the Brock Bill, Senator Brock's home state of Tennessee took steps to remove its own restrictive usury law limits by referendum. This happened against the backdrop of an Arkansas referendum in 1974 in which the Arkansas usury law was specifically retained. Under these circumstances, Congress was slow to bail out Arkansas lenders again.

The Brock Bill was ruled to be constitutional in concept, before its passage, by Arkansas' Attorney General.¹²⁹ As noted in Section I, it was held constitutional in fact in *Stephens Security Bank v. Eppivic Corp.*¹³⁰ Because of its close parallel with title 12, sections 85 and 86 of the United States Code, and the legislative intent to provide more equal treatment for state and national institutions, it is clear that the Brock Bill preempted both the state ceiling and the state penalty for usury.¹³¹

A close approximation of the Brock Bill was introduced in Congress by the Arkansas delegation (with apparent mixed feelings) in early 1979.¹³² It provided for expiration on January 1, 1981—two months after the vote on the Constitution of 1980 in Arkansas, apparently the last state where such congressional intervention makes any difference.

128. 12 U.S.C. § 1831(a).

129. Opinion 74-94, Arkansas Attorney General, July 22, 1974.

130. 411 F. Supp. 61 (W.D. Ark. 1976), *aff'd*, 553 F.2d 102 (8th Cir. 1977).

131. *First Nat'l Bank v. Nowlin*, 509 F.2d 872, 881 (8th Cir. 1975).

132. *Arkansas Gazette*, February 24, 1979; H.R. 2515, 91st Cong., First Session.

iii. *FHA-VA loans*

FHA and VA loans raise other questions, not all of which can be answered. The federal government sets the permissible maximum interest rate a lender may charge on such loans. It further sets the permissible maximum discount, and it collects a fee for the insurance of the loans, computed as a percentage of the outstanding balance.

The *Stephens Security Bank*¹³³ and *Nowlin*¹³⁴ cases may be applicable to this analysis, except that the Brock Bill specifically purported to pre-empt state law, while the applicable federal legislation, particularly in the case of FHA loans, does not.¹³⁵ If there is no federal preemption, is mortgage insurance (public or private) interest? The question is more than academic if the stated rate is nine and three-quarters percent and the insurance premium is one-half of one percent. Essentially, mortgage insurance is a fee for a guaranty, paid to a third party, which was held not to constitute interest in *Leonhard v. Flood*.¹³⁶ The following language in *Lockhart v. G.M.A.C.*,¹³⁷ which dealt with the purchase of single interest automobile casualty insurance upon debtor's failure to maintain insurance, may also be helpful:

Not every charge made to the borrower which benefits the lender will render a transaction usurious simply because the interest rate is a full 10%, particularly if the charge is reasonable, is made in good faith and is reimbursement for a payment to a third person for something appropriate in establishing or protecting of the lender's security. For instance, we have recognized the propriety of such charges as property inspection fees, expense of an abstract of title, title examination fees, insurance premiums paid a third party, recording fees, expense of obtaining a release of a prior lien, and title insurance premiums.¹³⁸

Our neighboring state of Tennessee as early as 1960 determined that such charges were not interest, but were instead "an expense incident to the necessity of furnishing the lender satisfactory secu-

133. *Stephens Sec. Bank v. Eppivic Corp.*, 411 F. Supp. 61 (W.D. Ark. 1976), *aff'd*, 553 F.2d 102 (8th Cir. 1977).

134. *First Nat'l Bank v. Nowlin*, 509 F.2d 872 (8th Cir. 1975).

135. 12 U.S.C. §1701(1).

136. 68 Ark. 162, 165, 56 S.W. 781, 782 (1900).

137. 252 Ark. 878, 880, 481 S.W.2d 350, 351 (1972).

138. *Id.* at 880, 481 S.W.2d at 351; *Ragge v. Bryan*, 249 Ark. 164, 458 S.W.2d 403 (1970); *United-Bilt Homes, Inc. v. Teague*, 245 Ark. 132, 432 S.W.2d 1 (1968); *Harris v. Guaranty Financial Corp.*, 244 Ark. 218, 424 S.W.2d 355 (1968); *Winston v. Personal Finance Co. of Pine Bluff*, 220 Ark. 580, 249 S.W.2d 315 (1952).

rity for the repayment of the money loaned for that purpose."¹³⁹

We believe the Arkansas Supreme Court will follow the rationale of *Leonhard*, *Lockhart* and the Tennessee Supreme Court and will consider these premiums in the category of other third party payments and, therefore, not interest. The court, however, does not often consider the usury law of other states in reaching its decisions and has a way of finding usury in unusual places. We do not, therefore, set forth our belief as the law.

iv. Is our constitution unconstitutional?

