



## **CRS Report for Congress**

# **Consumer Rental-Purchase (Rent-To-Own) Agreements**

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### **Summary**

A rent-to-own arrangement provides an alternative to purchasing merchandise. In a rent-to-own transaction (also known as a rental-purchase) the consumer agrees to a self-renewing weekly or monthly lease to rent a merchandise item. The terms of the lease include an option to purchase the item. Dealers in the rent-to-own industry typically offer high cost, durable, household items such as furniture, appliances, and home electronics. The industry attracts consumers who may have a hard time qualifying for credit, do not have enough cash for a purchase, and are unable or unwilling to wait and save for an item. The major downside to these arrangements is the final purchase price of the rent-to-own merchandise is much greater than the price of the same item bought from a retail store or financed over time.

Currently, rental-purchase transactions are not specifically regulated by federal law. For more than a decade, there has been considerable debate over the need for regulation of the rent-to-own industry. A recent Federal Trade Commission (FTC) survey provides insight into the experience of rent-to-own customers and consumer protection issues. Rent-to-own laws providing varying degrees of consumer protection have been enacted in 47 states. Legislative proposals for various forms of federal regulation have been introduced in the last several Congresses. In the 110<sup>th</sup> Congress, legislation (H.R. 1767) addressing rental-purchase transactions has been introduced. H.R. 1767 would define these transactions as lease agreements. In addition, the bill mandates disclosures and provides for federal regulation. The industry has been generally supportive of federal legislation that would provide a uniform regulatory framework and preclude states from applying credit laws to rental-purchase transactions. Consumer advocates have backed strong consumer protection proposals on both the federal and state level. They argue that rental-purchase transactions should be treated as credit sales.

This report gives background on the rent-to-own industry and the issues raised by rental-purchase agreements. Information on the FTC survey and the status of federal regulation and legislation is discussed. This report will be updated as warranted.

## Background

The rent-to-own industry provides a service directed toward consumers who do not have the cash to purchase high cost household products and who may be unable to get traditional credit (credit cards or store accounts). The rent-to-own industry can trace its origins to the 1960s and has grown rapidly. The Association of Progressive Rental Organizations (APRO) estimated that in 2005, there were 8,300 rent-to-own stores in the United States serving 2.7 million households. The industry's annual revenue was approximately \$6.6 billion.<sup>1</sup> The rental-purchase business was, initially, characterized by small regional chains and independent retailers that were facing increased competition from large electronic dealers and discount stores. There has been a significant consolidation in the industry. Most recently, in August 2006, the nation's largest operator Rent-A-Center, Inc. announced a merger with another national chain Rent-Way, Inc. In 2001 and 2002, Rent-A-Center was on *Fortune* magazine's list of the 100 fastest growing companies.

A rent-to-own arrangement provides a consumer with an alternative to buying merchandise. Rental-purchase items are typically high-cost household products such as furniture, large appliances, televisions, VCRs, stereos, and computers. Rental-purchase transactions are short-term (weekly or monthly), self-renewing leases. The consumer is not obligated to extend the lease beyond the current monthly or weekly period. If the agreement is not renewed the item may simply be returned. In addition, the consumer is provided with the option of purchasing the merchandise by either continuing to pay rent for a specified period of time (usually 12 to 24 months) or by early payment of a specified portion of the remaining lease payments.

Rent-to-own is popular with lower income, cash-strapped consumers. These consumers may not qualify for credit or a store's layaway plan. The benefits of rent-to-own are immediate, perhaps otherwise unattainable, access to a needed or desired product. The transaction typically does not require a down payment or a credit check. The weekly or monthly installment payments are relatively low when compared to the cost of the item. In addition, these arrangements provide a flexibility that may also be appealing to consumers wanting to test a product before purchase or those with transient employment. Rent-to-own agreements usually include delivery, setup, pickup, and repair service. The costs of these "free" services are reflected in the rent-to-own prices.

