

- 3) Specifies the parameters of the consumer's liability for loss of, or damage to, the property and those of permissible security deposits, and regulates the advertisement of rental-purchase agreements, including the sending of solicitation or other promotional materials. (CC §§ 1812.636-1812.641)
- 4) Establishes bright-line pricing caps for the cash price of the property and the total of payments under rental-purchase contracts, as specified. (CC § 1812.644 (b) and (c))

Existing law, Unlawful Contracts:

- 1) Provides generally that a contract is not lawful which is contrary to an express provision of law, to the policy of express law, or otherwise contrary to good morals. (CC §§ 1667-1670.8)
- 2) Provides for specified contracts which are considered as either void as against public policy or as unlawful. (Id.)

Existing law, the Health and Safety Code:

- 1) Establishes the Lockyer-Polanco-Farr Pet Protection Act, related to the retail sale of dogs and cats. Requires that pet dealers possess a permit in order to sell dogs and cats and provide consumers disclosures related to the pet, including breeder information, health records, and any known health condition. Requires that breeders maintain facilities and care requirements for pets. Specifies civil penalties for violating these sections. (Health and Safety Code (HSC) §§ 122125-122220)
- 2) Establishes the Polanco-Lockyer Pet Breeder Warranty Act, related to the sale of dogs by breeders. Defines a dog breeder as a person, firm, partnership, corporation that has sold, transferred or given away 20 or more dogs within one year that were bred and reared on the premises. Specifies information to disclose to the consumer, including records of diseases or illness. Requires dog breeders to maintain the health and safety of the dogs and prohibits them from knowingly selling a dog that is ill. (HSC §§ 122045-122110)
- 3) Prohibits pet stores from selling dogs or cats that are less than eight weeks old. (HSC § 122359)

This bill:

- 1) Establishes that a contract entered into on or after January 1, 2018 to transfer ownership of a dog or cat, in which ownership is contingent upon the making of payments over a period of time subsequent to the transfer of possession of the dog or cat, is void as against public policy.
- 2) Clarifies that Item #1) above does not apply to payments to repay an unsecured loan for the purchase of the dog or cat.

- 3) Establishes that a contract entered into on or after January 1, 2018 for the lease of a dog or cat, that provides for or offers the option of transferring ownership of the dog or cat at the end of the lease term, is void as against public policy.
- 4) Provides that, in addition to any other remedies provided by law, the consumer taking possession of a dog or cat transferred under the terms of a contract described in Item #1) or #3) above shall be deemed the owner of the dog or cat and shall be entitled to the return of all amounts he or she paid under the contract.

FISCAL EFFECT: This bill is not keyed fiscal by Legislative Counsel.

COMMENTS:

1. **Purpose.** This measure is sponsored by the American Society for the Prevention of Cruelty to Animals (ASPCA). According to the Author, consumer advocates and animal welfare advocates have raised concerns about a new kind of financing agreement being used by some pet stores in California that puts the safety and welfare of animals at risk—a contract where the consumer (often unwittingly) commits not to purchase, but to lease the desired dog or cat by making monthly payments that reflect near usurious financing fees to be charged that are predatory in nature. These are sometimes referred to as “puppy leasing agreements.”

As explained by the Author, existing California law regulates financial transactions to protect consumers under the KR-P Act and the Unruh Act. These laws provide specific requirements for the financing structure and disclosures that are intended to provide consumers with a better understanding of the transaction and prevent lending companies from charging usurious fees and interest on the transaction. Unfortunately, the puppy leasing agreements have not complied with these requirements. Furthermore, these laws do not anticipate these financing mechanisms would be utilized for a transaction involving a live animal. As such, existing law does not address the complexities of maintaining and caring for a companion animal, including the eventualities of sickness or death of the pet and the treatment and disposition of the pet in the case of default. This type of “good” is not appropriate for this type of financing due to these complexities and the need to ensure that the welfare of the animal, as well as the consumer, is protected.

As further explained by the Author, while the laws cited above should regulate these types of financial transactions, the puppy leasing companies have not complied with the disclosure, usury, and transparency requirements of the laws. Often times, families that lease these puppies and kittens pay twice, or even three times, the amount of the initial cost that the pet otherwise would have cost. A household with access to traditional credit outlets could avoid these additional usury costs. Given the emotional nature of purchasing a new pet, families often do not take the time to fully understand the financial implications of the transaction. Once the true cost is realized, these families must decide if they can keep their new furry friends, or if they have to cancel their contract. In the event of a default or cancellation, the future welfare of the pet is put into question given that the lending company has no interest in maintaining the pet.

