

STATE OF NORTH CAROLINA

WAKE COUNTY

IN A MATTER
BEFORE THE COMMISSIONER OF BANKS
DOCKET NO. 05:008:CF

IN RE:)	
)	NOTICE OF HEARING
ADVANCE AMERICA, CASH ADVANCE)	AND ORDER FOR
CENTERS OF NORTH CAROLINA, INC.)	A PRE-HEARING CONFERENCE
_____)	

TO: Advance America, Cash Advance Centers of North Carolina, Inc.

c/o National Registered Agents, Inc.
Registered Agent for Advance America, Cash
Advance Centers of North Carolina, Inc.
120 Penmarc Drive
Suite 118
Raleigh, NC 27604

and

c/o William M. Webster, IV,
President and C.E.O.
Advance America, Cash Advance Centers
of North Carolina, Inc.
135 North Church Street
Spartanburg, SC 29306

I. NOTICE OF THE HEARING

You are hereby notified that the Commissioner of Banks for the State of North Carolina, (hereinafter the "Commissioner"), will hold a hearing on April 19, 2005, at 9:30 a.m., or as soon after that hour as the same may be heard, in the manner and for the purposes hereinafter provided.

For the purpose of this Notice of Hearing, Advance America,

Cash Advance Centers of North Carolina, Inc., may be referred to as "Respondent" or "AANC."

II. LOCATION AND TERM OF THE HEARING

The hearing will be held in the Office of the Commissioner of Banks, hereinafter the "OCOB," 316 West Edenton Street, 2nd Floor Hearing Room, Raleigh, North Carolina, on the date and at the time specified above, and will continue from time to time thereafter until the same is fully concluded. If Respondent is not present, a decision will be reached in its absence and Respondent shall be deemed to have waived the right to a hearing.

III. THE HEARING PROCESS

1. The Hearing Procedure.

This is a contested case hearing before the Commissioner pursuant to the authority of Article 3A of Chapter 150B of the General Statutes of North Carolina, and G.S. §§ 53-107.1(c), 53-186, 53-187 and 53-285. Respondent is entitled to be represented by counsel and to present evidence and legal argument. The Attorney General may intervene to participate in the hearing pursuant to G.S. § 114-2.

Respondent is referred to Article 3A of Chapter 150B, and Article 15 of Chapter 53, of the North Carolina General Statutes, and Title 4, Subchapter 3B of the North Carolina Administrative Code for a more complete statement of rights.

2. Mandatory Pre-Hearing Conference.

Pursuant to 4 NCAC 3B .0226, the Commissioner of Banks will hold a Pre-Hearing Conference in this matter on a date to be agreed upon by the parties, at least thirty (30) days in advance of the hearing date. Respondent and Counsel to the OCOB are required to attend this conference to pursue a stipulation of facts, to resolve issues of evidence, and to reach agreement on any other matters which will reduce costs, save time or otherwise expedite the disposition of this action. Respondent is directed to contact the undersigned Counsel for the OCOB to make the necessary arrangements.

B. Purpose of the Hearing

The purpose of this hearing is to determine whether, upon the facts alleged in Section IV below, there is a basis to conclude that AANC, in the operation of its cash advance business in North Carolina, is engaged in the business of lending in violation of G.S. § 53-166(a); is attempting to evade the application of the Consumer Finance Act in violation of G.S. § 53-166(b); is engaged in the business of check cashing in violation of G.S. § 53-276; and whether, pursuant to the authority of G.S. §§ 53-187 and 53-285, there is reasonable cause for the Commissioner to issue an order to AANC to cease and desist or to refrain from violating

the Consumer Finance Act and the Check Casher Act, and to assess a civil money penalty under the Check Casher Act.

IV. FACTUAL ALLEGATIONS

On November 22, 2004, an investigative hearing into the cash advance business of AANC was conducted by the OCOB at which time AANC produced certain documents and tendered for examination under oath a vice president and counsel of Advance America, Cash Advance Centers, Inc. ("Advance America"), the parent company of AANC. AANC subsequently provided supplemental responses to issues raised during the course of the investigative hearing.

