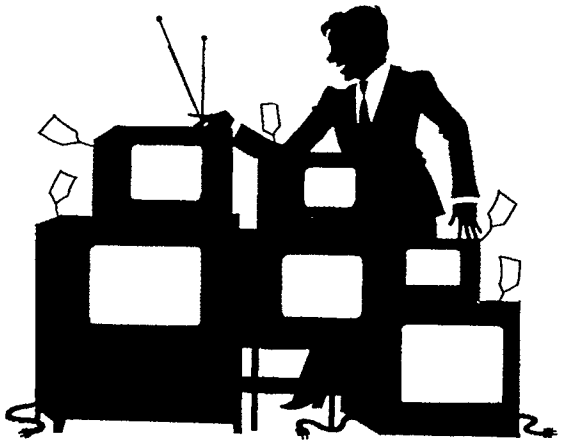


The Rent-To-Own Industry: Of Consuming Interest in North Carolina

by Anne Jackson

For most businesses, North Carolina law regulates interest rates and finance charges on furniture and appliance purchases. But for dealers in the state's growing rent-to-own industry, the sky may be the limit. While other businesses are limited to charging 24 percent on retail sales, these businesses often charge consumers what amounts to more than 100 percent—and sometimes more than 200 percent—on rent-to-purchase agreements. Are these charges fair, or should they be limited? What action, if any, should the 1988 General Assembly take when it convenes in Raleigh in June?

Jeanne Fenner didn't know much about the rent-to-own industry before 1982, when her housekeeper's sister asked her to look over a contract for a rent-to-own clothes washer. Fenner, then a Democratic state representative from Wilson, was dismayed to see that the contract called for 78 weekly payments of $14—a total purchase price of $1,092 for an appliance that would sell for about $350 at retail prices.

"She really didn't know rent-to-own from buying something on time," Fenner says now about the woman. Because she was living on what Fenner describes as "a very small disability check," the woman had liked the contract terms: no down payment and no credit check. But what she did not realize was that, like all rent-to-own agreements, she would own no equity in the appliance until the final payment was made. Neither did she know the actual cash price of the washer. Fenner says the rent-to-own dealer had refused to tell the purchaser.

Anne Jackson is a Raleigh writer who has covered the N.C. General Assembly for The New York Times *regional newspapers.*

Across North Carolina, scores of other consumers tell the same story—that they didn't know what they were getting, or what they weren't getting, for their money. The estimated 250 rent-to-own outlets in North Carolina—with names like Colortyme, Rent-A-Center and Remco—offer a variety of electronic equipment, furniture, and appliances. Old-line rental dealers—such as furniture rental companies which do not offer their items on a rent-to-own basis—have begun to describe themselves as strictly rental dealers, so they won't be confused with the rent-to-own industry.

But as the industry has grown in size and profitability, so has the controversy surrounding its practices. In 1984, the Attorney General's office obtained a $20,000 fine from Remco for mailing threatening notices to customers whose payments were overdue. (The industry blames the incident on a mistake by a secretary for a lawyer who was handling Remco's past-due accounts.) The mailgrams warned of felony prosecution unless Remco received "the cash market value of its merchandise within seventy-two hours." Other consumers have come home to find their homes entered and their appliances repossessed by dealers, while others complain of being harassed in their workplace and elsewhere.

Such hardball practices have stimulated a growing number of complaints over the past few years, and Fenner introduced the first proposal for regulating rent-to-own charges during the 1983 General Assembly session. Although unsuccessful, her effort began an on-again, off-again legislative debate that has spanned five years. When state lawmakers return to Raleigh this year, the thorny issue of rent-to-own regulation will be waiting for them once more.

"The Attorney General's office examined 342 contracts executed by one rent-to-own company in 1986. Fifty-one percent of the goods were used. Generally there was no difference between the stated cash price of the used goods and new goods, contrary to a representation made by the industry . . . . "

—Lacy Thornburg
Attorney General

The Attorney General Intervenes

Last year, advocates of regulation won an influential ally in N.C. Attorney General Lacy Thornburg. Thornburg blasted rent-to-own agreements as a "cruel hoax" on "the poorest of our citizens." A study by his office's Consumer Protection Section determined that some rent-to-own contracts charged as much as 350 percent in "effective annual percentage rates" and that only about 22 percent of the contracts culminated in sales—a percentage confirmed by the industry. In other words, fewer than one in four consumers who enter into a rent-to-own contract actually wind up owning the merchandise. For the vast majority of rent-to-own consumers, the furniture, television, or washing machine goes back to the rent-to-own dealer—there to be rented again to another consumer.

Thornburg also said in a series of memoranda to the legislature that rent-to-own consumers often *aren't getting new merchandise.* As often as not, *it's used goods.* "The Attorney General's office examined 342 contracts executed by one rent-to-own company in 1986," Thornburg says. "Fifty-one percent of the goods were *used.* Generally there was no difference between the stated cash price of the used goods and new goods, contrary to a representation made by the industry . . . ."[1]

There's nothing wrong with offering used goods for sale, says Lawrence Davis, an attorney for Rent-A-Center. "So what [if it's used]," says Davis. "They tell 'em it's used." And under legislation the industry has backed in other states, he says, dealers would be compelled to say whether an item is used.

Thornburg last year urged the Senate Judiciary I Committee to support a House-passed bill that "closes a loophole through which a relatively small but growing number of companies are able to charge the least fortunate of our citizens, not 18 percent (the maximum credit card rate); not 24 percent (the maximum installment rate); not 36 percent (the maximum small loan rate); but 250 percent per year or more in finance charges when they are trying to buy washing machines, furniture, televisions, and other goods."[2]

Davis says that without rent-to-own businesses, poor people with bad credit ratings would have to do without televisions, videocassette recorders, basic appliances like refrigerators, and even such items as rental tires. Rent-to-own businesses, he notes, provide these items at relatively low individual payments so poor people can afford them.