This bill would help by specifying that financing schemes that do not immediately transfer full ownership of a pet to a buyer may not be utilized to finance the purchase of a dog or cat. The Author argues that by precluding these types of transactions, we can protect consumers from unscrupulous lending practices involving the purchase of a pet and reduce the potential that the puppy, kitten or other animal will be relinquished to a shelter due to financial circumstances.

Furthermore, as stated by the Author, these laws do not anticipate these financing mechanisms would be utilized for a transaction involving a live animal. As such, existing law does not address the complexities of maintaining and caring for a companion animal, including the eventualities of sickness or death of the pet and the treatment and disposition of the pet in the case of default. Leasing or renting pets has become an increasingly common practice, but it comes at a high price, both financially and emotionally. This type of “good” is not appropriate for this type of financing due to these complexities and the need to ensure that the welfare of the animal, as well as the consumer, is protected.

2. Background.

- a) **Regulation of usury laws, retail installment contracts and rent-to-own agreements, generally.** Usury is defined by Black's Law Dictionary (5th Ed.) as an unconscionable and exorbitant rate or amount of interest, and a usurious loan is one whose interest rates are determined to be in excess of those permitted by a jurisdiction's usury laws. Under the California Constitution, the interest rate limit for sales contracts is 12 percent, while the interest rate on judgments is limited to 7 percent. (Cal. Const. Article XV, Sec. 1.) However, there are many exceptions to the usury laws, including for large banks and financial institutions, as well as for certain loans secured by real property. In addition, if a consumer expressly agrees to an interest rate higher than the statutory limit, then they effectively waive these protections. As a result, many consumer contracts (including virtually all credit card agreements) legally employ interest rates that exceed these limits.

Existing law, the California Retail Installment Sales Act, generally known as the Unruh Act (not to be confused with the Unruh Civil Rights Act, Section 51 of the Civil Code), regulates consumer retail installment contracts for the sale of personal goods and services on time and revolving charge accounts. Generally speaking, the Unruh Act governs contracts that provide for the purchase to be paid in four or more installments, or which impose a finance charge, higher price, or other cost to the buyer in exchange for deferred payment. As originally enacted, the Unruh Act limited the interest rate that could be charged under such contracts, but those restrictions were removed in 1988 and no such restrictions exist today in California (although they do in other states).

Rent-to-own (RTO) contracts, also known as rental-purchase contracts, differ from retail installment contracts because there is a lessor-lessee relationship established until the lessee ultimately purchases the property, either by making all of the required monthly payments or by exercising an option to purchase the property before the scheduled end of the lease term, pursuant to the terms of the contract. Existing law, the KR-P Act governs consumer rental transactions of

property for personal, household, or family purposes in which the renter has the option to apply a portion of the rent toward purchase of the property. In 2006, the Legislature enacted AB 594 (Ch. 410, Stats. 2006) to amend the KR-P Act to establish bright-line pricing limits that cap the cash price of the property and the total amount of payments that can be required under RTO contracts. RTO contracts are leases also subject to regulation under the federal Consumer Leasing Act.

b) **Recent reports of consumer experiences with pet leasing contracts raise significant consumer protection concerns.** According to the Author, the type of financing agreements for pet ownership identified by consumer advocates and highlighted in recent media reports are structured as leasing agreements rather than as lending agreements--in order to circumvent usury laws that cap what lenders can charge consumers—resulting in troubling examples of consumers charged exorbitant amounts beyond the cash price of the pet. The Author cites a number of accounts appearing in recent media articles describing the experiences of consumers who, knowingly or unknowingly, entered into a leasing agreement for a pet dog or cat at extremely high rates of financing:

- One family thought they had bought a dog for \$2,400 from a San Diego-area pet store, but without realizing it, had agreed to make 34 monthly lease payments of \$165, after which they had the right to buy the dog for a balloon payment of about two months' rent. Under the lease agreement, they would have paid the equivalent of more than 70 percent in annualized interest—nearly twice what credit card lenders charge. In addition, the lender could take back the dog if a payment was missed, and the family would be on the hook for an early repayment charge if the dog ran away or died. (Patrick Clark, "I'm Renting a Dog?" *Bloomberg* (March 1, 2017).
- Another family from Oceanside who entered into a leasing contract for a puppy that required 27 monthly payments totaling \$2,687, after which they had the right to pay \$93.52 to end the lease or twice that amount (\$187.04) to purchase the pet, plus additional fees and taxes. The pet store's initial asking price for the puppy in this case was just \$495. The family asserted that no store employees explained they were signing up for a lease rather than a purchase, and ultimately they returned to the store the day after taking the dog home and cancelled the contract. (Ashly McGlone, "Couple shocked at 'dog lease' deal." *San Diego Union-Tribune* (November 28, 2014.)