A totally new kind of federal question emerged in November, 1978, in *Quinn-Moore v. Adams*,¹⁴⁰ in which the state's right to set interest ceilings was challenged under the United States Constitution. Taking their cue from a California state court case decided at the trial level earlier in 1978,¹⁴¹ and currently on appeal, the *Quinn-Moore* plaintiffs sought a declaratory judgment voiding the ten percent constitutional limit as a burden on interstate commerce.¹⁴² Also invoked were the Supremacy Clause,¹⁴³ and the Due Process, Equal Protection, and Privileges and Immunities Clauses of the Fourteenth Amendment. The case has attracted as intervenors on both sides of the issue lenders and consumer groups and apparently presupposes an appeal to the United States Supreme Court whatever the Arkansas Supreme Court holds.¹⁴⁴

VI. SOME CONCLUSIONS AND A PROPOSAL

The developments in the Arkansas Supreme Court's expressed attitudes toward usury and usurers, as opposed to the developments in the money market, in the preceding seven years have been predictable and unexceptional. The virtual demise of any meaningful requirement that there be a bilateral agreement to pay and collect excessive interest may be conceptually troublesome. The *Cagle* and *Webster* cases, however, are at least consistent in spirit with the court's prior decisions.

We really didn't need *Bell v. Itek Leasing* to tell us that loans

139. *Silver Homes, Inc. v. Marx & Bendorf, Inc.*, 206 Tenn. 361, 368, 333 S.W.2d 810, 813 (1960).

140. No. 78-6045 (Pulaski Co. Cir. Nov. 1978).

141. *Committee Against Unfair Interest Limitations v. State of California*, No. C-158-433 (Los Angeles Co. Sup. 1978).

142. U.S. CONST. art. 1, § 8(3).

143. U.S. CONST. art. 6, § 2.

144. The case is scheduled to be tried in the fall of 1979.

disguised as leases would not pass muster. If *Mack Trucks* seems over-broad in its condemnation of certain rather common and economically justifiable lending practices, no one can say that the Arkansas Supreme Court ever hinted that those practices were acceptable. The court has always insisted that it would not take economics into consideration and that the Arkansas Constitution means exactly what it says. The case law of the last seven years merely serves to confirm those past declarations.

As we have indicated before, the effects of the constitutional provision have not really changed either. Like the court's opinions, these effects simply have become more clearly delineated. Consumer goods continue to cost more in Arkansas because the cash customer is forced to help pay for the cost of credit.¹⁴⁵ Loans which, because of the risk involved, call for a high rate of return, simply aren't made.¹⁴⁶ Money which can earn a higher return elsewhere goes there, instead of into the Arkansas housing market or into expansion of Arkansas businesses.¹⁴⁷ Because interest rates on savings are largely controlled by the "spread" between those rates and the rates charged on loans by the same institution, even Arkansas savers are penalized by the limitation. Finally, the provision has recently created a disparity between the rates chargeable by national banks and by state banks on most loans.

In return for these negative effects, Arkansas borrowers are provided with loan funds, if they can get them, at lower rates than borrowers in surrounding states. Arkansas borrowers also do not have to worry about figuring the rate allowed on a given loan—that has become increasingly clear.

But shouldn't there be *some* limit to protect borrowers who need it, and some way, constitutional or otherwise, to keep interest rates within reasonable limits? Although we might be inclined to choose "otherwise," we believe any realistic proposal for reform must at least begin with the Arkansas Constitution, and include specific protections set forth therein, to be acceptable to the Arkansas electorate. Any such proposal must also be reasonably brief and easy to understand. And it must assure meaningful protection.

