
Sunset Evaluation Update: Pawnbrokers

A Report to the
Governor
and the
Legislature of
the State of
Hawaii

Submitted by

THE AUDITOR
STATE OF HAWAII

Report No. 94-9
September 1994

Foreword

This report evaluates the regulation of pawnbrokers under Chapter 445, Part V, Hawaii Revised Statutes. This evaluation and the repeal of this law had been scheduled under the Sunset Law. Subsequently, Act 279 of 1994 removed the repeal date and with it the evaluation requirement. Nevertheless, since the work had already been done, we are issuing the report to help decision-makers in assessing the regulatory program.

The report presents our findings as to whether the regulatory program complies with policies in the Sunset Law and whether there is a reasonable need to regulate pawnbrokers to protect the health, safety, and welfare of the public. It includes our recommendation on whether the program should be continued, modified, or repealed. In accordance with Section 26H-5, HRS, the Appendix incorporates the draft legislation to improve the program.

We acknowledge the cooperation and assistance of the various county finance and police officials, state agencies, and other persons and organizations whom we contacted during the course of our evaluation. We appreciate the assistance of the Legislative Reference Bureau, which drafted the recommended legislation.

Marion Higa
State Auditor

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Chapter 1

Introduction

The Sunset Law, or the Hawaii Regulatory Licensing Reform Act, Chapter 26H, Hawaii Revised Statutes, establishes policies for occupational licensing. The law directs the State Auditor to evaluate licensing statutes scheduled for repeal to determine whether the health, safety, and welfare of the public are best served by reenactment, modification, or repeal.

This report evaluates whether the regulation of pawnbrokers under Chapter 445, Part V, HRS, complies with policies for occupational licensing in the Sunset Law. After our work was substantially completed, Act 279 of 1994 removed the December 31, 1995, repeal date for Chapter 445, Part V and made the regulatory program permanent. However, we are still issuing the report to assist decision makers in assessing the regulatory program.

Background on Pawnbrokers

Typically, pawnbrokers make loans to customers who pledge their goods as security. They charge customers monthly interest rates that vary with the size of the loan and the regulations of the state. Pawnbrokers are also able to generate large revenues by selling unredeemed merchandise. Jewelry, audio and video products, musical instruments, firearms, and tools are the most commonly pawned items.¹

Pawnbrokers do not assess the credit risk of their customers because they lend only on the basis of collateral or the value of the item pawned. Any screening that is done simply ensures the customer owns the item being pledged. Pawnbrokers' efforts are directed more toward evaluating the value of the collateral. Once the value is determined, a cash loan is advanced upon the completion of the pawn transaction agreement.²

In 1991, there were about 6,900 pawnshops in the United States.³ Currently in Hawaii, there are 45 licensed pawnbrokers in Honolulu, 3 on the Big Island, 5 on Maui, and none on Kauai.⁴

Regulatory Program

Part V of Chapter 445, HRS, requires pawnbrokers to be licensed by the counties and provides the primary regulations over pawnbrokers. Part V requires that all pawn transaction agreements be in writing to document and clarify all aspects of the transaction for both the pawnbroker and the customer. The provisions set the amount allowable for the pawn finance charges and the amount of time the customer has to redeem the pledged

goods. The statutes also require that copies of all pawn transactions be kept on the premises one year after the maturity date; that pawn transaction agreements comply with the federal Truth-in-Lending Act; and that pawnbrokers comply with Chapter 486M, HRS. Chapter 486M regulates the purchase and resale of previously owned or secondhand goods and specifically applies to pawnbrokers.

Under the general provisions of Chapter 445, the county councils may enact ordinances consistent with state law to govern the conduct of certain businesses. The law authorizes the treasurer or finance director of the county where the business will operate to issue licenses and collect fees. It forbids those businesses from operating without a license and designates the county police and authorized representatives of the county directors of finance as license inspectors.

In Honolulu, where complaints against pawnbrokers have been most prevalent, the City and County Department of Finance has accepted primary enforcement jurisdiction over Chapter 445, Part V. The neighbor island counties have yet to identify or exercise enforcement jurisdiction over Chapter 445, Part V, since they have received no complaints against pawnbrokers.

