

**PREPARED STATEMENT OF THE  
FEDERAL TRADE COMMISSION**

**on**

**Rent-to-Own Transactions**

**before the**

**HOUSE FINANCIAL SERVICES COMMITTEE**

**FINANCIAL INSTITUTIONS AND CONSUMER CREDIT SUBCOMMITTEE**

**July 26, 2011**

## **I. INTRODUCTION**

Mr. Chairman and members of the Committee: I am Charles Harwood, Deputy Director of the Federal Trade Commission's Bureau of Consumer Protection.<sup>1</sup> I appreciate the opportunity to appear before you today on behalf of the Commission to discuss the rent-to-own (RTO) industry.

This testimony today begins by briefly summarizing the Commission's role in enforcing laws that bear on financial issues relevant to the RTO industry. It then discusses the RTO industry itself. The testimony subsequently describes a report prepared by the Commission's Bureau of Economics and released by the Commission in 2000 and a related study prepared by the authors of the Bureau of Economics report. Finally, the testimony offers some general observations about consumer protection issues and regulation in this area.

## **II. THE FTC'S LEGAL AUTHORITY OVER THE RENT-TO-OWN INDUSTRY**

As part of its mandate to protect consumers, the Commission enforces the Federal Trade Commission Act, which broadly prohibits unfair or deceptive acts or practices in or affecting commerce.<sup>2</sup> The Commission also enforces a number of laws specifically governing lending and leasing practices, including the Truth in Lending Act ("TILA")<sup>3</sup> and the Consumer Leasing Act ("CLA"),<sup>4</sup> which require disclosures and establish certain substantive requirements in connection

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<sup>1</sup> The views expressed in this statement represent the views of the Commission. My oral statement and responses to questions you may have are my own and are not necessarily those of the Commission or any Commissioner.

<sup>2</sup> See 15 U.S.C. § 45(a).

<sup>3</sup> See 15 U.S.C. §§ 1601-1666j.

<sup>4</sup> See 15 U.S.C. §§ 1667-1667f. The CLA is an amendment to the TILA.

with consumer credit or lease transactions, respectively.<sup>5</sup> Under these laws, the Commission has jurisdiction over most non-bank lenders.<sup>6</sup> In addition to its law enforcement duties, the Commission also responds to requests for information about consumer financial issues from consumers, industry representatives, state law enforcement agencies, and the media, and disseminates educational materials to businesses and consumers.

As part of its enforcement efforts, the Commission collects over one million complaints annually about companies and a wide variety of business practices. These complaints can help the Commission detect patterns of wrongdoing and lead to investigations. The Commission enters all complaints it receives into the Consumer Sentinel Network, a secure online database that is used by thousands of civil and criminal law enforcement authorities worldwide. In 2010, a few hundred of the 1.1 million complaints that the Commission received and entered into Consumer Sentinel related to RTO transactions.

On July 21 of this year, the new Consumer Financial Protection Bureau (CFPB) formally began operations. In general, the FTC and CFPB share authority to enforce financial consumer protection laws.<sup>7</sup> Rulemaking authority under those laws for most credit and lease transactions

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<sup>5</sup> The Commission also enforces various other financial statutes, including the Equal Credit Opportunity Act, 15 U.S.C. §§ 1691-1691f, which, inter alia, prohibits discrimination against applicants for credit on the basis of age, race, sex, or other prohibited factors; the Fair Credit Reporting Act, 15 U.S.C. §§ 1681-1681x, which, inter alia, governs the use of consumer credit reports, and the Fair Debt Collection Practices Act, 15 U.S.C. §§ 1692-1692p, which, inter alia, prohibits certain abusive collection practices by debt collectors.

<sup>6</sup> See, e.g., 15 U.S.C. § 45(a); 15 U.S.C. § 1607.

<sup>7</sup> Under the FTC Act, the FTC has no jurisdiction over most depository institutions. 15 U.S.C. § 45(a)(2).

has transferred to the CFPB. The Commission is not aware of any determination on the part of the CFPB about its authority with respect to RTO transactions.

