STATE OF NORTH CAROLINA

COUNTY OF NEW HANOVER

IN THE GENERAL COURT OF JUSTICE

SUPERIOR COURT DIVISION

FILE NO.: 04-CVS-2860

JOHN R. KUCAN, JR., and
TERRY COATES, Plaintiffs,

VS.

ADVANCE AMERICA, CASH ADVANCE CENTERS OF NORTH CAROLINA, INC.; ADVANCE AMERICA, CASH ADVANCE CENTERS, INC.; and WILLIAM M. WEBSTER, IV
Defendants.

ORDER

A TRUE COPY
CLERK OF SUPERIOR COURT
NEW HANOVER COUNTY
BY: Katherine Thompson
Deputy Clerk of Superior Court

THIS CAUSE COMING ON TO BE HEARD AND BEING HEARD before the undersigned Superior Court Judge in New Hanover County Superior Court on March 17, 2009 upon remand from the N.C. Court of Appeals to consider in light of *Tillman v. Commercial Credit Loans, Inc.*, 362 N.C. 93, 655 S.E.2d 362 (2008) the defendants' motion to compel arbitration. Upon hearing testimony of witnesses, oral arguments, review of briefs, new evidence submitted and the entire record proper, the Court makes the following findings of fact:

1. The plaintiff John Kucan, Jr. is a resident of New Hanover County, North Carolina.

2. The plaintiff Terry Coates is a resident of Mecklenburg County, North Carolina.

3. The defendant Advance America, Cash Advance Centers of North Carolina, Inc. ("Advance America-NC") is a Delaware corporation with its sole or principle business operations in North Carolina. Advance America-NC participates in operating retail payday lending establishments throughout North Carolina including New Hanover County and Mecklenburg County, using the names "Advance America", and "National Cash Advance."Inc.

4. The defendant Advance America, Cash Advance Centers Inc., ("Advance America") is a Delaware corporation with its principle place of business in South Carolina.

5. The defendant William M. Webster, IV, is a resident of the state of South Carolina.

6. The plaintiffs Kucan and Coates have filed this action on behalf of a class of all persons who entered into a "payday loan" transaction at North Carolina offices of Advance America at anytime after August 31, 2001, in transactions that did not purport to involve a national bank as lender.

7. In their complaint, plaintiffs allege the defendants Advance America, Cash Advance Centers of North Carolina, Inc.; Advance America, Cash Advance Centers Inc.; and William M. Webster, IV operated an illegal lending business in North Carolina in violation of the North Carolina Consumer Finance Act, G.S. 53-164 et seq.: The North Carolina Check Cashing laws, G.S. 53-276; The North Carolina Unfair Trade Practice laws, G.S. 75-1.1 et seq.; and the North Carolina Usury laws, G.S. 24-1.1.

8. In March of 2009, prior to hearing, the defendants in this matter moved to strike exhibits 11, 12, and 13 attached to Plaintiffs' Motion and Tender of Additional Materials. The Court finds these exhibits irrelevant to the proceedings in this case, Hager et al v. Check Into Cash of North Carolina, et al. Defendants motion to strike in this case is allowed.

9. Prior to 1997, payday lending was illegal within the state of North Carolina. Payday lending became lawful upon the 1997 enactment of former G.S. 53-281. Former G.S. 53-281 contained a July 31, 2001 expiration date or sunset. After initially extending the sunset of said law by one month [North Carolina Session Law 2001-323], the General Assembly refused to renew authorization for payday lending. Legal authority for payday lending within the state of North Carolina thus expired August 31, 2001.

10. By "Urgent Memo" dated July 31, 2001, addressed to "All Check-Cashing business licenses who are engaged in "payday lending," the North Carolina Commissioner of Banks advised payday lenders that the expiration of G.S. 53-281 was eminent. By "Urgent Memo" dated August 30, 2001 addressed to "All Check-Cashing business licenses now engaged in "payday lending," the North Carolina Commissioner of Banks stated that G.S. 53-281 would expire the next day and further

stated: "there is no lawful basis for "payday lending" without such a law, including "payday lending" transactions effective by "agents" or "facilitators" of out of state lending institutions."

