



Arkansans Against Abusive Payday Lending

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PAYDAY LENDING IN ARKANSAS – LEGAL VERSION

In the mid-1990's businesses offering small, high-interest loans to consumers began to proliferate across the United States. These businesses became known as "payday loan" stores because the duration of the loans was typically tied to the borrower's pay period. A typical loan is about \$350 with an annual percentage rate (APR) from 390% to 780%. These high-interest, short term loans (typically two weeks to one month) require the full balance to be repaid on the borrower's next payday. As collateral, the payday lender holds the borrower's personal check or extracts an agreement authorizing electronic debiting (ACH) from the borrower's bank account.¹

Payday lending had a major hurdle to overcome in Arkansas, the Arkansas Constitution's prohibition against usury. The Arkansas Constitution, Article 19, Section 13 places a limit on the maximum interest rate that may be charged a borrower in a lending transaction:

(a) General Loans:

(i) The maximum lawful rate of interest on any contract entered into after the effective date hereof shall not exceed five percent (5%) per annum above the Federal Reserve Discount Rate at the time of the contract.

(b) Consumer Loans and Credit Sales: All contracts for consumer loans and credit sales having a greater rate of interest than seventeen percent per annum shall be void as to principal and interest and the General Assembly shall prohibit the same by law.

Ark. Code Ann. §§ 4-57-104, 4-57-105, provides that the parties to any contract shall not agree to the payment of interest exceeding the applicable rate set forth in the Arkansas Constitution, Article 19, § 13. Since payday lenders charge triple digit interest rates, the legality of these business practices has always been in serious doubt, and the numerous lawsuits against them were inevitable.

In an attempt to obtain legal cover from the usury prohibition found in the Arkansas Constitution, the payday loan industry was able to convince the Arkansas legislature to pass Act 1216 of 1999, the "Check-Cashers Act," codified at ARK. CODE ANN. § 23-52-100, et seq. The Check-Cashers Act allows for the licensing and regulation of businesses engaged in both payday lending, as well as check cashing, by the Arkansas State Board of Collection Agencies (ASBCA).²

¹Department of Defense Report to Congress On Predatory Lending Practices Directed at Member of the Armed Forces and Their Dependents, August 9, 2006. A copy of the full report is available at: http://www.defenselink.mil/pubs/pdfs/Report_to_Congress_final.pdf

² As a practical matter many payday lenders engage in check cashing, but not all check cashers engage in payday lending.

The Check-Cashers Act describes a typical payday loan called a deferred presentment transaction. A deferred presentment transaction occurs when the borrower writes a present-dated check to the lender for an amount greater than the borrower receives in cash. In return, the lender agrees to hold the check for two weeks to a month. If the borrower does not pay the lender the face amount of the check within the prescribed period, the lender presents the check for payment at the bank.

The legal cover sought by the payday loan industry was codified in ARK. CODE ANN. § 23-52-104(b) of the Check-Cashers Act, which formerly stated:

“The fee, when made and collected, shall not be deemed interest for any purpose of law, and a check-cashing transaction, including one with a deferred presentment option, shall not be and shall not be deemed to be a loan, loan contract, or a contract for the payment of interest notwithstanding any disclosures required by this chapter.”

In 2001, the Arkansas Supreme Court held “that section 23-52-104(b) is an invalid attempt to evade the usury provisions of the Arkansas Constitution.” *Luebbers v. Money Store, Inc.*, 344 Ark. 232, 40 S.W.3d 745 (2001).³ In 2005, the legislature repealed the provision formerly codified at ARK. CODE ANN. § 23-52-104(b) from the Arkansas Code.

Following the *Luebbers* decision, numerous lawsuits, mostly class actions, were filed against payday lenders in Arkansas for violations of the Arkansas Constitution’s prohibition against usury, as well as for violations of the Deceptive Trade Practices Act (DTPA). To the Attorney General’s knowledge no lawsuit against a payday lender for usury has resulted in an opinion adverse to the position outlined in the Attorney General’s Complaint.

A number of these class-action lawsuits against payday loan companies and their owners resulted in appellate rulings. Following decisions at the Circuit Court level, which generally certified class status or found mandatory arbitration clauses contained in the payday loan contracts to be unenforceable, the defendants filed appeals regarding those issues. The Arkansas Supreme Court affirmed the opinions of the Circuit Courts in every case. All of these opinions were adverse to the payday lenders. See *National Cash, Inc. v. Loveless*, 361 Ark. 112, 205 S.W.3d 127 (2005); *Cash In a Flash Check Advance of Arkansas, LLC v. Spencer*, 348 Ark. 459, 74 S.E.3d 600 (2002); *USA Check Cashers of Little Rock, Inc. v. Island*, 349 Ark. 71, 76 S.W.3d 243 (2002); *The Money Place, LLC v. Barnes*, 349 Ark. 411, 78 S.W.3d 714 (2002); *Tay-Tay, Inc., v. Young*, 349 Ark. 675, 80 S.W.3d 365 (2002); *Tay-Tay, Inc. v. Young*, 349 Ark. 369, 78 S.W.3d 721 (2002); *The/FRE, Inc. v. Martin*, 349 Ark. 507, 78 S.W.3d 723 (2002); *F & G Financial Services, Inc. v. Barnes*, 349 Ark. 420, 82 S.W.3d 162 (2002); *The Money Place, LLC v. Barnes*, 349 Ark. 518, 78 S.W.3d 730 (2002); *E-Z Cash Advance, Inc. v. Harris*, 347 Ark. 132, 60 S.W.3d 436 (2001).