### **III. THE RENT-TO-OWN INDUSTRY**

The RTO industry consists of dealers that rent consumer products with an option to buy. These products have traditionally included furniture, appliances, home electronics, jewelry, and computers. Some dealers may specialize in offering other particular types of products, such as musical instruments, tires and wheels, or automobiles.

In recent years, the RTO industry has gradually expanded its offerings to encompass a broader range of products. The Association of Progressive Rental Organizations (“APRO”), an RTO industry trade association representing many RTO stores, reports that the RTO model is being adapted to other product lines outside the traditional ones, including homes, fine art, bicycles, storage sheds, and riding lawnmowers.<sup>8</sup>

RTO agreements typically do not require any down payment or credit check, thus providing consumers with immediate access to household goods for a weekly or monthly payment. Generally, RTO agreements are self-renewing on a weekly or monthly basis, and consumers are under no obligation to continue making payments beyond the current weekly or monthly period. RTO transactions may be attractive to consumers who cannot afford a cash purchase, may be unable to qualify for traditional credit, or are unable or unwilling to wait until they can save enough money for a purchase.

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<sup>8</sup> See APRO, [About Rent-to-Own - Get to Know the Rent to Own Industry, www.rtohq.org/apro-rto-industry-overview.html](http://www.rtohq.org/apro-rto-industry-overview.html) (last visited July 8, 2011).

RTO agreements provide consumers with the option to purchase the goods, in most cases either by continuing to make payments for a specified period of time, usually 12 to 24 months, or by making an early payment of some specified proportion of the remaining payments. APRO reports that some RTO stores have begun to offer more payment options to consumers for purchasing merchandise, including the option to purchase goods within three to six months instead of the typical period of 12 to 24 months.<sup>9</sup> APRO estimates that in 2009 there were approximately 8,600 RTO stores in the United States and Canada, serving more than four million customers, and producing \$7 billion in annual revenues.<sup>10</sup>

#### **IV. KEY FINDINGS OF THE BUREAU OF ECONOMICS REPORT**

The Commission frequently conducts economic analyses of different markets and industries. This research, which generally is performed by the agency's Bureau of Economics, helps inform FTC policies and priorities and in some cases may provide the basis for recommendations for changes to law or industry practices. Thus, these analyses are important to the overall competition and consumer protection missions of the Commission.

In 2000, the Commission released a seminal report on the RTO industry prepared by the Commission's Bureau of Economics.<sup>11</sup> Subsequently, the authors of the Bureau of Economics

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<sup>9</sup> Id.

<sup>10</sup> Id.

<sup>11</sup> James M. Lacko, Signe-Mary McKernan & Manoj Hastak, Survey of Rent-to-Own Customers: Federal Trade Commission Bureau of Economics Staff Report (April 2000), available at <http://www.ftc.gov/reports/renttoown/renttoownr.pdf>.

report separately published additional analysis of the data collected for the original report,<sup>12</sup> and other research has been made public. This testimony discusses some of the key findings from those studies.

The Bureau of Economics initiated its RTO study following a decade or more of considerable debate about the RTO industry, to better understand the nature of the industry and allegations of consumer protection problems that had been raised. The Bureau of Economics report was the first independent, systematic examination of RTO transactions and was based on the findings of a nationwide survey of RTO customers.<sup>13</sup> The survey had three primary goals: (1) to examine which consumers used RTO transactions and how they differed from consumers who did not; (2) to determine whether RTO transactions typically resulted in the purchase of the rented merchandise; and (3) to determine whether abusive collection practices were widespread in the industry.

Some key findings from the survey include:

#### **Characteristics of a Rent-to-Own Transaction**

- Customers ultimately purchased 70% of the merchandise they obtained through RTO transactions. The purchase rate was consistently high (at least 60%) across most demographic groups.
- Sixty-seven percent of customers intended to purchase the merchandise when they began the RTO transaction.

