



Arkansas State Bank Department

Candace A. Franks
Commissioner

Asa Hutchinson
Governor

DATE: December 5, 2017
TO: Chief Executive Officer of the Institution Addressed
FROM: Candace A. Franks, Bank Commissioner
SUBJECT: Legal Lending Limit

Recently, my staff has had conversations with bankers regarding Bankers Healthcare Group and other similarly organized entities ("Seller") who sell loans to Arkansas banks and the calculation of the legal lending limit for these loans. The issue is whether the loans purchased by an Arkansas bank from a Seller should be aggregated and counted toward the legal lending limit for the Seller or should be counted solely toward the primary borrower's legal lending limit.

Under the business model in question, the Seller originates personal consumer loans or business loans where the business owner personally guarantees the loan. The loans are then sold by the Seller to an Arkansas bank. As part of the transaction, the Seller signs the note as an endorser without recourse and expressly transfers all rights to the note to the purchasing Arkansas bank.

Under the Uniform Commercial Code, which is codified under Title 4 of Arkansas Code, an endorser without recourse would not have any liability for a note they endorsed, and arguably, the loan amount should be counted toward the individual borrower's legal lending limit and not the Seller's legal lending limit. However, Arkansas Code § 23-47-501 alters this relationship for the purposes of calculating legal lending limits.

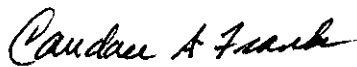
Arkansas Code § 23-47-501(b)(1) states "[o]bligations of a person as endorser or guarantor, accommodation or otherwise, of notes or other obligations shall be included in that person's loan limit." No distinction is made between notes that are endorsed and notes endorsed without recourse. Therefore, under Arkansas Code §23-47-501(b)(1), notes endorsed by the Seller will be aggregated and counted toward the Seller's legal lending limit. There is, however, an exception for consumer loans endorsed without recourse under Arkansas Code § 23-47-501(b)(2)(A) which

states “in the case of obligations on consumer loans which are endorsed without recourse, the twenty percent (20%) limitation shall be applied to each primary debtor, but not to the liability, in such capacity, of the endorser.” Arkansas Code § 23-47-501(b)(2)(B) defines consumer loans as “credit extended to a natural person in which the money is to be used primarily for personal, family, or household purposes.” Any consumer loan falling within this definition that is endorsed by the Seller as being without recourse would not be counted towards the Seller’s legal lending limit but would instead be counted towards the original borrower’s legal lending limit. Commercial loans and consumer loans that have not been endorsed without recourse and sold to an Arkansas bank are aggregated and counted toward Seller’s lending limit under Arkansas law.

If your bank may have purchased loans of this nature, we encourage you to review your loan portfolio and ensure that there are no issues with the legal lending limit for any Seller from whom you have been purchasing loans. Consumer loans that are endorsed without recourse should be counted toward the original borrower’s lending limit while all other types of loans should be aggregated and counted toward the Seller’s lending limit.

If my staff and I may be of any assistance to you regarding this issue, please contact us.

Sincerely,

A handwritten signature in black ink that reads "Candace A. Franks". The signature is written in a cursive, flowing style.

Candace A. Franks
Bank Commissioner

CAF/JA/bm