Other appellate cases dealt with issues other than class certification or invalid arbitration clauses. See *Ballard v. Martin*, 349 Ark. 564, 79 S.W.3d 838 (2002) (trial court did not abuse its discretion in finding class action settlement fair); *Anderson v. Stewart*, 366 Ark. 203, 234 S.W.3d 295 (2006) (trial court did not error in applying doctrine of ‘piercing the corporate veil’ and holding shareholders in a limited liability company individually liable for usury and Arkansas Deceptive Trade Practices Act).

³ The Court struck down a similar provision that attempted to remove fees from the definition of interest in the Arkansas Installment Loan Law in 1952. *Strickler v. State Auto Finance Co.*, 220 Ark. 565, 249 S.W.2d 307 (1952).

Earlier this year the Arkansas Supreme Court twice had an opportunity to address the legality of payday lending. In two cases, *Arkansas Board of Collection Agencies and Old Republic Surety Company v. McGhee, et al.*, 372 Ark. 136, ___ S.W.3d ___ (2008), and *Staton v Arkansas Board of Collection Agencies and American Manufactures Mutual Insurance Company*, 372 Ark. 387, ___ S.W.3d ___, (2008), the Court was asked to rule on whether surety bonds obtained by payday lenders as part of the licensing requirements under the Arkansas Check-Cashers Act could be used to satisfy judgments for usury violations.

In the first case, Old Republic Surety Company argued that the bond it had issued to a licensed payday lender, before the Luebbers decision, only covered violations of the Check-Cashers Act, not claims for usury. The Court disagreed, “[w]e do not view the Act as affording Old Republic blanket protection for purposes of the 1999 bond. The usury laws of this state, including what constitutes interest or fees, have been part of our constitution, statutory law, and case law for decades...It was incumbent upon Old Republic to know and abide by the clear public policy of this state as expressed by the Arkansas people in the Arkansas Constitution regardless of one legislative act (the Check-Cashers Act) that runs counter to that public policy.” *Old Republic v. McGhee*, 372 Ark. 136, ___ S.W.3d ___. It is important to note that the Court found liability for usury on a bond that was issued even before ARK. CODE ANN. 23-52-104(b) was ruled unconstitutional.

The Supreme Court used a similar analysis in another opinion shortly after the Old Republic decision. *American Manufactures Mutual Insurance Company* was in a nearly identical situation, and like Old Republic, American argued that the bonds issued to the payday lender were only issued to cover losses stemming from violations of the Check-Cashers Act or the Board’s rules and regulations. The Court found that the payday loan company had violated the Board’s regulations by charging usurious rates of interest, specifically, ASBCA Regulation XXI, which prohibits a check casher from engaging in deceptive trade practices. The Court noted its previous rulings in *Old Republic v. McGhee* and *State v. R&A Investments Co.*, 336 Ark. 289, 985 S.W.2d 299 (1999) (holding the practice of charging usurious interest rates was unconscionable and deceptive).⁴ *Staton v. Arkansas Board of Collection Agencies and American Manufactures Mutual Insurance Company*, 372 Ark. 387, ___ S.W.3d ___.

It is clear from the Arkansas Supreme Court’s opinions that the Check-Cashers Act does not, and has never, provided protection to businesses that violate the Arkansas Constitution’s prohibition against usury. It is incumbent upon Payday Lenders in Arkansas to know and abide by the clear public policy of this state as expressed by the Arkansas people in the Arkansas Constitution regardless of the passage of an Act that runs counter to that public policy.

Note: This article is a part of the BRIEF IN SUPPORT OF PLAINTIFF’S RESPONSE TO DEFENDANTS’ MOTION TO DISMISS written by Charles Saunders, Assistant Attorney General in the case of State of Arkansas ex rel. Dustin McDaniel, Attorney General vs. MSC Self Storage, LLC, D/B/A Merrill Check Cashing, MCC Self Storage, LLC, D/B/A Merrill Check Cashing, Raymond Merrill, and J. T. Compton Case No CV 2008-4715 Pulaski County, Arkansas. Arkansans Against Abusive Payday Lending believes this section of the brief to be a very clear and concise explanation of the Payday Lending situation in Arkansas.

⁴ Mid-South Title Loans offered auto title loans at or above 300% per annum. The Court declined to condone such “open, flagrant, and continuous violations of the Arkansas Constitution.” *State of Ark. v R & A Investment.*, 336 Ark. at 295, 785 S.W 2d at 302.