In an interview, Edward L. Winn III, gen-

eral counsel for the Texas-based Association for Progressive Rental Organizations (APRO), criticized efforts to regulate rent-to-own charges. Winn characterized those attempts as price-fixing by "lunatic legal aid lawyers" and "radical consumer activists." Winn contends that legislation offered by consumer representatives would limit the prices that could be charged both for the items themselves and for what the industry argues are rental charges rather than interest—thus "fixing" the price.

"We are providing [people at] a certain economic level nicer things than they could have otherwise," Winn says. Current regulatory proposals, he warns, would drive rent-to-own dealers in North Carolina out of business, penalizing "the poor folks who don't get to watch TV and don't get air conditioners and don't have furniture."

The Prospect for Legislative Action

The starting point for legislative deliberations in 1988 will be a 12-page bill hammered out by a three-member Senate subcommittee after two months of debate and sometimes raucous hearings during the 1987 session.[3] That proposal would allow rent-to-own dealers to charge rates that would yield effective interest rates as high as 48 percent (on 18-month contracts), require dealers to apply 70 percent of every payment to the purchase price, and allow for reinstatement of a contract after a missed payment.

The Senate bill was drafted as a compromise after the House, by a vote of 92-1, passed a bill to treat rent-to-own agreements like retail sales. That bill would have limited allowable charges to the 24 percent interest rate that state law allows retailers to charge for installment purchases.[4]

Neither the House nor Senate bill is acceptable, industry lobbyists say. "We're going to have to go in there [to the legislature] and duke it out again, I reckon," Winn said. "It's a survival issue—make no mistake."

Key observers on both sides of the issue predict that if a bill comes out of the 1988 legislative session, it probably will be fashioned after a New York law that requires half of each payment—rather than the 70 percent in the Senate Committee Substitute—to go toward the purchase price. Under North Carolina law, that would allow rent-to-own dealers to charge as much as 103 percent per year in effective interest rates—more than *four times* the maximum installment payment rate now allowed on retail purchases (see Tables 1 and 2). That would not be much of an improvement, consumer advocates say.

"That would cut out the very worst, but that probably would not change the average of what is being done now," says James C. Gulick, the special deputy attorney general who heads the state's Consumer Protection Section.

Is the 50 percent, New York-style formula one the industry could live with? "Experience [in New York] would tell that we probably could. But I don't know," says Colortyme General Counsel W.

Table 1. Effective Annual Interest Rates of Rent-To-Own Contracts Depending on Amount Applied to Equity and Length of Contract

Length of Contract	Percentage of Payment Applied to Equity						
	45%	50%*	60%	70%**	75%	80%	85%
	Interest Rates						
24 months:	92.38%	77.88%	54.81%	36.90%	29.29%	22.40%	16.35%
18 months:	122.33%	103.07%	72.42%	48.67%	38.65%	29.56%	21.22%
12 months:	181.06%	152.35%	106.72%	71.58%	56.73%	43.36%	31.14%
6 months:	348.01%	291.50%	202.61%	135.03%	106.74%	81.32%	58.20%

Note: Annual percentage rates for weekly, biweekly or semi-monthly agreements are slightly higher than those for equivalent monthly terms.

* As so-called "New York" proposal would allow
** As Senate Committee Substitute for HB 1108 would allow

Source: N.C. Legal Services Resource Center

"To compare rent-to-own dealers with retail merchants is just not fair. It's not comparable in any way."
—Lawrence Davis
Attorney for Rent-A-Center

Woodward "Woody" Webb of Raleigh.

Consumer representatives says the industry is misleading the General Assembly, and that it could actually live with the Senate Committee Substitute, which requires that 70 percent of payments be applied to the purchase price. Both Gulick and Margot Roten of the N.C. Legal Services Resource Center point out that the industry last year cited a contract offered by a Raleigh rental dealer—Ted's TV—as typical of the industry. In that case, the industry said, Ted's TV offered rent-to-own contracts for appliances at about the same cost as a local furniture store did on retail sales contracts. Both Roten and Gulick say the Ted's TV contract applied the equivalent of 79 percent of the consumer's payments to equity—more than either the New York bill or the Senate Subcommittee substitute would require. "Obviously, they can live with even more than 70 percent," notes Gulick.

The experience of other states with new rent-to-own laws is still being judged. In New York, consumer representatives say they are studying the results. In Michigan, where the state requires that 45 percent of each payment be applied to owner's equity in the merchandise, Assistant Attorney General Fred Hoffecker says there are "very few complaints anymore." Hoffecker says Michigan's law, which took effect in 1985, also requires complete disclosure of terms and costs, ensuring that consumers realize "that it's a costly way to purchase something." Prior to adoption of the law, says Hoffecker, "We were seeing complaints on a regular basis, but now it's almost disappeared.

North Carolina Interest Rate Regulation

At the heart of the dispute between the rent-to-own industry and consumer activists is this question: Is a rent-to-own contract *just* a rental contract with an option to buy, as the industry maintains, or is it a sales contract with regular payments that accomplish the same thing as a sales contract with interest provisions, as consumer representatives contend?

Consumer protection specialists maintain that rent-to-own contracts perform the same function as loan contracts—they require regular payments by a consumer to purchase an item, the item winds up costing more than it would if it were bought on a cash basis, and the difference between the cash price and the ultimate cost when the contract is completed amounts to finance charges that are not really different from interest on principal. They point out that North Carolina has a structured interest-rate regulation system that limits other businesses in what they can charge (see Table 2), and that to be fair to all parties, rent-to-own dealers also should be regulated—to create what the N.C. Retail Merchants Association, a supporter of regulating the industry, describes as a "level playing field."

Under current state law, banks and businesses with revolving charge accounts can charge consumers no more than 18 percent in annual interest rates. Retail merchants who sell furniture, appliances, and other items are limited to charging 24 percent interest—a higher rate than banks, because their cost of money is higher. And small loan companies can charge consumers up to 36 percent—a higher rate than retail merchants—because small loan companies operate on a smaller profit margin and take higher risks in offering loans to consumers with risky credit records. Consumer specialists like Roten say the rent-to-own industry could probably survive if it were treated like finance companies and limited to 36 percent, but she notes that the rent-to-own industry does have some higher costs—and says that an effective interest cap of 48 percent might be appropriate. That's what the Senate Subcommittee substitute would allow.

