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By email: christian.mikula at treasury.gov.au

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Dear Christian

Consumer Lease reform

We welcome the opportunity to contribute to the proposed reforms of disclosure and early termination fees in consumer lease contracts.

Briefly, this submission argues that:

- there is no difference between a consumer lease which is structured and marketed as a rent-to-own arrangement and a credit contract;
- the purported benefits of consumer leases (compared to credit contracts) are generally non-existent;
- there is no sound argument why consumer lease providers should not have to disclose the cash value of goods for lease, the total value of the lease and a comparison interest rate;
- we do not support Treasury's proposed formula for calculating early termination fees. We suggest the formula should be based on a pre-estimate of the lessor's administrative and collection costs.

About Consumer Action

Consumer Action is an independent, not-for-profit, campaign-focused casework and policy organisation. Consumer Action offers free legal advice, pursues consumer litigation and provides financial counselling to vulnerable and disadvantaged consumers across Victoria. Consumer Action is also a nationally-recognised and influential policy and research body, pursuing a law reform agenda across a range of important consumer issues at a governmental level, in the media, and in the community directly.

The argument for price disclosure and purported differences between consumer leases and credit contracts

Consumer lease providers at the last consultation group meeting argued that consumer leases are different to credit contracts and so should not be required to disclose cost in the same way.

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We strongly disagree. To the extent that consumer leases are structured and marketed as a 'rent-to-own' arrangement, there is absolutely no difference between a lease and a credit contract. In each situation, a consumer enters a contract intending to own goods, and pays a price in excess of the cash value of those goods in instalments determined by contract.

Consumer lease providers represented at the consultation group (Radio Rentals, Rent the Roo and Flexirent) use deliberate and considered strategies to attract customers by promising an opportunity to own goods—that is, to make their service seem like a credit contract. For example, Radio Rentals heavily promotes its "rent try buy" arrangement; the website of Rent the Roo states its "exclusive Give-a-way offer lets you keep the item at the end of the rental agreement"; and Flexirent has "Flexikeep" which states "pay an optional payment equivalent to one monthly rental payment and keep the rental equipment forever". For these lease providers to then argue that their services are not at all like credit contracts is frankly disingenuous.

Even where lessors do not publicly offer rent-to-buy arrangements (or where a consumer intends to return leased goods at the end of the term), lessors market their service as a better option than buying. It is only reasonable that lessors making this kind of claim are upfront about the cost of their leases to allow consumers to make an informed decision about the benefits of a lease agreement compared to a credit contract.

The argued benefits of consumer leases

Part of the argument that fixed term consumer leases are different to credit contracts is that leases have a number of benefits that credit contracts do not. However, these purported benefits are of marginal value or completely non-existent.

Purported benefit: the consumer has the freedom to hand goods the goods back if they no longer want them.

Most consumer leases offer no such flexibility. Prices quoted by lease providers are only available if consumer agrees to rent the goods for a minimum term (usually 1-3 years). The consumer must pay termination fees if they wish to hand the goods back before the end of the term.

Purported Benefit: the consumer has the ability to 'upgrade' to new goods as old goods become obsolete

A consumer has a very similar ability to 'upgrade' if they buy the goods through a credit contract as they do if they lease them. Lessors generally only allow consumers to upgrade once they have completed the minimum lease term. After completing the minimum term, the consumer will have paid the same or more than if they had bought those goods on a credit contract. Whether the consumer enters a lease or a credit contract, they are free to 'upgrade' once they have made the number of payments required by the contract but not before.

Buying on credit will actually be advantageous in many cases because selling the goods second hand allows the consumer to offset the cost of upgrading with the sale price of the old goods. We doubt the consumer would be any better off even under a lease arrangement where the lessor gives a 25% discount of the cost of new lease if they agree to upgrade (as mentioned by the discussion paper).

Purported benefit: consumer leases are an accessible, low cost form of finance for those who are not eligible for credit.

A consumer lease is not 'low cost'—to our knowledge, leasing household goods for a minimum term will commonly require the consumer to pay around twice the ticket price available for paying cash. We have seen consumer lease contracts that have annualised interest rates of between 35 and 150 per cent.

Further, we do not see why a consumer lease should be any more accessible to a low income consumer than a credit contract. A person who cannot afford to buy household goods through a credit contract presumably could afford lease payments for the same goods either (assuming the term of the credit contract and lease are similar).

Purported benefit: consumer lease providers will replace goods which are faulty or break down.

This is no different to buying goods on credit or for cash. The consumer guarantees provisions in the Australian Consumer Law and the ASIC Act give consumers right to a refund, repair or replacement where goods do not meet minimum standards. We doubt any lease provider is offering service above that already required by the law.

Purported Benefit: consumer lease contracts come with insurance for accidental damage and theft.

Insurance may be of value to the extent that it is less expensive or more accessible than cover a consumer could access themselves.