The Office of Consumer Protection, within the State Department of Commerce and Consumer Affairs, has jurisdiction over pawnbrokers through Section 480-2, HRS, to the extent that their acts or practices amount to unfair or deceptive trade practices. The Legal Aid Society of Hawaii and private attorneys also handle pawnbroker cases for violations of Section 480-2 and Chapter 445, Part V. The police have jurisdiction to enforce Chapter 486M, which provides a criminal penalty (misdemeanor) for violations relating to secondhand goods.

Previous Sunset Report

Our 1991 report on auctions, pawnbrokers, secondhand dealers, and scrap dealers recommended that the Legislature return control over licensure of these businesses to the counties.⁵ We also recommended removing their regulation from the sunset schedule.

The Legislature returned control over the licensing of auctions, secondhand dealers, and scrap dealers to the counties, and removed them from the sunset schedule. However, for pawnbrokers, the Legislature maintained licensure by the counties and inclusion in the sunset schedule.

In 1992, the Legislature found problems with Part V and enacted significant amendments to it. The Legislature took note of a federal court ruling in 1991 that determined that typical sale transactions by pawnbrokers were actually loans subject to the required disclosures of the federal Truth-in-Lending Act. Pawnbrokers were engaging in these sales

with buy-back options and buy-back fees because the interest rate set for pawn transactions in the law had not been sufficient to cover their costs and make a reasonable profit. These transactions, however, did not guarantee customers the ability to re-purchase their goods. Thus, the legislative purpose of the amendments was to establish a new statutory scheme where pawnbrokers could expect a reasonable profit and customers could expect to recover their possessions.

Objectives of the Evaluation

This evaluation sought to determine whether the regulation of pawnbrokers complies with the policies in the Sunset Law. Specifically, the objectives were to:

1. Determine whether there is a reasonable need to regulate pawnbrokers to protect the health, safety, and welfare of the public;
2. Determine whether current regulatory requirements are appropriate for protecting the public;
3. Establish whether the regulatory program is being implemented effectively and efficiently; and
4. Make recommendations based on findings in these areas.

Scope and Methodology

To accomplish these objectives, we reviewed literature on pawnbrokers and their regulation. We reviewed the statutes on pawnbrokers in Hawaii, as well as those of other states, and the changes that have taken place since our 1991 sunset evaluation. We interviewed personnel from the finance and police departments of the counties of Honolulu, Maui, Kauai, and Hawaii; Department of Commerce and Consumer Affairs; Better Business Bureau of Hawaii; and Legal Aid Society of Hawaii. We also interviewed members of the National Pawnbrokers Association and the Hawaii Pawnbroker and Secondhand Dealers Association. We reviewed complaint files at the Office of Consumer Protection.

Our work was performed from January 1994 through June 1994 in accordance with generally accepted government auditing standards.

Chapter 2

Findings and Recommendations

We recommend that pawnbrokers continue to be licensed by the counties pursuant to Chapter 445, Part V, Hawaii Revised Statutes. In 1992, the Legislature made major amendments to the law. We recommend that the Legislature further amend the law to prohibit certain convicted felons from obtaining licensure.

Summary of Findings

1. There is a need to continue the licensing of pawnbrokers to protect the public's welfare.
2. A person convicted of a felony directly relating to the person's possible performance as a pawnbroker should not hold a pawnbroker's license. A criminal history check should be required prior to licensing.

Counties Should Continue to Regulate Pawnbrokers

Chapter 445, Part V, should be continued to regulate pawnbrokers. Pawnbrokers engage in transactions that could be financially harmful to the public. Licensure of pawnbrokers also assists the county police departments in locating and monitoring pawnbrokers to prevent the trafficking of stolen property.

Pawnbrokers can cause financial harm

Pawnbrokers have the potential to engage in activities that are financially harmful to the public. Pawnshops, one of many types of financial entities that lend money to consumers, are of concern for two main reasons. First, pawnbrokers lend money to persons who are excluded from mainstream financial markets—generally poorer and more vulnerable customers.¹ Second, interest and other charges are much higher than those for other types of loans.²

Pawnshop customers are considered to be high credit risks and are therefore unable to borrow from mainstream lenders on an unsecured basis. They often require very small loans that mainstream lenders will not provide even on a secured basis. (In contrast, pawnbrokers allow borrowers to leave personal property with them as collateral for small loans.) Those who are excluded from mainstream consumer credit sources are believed to be poor and poorly educated and are more likely to have unstable income and employment.³

According to an attorney at the Legal Aid Society of Hawaii, it is often difficult for customers to file suits against pawnbrokers. This is because customers who resort to pawning their belongings are poor, do not have much clout, and are sometimes intimidated by the pawnbroker.