But rent-to-own dealers reject any contention that they are lending money, or that they should be restricted in what they charge. "To compare rent-to-own dealers with retail merchants is just not fair," says Davis. "It's not comparable in any way. Unlike retail merchants' installment sales customers or small loan customers who could unwittingly sign up for excessive future obligations, the rent-to-own dealers' customers do not sign up for any future obligation except to return the merchandise at the end of the rental period of a week or a month for which payment has already been paid. There is no extension of credit and no loan is involved in any way. The

Table 2. Regulated Interest Rates for Other Types of Transactions

Type of Loan	Current Maximum Interest Rate	Statutory Citation
Credit Card Transactions	18 %	G.S. 24-11 and G.S. 25A
Retail Installment Sales	24 %	G.S. 25A
Small Loans	36 %	G.S. 53, Article 15
Rent-To-Own Contracts	No Limit	None
[Proposed Senate Subcommittee Substitute]	**[48.67%]**	**[SCS for HB 1108]**

customer is not required to make a long-term commitment which could be beyond the customer's means. The transaction is like a cash sale because payment is up front and is not truly comparable to an installment retail sale or loan, which would carry future payment obligations. The future ownership option does not substantially change this fact," Davis adds.

In a strongly worded memo to the Senate Subcommittee last year, industry attorney Samuel Choate said it was apparent that Attorney General Thornburg did not understand the rent-to-own industry.[5] Choate explained the industry's view that without debt, there can be no creditor-debtor relationship requiring interest. Because rent-to-own contracts can be interrupted at any time by the consumer, without further financial obligations by the consumer, rent-to-own contracts cannot be regarded as either sales or as loan contracts. Rent-to-own customers, he points out, "are given *an option* to own but *no obligation.*"

Adds Choate, "It was disappointing . . . to discover that the Attorney General of North Carolina could not recognize the difference between a debt and a lease with an option to renew. It was equally as disappointing to see the Attorney General take the position that an item so uniquely a creature of debt as interest could be discussed in the context of a lease with no obligation."

Industry lawyers say dealers must charge higher prices on their goods than other retail businesses because their costs are higher—as much as 56 percent higher, the industry claims. And it says the reason so few consumers wind up owning merchandise is that many of them have no intention of owning—only 55 percent of rent-to-own customers plan eventually to own what they rent. Many consumers decide they cannot afford the item, decide they no longer need it, decide to switch to another item, or decide they only need it for a short period, says Choate.

The Fenner Treatment

Jeanne Fenner's 1983 bill would have treated rent-to-own contracts like retail sales, subject to the 24 percent interest cap. Like the similar bill that would come four years later in the 1987 session, it passed the House easily before running into trouble in the Senate. What emerged in 1983 was a law that merely encouraged dealers to disclose the cash price of rent-to-own merchandise and exempted most rent-to-own contracts from the retail installment sales act.[6] Rent-to-own contracts that required a final balloon payment of more than 10 percent of the item's cash price would not be regulated. The Senate "was pressured into adding that little loophole," says Roten.

Fenner's efforts only won her a place on the industry's political hit list.[7] The Wilson County Democrat lost her re-election bid in 1985 (in a special election mandated by a controversial redistricting plan) to Republican Larry Etheridge after political action committees funded by rent-to-own dealers from as far away as Texas poured more than $6,000 into Etheridge's campaign. That's an unusually large amount from one industry, especially in a

> *"A lot of people feel like it's a rip-off, and government has a place in regulating situations like that"*
>
> —Rep. Joe Hackney (D-Orange)

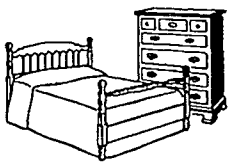
Table 3. State Regulation of Rent-To-Own Transactions

State	No Regulation	Rent-to-Own Transactions Exempt From Retail Sales Regulations	Rent-To-Own Transactions Subject to Retail Sales Laws	Requires That a Certain Percentage of Payment Be Applied to Equity	Requires Disclosure of Charges
Alabama					X
Alaska	X				
Arizona	X				
Arkansas					X
California	X				
Colorado	X				
Connecticut	X				
Delaware	X				
Florida	X*				
Georgia					X
Hawaii	X				
Idaho	X				
Illinois	X				
Indiana					X
Iowa					X
Kansas	X				
Kentucky	X				
Louisiana	X				
Maine		X			
Maryland	X				
Massachusetts					X
Michigan				X (45% to equity)	X
Minnesota		X			
Mississippi	X				
Missouri					X
Montana	X				
Nebraska	X				
Nevada	X				
New Hampshire	X				
New Jersey	X				
New Mexico	X				
New York				X (50% to equity)	X
North Carolina		**X**			
North Dakota	X				
Ohio	X*			X (50% to equity)	
Oklahoma	X				
Oregon	X				
Pennsylvania			X (18% rate cap)		
Rhode Island	X				
South Carolina					X
South Dakota	X				
Tennessee					X
Texas					X
Utah	X				
Vermont	X				
Virginia					X
Washington	X				
West Virginia	X				
Wisconsin		X			
Wyoming	X				
Totals:	**32**	**4**	**1**	**3**	**13**

* Disclosure legislation pending in current legislature.
Source: N.C. Attorney General's Office and Association of Progressive Rental Organizations

modest-sized county like Wilson. The same thing occurred in 1986, when Fenner ran for an N.C. Senate seat. Her opponent got $15,000 from rent-to-own industry officials in the 1986 race. "I think it certainly had its impact," she says. "You take away $15,000 from any campaign—it pays for telephone banks, it pays for a lot."

Etheridge spent $12,000 in his 1985 upset campaign, while Fenner spent about $2,000 in the general election and $5,700 to win an earlier four-way Democratic primary. The average winner in 1984 House races spent about $5,000.