However, this feature may be of no benefit whatsoever. We note that RentSmart's terms and conditions require lessees to 'take out and maintain property insurance against your liability for loss or damage to the Equipment for all risks and for its replacement value'¹ despite claiming that one of the benefits of renting with Rentsmart is that 'you have cover for equipment loss, accidental damage and theft'.² It is unclear to us what benefit RentSmart's cover provides if a consumer is also required to purchase their own insurance which (presumably) covers the same risks.

Disclosure of cash value of leased goods

Consumer lease providers at Treasury's last consultation meeting made several arguments why they should not be required to disclose cash value of leased goods. None in our view are persuasive.

Assertion: Cash value is irrelevant because consumers are only interested in the price per week

We agree with Treasury that this argument is absurd. It suggests that consumers have no interest in to total cost they are paying to access goods.

Assertion: Cash value is irrelevant because consumers do not want to own the leased goods.

Radio Rentals, Rent the Roo and FlexiRent (as well as other lessors) all prominently promote rent-to-own arrangements, not only short-term leases where products are handed back to the

¹ Clause 11(a). Accessed on 1 November 2012 from <http://www.rentsmart.com.au/Terms-and-Conditions>

² See RentSmart's website at <http://www.rentsmart.com.au/Personal>. Accessed 1 November 2012.

lessor. It seems implausible that there would be so many firms promoting this service if it didn't attract customers.

Assertion: It is not necessary to disclose the cash value of goods as consumers will have shopped around and will already know the value of those goods.

We agree that most consumers know the range of prices available before making a purchase. However, it is still necessary to disclose the cash price of leased goods in order to plainly show the premium being charged by the lease provider and allow consumers to make an informed choice about whether a lease is the best option for them.

Assertion: There are difficulties in assessing cash value of the goods, especially second hand goods or goods not sold by other Australian suppliers.

We agree with Treasury that it should be relatively simple to attach a value in good faith to any new goods leased. It should also be quite possible for to value second hand goods. We would expect that firms who lease second hand goods already have a method of valuing these goods for their own accounting purposes.

Disclosing total cost and comparison interest rate

We agree that once the cash value of leased goods is able to be determined, there should be no obstacle to providing a comparison interest rate. We also agree that where a contract offers ancillary services (such as internet access, repayment waivers, insurance or extended warranties) the costs of those services should be disclosed where the consumer has a choice of whether to not to buy them.

Broadly, we believe that both the total cost of fixed term lease and a comparison interest rate should be disclosed. A consumer cannot be expected to make an informed choice to buy goods from a particular trader unless the total price is disclosed. Nor could it be said that a lease meets the consumer's purpose and objectives (for the purposes of a responsible lending assessment) unless the consumer is aware of the cost of the lease when they apply for it.

A comparison rate is necessary to compare the cost of leasing goods with the cost of buying the same goods on credit. As we have argued already, a rent to own arrangement is no different to a credit contract, so a standard measure of cost of credit should be available to consumers to compare cost between credit and rent to own offers. Even where the consumer does not intend to own the leased goods (for example, if they plan to lease a computer for two years, return it and upgrade), they should be able to compare the cost of leasing with buying on credit to allow them to make an informed choice.

Early termination fee formula

Treasury has proposed that a termination fee formula would be 'based on present value of future payments, less an offset for early return of goods'. We do not support this kind of approach. The purpose of a termination fee should be to allow an innocent party to recoup losses caused by a the other party's breach, not to recoup value of the remainder of the contract (less offsets).³

³ We note that Consumer Affairs Victoria considered how a fair formula for early termination fees might be calculated in a 2010 paper *Options for Fair Early Termination Fees in Consumer Contracts*

A formula based on present value of future payments is likely to allow termination fees that are out of all proportion to the damage likely to be suffered by the lessor and so amount to a penalty. The formula creates this risk because it considers elements that are not directly relevant to losses incurred by the lessor (the future payments) and ignores elements that are relevant (administrative costs related to termination, for example).

The termination fee formula should be based on a genuine pre-estimate of the administrative and collection costs incurred by the lessor. This kind of formula could also include reference to 'wasted costs' such as front-end inducements offered by the lessor that they have not been recovered at the time of termination. This is far less likely to result in a fee that is out of all proportions to the lessor's loss because the formula is actually focused on calculating that loss.

It is likely that the formula in the regulations will displace the common law doctrine of penalty and statutory unfair contract terms protections to the extent that they apply to these particular fees. If there is any significant risk that the formula will provide less protection than the law relating to penalties and unfair contract terms law currently does, we suggest it would be better to have no formula at all.

If Treasury wishes to go ahead with a formula based on present value of remaining payments, it should be offset against the resale or rehire value of the goods. The offset would also need to include any savings made by the lessor for not having to provide any additional services such as internet access (as noted by the discussion paper).

We also recommend that a formula based present value should be accompanied by a fee cap to reduce the risk that the formula creates unconscionable fees. The cap could be expressed as a percentage of the total repayments remaining under the contract. It could either be a solid cap or create a presumption that a fee greater than the cap is a penalty or unfair contract term.

Please contact David Leermakers on 03 9670 5088 or at david@consumeraction.org.au if you have any questions about this submission.

Yours sincerely

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