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<sup>12</sup> Signe-Mary McKernan, James M. Lacko & Manoj Hastak, Empirical Evidence on the Determinants of Rent-to-Own Use and Purchase Behavior, 17 Econ. Dev. Q. 33 (2003), available at <http://edq.sagepub.com/content/17/1/33.abstract>.

<sup>13</sup> See supra note 12. The Bureau of Economics telephone survey contacted over 12,000 randomly-selected U.S. households from December 1998 to February 1999. From this sample, 532 households that had engaged in RTO transactions within the previous five years were identified and interviewed with respect to their RTO experiences. See id. at 17-23.

- Actual purchases were consistent with customer purchase intentions. Eighty-seven percent of the customers who intended to purchase the rent-to-own merchandise actually did purchase it. Similarly, 90% of the customers who intended to rent temporarily and return the merchandise actually did return it. Customers who were unsure of their intentions when they began renting divided fairly evenly, with 47% purchasing the merchandise and 44% returning it.
- Thirty-eight percent of rented items were home electronics products, 36% were items of furniture, and 25% were appliances. The most commonly rented items were televisions, sofas, washers, VCRs, and stereos, which together accounted for over half of all rented merchandise.
- Merchandise purchased through an RTO transaction was rented for an average of 14 months before purchase. Forty-seven percent of the purchases took place in the first year. Merchandise not purchased by consumers was rented for an average of five months before it was returned. Eighty-one percent of returns took place within six months.

### **Demographics**

- Thirty-one percent of RTO customers in the survey were African American, 79% were 18 to 44 years old, 73% had a high school education or less, and 59% had household incomes of less than \$25,000.

### **Customer Satisfaction**

- According to the survey findings, 75% of RTO customers were satisfied with their experience with RTO transactions. Satisfied customers gave a wide variety of reasons for their satisfaction, favorably noting many aspects of the transaction, the merchandise and services, and the treatment they received from store employees. Nineteen percent of all RTO customers interviewed were dissatisfied with their experience, and most cited high prices as the reason. Complaints about high prices were made by 27% of all RTO customers, including nearly 70% of dissatisfied customers. Fewer customers complained about problems with the merchandise or repair service, the treatment received from store employees, the imposition of hidden or added costs, or other issues.
- Nearly half of all RTO customers had made at least one late payment. Sixty-four percent of customers who made late payments reported that the treatment they received from the store when they were late was either “very good” or “good,” and another 20% reported that the treatment was “fair.” Fifteen percent of late customers reported being treated poorly when they were late, including 11% who indicated possibly abusive collection practices.

In 2003, the authors of the Bureau of Economics report published a follow-up study in the Economic Development Quarterly (the 2003 study) to contribute further research on how consumers use RTO transactions.<sup>14</sup> One goal of this follow-up study was to explore the distinctions between consumers who use RTO transactions to purchase merchandise and those who rent temporarily instead. The 2003 study included further analysis of the data collected for the earlier Bureau of Economics report and presented additional findings.<sup>15</sup> For example, the 2003 study found some evidence that state laws requiring disclosure of the total purchase cost on product labels of RTO products were associated with lower levels of consumers who intended to purchase RTO merchandise and higher levels of those who intended only to rent temporarily. The 2003 study made preliminary findings that consumers living in states that required disclosure of the total purchase costs on product labels were 30 percent less likely to use RTO transactions with the intent to purchase than consumers living in other states. According to the 2003 study, these results would be consistent with a conclusion that some customers underestimate the cost of RTO transactions in the absence of the total cost disclosures (perhaps focusing instead on the low payments and immediate access) and that the disclosures more fully inform these consumers, leading some to make different decisions.<sup>16</sup> The new analysis further found that the characteristics

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<sup>14</sup> See supra note 13.

<sup>15</sup> Id.