Pawnbrokers charge high rates. Interest rates for pawnbrokers and other lenders vary greatly under the law. For example, under Section 478-4, HRS, financial institutions (other than a trust company or credit union) may charge interest not exceeding 2 percent a month or 24 percent a year for a consumer credit transaction. Credit card agreements may have an interest rate of not more than 18 percent a year. Pawnbrokers, however, are allowed to charge an interest rate of 20 percent a month or 240 percent a year.

Complaints support the need for licensure

In Hawaii, from 1987 to the present, 31 complaints against pawnbrokers were filed with the State Office of Consumer Protection. In one case, the complainant alleged that the respondent charged 20 percent to 40 percent monthly interest on loans (equivalent to 240 percent to 480 percent per year). In another case, the complainant alleged that he was unable to redeem his pawned items because the respondent closed her business and could not be located. In another case, the complainant alleged that his pawned item had been sold prior to the redemption date and he was unable to retrieve his property.

Complaints are also on record at Legal Aid. About 8 to 10 cases in the past several years involved pawnshops. Legal Aid has also referred a number of cases involving pawnbrokers to other agencies. Most of these cases originated in 1989 and 1990 and involved violations of the federal Truth-In-Lending Act, the law on unfair and deceptive trade practices, and the pawnbroker law. Three cases that originated in 1993 are presently ongoing. Court actions have already been filed for two of them. One involves a woman who claims that the stone in her ring was switched when she pawned her ring, and the other two allege non-compliance with the Truth-In-Lending disclosure law.

Since pawnbrokers typically cater to the poor, and the interest rates charged by pawnbrokers are much higher than those of financial institutions, attorneys at Legal Aid believe that pawnbrokers should be licensed and regulated.

Felons Convicted of Certain Crimes Should Not Hold a License

The purpose of licensing pawnbrokers is to prevent dishonest practices that could harm the public. Therefore, it is inappropriate to license a person convicted of a felony directly relating to the person's possible performance as a pawnbroker. Section 831-3.1, HRS, provides that the State or its political subdivisions may consider as a justification for the

refusal, suspension, or revocation of a license, any conviction of a penal offense that directly relates to the person's possible performance in the occupation licensed. The agency must first conduct an investigation in accordance with Chapter 91, HRS, to determine whether the person has been sufficiently rehabilitated to warrant public trust.

In licensing pawnbrokers, the counties should screen out those who have been dishonest in the past, since pawnbrokers have the opportunity to deal in stolen goods and may cause financial loss to consumers. The conviction of a felony for crimes such as theft, robbery, or extortion, which deal with property and involve dishonesty and harm, should constitute a ground upon which a license may be denied, suspended or revoked.

One of the two pawnbroker cases, for which Legal Aid filed legal actions in 1993, involves a convicted felon. The Legal Aid attorney handling the case believes that prohibiting felons convicted of crimes such as trafficking in stolen property or fraudulent schemes would help to prevent abuse in the pawnbroker trade.

Several other states prohibit convicted felons from holding a pawnbroker license. California, Missouri, Arizona, Texas, Oklahoma, and Alabama require that the conviction be for a crime directly relating to the duties and responsibilities of the occupation of pawnbrokers. Missouri and Texas specifically prohibit licensure for persons convicted of misdemeanors in addition to felonies. North Carolina and Louisiana prohibit any felon convicted within the last ten years from obtaining licensure.

Chapter 445, Part V, HRS, should be amended to allow the counties to deny, suspend, or revoke a license based on a conviction of a felony directly relating to the possible performance of the felon as a pawnbroker. A denial, suspension, or revocation based on a conviction of a felony must be performed in accordance with the requirements of Section 831-3.1, HRS.

A criminal history check is needed

If the law is amended to prohibit certain felons from holding a pawnbroker license, a criminal history check of applicants for licensure or relicensure would be needed. The Hawaii Criminal Justice Data Center, within the Department of the Attorney General, keeps records of criminal convictions in Hawaii and makes information on convictions available to the public.

