



State of North Carolina

Office of the Commissioner of Banks

Beverly E. Perdue
Governor

Joseph A. Smith, Jr.
Commissioner of Banks

February 2011

BY HAND DELIVERY

Honorable Phil Berger
President Pro Tempore of the Senate
N.C. Senate
16 W. Jones Street, Room 2007
Raleigh, NC 27601-2808

Honorable Thom Tillis
Speaker of the House
N.C. House of Representatives
16 W. Jones Street, Room 2304
Raleigh, NC 27601-1096

RE: 2010 Consumer Finance Study

Dear Senator Berger and Representative Tillis:

Pursuant to the instructions of the 2009 – 2010 Session of the General Assembly of North Carolina, more fully described below, I am delivering to you under cover of this letter a study of the North Carolina Consumer Finance Act.

The North Carolina Consumer Finance Act ("CFA"), N.C.G.S § 53-164, is a carefully drafted and comprehensive exception to North Carolina's usury law. Its provisions squarely set the limits of permissible activity and make clear that the CFA is not a mechanism for circumventing the State's general usury law. The result has been the creation of a narrowly bounded and particularly delineated lending industry which makes small installment loans. The CFA grants to the North Carolina Commissioner of Banks (the "Commissioner") the responsibility to regulate this activity through licensure of consumer finance companies and enforcement of the normative provisions of relevant North Carolina law. It does not confer on the Commissioner the authority to set fees and charges, all of which are subject to statutory limits.

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For the year ended December 31, 2009, companies making small consumer loans in North Carolina had outstanding loans of \$1.2 billion and stated equity of \$245.9 million. This compares with aggregate North Carolina net loans outstanding of North Carolina state-chartered banks of \$159.3 billion and equity capital of such banks of \$28.2 billion. Six consumer finance companies made 80% of the small loans outstanding, with 75 companies accounting for the remainder. Two of the six largest consumer finance companies made 66% of the small loans outstanding. The average amount of such loans was \$2,341.

The 2009 Session of the General Assembly of North Carolina established a Joint Legislative Study Commission on the Modernization of North Carolina Banking Laws and the Consumer Finance Act (the "Commission"), which in 2010 conducted a study of the CFA. At the conclusion of the study, the Commission recommended that the Commissioner do a further study and report to the General Assembly on the topics set out in the original study: the rise in operating costs for the industry and what impact it was having on the delivery of the product, the maximum amount that could be extended to any single borrower, the rate and fee structure, and "strategies for increasing consumer protection and disclosure." The North Carolina Office of the Commissioner of Banks ("NCCOB") was also asked to do a series of tasks including: revisiting past data, reviewing and possibly changing the annual report form, gathering new data, and analyzing this new data. The Commission's recommendations require that any CFA modifications balance "all appropriate consumer protections" with "the requirement for potential profitability of the lender."

Pursuant to the Commission's recommendations, NCCOB sponsored four meetings participated in by representatives of the consumer finance industry and consumer advocates. In addition, NCCOB sponsored preparation by the UNC Center for Community Capital of an analysis of industry profitability based on existing reports submitted to NCCOB as required under the CFA.

On the basis of the foregoing, the Commissioner finds that:

- While there has been an increase in operating expenses of North Carolina consumer finance companies over time, the increases have been covered in substantial part by an increase in the average loan amount. As a result, the majority of these companies remain profitable and the potential for profitability continues to exist under the current framework, although lenders may not be as profitable as they would like.
- The adjustment of the consumer loan market mentioned above has resulted in a concentration of loan activity in six consumer finance companies and a modest reduction in the number of companies making consumer loans. These developments mirror comparable developments in the banking industry: concentration of assets and activities in a relatively small number of banks.

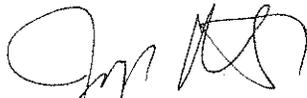
- While some concerns have been expressed, based on anecdotal evidence, regarding persistent refinancing of consumer loans, no compelling evidence was submitted by consumer advocates or discovered in a review of NCCOB and Justice Department files to support the view that refinancing is an abuse of consumers or in need of remediation.

In light of the foregoing findings and after careful consideration of the following report and submissions from meeting participants, the Commissioner does not recommend any changes in the CFA, either to enhance industry revenue or increase consumer protections.

It should be noted that, as a result of the study, Annual Report forms for consumer finance companies have been revised to enhance and standardize the information included in such reports, so that the industry may be more effectively monitored by all stakeholders.

The conclusions of this report are not intended to suggest that the financial services provided to unbanked and under-banked North Carolinians are satisfactory. It is to suggest that efficient and low cost services to this market cannot be fully achieved either by traditional depository institutions or traditional small loan companies. The Commissioner recommends that future studies on this topic focus on the utilization of advanced communications and information processing technology to reduce the costs and manage risks of financial services to this market.

Sincerely,

A handwritten signature in black ink, appearing to read 'Joseph A. Smith, Jr.', written over a faint, illegible typed name.

Joseph A. Smith, Jr.
Commissioner of Banks