<sup>16</sup> Id. The 2003 study also found an association between purchase outcomes and reinstatement rights, which require that consumers who are late in making payments be reinstated in the rental agreement with full credit for past payment, as long as overdue amounts are paid within a specified period of time. The association between purchase outcomes and reinstatement rights suggests that customers in states with reinstatement laws were more likely than customers in other states to ultimately purchase the merchandise.



of customers entering RTO transactions with the intent to purchase differed significantly from those intending a temporary rental, suggesting that the RTO industry serves two separate and distinct markets. According to the 2003 study, for example, individuals with lower incomes or less education were substantially more likely to enter RTO transactions with the intent to purchase. Of those intending to purchase, however, lower-income customers were significantly less likely to complete a purchase than moderate-income customers, suggesting that these customers may not have had sufficient income to make the purchase.<sup>17</sup>

Several industry and other studies using industry-supplied store reporting data also have been published since 2001. These studies generally concluded that the purchase rate for RTO transactions was lower (less than 40 percent) than the rate found in the Bureau of Economics report (70 percent).<sup>18</sup> The discrepancy in the purchase rate findings might be attributed to differences in the study methodologies.

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<sup>17</sup> Id.

<sup>18</sup> See, e.g., Michael H. Anderson & Raymond Jackson, Rent-To-Own Agreements: Purchases or Rentals?, 20 J. of Applied Bus. Res. (2004) (finding that customers purchase in 39% of agreements); Michael H. Anderson & Sanjiv Jaggia, Rent-to-Own Agreements: Customer Characteristics and Contract Outcomes, 61 J. Econ. & Bus. 51 (2009) (finding that 72.88% of completed RTO transaction agreements resulted in merchandise being returned to the store); Michael Anderson & Sanjiv Jaggia, Return, Purchase, or Skip? Outcome, Duration, and Consumer Behavior in the Rent-to-Own Market, Empirical Econ. (2011) available at <http://www.springerlink.com/content/42n382414415wjh1/> (finding a 23.6% purchase rate); APRO, About Rent-To-Own - Rent-to-own Prices, <http://www.rtohq.org/apro-rent-to-own-prices.html> (last visited July 21, 2011) (identifying purchase rate as 25%); APRO, About Rent-to-Own - RTO: Rent-to-Own Changing With the Times, <http://www.rtohq.org/apro-rto-change-with-times.html> (last visited July 21, 2011) (identifying purchase rate as 25%).

## V. CONSUMER PROTECTION ISSUES

The Bureau of Economics report referred to a number of potential consumer protection concerns raised by consumer advocates and others about the RTO industry, including the prices charged by the industry for purchasing the merchandise (which can be two to three times higher than retail prices), the treatment of customers during the collection of overdue rental payments, the repossession of merchandise after customers have paid substantial amounts towards ownership, the adequacy of information provided to customers about the transaction, and the disclosure of whether merchandise was new or used. Consumer advocates also have argued that RTO transactions are really credit sales, not leases, and should be subject to federal and state consumer credit laws.<sup>19</sup>

Currently, RTO transactions are not specifically covered by federal laws that govern credit or lease transactions, namely, the TILA and the CLA, and there is no specific statute that applies to RTO transactions. Federal legislation that would specifically regulate RTO transactions has been proposed many times in the past. Some of these proposals would have applied federal and

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<sup>19</sup> See, e.g., U.S. Public Interest Research Group, Preemption Alert, 4 (Mar. 2006), <http://www.uspirg.org/html/preemptionalert/march06.pdf> (Federal rent-to-own legislation supported by the industry would prohibit states from “enforcing stronger, more pro-consumer lending laws, such as usury ceilings, interest rate disclosures, or other loan protections against rent-to-own stores”); AARP New Jersey, Testimony by Patricia Kelmar Before the NJ Assembly Consumer Affairs Committee (June 5, 2006), available at [http://www.clnj.org/rto\\_aarp\\_testimony\\_a695.pdf](http://www.clnj.org/rto_aarp_testimony_a695.pdf) (urging enforcement of the “Retail Installment Sales laws in rent to own situations”); see also Consideration of Regulatory Relief Proposals, Before the Senate Comm. on Banking, Housing and Urban Affairs, 109<sup>th</sup> Cong. 2d Sess. (Mar. 1, 2006), available at [http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore\\_id=8686a52a-58ef-40fc-bdb4-d500d9615b49](http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=8686a52a-58ef-40fc-bdb4-d500d9615b49) ((Joint testimony of Consumer Federation of America, National Consumer Law Center, and U.S. Public Interest Research Group, ACORN, Center for Responsible Lending, Consumers Union, National Community Reinvestment Coalition, opposing S.603 “The Consumer Rental-Purchase Agreement Act of 2005”).

state credit laws to the RTO industry, while other proposals would have regulated RTO transactions as leases.