The APRO's Winn had a role in the 1985 election. Winn told *The Charlotte Observer* in 1985 that he "sent out a memo to North Carolina dealers saying, "Jeannie Fenner's up for re-election. She's the one who tried to run you out of business." Contributions from across the state and the country poured into Etheridge's campaign, and when the dust settled, Fenner was out and Etheridge was in.

The rent-to-own issue slumbered through the 1985-86 General Assembly session, but awoke with a roar in 1987. Rep. Joe Hackney (D-Orange), with the backing of the Attorney General's office and the N.C. Legal Services Resource Center, introduced the bill that created the 1987 debate. Hackney's bill passed the House before industry lobbyists could marshal their forces against it. (In fact, hardly anyone was against the bill, including Etheridge. When the House voted 92-1 to pass the rent-to-own legislation, the new state representative from Wilson County did not vote. He was not on the floor at the time. Etheridge missed that and other votes because he was ill with pneumonia at the time.)

"I frankly thought on an issue like that, the more quickly it moved the better off we were," Hackney says. While the industry describes his bill as price

How Can a 25-Inch TV Cost $1100?

On Feb. 21, 1986, Ms. Lynda D.* decided to buy a television. She called Lion TV, a rent-to-own dealer, and asked them about the prices for various models. After some discussion, she agreed to purchase a 25-inch TV at a cost of $60 a month. The Lion TV salesperson said that the TV would be delivered to her home that afternoon for her inspection and that if she liked it she would be requested to sign certain documents. The television was delivered, Ms. D. signed the attached rental agreement, and paid Lion TV $60.

The agreement provided that payments could be made weekly, biweekly, or monthly. To purchase this television valued at $604.80, payments of $60 were required to be made for 17 months, plus an additional payment of $66.53 (for a total of $1,086.53). The *annual percentage rate* on this contract was in excess of *80 percent.*

Ms. D made irregular payments, sometimes weekly, biweekly, or monthly, all of which were accepted by Lion TV. Her last payment was made Dec. 20, 1986. She had paid a total of $561.

Although Lion TV had her home address and telephone number, and despite her request not to be contacted at work, on two occasions in late November 1986 a Lion TV employee confronted Ms. D. at her workplace and complained about her missed payments. She made two payments in December, which were accepted.

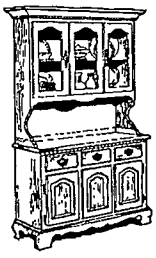
On Jan. 3, 1987, a Lion's employee swore out a criminal warrant against Ms. D. for failure to return rental property. The case was dismissed because no demand had been made to return the property. Immediately after the dismissal, a notice demanding the return of the property was left on Ms. D.'s front door, in plain view of all passersby. After an attorney intervened on Ms. D.'s behalf, the case was settled.

—*Margot Roten*
N.C. Legal Services Resource Center
Testimony supplied to Senate Judiciary I subcommittee on HB 1108 in 1987

* The consumer's name has been abbreviated for this article at her attorney's request.

fixing—it would limit the amount dealers could charge on transactions—Hackney points out that many consumers don't think such contracts are fair. "A lot of people feel like it's a rip-off, and government has a place in regulating situations like that," Hackney says.

By the time Hackney's bill got to the Senate, industry representatives were prepared. Winn flew in from Texas, Choate came from Washington, D.C., and former Speaker of the House Phil Godwin was summoned from Gatesville. The industry also signed on Davis, a former legislator and candidate for the U.S. Senate, and former N.C. Attorney General and 1984 gubernatorial candidate Rufus Edmisten, who once championed consumer protection legislation. At several meetings, the crowd of industry lobbyists and rent-to-own dealers spilled out of the committee room and into a hallway.



Sen. Charles Hipps (D-Haywood), the Judiciary I subcommittee chairman, recalls that at most meetings, lobbyists were "stacked up like cord wood," and he once quipped that the committee meeting would have to be moved "to the Dean Dome"—the 22,441-seat Smith Arena in Chapel Hill.

Choate proved himself to be a fierce opponent of the rent-to-own bill—even interjecting himself into the news gathering process. Once two reporters were interviewing Hipps after a committee meeting, and one scribe asked how much of a weekly payment might be applied to ownership. "That's not a fair question. He hasn't taken evidence on that in a subcommittee," interrupted Choate. Says Hipps, a lawyer himself, "I thought to myself, 'This isn't court. What is this nonsense?' That sort of ended most of our goodwill and rapport."

Davis says Choate later apologized to Hipps, but the damage was done. Legislators continue to grumble about "hired gun" lobbyists the industry

What More Does a Free Enterprise System Require?

As the attorney for Lion TV in the matter of Lynda D., I state for the purpose of correcting the record developed by the N.C. Legal Services Resource Center (which was not, incidentally, even involved in the case) that the documents in the file show that:

- Ms. D. signed the rental agreement on Feb. 21, 1986, not in one place but in two places, attesting that she had read and understood the agreement and, in particular, the ownership option provision.
- The agreement clearly revealed that the 25-inch Quasar television set was new and had a cash value of $604.80.
- The agreement also clearly disclosed that Ms. D. would have to pay $60 per month for 17 months and one additional payment of $66.53 in order to own the set (i.e. to stop renting and acquire outright ownership). These terms were set out not once but twice in the agreement and specifically signed off on by Ms. D. At the time Ms. D. signed the agreement she was employed by Sears in "Ladies Security."
- The agreement clearly provided that rental payments were due on or before the last day of the previous rental period.

According to the store files, Ms. D. made exactly one payment on time (her first payment due on Feb. 21, 1986) in over nine months. A demand letter was finally sent on Nov. 16, 1986, requesting that the set be returned within five days for failure to make timely rental payments. As a matter of practice, if Ms. D. had brought her account current and agreed to pay her rent on time in the future, no further action would have been taken. Because Ms. D. did not return the television set or bring her account current, a warrant was applied for and issued on Jan. 3, 1987, by a Wake County magistrate.

