

STATE OF NORTH CAROLINA

WAKE COUNTY

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

IN RE:)
)
ADVANCE AMERICA, CASH ADVANCE)
CENTERS OF NORTH CAROLINA, INC.) **AMENDED**
) **NOTICE OF HEARING**
) **AND ORDER FOR**
) **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

This Amended Notice of Hearing supplements the prior Notice Hearing dated February 1, 2005. The purpose of the Amended Notice is to incorporate additional factual allegations that relate to changes in the Respondent's operations announced by the Respondent on or about July 8, 2005.

You are hereby notified that the Commissioner of Banks for the State of North Carolina, (hereinafter the "Commissioner"), will hold a hearing on September 2, 2005, 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 specified above, and will continue from time to time thereafter until the same is fully concluded.

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 has intervened in these proceedings by prior order of the Commissioner and is authorized 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 may hold a Pre-Hearing Conference in this matter on a date to be agreed upon by the parties, at least ten (10) 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); 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.

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. As of June 30, 2005, in 29 of the states in which it does business, Advance America, through its wholly-owned subsidiaries, offered and made 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. Until June 30, 2005, in 5 states where payday lending was not authorized or was not feasible because of usury limitations (Arkansas, Michigan, North Carolina, Pennsylvania and Texas), Advance America's subsidiaries operated under 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.") On information and belief, after July 1, 2005, the Advance America subsidiary in Michigan converted to the standard business model and began offering direct loans to consumers due to recently enacted legislation authorizing payday lending in Michigan. On information and belief, after July 1, 2005, the Advance America subsidiary in Texas ceased operating under the agency model and converted to a credit service organization under Texas law. Arkansas, North Carolina and Pennsylvania are currently the only states in which Advance America subsidiaries operate under the agency business 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 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 are 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 Cashier 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 retained 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 was responsible under the Marketing and Servicing Agreement for underwriting, approving loans and funding payday loans originated by AANC, AANC was contractually responsible for the net charge-offs of loans during a given period of time that exceeded 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 obligated AANC to bear the net charge-offs in excess of 3.5% of amounts advanced during any given period of time. Advance America maintained a substantial contingent liability to RBT for potential loan losses. As of December 2004, 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 represented its contingent liability to RBT for North Carolina and Texas operations. AANC's obligation to RBT, including its excess loan obligation were 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 the bank'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 the bank. RBT did 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 assessed a loan fee of \$17.50 per \$100 cash advance on its North Carolina transactions. The RBT truth-in-lending disclosure revealed that, based on a period of 14 days, such a charge amounted to an annual percentage rate of 456.26%.
23. At no time has RBT made payday loans in Kentucky to Kentucky residents. 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 had no bank branches or physical presence in North Carolina and has not registered any loan production offices in this State. It is not and has not been registered with the North Carolina Secretary of State to do business in this State.
25. From at least March 2003 until July 6, 2005, AANC received 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 was 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 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 North Carolina fee revenue to it from RBT amounted to \$2.2 million per month.
27. On or about July 5, 2005, AANC terminated its contractual relationship with RBT.
28. On or about July 7, 2005, AANC began offering and arranging payday loans in North Carolina pursuant to a new contractual arrangement with First Fidelity Bank of Burke, South Dakota.
29. Pursuant to its arrangement with First Fidelity Bank, AANC currently offers payday loans in North Carolina with loan fees of \$20 for every \$100 in cash advanced. On information and belief, in a typical loan transaction with a cash advance of \$300, AANC's customer will write a check for \$360 (payable to First Fidelity Bank), receive \$300 in loan proceeds, and then return in two weeks to repay the transaction in cash and redeem the check. The \$60 fee in such a transaction is a finance charge and the annual percentage rate for such a transaction with a 14-day repayment term is 521%.
30. AANC, in conjunction with First Fidelity Bank, and to comply with new FDIC guidelines on payday lending, offers short-term installment loans to consumers in addition to payday loans. These loans also carry interest rates far in excess of the usury limits for consumer loans under North Carolina law.
31. On information and belief, as with AANC's prior relationships with PNB and RBT, AANC continues 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 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 deposit customer payments in a First Fidelity account; and to collect on delinquent customer accounts.

32. On information and belief, as with AANC's prior relationships with PNB and RBT, AANC continues to receive the predominant share of the loan proceeds pursuant to a billing arrangement with First Fidelity Bank.
33. First Fidelity Bank 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.
34. Since September 2001, AANC has offered, arranged, originated, processed, and collected on loans in this State with effective annual interest rates in excess of 400 percent, and continues to do so at the present time.
35. AANC currently maintains 117 locations in North Carolina at which it offers cash advances to North Carolina residents.
36. AANC is not licensed as a consumer finance lender in North Carolina under the provisions of the Consumer Finance Act, and has not been so licensed at all times relevant hereto.
37. AANC is not and has not been 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.
38. AANC is not and has not been 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.

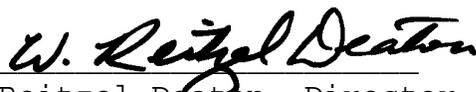
3. The Consumer Finance Act authorizes the Commissioner of Banks, when the Commissioner has reasonable cause to believe that any person is violating or threatening to violate the provisions of the Consumer Finance Act, to order such person to cease and desist from such action and to pursue injunctive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

4. 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.

5. 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 if AANC is found to be in violation of the Consumer Finance Act, to issue an order to cease and desist such violation.

Issued this 11th day of July, 2005.



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
9001 Mail Service Center
Raleigh, North Carolina 27699-9001
Phone: (919) 716-6800
Fax: (919) 716-6755

CERTIFICATE OF SERVICE

THE UNDERSIGNED hereby certifies that he has this day served a copy of the foregoing Amended Notice of Hearing on counsel of record for the Respondent Advance America, Cash Advance Centers of North Carolina, Inc. by hand delivery of said Notice at the Office of the Commissioner of Banks, Raleigh, North Carolina,

This the 11th of day of July, 2005.



L. McNeil Chestnut
Special Deputy Attorney General
North Carolina Department of Justice
9001 Mail Service Center
Raleigh, North Carolina 27699-9001
Phone: (919) 716-6800
Fax: (919) 716-6755