11. After payday lending authorization in North Carolina expired, Advance America-NC began a contractual arrangement with an out of state bank in connection with its North Carolina operations. Under this arrangement Advance America-NC maintains it served as the marketing and servicing agent of Republic Bank & Trust from March 2003 until and through July 2005. Prior to March 2003, Advance America, NC maintained it served as the processing, marketing and servicing agent for Peoples National Bank, from September 11, 2001 until February 2003. From July 2005 until the present, Advance America, NC maintained it acted as the processing, marketing and servicing agent for First Fidelity Bank, a state charted Federal Insured Bank located and chartered in South Dakota.

12. The small loan business is closely regulated under North Carolina Law. The North Carolina Consumer Finance Act, G.S. 53-164 et seq., assigns regulatory responsibility over the small loan business to the North Carolina Commissioner of Banks. The Commissioner of Banks also has regulatory over sight over check-cashing businesses under N.C.G.S. 53-275 et seq.

12. The North Carolina Commissioner of Banks conducted a contested case hearing against one of the defendants in this case, Advance America, Cash Advance Centers of North Carolina, Inc., to determine whether that company was in violation of the North Carolina Consumer Finance Act by reason of its payday lending business in North Carolina purportedly undertaken as agent for an out-of-state bank. [*In re Advance America, Cash Advance Centers of North Carolina, Inc.*, docket no. 05:008:CF.] An order in that proceeding was rendered on December 22, 2005. That order is currently on appeal, having previously been appealed to the Court of Appeals and remanded. [*In re Advance America*, 189 N.C. App.115, 657 S.E.2d 405 (2008).]

13. N.C.G.S 53-187 provides for actions by the Attorney General and Banking Commissioner. Additionally Chapter 75 provides for prosecution of actions by the Attorney General. The proceeding by the Commissioner of Banks does not seek restitution for individual payday borrowers. Additionally, the Court notes there is no evidence of any action by the Attorney General seeking monetary restitution for individual borrowers, although the Attorney General has entered into

consent orders with two defendants not a party to this action. Neither of those consent orders provided for monetary restitution for individual payday borrowers.

14. G.S. 53-166(d) provides that "any contract of loan" that violates the North Carolina Consumer Finance Act (G.S. 53-164-191)" shall be void."

15. Under the Advance America form of payday lending as practiced in North Carolina an Advance America customer in need of loan writes a personal check at one of the defendant's loan offices for a stated amount, obtaining a promise that the check will not be presented for payment for up to 14 days.

16. Plaintiff Kucan received 16 payday loans from Advance America's Wilmington office between May 2003 and August 2004. The loan amount was $425 each time, and the fee for each such loan was $75. Most of the loan transactions that plaintiff Kucan entered into were "rollovers," back-to-back transactions in which he took out a new loan on the same day that the old loan was due. In such cases, plaintiff Kucan did not repay the principal, but instead paid a fee to extend the loan. Most of these loans were "rollovers."

17. The plaintiff Coates received 3 payday loans in December 2003 through January 2004 in the amounts of $200 and $300, from an Advance America branch in Charlotte. These sequential loans were "rollovers." The annual percentage rate (APR) for these loans was 456.25%

18. Advance America custom and practice is to hold the customers check until the due date of the loan. If the customer does not come back to pay the loan when due, Advance America will deposit the check.

19. Advance America's practice of holding the customer's check as security for the loan gave Advance America considerable leverage over the consumer in collecting the payday debt. If an Advance America customer cannot afford to pay back the loan when due and lacks the funds to cover the check if deposited by Advance America, the customer is faced with a choice of having the check returned for non sufficient funds or taking out a new payday loan for an additional fee.

20. Both plaintiffs have testified that they were fearful that criminal charges would be brought against them by Advance America if their check

was deposited on the due date with sufficient funds in their checking account to cover said checks.