With these requirements in mind, as well as certain similar proposals under consideration by the Constitutional Convention as of this writing, we propose the following amended article:

145. Interview with Dr. Charles Venus, consulting economist in Little Rock, Ark. (February, 1979).

146. *Id.*

147. *Id.*

Section 1. All contracts for a greater rate of interest than ten percent per annum shall be void, as to principal and interest, and the General Assembly shall prohibit the same by law, except as otherwise provided herein;

Section 2. All contracts which state no rate of interest shall be at six percent per annum;

Section 3. Except as the General Assembly may otherwise provide, the defense of usury shall not be available to a corporation or to a limited partnership;

Section 4. The General Assembly may provide by law that contracts for loans of money by financial institutions licensed as lenders by the State of Arkansas; that loans of money by financial institutions the deposits of which are insured by an agency of the United States government; and that loans of money the repayment of which is guaranteed or insured in whole or in part by an agency of the United States government may bear interest at a rate not exceeding that allowed by the appropriate laws and regulations of the United States with respect to such loans or contracts or, in the absence of such laws and regulations, at a rate established by the General Assembly.

Section 5. The General Assembly may provide by law what charges shall and what charges shall not be considered as interest within the meaning of this article.

By tracking current constitutional language, we preserve the value of case law and policy built up under the 1874 Constitution.

Essentially, Section 3 eliminates many business loans from the prohibition, while retaining it as to sole proprietors, normal partnerships and unincorporated farmers. Sophisticated investors often use limited partnerships. Corporations also imply the idea of some financial sophistication. The underlying theory here conforms to that developed by the Arkansas Supreme Court in the area of fraud and intent. We will protect the less sophisticated borrower, but we will allow those who know what they are doing to take risks they deem reasonable.

Section 4 allows banks, savings and loans and FHA-VA lenders to follow the national money market. Mortgage bankers are licensed and regulated by the State, hence, the General Assembly would set the maximum rate for their non-FHA-VA loans. Licensed lenders are not loan sharks. The state can deal with them without resorting to a usury bludgeon. Under Section 5, the General Assembly could also make policy decisions about genuine commitment fees, dis-

counts, and consumer credit costs.¹⁴⁸

The severe penalty for charging excessive interest remains the same. By leaving the penalty, we show we still mean business. The proposal also makes what the authors consider a reasonable compromise between seeking to inject a comprehensive, statute-like scheme into the constitution and giving the General Assembly untrammelled discretion in the area. Decisions of the last seven years evidence no inclination on the part of the Arkansas Supreme Court to compromise on the constitutional limit. The protection is there, even if it hurts more than it helps.

A few conceptual loose-ends regarding usury remain unattended to. The Arkansas Supreme Court has yet to deal with a genuine commitment fee or an actuarially defensible discount, *Mack Trucks* notwithstanding. Some questions on leasing remain unanswered. And the role of intent in the law has lost rather than gained clarity in recent decisions. But it is difficult to conceive of decisions in these areas which would represent a significant departure from the pattern already established by the Arkansas Supreme Court, or which would have any substantial effect on Arkansas' economy. Any significant changes in the law of usury in Arkansas can only come from the Constitutional Convention and the electorate.

148. The basic text of this article was already on its way to the printer when the Arkansas Constitutional Convention completed its proposed draft of the new constitution. Unless altered when the Convention reconvenes briefly in 1980, apparently the draft will give the electorate a separate vote on the usury article, choosing between the present article and a new article essentially tying the Arkansas rate to the federal discount rate.

This method is, to some extent, like the constitutional mechanism for setting salaries of constitutional officers—the idea apparently was to set the rate as high as it could reasonably be expected to go, and high enough so that one could quit worrying about discounts, points, commitment fees, etc.

This approach plainly begs the question and, further, pegs the rate to a standard which may be re-defined or even eliminated entirely by Congress—the discount rate on 90-day commercial paper in our federal reserve district.

While the Convention's proposal (if adopted) would in fact offer some relief, we would strongly urge the Convention to reconsider its work to see if it has not placed too high a value on absolute simplicity. While not advancing our own proposal as a panacea, we believe the voters could in fact make an intelligent decision on a proposed article which specifically addressed such problems as (a) differentiating between different types of borrowers; (b) uncertainty as to the meaning or effect of discounts, commitment fees and mortgage insurance; and (c) allowing regulated lenders to operate within the framework of their own place in the governmental and economic scheme, rather than in accordance with an arbitrary standard.

We also believe such an approach would be good politics, as it would tend to banish the spectre of an across-the-board increase in interest rates to the highest level permitted by the article for all loans. Winning voter approval for a new usury article is not going to be easy, and we simply suggest that the Convention consider whether a finer tuned article might be easier to sell in fact, as well as more functional in operation.