Based upon the investigation into this matter, the documents produced, and supplemental responses, there is reasonable cause to believe that:

1. AANC is a Delaware corporation with headquarters at 135 North Church Street, Spartanburg, South Carolina, and is duly authorized to do business in the State of North Carolina.
2. AANC's sole business in North Carolina is the ownership and operation of deferred deposit cash advance centers. AANC currently operates 118 such cash advance centers in North Carolina. As is more fully set out below, AANC's operations in North Carolina were originally conducted under what Advance America calls the "standard business model" and, since August 31, 2001, have been conducted under what the company calls the "agency model."
3. AANC is a wholly owned subsidiary of Advance America whose headquarters is also at 135 North Church Street, Spartanburg, South Carolina. Advance America does business in 34 states and operates through wholly-owned subsidiaries in each of those states. The sole business of Advance America through its subsidiaries is the making or originating of deferred deposit check

cashing transactions, commonly referred to as "payday loans." Advance America is the largest provider of payday loans in the United States.

4. In 2001, Advance America acquired McKenzie Check Advance, LLC, another entity engaged in the payday lending business. As a result of this, Advance America controlled two subsidiaries which were engaged in the payday lending business in North Carolina, AANC and McKenzie Check Advance of North Carolina, LLC, d/b/a/ National Cash Advance, a Tennessee limited liability company (hereinafter "NCA"). In August 2003, NCA was consolidated into AANC, with the resulting firm operating as AANC.
5. A deferred deposit cash advance or payday loan is the advance of cash for a short term, typically a period of 14 days, secured by a check drawn on the consumer's bank account in an amount equal to the amount of the cash advance plus a fee. The fee is a finance charge.
6. In 29 of the states in which it does business, Advance America, through its wholly-owned subsidiaries, offers and makes payday loans directly to consumers. (This method of lending is referred to as the "standard business model.") Advance America's respective subsidiaries are licensed lenders in states where licensing is required for payday lenders.
7. In 5 states where payday lending is not authorized or is not feasible because of usury limitations (Arkansas, Michigan, North Carolina, Pennsylvania and Texas), Advance America's subsidiaries have entered into marketing, servicing and collection service agreements with out-of-state state-chartered banks to provide payday loans. (This arrangement is referred to as the "agency model.")
8. Under the agency model, an Advance America subsidiary originates payday loans at its cash advance centers, disburses loan proceeds and collects loan payments from customers. However, the loan proceeds are provided by an out-of-state bank, the loan documents are in the name of the bank, and customer repayments are deposited by the subsidiary into an account controlled by the bank. The bank partnering with an Advance America subsidiary claims the right to "export" the interest rates and fees allowed by the bank's home state

notwithstanding the usury rate in the customer's home state. Advance America subsidiaries are currently using state chartered banks located in South Dakota, Kentucky and Washington because banking supervisors of banks organized under federal law have effectively prohibited national banks and federal thrifts from making loans through payday lending companies.

9. Advance America's management structure and its support and supervision of its subsidiaries is essentially the same for both the standard and agency models.
10. From October 1, 1997, through August 31, 2001, North Carolina law, at G.S. § 53-281, provided authority for licensed check cashers to make payday loans through a deferred deposit lending provision in the check cashing licensing law. The statute allowed licensees to defer deposit of checks in the amount of \$300 or less for a period not to exceed 31 days and to charge a fee not in excess of 15% of the face amount of the check.
11. AANC was licensed as a check casher under G.S. § 53-275 *et seq.* during the period October 1, 1997 through August 31, 2001, and made direct payday or deferred deposit loans to North Carolina consumers pursuant to G.S. § 53-281 during that time period. McKenzie Check Advance of North Carolina, LLC, operated in a similar manner under the name "National Cash Advance" during this time period. An AANC or NCA customer with no funds in his or her checking account could write a check and receive an immediate cash advance. Deferred deposit transactions made by AANC and NCA under G.S. § 53-281 were made with the funds of such firms and under their respective policies and procedures.
12. During the year 2000, AANC and NCA earned \$31.6 million in revenue from their North Carolina payday loan operations.
13. Pursuant to the terms of the North Carolina Check Casher Act, the provision for payday lending, G.S. § 53-281, was scheduled to expire on July 31, 2001. The North Carolina General Assembly extended the expiration of G.S. § 53-281 for one month to August 31, 2001. After that date, there has been no statutory authority for check cashing businesses or others to make payday loans that do not comply with North Carolina law.