The largest drawback to these arrangements is the final purchase price of an item bought through rent-to-own. The total of the installment payments can be two to three times (sometimes more) the retail price of the item. Consumer advocates state one way to clearly see the high final cost of a rental purchase item is by calculating what the effective annual percentage rate (APR) for the transaction would be. The difference between the cash price of an item and the sum of all payments included in a rental-purchase agreement would represent the finance charge. Testimony at recent hearings provided a table presenting effective APRs, the retail price of an item, and the total rental purchase price. One example was a 19-inch color television with a retail price of \$300.

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<sup>1</sup> Industry statistics can be found on the APRO website at [<http://www.rtohq.org>].

The rent-to-own agreement was for \$16 per week for 52 weeks resulting in a total purchase price of \$832. The APR for this transaction would be about 254%.<sup>2</sup>

Consumer advocates warn of other potential problems in rent-to-own arrangements. They indicate that consumers need to make sure they know if the rent-to-own item is new, used, or previously rented. In addition, they recommend that the consumer inquire if there is a grace period for a missed payment and if a penalty is charged. They call for discussion of other fees such as insurance and home pick-up as well as any taxes. From their perspective, the agreement should address what happens if the merchandise is broken, lost, or stolen. Consumer advocates also argue reinstatement rights should be part of rent-to-own agreement. This protection would allow customers that miss a payment to be reinstated in the agreement, with credit for past payments, if overdue amounts are paid in a timely fashion.

## FTC Survey

The Federal Trade Commission (FTC) conducted a nationwide survey of rent-to-own customers in the late 1990s to provide an independent body of information on the typical rent-to-own customer and their experience with the industry. The FTC published a report on the survey's findings to help inform the ongoing debate over proposals for national regulation. The report gives an overview of the industry, presents the results of the survey, and provides a discussion of public policy issues.<sup>3</sup> Three primary goals of the survey were identified: (1) to examine who uses rent-to-own transactions and how they differ from consumers who do not; (2) to determine whether rent-to-own transactions typically result in the purchase of the rented merchandise; and (3) to determine whether abusive collection practices are widespread in the industry.

The major findings of the survey include the following. In general, rent-to-own customers compared to consumers who had not made rent-to-own transactions have lower incomes, have less education, rent their residence, and live in non-suburban areas. The survey found that 70% of rent-to-own merchandise was purchased by the customer. The average rental period for items purchased was 14 months. Items returned to the store were rented for an average of five months. The reason given for over half of the returns was that the item was no longer needed. About 24% of the returns were for financial reasons. The great majority (75%) were satisfied with their rental-purchase experience. The survey found that over one-third of rent-to-own customers had rented merchandise on more than one occasion in the last five years. The most cited reason for an unsatisfactory experience was the high price of rental-purchase. Almost 50% of the rent-to-own customers surveyed had been late with a payment. Two-thirds of the late customers indicated that they received good or very good treatment from the store when they were late with a payment. Poor treatment was reported by 15% of these customers

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<sup>2</sup> U.S. Congress, House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, *The Consumer Rental Purchase Agreement Act (H.R. 1701)*, unpublished hearings on H.R. 1701, 107<sup>th</sup> Cong., 1<sup>st</sup> sess., July 12, 2001.

<sup>3</sup> Federal Trade Commission, Bureau of Economics, *Survey of Rent-to-Own Customers*, staff report by James M. Lacko, Signe-Mary McKernan, and Manoj Hastak, April 2000, 150p.

and 11% of late customers described treatment that indicated possibly abusive collection practices.

Chapter seven of the FTC report provides an overview of some of the major policy issues addressed by various states and proposed in federal legislation. The report focuses on five areas of concern; disclosure of total cost and other purchase terms, APR disclosure, price restrictions, regulation of payment collection practices, and regulation of reinstatement rights. This section of the report includes a discussion of policy options and issues related to these areas of concern.

The report strongly supports clear and accurate disclosure of cost and other purchase terms at the point of sale, in advertising, and in agreements. The survey found most rent-to-own merchandise was purchased and therefore consumers need information on the total cost of an item to compare a rental purchase to any alternatives. The report recommended that the total cost numbers include the sum of all weekly or monthly rental payments and all other mandatory fees and charges. The report recommended disclosure of this information at the store (on product labels or tags) on all displayed merchandise. Other basic terms of purchase, such as the amount of the periodic payment and whether the item was new or used, were also recommended for inclusion on the label. It was urged that total cost and other basic terms of purchase also be disclosed in advertising and that agreement documents disclose all of the terms and conditions of the rent-to-own transaction.