The matter was ultimately settled when Ms. D. voluntarily paid Lion TV a sum certain to buy the set. The documents and store files referred to herein are available for inspection and verification by anyone at any time.

—W. Woodard Webb
Legal Counsel, Lion TV

brought in from out of state to fight the bill. And several legislators also have pointed out that, as of May 4, 1988, neither Winn nor Choate had registered to lobby with the legislature, according to the N.C. Secretary of State's office.[8]

Rent-to-own dealers fought the bill by arguing that their profit margins are already slim because they provide service on rental items, and because they take a risk on low-income consumers that other merchants and lenders will not take. Choate told the legislators that under the Hackney bill, on an appliance with a retail price of $200, the industry could charge only $285 in fees over an 18-month lease—a margin of only $4.72 per month for the dealer. But committee members weren't impressed, pointing out that such an appliance with a "retail price" of $200 would have cost the dealer *far less* at wholesale prices—and would allow the dealer to make much more money on the transaction.

Hipps' subcommittee examined laws from other states and spent an estimated "50 or 60 hours," he says, in meetings and discussions with individual lobbyists. Hipps had asked the subcommittee staff to come up with what they believed was the toughest law in the nation. What the staff came back with was the New York law—requiring 50 percent of payments to equity, and allowing 103 percent interest rates on an 18-month contract. Hipps' subcommittee then beefed up that law to arrive at the 70-percent-to-equity formula, allowing an equivalent interest rate of 48.67 percent on 18-month contracts.

Hipps was pleased with the bill that emerged. "It was a consumer-oriented bill, but I didn't think it was a death-defying act," he said. "The subcommittee report is probably the toughest [proposed law] in the nation, yet it probably doesn't go far enough."

Barnes Balks

It went too far for some, however. Sen. Henson Barnes (D-Wayne), chairman of the Judiciary I Committee assigned to study the bill, thought the proposal went overboard, and he never called a committee meeting to act on the panel's report. "If they're going to have a bill that's going to wipe out the industry, I don't think we'd be doing North Carolina any good," Barnes says. "There are some folks who would not have furniture if they could not

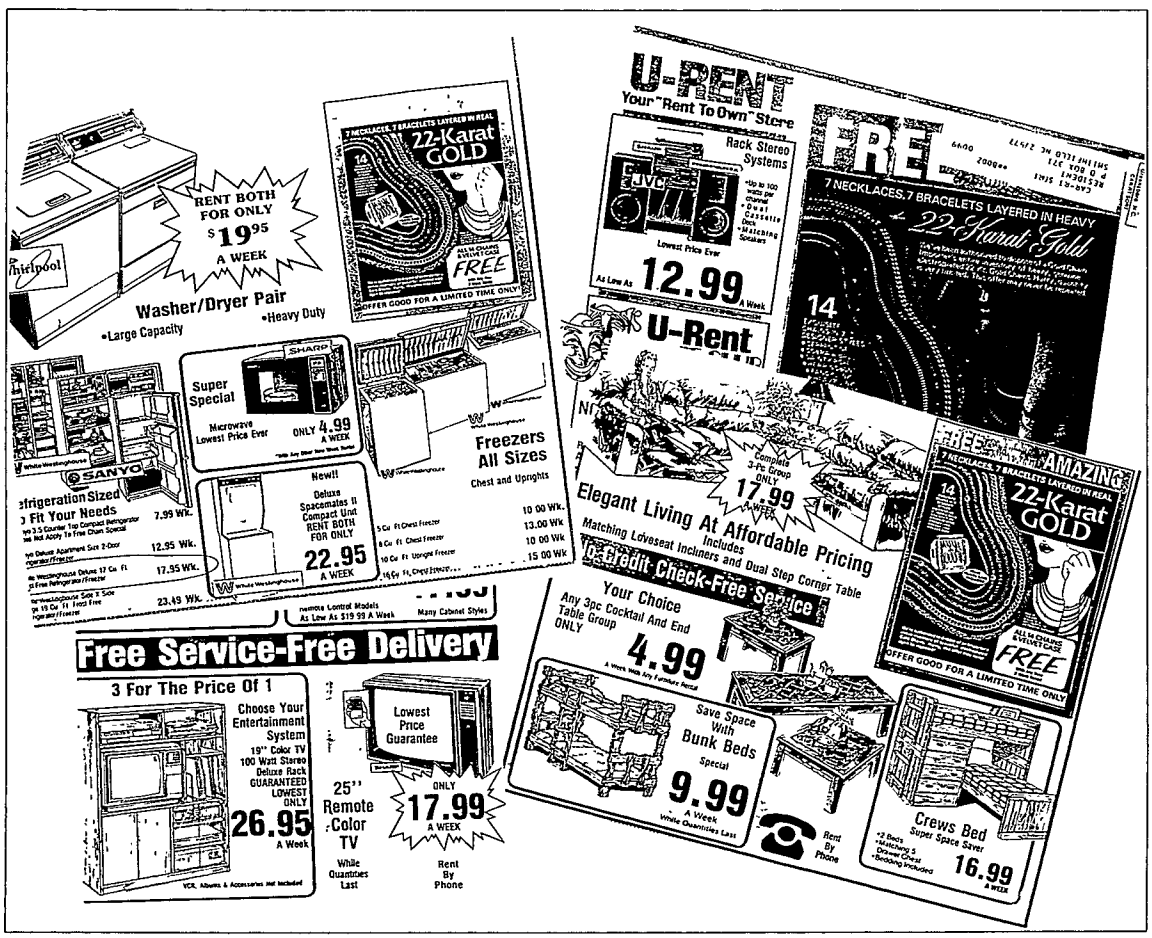


Table 4. Advantages and Disadvantages of Rent-To-Own Contracts

Advantages	Disadvantages
Poor consumers with bad credit can buy appliances and other goods they might not otherwise be able to afford.	Consumers are not often told (a) the actual price of the appliance, (b) how much they will have to pay the dealer, or (c) how much those charges would add up to in annual interest rates — as much as 350%.
Payments on rent-to-own contracts are low and can be made weekly, biweekly, or monthly.	Rent-to-own merchandise is often used, not new, and may have been used by more than one rent-to-own consumer in the past.
Dealers take care of delivery of appliances and provide free service when they malfunction.	Few rent-to-own consumers — fewer than one in every four — wind up owning the article they have contracted to buy and made payments for.
Consumers can halt their rental agreement anytime and return the item to the dealer without penalty.	Rent-to-own consumers often must pay a large balloon payment — sometimes nearly as much as they would have paid if they bought the item on a cash basis — at the end of the contract before they "own" the appliance.
	Consumers may be harassed by bill collectors if they miss payments, and may be prosecuted in criminal court for failure to return merchandise.

get it by paying for it over a period of time."