14. When the North Carolina deferred deposit statute expired on August 31, 2001, AANC ceased making direct loans for consideration to North Carolina consumers and relinquished its license as a check cashing business. However, AANC continued its payday lending presence in this State and continued to operate its existing cash advance centers. AANC remained in business by entering into a "Marketing and Servicing Agreement" with Peoples National Bank of Paris, Texas ("PNB").
15. Through its agreement with PNB, which became effective on September 12, 2001, AANC continued to advertise payday loans, solicit customers, service its same customers, operate its same cash advance store locations, receive and process loan application information, prepare and execute loan documents, disburse loan proceeds, receive payments on the loans, and handle delinquency collections. For these services, PNB paid AANC a substantial portion of the loan fees collected by AANC for PNB.
16. From the customer's perspective, the loan process with PNB loans remained substantially the same as with the loans formerly made directly by AANC. The documentation required by PNB to obtain a loan was substantially the same. Customers continued to write checks which were held by AANC, receive cash proceeds at AANC stores, and repay the loans in 14 day intervals at AANC stores. In order to obtain a \$100 fourteen day cash advance in a PNB transaction, the customer would write a check for \$117, yielding a 443.21% annual percentage rate, the same terms as the former AANC direct loan.
17. On January 29, 2003, Advance America agreed to the terms of a Consent Order issued by the Office of the Comptroller of the Currency ("OCC"), an agency of the United States Department of the Treasury and the primary supervisor of national banks, through which, among other provisions, (a) AANC was required to cease, not later than February 28, 2003, providing services related to the origination, renewal and rollover of PNB funded loans and to terminate the PNB Marketing and Servicing Agreement; and (b) Advance America was prohibited from entering into any written or oral agreement to market, originate, service or collect a payday loan offered through a national bank without a

prior written determination of no objection from the OCC.

18. After the OCC required AANC to withdraw from its relationship with PNB, AANC continued its payday lending presence in this State by marketing, originating, servicing, and collecting payday loans through an arrangement with Republic Bank and Trust Company ("RBT"), a state-chartered bank based in Louisville, Kentucky. AANC's Marketing and Servicing Agreement with RBT became effective on or about March 1, 2003.
19. Under its arrangement with RBT, AANC has the responsibility to manage and operate its cash advance centers in North Carolina; to hire, train and supervise personnel who work in the cash advance centers; to advertise the payday lending product; to accept applications and customer documentation for payday loans originated; to enter customer information into a loan approval system; to advise customers whether or not the loan has been approved; to provide RBT contracts and disclosure forms to customers for execution; to disburse the loan proceeds to customers; to record and account for the payday loan transactions; to receive customer payments; to transmit customer payments to RBT; and to collect on delinquent customer accounts.
20. Although RBT is contractually responsible for underwriting, approving loans and funding payday loans originated by AANC, AANC is responsible for the net charge-offs of loans during a given period of time that exceed 20% of the fees generated by such loans. With a loan fee of \$17.50 per \$100 of the amount advanced to the consumer, this agreement obligates AANC to bear the net charge-offs in excess of 3.5% of amounts advanced during any given period of time. Advance America maintains a substantial contingent liability to RBT for potential loan losses. Advance America has estimated its total contingent liability under its bank agency model in 5 states to be \$57.1 million, of which \$25.8 million is its contingent liability to RBT for North Carolina and Texas operations. AANC's obligation to RBT, including its excess loan obligation are

guaranteed by Advance America and secured by a pledge of collateral.

21. Advance America is responsible for most of the advertising for AANC. On a nationwide basis, including national television advertising, Advance America advertises the availability of payday loans at Advance America cash advance locations. Advertising of the payday loan product is done in the Advance America name with the Advance America logo, while the identification of RBT's role is displayed in a substantially smaller type size. Store signage also emphasizes the name and logo of Advance America, with far less prominent disclosure of the role of RBT. RBT does not directly advertise the availability of its loans in North Carolina.
22. RBT has the authority to make deferred presentment loans under Chapter 368 of the Kentucky Revised Statutes. Pursuant to this authority, RBT assesses a loan fee of \$17.50 per \$100 cash advance on its North Carolina transactions. The RBT truth-in-lending disclosure reveals that, based on a period of 14 days, such a charge amounts to an annual percentage rate of 456.26%.
23. RBT does not make payday loans in Kentucky. An Advance America subsidiary does make payday loans in Kentucky to Kentucky residents but makes these loans directly, not through RBT or any other bank.
24. RBT has no bank branches or physical presence in North Carolina and has not registered any loan production offices in this State. It is not registered with the North Carolina Secretary of State to do business in this State.
25. AANC receives compensation from RBT for its loan origination business in the form of a biweekly "processing, marketing and servicing fee." The payment to AANC by RBT is based on (a) a percentage of the fees on payday loans generated by AANC at its cash advance centers; (b) the level of net charge-offs borne by AANC; and (c) other incidental charges received. AANC's service fee revenue from RBT totaled approximately \$27.2 million in 2003 and \$22.4 million in the first nine months of 2004.