21. The plaintiff Kucan obtained his first payday cash advance through Advance America-NC, on May 21, 2003. Defendants maintain this cash advance loan is provided by Republic Bank and Trust. On that date Mr. Kucan filled out and signed a payday cash advance application ("the Customer Agreement") in an Advance America-NC location. Mr. Kucan borrowed $425, paying a finance charge of $75 at that time.

22. To obtain said loan the plaintiff Kucan signed the Customer Agreement. The Customer Agreement is a one-page form, drafted by Republic Bank which contains an express "Waiver of Jury Trial and Arbitration Agreement." Directly above the signature line on the first page of the Customer Agreement appears a highlighted acknowledgement stating in bold letters **"Please note that this Customer Agreement contains a binding arbitration . . . . You further acknowledge that you have read, understand, and agree to all of the terms on both sides of this Customer Agreement, including the provision on the other side entitled, 'Waiver of Jury Trial and Arbitration Agreement.'"**

23. The Waiver of Jury Trial and Arbitration Agreement contained on the reverse (the "Republic Bank Arbitration Agreement") begins as follows:

> Advance America is the marketer/servicer in connection with your deferred deposit transaction with the Bank, which is evidenced by the Customer Agreement on the other side of this Waiver of Jury Trial and Arbitration Agreement ("Arbitration Provision"). In consideration of the services Advance America provides to you as the agent of the Bank in connection with this Customer Agreement, and in consideration of the Bank entering into a deferred deposit transaction with you, and in consideration of your promises made under this Customer Agreement, and for other good and valuable consideration, the receipt of which is acknowledged, you, the Bank and Advance America agree to this Waiver of Jury Trial and Arbitration Provision ("Arbitration Provision") as set forth below.

24. The Agreement defines the parties and matters subject to arbitration, giving the term "dispute" and "disputes" the broadest possible meaning, to include all claims regarding the validity of the arbitration provision, all claims arising out of the loan agreement, all common law claims based upon contract, tort, fraud or intentional torts, all claims

based on violations of any statute, and all class claims asserted by the customer.

25. The Arbitration Agreement contains a choice of law provision. It provides that the Agreement will be governed by the Federal Arbitration Act (FAA). If for any reason the FAA is found not to apply to the transaction, the agreement states that Kentucky law is to apply.

26. The waiver of jury trial and ability to participate in a class action in the agreement states:

> You acknowledge and agree that by entering into this Arbitration Provision:
>
> (a) YOU ARE WAIVING YOUR RIGHT TO HAVE A TRIAL BY JURY TO RESOLVE ANY DISPUTE ALLEGED AGAINST US OR RELATED THIRD PARTIES;
> (b) YOU ARE WAIVING YOUR RIGHT TO HAVE A COURT, OTHER THAN A SMALL CLAIMS TRIBUNAL, RESOLVE ANY DISPUTE ALLEGED AGAINST US OR RELATED THIRD PARTIES; and
> (c) YOU ARE WAIVING YOUR RIGHT TO SERVE AS A REPRESENTATIVE, AS A PRIVATE ATTORNEY GENERAL OR IN ANY OTHER REPRESENTATIVE CAPACITY, AND/OR TO PARTICIPATE AS A MEMBER OF A CLASS OF CLAIMANTS, IN ANY LAWSUIT FILED AGAINST US AND/OR RELATED THIRD PARTIES.

27. Although the Republic Bank Arbitration Agreement allows either party to seek adjudication in a small claims tribunal, the agreement provides that an appeal of such ruling by either party must be brought in arbitration. The agreements specify that if the plaintiffs chose arbitration rather than proceeding through a small claims tribunal, Advance America will pay their arbitration filing fees at the request of the plaintiff.

28. The Arbitration Agreement provides that Republic Bank or Advance America will advance certain arbitration fees, including the filing, administrative, hearing and arbitrator's fees. The Agreement provides that "[t]hroughout the arbitration, each party shall bear his or her own attorneys' fees and expenses, such as witness and expert witness fees."