Barnes said he would instruct the subcommittee to go back to work in June 1988 and draw up a second compromise. He said he liked the New York law, which he has discussed with members of the Attorney General's staff in that state. "They think they've gone far enough," Barnes said.

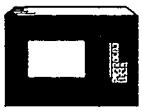
While he agrees that the fee on some rent-to-own contracts "shocks our conscience," Barnes warned against over-regulation in a recent edition of *Barnotes*, a newsletter published by the N.C. Bar Association. "No one stops to question the idea that the customer can simply refuse to purchase the overpriced appliances . . .," he wrote. "If we are not careful, we are going to regulate everything from your civil rights to your rent."[9]

Industry representatives concur. "If the prospective clients are told up front exactly what they're getting into and they're free to turn around and walk out of the store . . ., why doesn't that satisfy all the requirements of a free enterprise system?" asks Webb, the Colortyme lawyer who also represents about 250 stores that make up the N.C. Association of Rent-to-Own Dealers.

Webb says regulations should be limited to disclosure requirements—not currently required in North Carolina, but which would be mandated under the pending committee substitute—because rent-to-own payments do not constitute interest payments. Since no equity changes hands until the final payment, "there is no debt upon which a finance charge can be fixed," he says. "That's the legal confusion

that seems to throw most people."

Attorney General Thornburg, however, criticizes such contentions. "With one breath the industry claims it offers poor people with poor credit the means to buy goods they could not otherwise afford," he wrote in a memorandum last year to members of Barnes' Senate committee. "With the next the industry denies it is in the business of selling."[10]



Adds Gulick, the consumer protection chief, "The ownership 'carrot,' if you will, is used as a selling come-on, and a great many customers enter into it because they want to buy." Rent-to-own dealers, he said, "sell ownership and yet they turn around and want to make it a rental contract."

The industry embraces another view, however. "We see it as a way to allow consumers to use an item" until the consumer exercises his final-payment option to buy, says Rent-A-Center's Davis.

Thornburg believes that simple disclosure of terms is not enough. The rent-to-own industry has supported such legislation in the past, he says, because those laws usually define rent-to-own sales as special contracts, not as installment loans or installment purchases. That puts rent-to-own businesses in a special category, he says. "Primarily these are disclosure statutes, which do little more than give official sanction to the industry's current practices," Thornburg told the committee in his memo. "I urge you to reject this approach. I do not think it will provide adequate protection to those customers...."

Criminal Courts: Chamber of Justice or Collection Agency for Rental Dealers?

Should North Carolina's criminal courts be used as a collection agency for rent-to-own dealers whose customers are behind on their payments? It depends upon the circumstances, says the N.C. Attorney General's office, which hopes to prevent a deluge of collection cases from overwhelming the court system. The Attorney General has received several complaints from local district attorneys' offices that the courts are being used as collection agencies by rent-to-own dealers. "Our office has had a recent flood of cases charging failure to return hired property," notes James W. Copeland Jr., assistant district attorney in Wayne County.[1]

Copeland and others have complained that rent-to-own dealers are swearing out criminal warrants under G.S. 14-167, a state law that makes it a crime to fail to return rented property.[2] The law was written to protect dealers from customers who, for instance, rent a car and then fail to return it at the end of the rental period. But rent-to-own dealers are seeking criminal warrants against consumers who are late or who cease making payments on a rental contract and who do not immediately return property.

"In essence," says R. Alfred Patrick, assistant district attorney in Wilkes County, "the lessor [rent-to-own dealer] uses the criminal court as a collection agency; this can be quite aggravating since the equities are rarely [present] with the lessor acting as a prosecuting witness."[3]

In response, the Attorney General's office has advised prosecutors that they should wait until the stated end of the rental contract—not just until the consumer stops paying—before prosecuting such cases. "Prosecution under G.S. 14-167... would only be appropriate if the property were not returned after expiration of the lease...," says William P. Hart, an assistant attorney general.[4] Only if the dealer has evidence that the consumer has sold or otherwise disposed of the property should prosecutors pursue a case before the end of the contract.

That advice may relieve the courts of the burden of some rent-to-own cases. James Gulick, director of the Consumer Protection Section in the Attorney General's office, says those cases were running up to 20 a week in at least one judicial district. "We view the use of the criminal process in these cases as a big problem, and some

Nationally, four states—Maine, Minnesota, North Carolina, and Wisconsin—treat rent-to-own contracts like retail sales, but exempt them from rate regulation. One state—Pennsylvania—defines rent-to-own contracts as retail sales *and* applies a rate cap of 18 percent. Three other states—Michigan, New York, and Ohio—require that a percentage of every payment be applied to equity. New York and Ohio require that 50 percent be applied to equity, while Michigan requires that 45 percent apply to equity. Thirteen states have passed laws that recognize rent-to-own agreements as special contracts and require certain disclosures, such as the total of payments and the cash price (see Table 3). The toughest rate control law on rent-to-own businesses is Pennsylvania's. That law, which took effect March 1, 1988, was enacted in the closing days of the legislative session and took the industry by surprise. The APRO's Winn said the Pennsylvania law, if it stands, will mean the end of the rent-to-own business in that state. Overhead costs like delivery and free repair make it impossible for dealers to make a profit at such rates, industry spokesmen say.

