



# the PRICE CAP TRAP in rent-to-own

**W**hat do prices do? “Prices impose the most effective kind of rationing—self-rationing,” according to Thomas Sowell, author of “Pricing 101,” published in the National Review Online, February 21, 2007 ([www.nationalreview.com](http://www.nationalreview.com)). “Why is rationing necessary? Because what everybody wants usually adds up to more than there is.”

“It doesn’t matter whether you are talking about a capitalist economy, a socialist economy, a feudal economy or whatever. Resources are limited but desires are not. That is the basic and defining problem of economics.”

“Prices force you to limit your claims on what other people have produced to the value of what you have produced for other people. Prices force you to limit how much of product A you buy because you need to keep some money to buy product B.”

“While prices convey these limitations, they do not cause them. No economy—capitalist, socialist, feudal or whatever—can keep consuming more than it produces. Producing more of product A means using up resources needed to produce product B.”

“Simple and obvious as all of this may seem, politicians blithely ignore it when they promise to make the prices of housing or health care or other things ‘reasonable’ or ‘affordable.’”

By Ed Winn III



**D**espite the futility of government efforts to correct various perceived societal ills and inequalities by fixing prices, governments continue to do it. The notion has an undeniable, albeit illogical, appeal to many people, especially consumers. It especially appeals

to people who do not have to make payrolls and who otherwise favor big government as the answer to society's shortcomings.

The latest example of price fixing in the rent-to-own context comes from California. California rental dealers ultimately acquiesced to this scheme because they were being threatened with ruinous litigation from the attorney general in the state and from the plaintiff's bar as well.

California is hardly the first state to deem price controls an appropriate response to the perceived abuses of rent-to-own. The very first state rental-purchase statute, enacted in Michigan in 1984, imposed a price cap on the total RTO price of 2.2 times the cash price, and the history of state regulation of rent-to-own ever since has been a battle over, among other things, RTO pricing, which opponents repeatedly insist is "too high."

There are two different levels of prices that have been fixed here and there in the RTO industry: the cash price and the total RTO price. Politicians have seen fit to fix both. Early on, when negotiating state rental-purchase legislation, rental dealers resisted the mandatory disclosure of cash

prices at all. Dealers argued that they never actually sold any merchandise for cash and that

Statutory limits on cash prices*	
Computers and appliances	1.65
Electronics	1.7
Auto, jewelry, furniture and music	1.9
Other	1.9

the cash price was irrelevant to the RTO transaction. Opponents argued that the cash price was an important disclosure to allow consumers to comparison shop and to understand how much more than retail the RTO transaction cost. Disclosing the cash price was an

issue for rental dealers, but it was never the issue for rental dealers. Getting legal recognition of the transaction was always the issue for dealers and in exchange for that legal recognition, dealers agreed to make numerous disclosures, including the cash price of the merchandise in most states. To date, only 10 of the 47 states with rental-purchase statutes do not require a cash price disclosure or some variant of it ("estimated fair market value" in Georgia; "retail value" in West Virginia).

Every state rental-purchase statute, on the other hand, requires disclosure of the total RTO price and the industry

has no quarrel with making this disclosure. Merely disclosing this amount is not enough, however, in 10 states where the total RTO price is fixed by law. These are the states with price caps on the total RTO price: California, Connecticut, Hawaii, Iowa, Maine, Michigan, New York, Ohio, Pennsylvania and West Virginia.