The report suggests that potential costs and benefits should be thoroughly examined before regulatory policies addressing the other four areas of concern are adopted and that regulation of the rent-to-own industry should attempt to balance two priorities: (1) ensuring that rent-to-own consumers have the information and protections needed to make informed decisions, and (2) avoiding prohibitive industry costs that could substantially reduce the availability of rental-purchase transactions. The report acknowledges that rental-purchase transactions can be an expensive method of purchasing merchandise and concludes that consumers should be made aware of the costs of purchasing through rent-to-own transactions. At the same time, the survey found a relatively high level of customer satisfaction with rental-purchase transactions, suggesting that the rent-to-own industry does provide a service that meets the needs of certain consumers.

## Regulation and Legislation

Currently, federal consumer protection laws do not specifically regulate rent-to-own transactions. The disclosure requirements of the Truth-in-Lending-Act (TILA)<sup>4</sup> and the Consumer Leasing Act (CLA)<sup>5</sup> do not apply to the rent-to-own industry. TILA is a disclosure law implemented by Federal Reserve Regulation Z. TILA requires consumer creditors to disclose an APR and other loan terms. Rent-to-own transactions are not covered because Regulation Z excludes leases that are terminable without penalty by the consumer. CLA requires disclosures concerning the terms of personal property leases.

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<sup>4</sup> P.L. 90-321, tit.1, 82 Stat. 146, 15 U.S.C. 1601 *et seq.*

<sup>5</sup> P.L. 94-240, 90 Stat. 257, 15 U.S.C. 1667.

CLA is implemented by Federal Reserve Regulation M. To be covered a lease must be in excess of four months. Since rent-to-own agreements are short-term (monthly or weekly), self-renewing leases, they are not covered by Regulation M.

Rent-to-own transactions are addressed by state law. By the summer of 2001, 47 states had laws governing rental-purchase transactions. The laws vary from state to state but generally treat rent-to-own transactions as leases. A variety of disclosures are required by the state laws but only 18 states provide for cost disclosures on merchandise tags or labels.<sup>6</sup>

Consumer groups have worked to strengthen state laws, criticizing most of the laws for providing inadequate protection. Generally consumer advocates support federal legislation that would subject these transactions to existing federal credit laws and address policy issues discussed in the FTC report. These groups also argue against proposals that would preempt more protective state law.

The rent-to-own industry has generally supported federal legislation as a means of creating a uniform regulatory framework. However, industry representatives have fought proposals that would define these transactions as credit sales. Generally the industry has supported the various state actions because the state laws viewed rent-to-own transactions as leases and provided for disclosures the industry considered reasonable.

Legislation has been introduced in each Congress during the last decade dealing with the rental-purchase industry. The proposals have not been uniform. Some defined rent-to-own transactions as leases and others would have subjected the industry to federal credit laws and state usury laws. A variety of disclosures have been proposed. In addition, legislation has addressed abusive payment collection practices and the issue of reinstatement rights.

Currently, one bill, H.R. 1767, has been introduced in the 110<sup>th</sup> Congress. The bill would provide for uniform disclosure requirements including total costs, the amount and timing of the payments, and the consumer's right to terminate the agreement. In addition, the bill would require consumer protections governing account statements, renegotiations and extensions, disclosures at the point of sale, and advertising disclosures. H.R. 1767 would also define rent-to-own transactions as lease agreements, and it would prevent states from characterizing rental-purchase agreements as credit transactions. The legislation was introduced on March 29, 2007, and referred to the Committee on Financial Services.

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<sup>6</sup> U.S. Congress, House, Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, *The Consumer Rental Purchase Agreement Act (H.R. 1701)*, unpublished hearings on H.R. 1701, 107<sup>th</sup> Cong., 1<sup>st</sup> sess., July 12, 2001.