29. No severability clause exists in the loan agreement, arbitration clause or contract as a whole.

30. According to the Arbitration Agreements terms, Mr. Kucan retained all of his substantive rights in individual arbitration, but agreed to give up the right to a trial by jury or participate in a class action.

31. Over the course of approximately fifteen months, the plaintiff Kucan voluntarily signed this Arbitration Agreement sixteen times in connection with different payday cash advances. The process for each of Mr. Kucan's sixteen cash advances was similar to the one described above for obtaining his May 21, 2003 cash advance.

32. Mr. Kucan never read any Arbitration Agreement until after speaking with his current attorneys, approximately one year after entering into his first Customer and Arbitration Agreements.

33. Plaintiff Coates obtained three payday cash advances through Advance America-NC locations, within a three-week period. His experience in obtaining them was similar to Mr. Kucan's, described above. Each time Mr. Coates obtained his loan, he signed both the Customer Agreement and the Arbitration Agreement. The terms of Mr. Coates' Arbitration Agreements were identical to those of the plaintiff Kucan, quoted above.

34. Plaintiff Coates never read any portion of the Customer Agreement or the Arbitration Agreement until his deposition.

35. To obtain their payday loans, Plaintiffs Kucan and Coates both signed and dated Customer Agreements prepared by Republic Bank. Each one had an Arbitration Agreement on the back. The signature of Ken Snips, President of Republic Bank, is stamped on each agreement.

36. There is no evidence of any arbitration claims filed in North Carolina involving these defendants, the banks with which Advance America has had a contractual relationship, or any defendant or bank in the other matters before this Court entitled *McQuillan v. Check 'n Go* and *Hager v. Check Into Cash*, cases nos. 04-CVS-2858 and 04-CVS-2859.

37. All evidence before the Court is that every payday lender doing business in North Carolina requires borrowers to execute loan agreements with mandatory pre-dispute binding arbitration clauses banning class actions.

38. The claims at issue in this case are modest in amount. The amount of plaintiff Kucan's damages claim for violation of the Consumer Finance Act, including recovery of principal payments as provided in the Act,

but without trebling, is $5,450.00. Even with damages treble the amount of his injury, the amount of plaintiff Kucan's claim is $7,850.00. The amount of the damages at issue in his case for Mr. Coates, including for recovery of his repayment of principal, is $440.00. With damages treble the amount of his injury, the amount of his claim is $720.00.

39. Plaintiffs offered the affidavit testimony of twenty-two attorneys as well as deposition testimony of nineteen of the attorneys, each offering their opinion it was unlikely an individual, proceeding on an individual (non-class) basis, would be able to obtain legal counsel to prosecute claims against Check Into Cash.

40. For reasons set out in this Court's order dated December 31, 2005, the Court excluded the testimony of five of these attorneys. Plaintiffs have subsequently withdrawn the testimony of two of the attorneys. The Court otherwise admits and considers the affidavits and depositions of the remaining proposed attorney experts. The Court otherwise considers the defendants arguments in the motion to strike in determining the weight to be given to the testimony proffered through these attorneys.

41. Each of the before mentioned attorneys accepted as experts has offered his/her opinion that because the stakes of an individual arbitration on behalf of a payday borrower are so small, no attorney would represent a payday borrower claim on an individual basis. They go further to state that this is true despite the availability of statutory attorney fees under N.C.G.S. 75-1.1 et seq.

42. Plaintiffs have submitted the affidavits and depositions of two financial experts. One, Ronald E. Copley, holds a Ph.D. in Finance, has been a tenured professor of Finance at the University of North Carolina at Wilmington, is a Certified Financial Analyst, and is a licensed investment advisor. Dr. Copley has reviewed the COB Order and opined it would require a minimum of 100 hours to perform financial analysis similar to the analysis performed by the Commissioner of Banks. The others, Michael J. Minikus, a North Carolina certified public accountant, expressed it would require a minimum of 65 hours to perform an analysis similar to the analysis performed by the Commissioner. Dr. Copley charges $200 per hour for his services. Mr. Minikus charges $125 per hour for his services.