Most of these states have fixed the total rent-to-own price at two times the cash price (although in California it

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is at 2.25 times the cash price; in Michigan it is 2.2 times the cash price; and in West Virginia it is 2.4 times the cash price). Rental dealers in those 10 states face a Hobson's choice on some items in their stores. Suppose, for example, that the market rental rate for an item is \$100 per month. That means that the RTO marketplace is a competitive one with several rental stores in the trade area all battling it out for customers, the item is a popular, readily available one and rental dealers are charging, on average, \$100 per month for the item on an 18-month agreement. In order to write this agreement, a dealer would have to set the cash price for the item at \$900 by law (in a two-times-cash-price state). The dilemma for the dealers is that

\$900 may or may not approximate the real cash selling price for the item in that market at that time. Sometimes, with rapidly declining retail prices for certain electronics, the real cash selling price among retailers may have declined significantly below \$900. This can occur because the price cap inserted by the politicians is a wholly artificial one and has never borne any necessary relationship to real prices in the marketplace. Nor can it ever because the legislature swooped in to fix prices once 20 years ago in some cases and the price for some electronics is changing monthly, sometimes more often than that. Rental dealers, then, either must drop rental rates below market, which they cannot do for long without going out of business, or they must disclose an artificial cash price with the potential ill-will such inaccurate prices can cause. The goal of the price fix was to help consumers by holding down prices in RTO stores. The result, which is the result every time the government steps in to fix prices, has been skewed, inaccurate pricing information that is as likely to mislead consumers as it is to make products more affordable for them.

Statutory limits on cash prices*	
Appliances	2.0
Electronics	2.0
Furniture	2.0
Other	2.0

Unfortunately, there is no market fix once the legislature has done its damage. The only fix is to go back to the legislatures that thought it was such a good idea to fix prices in the first place and persuade them to unfix them so that the marketplace can do its job.

Fixing the total RTO price has not been enough for some states. Four of the 10 have also determined that fixing cash prices in RTO stores would further the cause of consumer protection in those states.

The first state to fix cash prices was West Virginia in 1994. Maine and Hawaii followed suit shortly thereafter, and most recently, California. All four states limit cash prices to a percentage over the rental dealer's wholesale cost. There is no uniformity among the states regarding where cash prices in RTO stores should be fixed. Politicians have not agreed as to the level at which RTO cash prices should be fixed, only that they should be fixed by law. The chart below shows the different levels at which cash prices have been fixed in the four states by category of goods.

Statutory limits on cash prices*	
Appliances	1.75
Electronics (less than \$150)	1.75
Electronics (more than \$150)	2.0
Furniture and jewelry	2.5
Other	2.0

Statutory limits on cash prices*	
Appliances	1.56
Electronics	1.56
Jewelry	1.82
Other	1.67

California's price fixing scheme is the most restrictive. The new California statue goes on to fix not only the prices of new goods, but the prices of used goods, as well, with a statutory depreciation formula. West Virginia has a similar depreciation formula for pricing used goods in RTO stores.

When the dual price caps are applied in these four states, the range of overall turns as a function of dealer cost that rental dealers can get looks like this:

- ▶ California: 1.65 x 2.25 = 3.71 turns; 1.9 x 2.25 = 4.27 turns
- ▶ Hawaii: 2 x 2 = 4.0 turns
- ▶ Maine: 1.75 x 2 = 3.0 turns; 2.5 x 2 = 5.0 turns
- ▶ West Virginia: 1.56 times 2.4 = 3.74 turns; 1.82 x 2.4 = 4.37 turns

**T**he buyers and sellers who make up the marketplace and who are responsible, finally, for producing, distributing, and consuming goods and services, understand that there is no free lunch. If only politicians could accept this fundamental economic truth, then maybe they would get out of the price fixing business once and for all and let those buyers and sellers set prices where they ought to be. ■

*Ed Winn III is APRO's general counsel. His e-mail address is edwinn@mwwmlaw.com*

**Thank you!**



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Thanks must also go to the more than 200 attendees who represented the rent-to-own industry before the U.S. Congress during the Legislative Conference.

APRO asks that the entire rent-to-own industry unite in supporting passage of HR 1767 and S 1012—the Consumer Rental-Purchase Agreement Act. Please communicate with U.S. House of Representatives and U.S. Senate members and urge them to co-sponsor this important federal legislation. For more information on this legislation, contact Richard May at 800/204-2776, ext. 103, rmay@aprovision.org; or visit rtohq.org.



\* All multiples are times the dealer cost, including freight and excluding rebates, discounts and the like.