26. During its relationship with RBT, RBT has paid AANC a large majority of the gross finance charges from payday loans generated in AANC's cash advance centers. Advance America has estimated that the current North Carolina fee revenue to it from RBT amounts to \$2.2 million per month.
27. AANC is currently offering, arranging, and collecting on loans in this State with effective annual interest rates in excess of 400 percent.
28. AANC currently maintains 118 locations in North Carolina at which it offers cash advances to North Carolina residents.
29. AANC receives checks from customers and pays out cash in return for the checks and receives consideration for such transaction.
30. AANC is not licensed as a consumer finance lender in North Carolina under the provisions of the Consumer Finance Act.
31. AANC is not licensed as a check cashing business in North Carolina pursuant to G.S. § 53-275 *et seq.*
32. AANC is not registered with the North Carolina Secretary of State as a loan broker pursuant to G.S. § 66-109 and does not provide customers with any of the disclosures specified in G.S. § 66-107.
33. AANC is not licensed in this State as a collection agency pursuant to G.S. § 58-70-1.

CLAIMS FOR RELIEF

1. The North Carolina Consumer Finance Act ("CFA") provides at G.S. § 53-166(a) that no person shall engage in the business of lending in amounts of ten thousand dollars (\$10,000) or less and contract for, exact, or receive, directly or indirectly, or in connection with any such loan, any charges whether for interest, compensation, consideration, or expense, or

any other purpose whatsoever, which in the aggregate are greater than permitted by chapter 24, except as provided in and authorized by Article 15 (the CFA), and without having first obtained a license from the Commissioner. For the purposes of the CFA, the term "lending" includes, but is not limited to, endorsing, or otherwise securing loans or contracts for the payment of loans.

2. The CFA further provides at G.S. 53-166(b) that the provisions of G.S. § 53-166(a) shall apply to any person who seeks to avoid its application by any device, subterfuge or pretense whatsoever.

3. The North Carolina Check Casher Act, Article 22 of Chapter 53 of the General Statutes, G.S. § 53-275, et. seq. provides at G.S. § 53-276 that no person or entity may engage in the business of cashing checks, drafts or money orders for consideration without first obtaining a license under Article 22 and that no person may avoid the requirements of Article 22 by providing a check or other currency equivalent when cashing payment instruments.

4. The Consumer Finance Act authorizes the Commissioner of Banks, when the Commissioner has reasonable cause to believe that any person is violating or threatening to violate the provisions of the Consumer Finance Act, to order such person to cease and desist from such action and to pursue injunctive relief to

enforce such order.

5. Based on the foregoing, there is reasonable cause to believe that AANC may be engaged in the business of lending within the meaning of G.S. § 53-166; that it regularly offers, arranges, originates and collects on consumer loans with interest rates in excess of the rates authorized by Chapter 24 of the General Statutes; that it contracts for, exacts or receives in connection with such loans, directly or indirectly, charges which in the aggregate are greater than permitted by Chapter 24; and that it is not licensed as a consumer finance licensee pursuant to G.S. § 53-166.

6. Further, there is good cause to believe that AANC may be cashing checks for consideration in violation of G.S. § 53-276.

7. Therefore, good cause exists for the Commissioner of Banks to conduct a hearing to receive evidence and legal argument as to the foregoing questions relating to AANC's compliance with North Carolina law and (a) if AANC is found to be in violation of the Consumer Finance Act, to issue an order to cease and desist such violation; and (b) if AANC is found to be in violation of the Check Casher Act, to issue an order to cease and desist such violation and to assess such civil money penalties as may be appropriate.

Issued this 1st day of February, 2005.

W. Reitzel Deaton

W. Reitzel Deaton, Director
Consumer Finance Division
Office of the Commissioner of Banks

Of Counsel:

L. McNeil Chestnut
Special Deputy Attorney General
Administrative Division
North Carolina Department of Justice
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Raleigh, North Carolina 27699-9001
Phone: (919) 716-6800
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CERTIFICATE OF SERVICE

THE UNDERSIGNED hereby certifies that he has this day served a copy of the foregoing Notice of Hearing by placing a copy of the same in the United States Post Office at Raleigh, North Carolina, certified mail, return receipt requested, postage prepaid and addressed to:

National Registered Agents, Inc.
Registered Agent for Advance America, Cash
Advance Centers of North Carolina, Inc.
120 Penmarc Drive
Suite 118
Raleigh, NC 27604

and

William M. Webster, IV
President and C.E.O.
Advance America Cash Advance Centers
of North Carolina, Inc.
135 North Church Street
Spartanburg, SC 29306

This the 1st day of February, 2005.

S/ _____
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