In both cases, the financing agreement offered at the pet store was through a company called Wags Lending, perhaps the most well-known of several companies that offer these types of financing agreements through pet stores in California. Started in 2013, Wags Lending was reportedly already used by 350 pet retail stores and breeders in 40 states by its first year of operation. According to a Bloomberg writer, Wags Lending charges effective interest rates ranging from about 36 percent to 170 percent on an annualized basis, based on sample rates published on its website. This fact is not immediately apparent because Wags doesn't show its pricing in terms of Annual Percentage Rate, since it asserts it is underwriting leases, not loans. Importantly, because the contracts at issue in this bill are deliberately structured as lease agreements rather than loan

agreements, they are not subject to usury laws or other laws regulating lenders, and this is true not only in California but likely in many other states where these contracts are being used.

According to the Author (referring to Wags Lending), the primary lending company engaged in this type of financing states that the company focuses the financing in underserved communities with little or no access to credit. Additionally, (the CEO) has stated that the financing is targeted to the purchase of goods that are highly emotional in nature. The predatory nature of the financing scheme raises a number of consumer protection issues. If a buyer could simply purchase the pet on a traditional credit card, they could avoid a large proportion of the cost. Instead, for many low income or uninformed buyers, this becomes an unscrupulous financing scheme that could result in financial strains requiring the consumer to default

The Assembly Judiciary Committee's analysis dated April 4, 2017, refers to passages in the *Bloomberg* and *San Diego Union-Tribune* articles, cited above, including comments made by the CEO and founder of Wags Lending, to support the following contentions made by the Author. First, the closed-end lease model was selected from a number of different credit models under consideration specifically because it is exempt from usury laws in all 50 states. Second, the company's leasing agreements are intended to target consumers who don't have access to other forms of credit but still wish to acquire an expensive dog or cat by financing its purchase. And third, that the company specifically targets pet consumers (usually more expensive purebred animals) because of the emotional aspect of the purchase (quoting the CEO as saying "We like niches where we're dealing with emotional borrowers" to explain the types of purchases the parent company of Wags Lending chooses to finance.)

At the time of the Assembly Judiciary Committee analysis, the Committee had not received correspondence from Wags Lending or any other companies who offer pet leasing agreements. In the interest of balance, however, Committee staff noted that, in the same articles cited by the Author, Wags Lending has defended its business practices from charges that they are predatory in nature. Specifically, Wags Lending has contended that: (1) it is transparent in its advertising and its contracts about the leasing structure of these agreements, and that any consumer who entered into such a contract without realizing he or she was leasing-to-own the pet rather than purchasing it outright bears responsibility for signing the contract without reading it first; (2) it offers consumers with credit limitations a way to finance the purchase of an expensive purebred dog or cat that simply can't be found at animal shelters; and (3) it complies with all applicable federal and state leasing laws, and even offers a money-back guarantee for the first 30 days.

- c) **Pet leasing contracts may also threaten the safety and welfare of the animal.** Whether these types of financing agreements are better regulated as loans rather than leases, the proponents of the bill take the broader view that leases for dogs and cats should be deemed void against public policy because of the threat to animal welfare that they may create. Specifically, they contend that the repossession or potential repossession of pet dogs or cats pursuant to a

lease contract creates unique animal welfare concerns that don't arise with respect to furniture, appliances or other inanimate forms of property, and therefore it should be against the public policy of California to allow rent-to-own contracts for dogs and cats.

Pet leasing agreements specifically contemplate several ways in which the pet could end up back in the possession of the lessor. First, the lessor may repossess the animal if the consumer defaults on the lease payments (increasingly likely given that the consumer presumably could not afford to buy the pet outright for the initial store price). Second, even if the consumer makes all the required monthly lease payments, he or she may decline to exercise the option to purchase the animal—effectively returning the pet to the lessor or financing company. Finally, the lessor may unilaterally repossess the pet if conditions of the lease are violated (e.g. it learns the animal is being mistreated or not being cared for properly).