"We're rent-to-rent dealers now [in Pennsylvania]," Winn said. "Customers no longer have a purchase option. They like to hope they get to own that of these companies are using it very widely."

Meanwhile, legislation is pending in the General Assembly to accomplish much the same goal—permitting prosecution only after the rental contract's full term has expired.[5] Supported by the N.C. Legal Services Resource Center and backed by Rep. Dan Blue (D-Wake) and Sen. Joe Johnson (D-Wake), the legislation—which creates a new provision limiting criminal prosecution of rental contracts with purchase options—is pending in the Senate Judiciary II Committee, where it has a fair chance of passage in the 1988 short session.

Sen. Charles Hipps (D-Haywood), chairman of a Senate subcommittee dealing with other rent-to-own legislation, says rent-to-own dealers should pursue recovery cases in civil court, just as other businesses do, and not in the criminal courts. "We don't need to have collections in criminal court," says Hipps. "These merchants [rent-to-own dealers] are the ones who let this stuff out on contract, and their remedy should be in civil court, not criminal court."

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FOOTNOTES

[1] Letter from James W. Copeland Jr., assistant district attorney, Eighth Prosecutorial District, to James Coman, Special Prosecution Division, Attorney General's Office, Feb. 18, 1988.

[2] G.S. 14-167 (Chapter 61, 1927 Session Laws, and amended in Chapter 1063, 1965 Session Laws, and Chapter 1224, 1969 Session Laws).

[3] Letter from R. Alfred Patrick, assistant district attorney, Twenty-third Prosecutorial District, to Lacy H. Thornburg, attorney general, Oct. 1, 1987.

[4] Letter from William P. Hart, assistant attorney general, for Lacy H. Thornburg, attorney general, to R. Alfred Patrick, assistant district attorney, Twenty-third Prosecutorial District, Oct. 15, 1987.

[5] HB 1240, "An Act to Make Certain Changes in the Law Regarding Fraudulent Disposal of Property," sponsored by Rep. Dan Blue (D-Wake); and SB 863, sponsored by Sen. Joe Johnson (D-Wake), pending in Senate Judiciary II Committee, 1987 General Assembly (Second Session 1988).

> *"If we are not careful, we are going to regulate everything from your civil rights to your rent."*
> —Rep. Henson Barnes (D-Wayne)

stuff that they rent. Now they can't do that."

Legislators and lobbyists agree that North Carolina is not likely to adopt regulations as stringent as Pennsylvania's. Hipps predicted that the regulatory issue will be resolved "more in line with Senator Barnes' theory (the New York bill) of where it should go than the subcommittee's theory of where it should go." Says the industry's Webb, "We're encouraged by the spirit of compromise we see from the Senate."

Hipps says that about 10 of the 50 senators—perhaps remembering Fenner's experience—had told him they were not eager to vote on rent-to-own regulations of *any* kind. But he adds: "If [a bill] comes out of committee with Henson's support, then there's a good chance it will pass."

But whether such a bill would be accepted by the House is another matter. Hackney is adamantly opposed to the bill that Barnes favors, and says he has already compromised by considering the Senate subcommittee substitute bill as a good alternative to his own bill. "We'd be worse off with [the New York style bill] than we would with nothing," contends Hackney. "Most of the dealers usually charge the same thing the New York bill would permit, so we won't have gained a thing."

But if the House is firm in its rejection of Barnes' approach, says Barnes, it may be the legislature will do nothing this year. "If they [the House] work it out, they can get a bill this year," says Barnes. "If not, maybe it'd be better to keep that sucker where it is right now [inactive in the Senate]."

This is an election year, of course, and some consumer advocates hope the prospects of facing the electorate will enhance chances for the Committee Substitute on HB 1108. But legislators have heard a great deal from the industry and very little from their other constituents about the rent-to-own issue, Hipps notes, and some don't like the notion of "playing Big Brother, trying to protect people from themselves," he says. "The average Joe Six-Pack doesn't know anything about that bill or care. He just wants that TV now."

Fenner, who attended many of the subcommittee meetings last year, agrees with Hackney that the legislature should take a strong regulatory stance. "I would dare say that if this was a middle-income [or] high-income problem, there would have been a law a long time ago," she says.

FOOTNOTES

[1]Memorandum from Lacy H. Thornburg, Attorney General, to Senate Judiciary I Committee Members, July 9, 1987, regarding HB 1108, p. 3.

[2]*Ibid.*, p. 1.

[3]Senate Committee Substitute for House Bill 1108, pending in Senate Judiciary I Committee, 1987-1988 General Assembly.

[4]Retail Installment Sales Act, G.S. 25A (Chapter 796 of the 1971 Session Laws, as amended by Chapter 686 of the 1983 Session laws).

[5]Memorandum from Sam Choate, counsel to the North Carolina Rental Dealers Association, to members of the Senate Judiciary I Committee, July 14, 1987, p. 1.

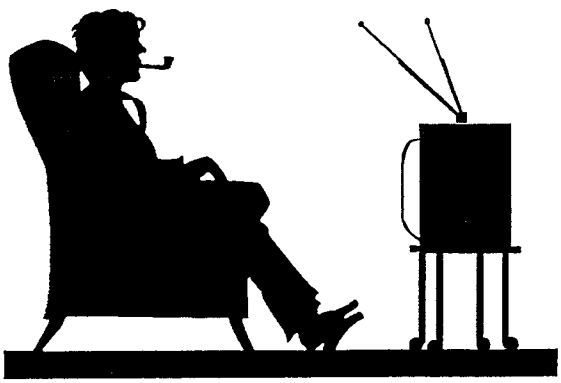
[6]See G.S. 25A-2(e) (Chapter 686, Sections 2 and 3, of the 1983 Session Laws).