The Honolulu Liquor Commission already uses the services of the center to screen applicants for licensure to sell liquor. Convicted felons are prohibited by statute from obtaining a liquor license. Each license applicant fills out a request form that the commission sends to the data center. The data center does the criminal history check and mails the results to the commission in about two weeks. The center currently does

not charge the commission for this service. The various county Departments of Finance could work with the data center to develop procedures to conduct criminal history checks which would accommodate the departments and the data center.

Recommendations

1. The Legislature should continue the regulation of pawnbrokers in Chapter 445, Part V, Hawaii Revised Statutes.
2. The Legislature should amend Part V to allow the counties to deny, suspend, or revoke a pawnbroker license for persons convicted of a felony that relates directly to the person's possible performance as a pawnbroker. A criminal history check should be conducted before a license is issued or reissued.

Notes

Chapter 1

1. Michael Hartnett, "Pawnshops With Panache," *Entrepreneur Magazine*, October 1988, p. 64.
2. John P. Caskey and Brian J. Zikmund, "Pawnshops: The Consumer's Lender of Last Resort," *Federal Reserve Bank of Kansas City Economic Review*, March/April 1990, p. 11.
3. *Ibid.*, p. 8.
4. Information provided by the various county finance directors.
5. Hawaii, Office of the Auditor, *Sunset Evaluation Report: Auctions, Pawnbrokers, Secondhand Dealers, and Scrap Dealers*, Report No. 91-19, Honolulu, December 1991.

Chapter 2

1. John P. Caskey and Brian J. Zikmund, "Pawnshops: The Consumer's Lender of Last Resort," *Federal Reserve Bank of Kansas City Economic Review*, March/April 1990, p. 6.
2. *Ibid.*, p. 11.
3. *Ibid.*, p. 6.

Responses of the Affected Agencies

Comments on Agency Responses

We transmitted a draft of this report to the City and County of Honolulu and the counties of Hawaii, Maui, and Kauai on July 27, 1994. A copy of the transmittal letter to the City and County of Honolulu is included as Attachment 1. Similar letters were sent to the other counties. The City and County of Honolulu submitted a written response which is included as Attachment 2. The counties of Kauai, Maui, and Hawaii did not respond.

The City and County of Honolulu concurs with our recommendation that pawnbrokers continue to be licensed by the counties pursuant to Chapter 445, Part V, Hawaii Revised Statutes, and that the statutes be amended to allow the counties to deny a pawnbroker license to persons convicted of a felony that relates directly to the person's possible performance as a pawnbroker.

ATTACHMENT 1

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917



MARION M. HIGA
State Auditor

(808) 587-0800
FAX: (808) 587-0830

July 27, 1994

COPY

The Honorable Jeremy Harris, Acting Mayor
City and County of Honolulu
Honolulu Hale
Honolulu, Hawaii 96813

Dear Mayor Harris:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Sunset Evaluation Update: Pawnbrokers*. We ask that you telephone us by Friday, July 29, 1994, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Friday, August 26, 1994.

The Mayors of the Counties of Hawaii, Maui, and Kauai; the Governor; and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

Marion M. Higa
State Auditor

Enclosures

CITY AND COUNTY OF HONOLULU

HONOLULU, HAWAII 96813

RECEIVED

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OFFICE OF THE AUDITOR
STATE OF HAWAII

RUSSELL W. MIYAKE
DIRECTOR

GLEN S. NONAKA
DEPUTY DIRECTOR

JEREMY HARRIS
FRANK F. PASTI
MAYOR



August 17, 1994

Ms. Marion M. Higa
State Auditor
Office of the Auditor
State of Hawaii
465 South King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

Since the licensing of pawnbrokers is the responsibility of the Department of Finance, Mayor Harris has asked that I respond to your letter of July 27 regarding your report, Sunset Evaluation Update: Pawnbrokers.

We concur that pawnbrokers should continue to be licensed by the counties and the counties be allowed to deny a pawnbroker license for persons convicted of a felony that relates directly to the person's possible performance as a pawnbroker.