According to the proponents, the pet store that initially housed the dog or cat is no longer party to the transaction once the lease agreement is effective, and it is not unusual for the financing company to have assigned the contract to a third party company that primarily specializes in managing or collecting on debt obligations. Under these circumstances, what is to happen to the pet when the lease is terminated or expires?

According to the articles cited by the Author, Wags Lending says that return of pets after the full term of the contract is rare, and that it does take steps to find new homes for pets in cases where the lease was ended early, including trying to convince the pet store to take back the pet. However, as discussed above, it is hard to assess what remarketed value or diminished "realized value" the asset has after repossession when the asset is a dog or cat that has been separated from the family it lived with for months or years previously.

Furthermore, a financing company or debt collection company is not in the business of re-homing pets or reselling them on the market, so it is conceivable and even likely that such pets will unfortunately end up being relinquished to animal shelters if they cannot be resold or found a new home by the company repossessing them.

- 3. Arguments in Support.** The sponsors of this bill, the ASPCA, argue that the cost to purchase a puppy or kitten from a retailer or breeder can be costly. In some cases, the cost can rise to as high as several thousands of dollars. As a result, a developing trend has been to offer consumers financing options that make adopting a new pet appear to be more accessible. One such company partners with pet retailers to offer consumers puppy leasing options akin to a "rent-to-own" scheme. The structure is much like a car lease, in which the consumer pays fixed monthly payments and is then given the opportunity to purchase the puppy, kitten, or other pet at the end of the term by making a balloon payment. At the end of the lease term, the lessee may have paid twice or even three times the amount of the initial cost that the pet otherwise would have cost.

The ASPCA states that unlike other common forms of financing, the company has structured the financing so that there are no restrictions on the fees or interest that are charged, otherwise known as usurious financing rates. The structure of the financing raises a number of ethical questions. The primary lending company engaged in this type of financing states that the company focuses the financing in underserved communities with little or no access to credit. Additionally, the CEO of the company has stated that the financing is targeted to the purchase of goods that are highly emotional in nature. As a result of these factors, it is not surprising that 12 percent of their customers default or fail to live up to their deals. That figure is nearly six times greater than the national average for all delinquent commercial loans for the last quarter of 2015. According to the Federal Reserve, that figure is 2.19 percent. At the height of the mortgage crisis, the home delinquent rate in the first quarter of 2010 was 11.2 percent.

The ASPCA further states that the predatory nature of the financing scheme raises a number of consumer protection issues. If a buyer could simply purchase the pet on a traditional credit card, they could avoid a large proportion of the cost. Instead, for many low income or uninformed buyers, this becomes an unscrupulous financing scheme that could result in financial strains requiring the consumer to default and ultimately, creating long term damage to credit the credit of consumers.

The ASPCA also indicates that the probability of default leads to a second ethical question about what happens to the new pet if the consumer can no longer afford payments. The contract between the lending company and consumer fully removes the pet store from the transaction. As such, the likely answer in the case of default is that the animal will get relinquished to a shelter, further increasing the already outsized shelter population in California.

The Humane Society of the United States (HSUS), the San Diego Humane Society and Social Compassion in Legislation are also in support of this measure for the reasons as stated above and are seriously concerned about this detrimental form of financing that is contrary to public policy, in that allows usurious fees to be charged to the consumer, is predatory in nature, and puts the safety and welfare of animals at risk. Unlike other common forms of financing, companies that provide these arrangements have structured the financing so that there is no restriction on the fees or interest that are charged. These deficiencies are unique among similar financing mechanisms found in California law and do not provide consumers with a clear understanding of the transaction and does not prevent these lending companies from charging usurious fees. In addition to these significant deficiencies in the financing scheme, existing law does not anticipate that a leasing mechanism would be utilized for a transaction involving a live animal. Therefore, it does not address the complexities of maintaining and caring for a companion animal, including the eventualities of sickness or death of the pet and the treatment and disposition of the pet in case of default. As such, the practice of leasing should be prohibited in order to ensure that the welfare of the animal is protected.

NOTE: Double-referral to Senate Committee on Judiciary, second.

SUPPORT AND OPPOSITION:

Support:

American Society for the Prevention of Cruelty to Animals (Sponsor)
Humane Society of the United States
San Diego Humane Society
State Humane Association of California
Social Compassion in Legislation

Opposition:

None on file as of June 13, 2017.

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