[7]For more on the political impact of Fenner's bill, see Katherine White, "Rent-To-Own Firms Spent Freely To Defeat Legislative Foe," *The Charlotte Observer*, Special Reprint From *The Charlotte Observers* of June 16-25, 1985, p. 5; and Jim Morrill, "Challenge Proves Costly," *The Charlotte Observer*, April 15, 1987, p. A1.

[8]G.S. 120-47 (Chapter 820 of the 1975 Session Laws), which requires paid lobbyists to register with the state. Failure to register, a misdemeanor, can bring a fine of from $50 to $1,000, plus up to two years imprisonment, and prohibits the individual from lobbying the N.C. General Assembly for two years following conviction.

[9]Henson P. Barnes, "Legislative Trends Affecting The General Practice Of Law," *Barnotes*, publication of the N.C. Bar Association, December 1987/January 1988, pp. 1, 6, and 7.

[10]Memorandum from Lacy H. Thornburg, Attorney General, to Senate Judiciary I Committee Members, July 9, 1987, regarding HB 1108, p. 1.



RECOMMENDATION

North Carolina Should Regulate Rent-To-Own Contract Sales

North Carolina's rent-to-own industry provides a service to many consumers by making items available on a rent-to-own basis. However, many of these individuals are poor and cannot afford to purchase appliances and other items from conventional lenders, where they must pay annual interest rates ranging from 24 to 36 percent. Instead, they turn to rent-to-own dealers, and because state law does not regulate charges by this industry, low-income consumers pay prices equivalent to 100 percent or more and in some cases, more than 200 percent. The N.C. General Assembly has received testimony from retail merchants that would justify regulating rent-to-own contracts on the same footing as retail installment sales—at an effective rate of 24 percent on 18-month contracts. But because the rent-to-own industry must take greater risks on consumers with no credit ratings or poor credit records, some legislators believe they should be allowed to charge more than retail merchants, setting an effective annual interest rate cap at 36 percent, the same as small loan or finance companies.

Still others believe rent-to-own companies, with their higher costs of operating—including costs related to taking greater credit risks, providing free delivery, providing free service, and allowing consumers to cease making payments and terminate contracts without penalty—should be allowed to charge closer to 50 percent. Yet another alternative is legislation similar to that enacted for New York, Michigan, and Ohio which sets effective interest rate caps of roughly 100 percent. Such legislation might win the approval of the 1988 N.C. Senate, but House leaders have sworn to reject it in the short session of the N.C. General Assembly because, they argue, rates of 100 percent are unconscionable. They also say such rates would give the rent-to-own industry an unfair competitive advantage over other retail merchants.

Based on this research, the fact that rent-to-own purchases differ only slightly from credit and installment sales, and the desirable public policy goal of maintaining a competitive equilibrium among the various types of regulated business transactions in North Carolina, the N.C. Center for Public Policy Research recommends that the N.C. General Assembly adopt legislation regulating rent-to-own contracts as a separate type of sales transaction. This would impose the equivalent of an effective interest rate ceiling of 48.67 percent on rent-to-own contracts, giving the industry more than a 12 percent interest rate advantage over small loan companies, more than a 24 percent interest rate advantage over retail merchants, and more than a 30 percent interest rate advantage over bank credit card and other revolving charge account transactions.

The Center believes there are two reasons justifying a higher interest rate for rent-to-own transactions: (1) Such contracts include the cost of free servicing of the appliances or other items sold under the rent-to-own contract; and (2) the transactions involve customers who are greater credit risks than customers of other businesses. However, the Center could find no evidence that would justify interests rates as high as are currently allowed under North Carolina's system of token regulation of rent-to-own contracts. As William L. Rustin of the N.C. Retail Merchants Association puts it, "It would seem logical that this type of transaction, where equity changes from a seller to a buyer, should have some way to restrict the interest rate that is charged, and that rate should not be out of line with charges that

— continued on page 16

RECOMMENDATION

—continued

other businesses are restricted to in North Carolina."

The new law should require disclosure of all contract terms, require that at least 70 per cent of each rental contract payment be applied to the cost of the item rented, and direct the N.C. Attorney General to monitor rent-to-own transactions and report to the 1991 General Assembly. That report should gauge the industry's compliance with the law and make recommendations on whether interest rates should be reduced to match those of small loan companies (36 percent) or retail merchants (24 percent), or increased to ensure the viability of the industry.

Specifically, the law should require:

1. That consumers be told *in writing* the actual sales prices of the item they are renting-to-own, the total sum of the payments they will make to the dealer under the contract, and the effective annual interest rate equivalent that they will be charged.

2. That a minimum of 70 percent of each rent-to-own contract payment be credited to the consumer's ownership of the item (producing an effective equivalent interest rate cap of 48.67 percent on an 18-month contract); and

3. That the N.C. Attorney General be directed to monitor rent-to-own contracts to determine compliance with the new law, to determine whether there are abuses of the law, and to file a report to the 1991 Regular Session of the N.C. General Assembly on the status of the rent-to-own business in North Carolina, including recommendations on whether any further amendments are needed to correct abuses in the field or to ensure the industry's viability.

4. In addition, the N.C. General Assembly should adopt legislation to limit the use of the *criminal* courts as collection agencies for rent-to-own dealers. Rent-to-own dealers would continue to have full access to civil courts for past-due collection procedures, as other lenders have under current law, and would still have access to criminal courts where there is evidence of commission of a crime in the unauthorized disposal of rental property.

—Jack Betts
N.C. Center for Public Policy Research

Greg Gibson

Old Enough to Drive a Car, Old Enough to Drive a Bus?

by David S. Perkins

Since the end of the Great Depression, North Carolina has allowed almost anyone with a bus driver's license and a few months' experience to drive a school bus. But nationally, many states have begun to raise the age for drivers of school buses. Now the U.S. Labor Department has decreed that North Carolina should join the ranks of those states requiring drivers to be at least 18 years old—but the N.C. General Assembly has to cough up $18.8 million to pay for more adult drivers. What's the state's safety record in school bus driving—and what other safety concerns should the 1988 legislature address?