43. Defendants have made a motion to strike the testimony of Dr. Copley and Mr. Minikus. The Court finds these witnesses proper to testify as experts, and admits and considers their affidavits and depositions.

44. After this case was remanded by the Court of Appeals in May of 2008, the plaintiffs requested permission to submit live testimony from two of their attorney experts: Glenn Barfield, an attorney in private practice and the former chair of the Legal Aid of North Carolina Board of Directors; and George Hausen, Executive Director of Legal Aid of North Carolina. Mr. Hausen and Mr. Barfield testified at the evidentiary hearing conducted by this Court on March 17, 2009. The Court attaches particular weight to these attorney witnesses, having had the opportunity to observe their demeanor and because of their substantial efforts to make legal services available to persons of modest means. Based upon the testimony of Mr. Barfield the Court finds it unlikely an attorney would bring an individual case for a payday lending customer in court or arbitration due to the complexity of the cases and the lack of economic feasibility of such representation. Additionally, based upon the testimony of Mr. Hausen the Court finds it very unlikely an individual payday borrower could obtain Legal Aid or pro bono representation in such a matter.

45. Additionally as the Consumer Finance Act and Check Cashing law which serve as the basis for plaintiff's actions contain exemptions for banks, plaintiffs must prove the transactions at issue are not exempt or preempted. This will require extensive depositions, document review and expert analysis, as is reflected by the order of the Commissioner of Banks. The costs of expert witnesses alone would likely exceed the amounts at issue in individual cases.

46. The Court finds payday borrowers would not be able to effectively prosecute the type of claims raised by plaintiffs here, even if the claims are legally justified and correct, if payday borrowers are required to proceed on an individual rather than class basis.

47. The Court previously (2005 Order) found as a fact that one of the attorneys submitting an affidavit in support of the plaintiffs argument, to wit Catherine S. Parker Lowe, had represented an individual consumer in *Britt v. Jones*, 123 N.C. App.108, 472 S.E.2d 199 (1996). In that case Ms. Lowe's representation of the individual consumer involved allegations that the consumer paid usurious interest in connection to loans made to her. In that matter Ms. Lowe represented the plaintiff and received a trebling of the damages award under the unfair trade practices claim and $4,100 in attorney's fees. The *Britt v.*

Jones case, however, was less complex than the instant case. The complaint in *Britt v. Jones* was 6 pages in its entirety, compared to 38 pages in this case. The trial court's judgment in *Britt v. Jones* was 7 pages, double spaced. In contrast, the COB Order was 54 pages, single spaced. The claim at issue in *Britt v. Jones* was simply that the interest charged exceeded the allowable interest rate. The issues in the payday cases involve choice of law, control of a relationship with several banks, a predominant economic interest test, evasive intent, applicability of exemptions, and federal preemption.

48. The Court finds the arbitration agreements involved in this matter do not limit any of the claims, damages or substantive remedies (including attorneys' fees, treble damages and restitution) available to the plaintiffs, and further finds the arbitration agreements cannot and do not prevent state agencies from intervening on behalf of the North Carolina consumers.

49. The arbitration agreement and class action waiver effectively prevent these plaintiffs and others similarly situated from procuring adequate legal representation.

50. In light of the large number of Advance America North Carolina loans, the fact there has never been any arbitration proceeding arising from this business lends support to the finding that the class action prohibition operates as an exculpatory clause.

51. As noted above in finding 13, the proceeding by the Commissioner of Banks does not seek restitution for individual payday borrowers. Additionally, the Court notes there is no evidence of any action by the Attorney General seeking monetary restitution for individual borrowers, although the Attorney General has entered into a settlement with two payday lending defendants not a party to this action. Neither of those settlements provided for monetary restitution for individual payday borrowers.