Today, forty-seven states and the District of Columbia have laws regulating RTO transactions in a manner similar to leases. These laws vary from state to state, requiring a variety of disclosures and imposing other requirements and prohibitions, such as setting caps on fees that can be charged over and above a baseline cost of the product (for example, the wholesale cost to the store or the price charged to a consumer to purchase the product outright). Although these state laws regulate RTO transactions as lease sales,<sup>20</sup> courts in several states, most notably Wisconsin, Minnesota, and New Jersey, have ruled that RTO transactions are credit sales and subject to state laws governing credit sales.<sup>21</sup> Vermont does not regulate RTO transactions as credit sales,<sup>22</sup> but does require disclosure of the “effective APR.”

An important factual issue in the debate over whether RTO transactions are sales or leases continues to be the extent to which RTO customers purchase the rented merchandise. As described earlier, the Bureau of Economics report found that 70 percent of RTO merchandise is purchased by the customer. In contrast, other studies have found that, based on store reporting data, less than 40 percent of RTO merchandise ultimately is purchased, and that the rest is returned to the dealer after a relatively short rental duration.

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<sup>20</sup> See supra note 12 at 7.

<sup>21</sup> Id.

<sup>22</sup> See Vermont Rule CF 115 (1997); 9 V.S.A. § 41b (2011); see also TILA, 15 U.S.C. §§ 1601-1666j.

Having found a high purchase rate, the Bureau of Economics recommended in its report that the basic terms of the RTO transaction, in particular the total cost of purchase, should be fully disclosed to consumers before they enter into the agreement. Information regarding the total cost of purchase, including all mandatory fees and charges,<sup>23</sup> would allow consumers to compare the cost of an RTO transaction to alternatives and would be most useful if it were available while the customer was shopping.

A bill to amend the Consumer Credit Protection Act to cover RTO transactions is currently before the Subcommittee. The bill includes provisions that would require disclosures to consumers of certain payment terms in RTO agreements and advertisements and at the point of rental. The bill also would prohibit RTO stores from engaging in certain repossession and collection activities. The Commission does not take a position on the legislation.<sup>24</sup> In general, the Commission supports efforts to improve disclosures by making them clear, conspicuous, understandable, and useful for consumers when they shop for and compare products and services.

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<sup>23</sup> Commissioner Brill believes disclosures of effective interest rates are successfully being employed in states where they are required, and can be useful to the consumer in comparing the cost of a RTO transaction to other payment options. In addition, Commissioner Brill believes treating RTO transactions as credit sales may trigger other important consumer protections.

<sup>24</sup> Commissioner Brill, joined by Chairman Leibowitz, notes that the full Commission has not taken a position on H.R. 1588 as a whole or the preemption provisions contained therein. Over 40 states already have laws that generally provide the protections contained in the bill. Four states – Minnesota, New Jersey, Vermont and Wisconsin – have laws that are more protective of consumers in that they require disclosures of effective interest rates or treat RTO transactions as credit transactions. H. R. 1588 would preempt the laws in these four states. Commissioner Brill and Chairman Leibowitz do not support preemption of state laws that are more protective of consumers engaged in rent-to-own transactions, and believe that Congress should continue to allow states to be “laboratories of democracy” in this area.

Commission staff would be happy to provide technical assistance to the Subcommittee generally with respect to effective disclosures.

## **VI. CONCLUSION**

The availability of RTO products may fill an important need for some consumers. But the market will function properly only if the practices of RTO businesses are transparent, fair, and honest. The Commission will continue to work with Congress to ensure that consumers are protected when they enter into RTO transactions.