To clarify the type of felony convictions and period of time such conviction will be held against an applicant, we recommend that the amendment to Chapter 445, Part V, HRS, name the specific crimes that would disqualify an applicant and the length of time between conviction and when the convicted person may subsequently apply for a license.

If you have any further questions concerning this matter, please contact Mr. Dennis Kamimura, Licensing Administrator, at 532-7793.

Sincerely,

GLEN S. NONAKA
Acting Director of Finance

GSN:bk

cc: Jeremy Harris, Mayor

Proposed Legislation

EIGHTEENTH LEGISLATURE, 1995
STATE OF HAWAII

A BILL FOR AN ACT

RELATING TO PAWNBROKERS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. Chapter 445, Hawaii Revised Statutes, is amended
2 by adding a new section to part V to be appropriately designated
3 and to read as follows:

4 "§445- Revocation, suspension, or denial of licenses.

5 (a) In addition to any other actions authorized by law, any
6 license to engage in business as a pawnbroker may be revoked,
7 suspended, or denied for a felony conviction, whether by nolo
8 contendere or otherwise, of a penal offense directly related to
9 the qualifications, functions, or duties of pawnbrokers. Such a
10 penal offense includes, but is not limited to, robbery, theft,
11 extortion, trafficking in stolen property, or fraudulent
12 transactions involving property.

13 (b) Any revocation, suspension, or denial of a license to
14 engage in business as a pawnbroker pursuant to this section shall
15 be made in accordance with section 831-3.1.

16 (c) The county director of finance, or the director's
17 representative, shall request a criminal history record check on
18 every applicant for licensure or relicensure to engage in
19 business as a pawnbroker in accordance with section 846- ."

1 SECTION 2. Chapter 846, Hawaii Revised Statutes, is amended
2 by adding a new section to part III to be appropriately
3 designated and to read as follows:

4 "§846- Pawnbrokers; criminal history record checks. (a)
5 The county director of finance, or the director's representative,
6 shall request a criminal history record check on every applicant
7 for licensure or relicensure to engage in business as a
8 pawnbroker. For the purposes of this section, "criminal history
9 record check" means an examination or search for evidence of an
10 individual's criminal history by means of:

11 (1) A search for the individual's fingerprints in the
12 national criminal history record files and, if found,
13 an analysis and any other information available
14 pertaining thereto; and

15 (2) A criminal history record check conducted by the
16 Hawaii criminal justice data center; provided that the
17 Hawaii criminal justice data center may charge a
18 reasonable fee for criminal history record checks
19 performed.

20 (b) The criminal history record check procedure shall
21 require the applicant to disclose whether:

22 (1) The applicant has been convicted in any jurisdiction of

1 a felony that directly relates to the qualifications,
2 functions, or duties of pawnbrokers as provided in
3 section 445- ; and

4 (2) The judgment of conviction has not been vacated.

5 (c) The criminal history disclosure made by the applicant
6 may be verified by the county director of finance, or the
7 director's representative, by means of information obtained
8 through the Hawaii criminal justice data center. The applicant
9 shall provide the Hawaii criminal justice data center with
10 personal identifying information which shall include, at a
11 minimum, the applicant's name, social security number, date of
12 birth, and sex. This information shall be secured only for the
13 purpose of conducting the criminal history record check
14 authorized by this section.

15 (d) The applicant shall submit to the county director of
16 finance, or the director's representative:

17 (1) A statement signed under penalty of perjury whether the
18 applicant for licensure or relicensure has ever been
19 convicted of a felony that directly relates to the
20 qualifications, functions, or duties of pawnbrokers as
21 provided in section 445- ;

22 (2) Written consent to the county director of finance, or

1 the director's representative, to request and obtain
2 criminal history record information for verification;
3 and

4 (3) Permission to be fingerprinted.

5 (e) The information obtained through the Hawaii criminal
6 justice data center on the applicant shall be used exclusively
7 for the stated purpose for which it was obtained and shall be
8 subject to applicable federal laws and regulations currently or
9 hereafter in effect."

10 SECTION 3. This Act does not affect rights and duties that
11 matured, penalties that were incurred, and proceedings that were
12 begun, before its effective date.

13 SECTION 4. New statutory material is underscored.

14 SECTION 5. This Act shall take effect upon its approval.

15

16

INTRODUCED BY: _____

17