52. Advance America operated 2408 payday cash advance centers in 34 states as of December 31, 2004, claiming in a 2004 filing with the Securities and Exchange Commission to be the largest provider of payday cash advance services in the United States.

53. The plaintiffs, in contrast, are relatively unsophisticated although each graduated from a community college.

54. Although they had some other possibilities at the time of most of these loans plaintiffs needed money at the time they entered into the payday transactions with defendant.

55. There exists a great disparity in bargaining power between defendants and plaintiffs.

56. Plaintiffs had no ability to negotiate different terms at the time of these transactions as the customer agreement and arbitration clause are standard form documents drafted by Republic Bank & Trust, who exclusively controlled the approval process, terms and conditions of each loan. Thus the terms of the loan agreements, including the arbitration agreement, were non-negotiable.

57. Plaintiffs lacked any meaningful choice to obtain short-term consumer credit without agreeing to an arbitration clause prohibiting participation in a class action.

BASED UPON THE FOREGOING FINDINGS OF FACT, THE COURT CONCLUDES AS A MATTER OF LAW:

1. As this case is between North Carolina plaintiffs, a Delaware Corporation with its sole or principle business operations in North Carolina, and a South Carolina resident, over payday loan transactions all taking place within the state of North Carolina, this dispute is governed by North Carolina law. The Kentucky choice of law clause contained in the payday loan documents is invalid.

2. Plaintiffs have met their burden in establishing before the Court the existence of procedural unconscionability in the terms of the loan agreement and arbitration clause used in these loan transactions. The Court makes this legal conclusion having considered and finding inequality in bargaining power between the parties to this agreement; the advantage of defendant in the practice of holding customer's checks as security for a payday loan; the remedies preserved by defendants for collecting those checks rendering the arbitration clause one-sided; that any payday borrower seeking such a loan in N.C. has no alternative to executing such an agreement; and the non-negotiable terms of the loan agreement set forth in the documents. Accordingly, the Court concludes the agreements to be procedurally unconscionable.

3. Plaintiffs have met their burden in establishing before the Court the existence of substantive unconscionability in the terms of the loan agreement and arbitration clause used in these loan transactions. This legal conclusion is made having considered and finding defendants loan business is structured in a manner to make a legal challenge to their loans complex; these complexities will require expert analysis and significant expenditures of legal effort; the amounts at issue in individual claims are insufficient to attract counsel on a pro bono or contingency fee basis, and cannot justify payment of counsel on an hourly rate; that the costs of expert witnesses would very likely exceed any individual case recovery. Further, from the above, the Court concludes these exculpatory effects are one-sided, falling upon the consumer only and are such as to deter any individual from pursuit of a claim against the defendant. Based upon the above the Court concludes the arbitration clauses at issue under these facts and circumstance are substantively unconscionable.

4. Having considered all facts and circumstances of this matter, the Court concludes plaintiffs have established the loan agreements and arbitration clauses to be unconscionable and thus unenforceable.

5. As the contracts and agreements lack any severability clause, to require plaintiffs to proceed through arbitration would require a rewriting of the agreements, which the Court should decline to do.

6. The prohibition of class actions in these agreements operates, in purpose and effect, as an exculpatory clause.

7. Serving as an exculpatory clause in contract between parties of disproportionate power in a heavily regulated industry, the contractual prohibition against class action participation violates public policy of the State of North Carolina and is therefore unenforceable.

8. Serving as an exculpatory clause in contract between parties of disproportionate power in a heavily regulated industry, the arbitration clauses containing the prohibition against class action participation violates public policy of the State of North Carolina and is therefore unenforceable.

9. The defendant's motion to compel arbitration and stay proceedings should be denied.

IT IS NOW, THEREFORE, ORDERED, in accordance with the foregoing findings of fact and conclusions of law that the defendant's motion to compel arbitration and stay proceedings in this matter is hereby DENIED.

This the 26th day of June, 2009.

D. Jack Hooks, Jr., Judge Presiding