



# UNIVERSITY OF FLORIDA

Cooperative Extension Service  
Institute of Food and Agricultural Sciences

## Rent-To-Own<sup>1</sup>

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*"No Credit Hassle!"*

*"No Long-Term Commitment!"*

*"No Down Payment"*

*"Free Service in Your Home!"*

Rent-to-own (RTO) businesses are using such ads to attract customers. There are a host of local RTO establishments and a few nationwide franchises, and the number is increasing rapidly.

RTOs are in regulatory limbo because their unique marketing approaches do not fit into the traditional merchandising methods. Are they retailers who extend credit to high risk borrowers, leasing agencies offering long term leases, or are they rental agencies?

Although RTO merchandising has only recently gained considerable attention, it is not a new concept. It originated with an English piano manufacturer who wanted to increase his business by making it easier for customers to buy pianos. He created the "hire-purchase" marketing concept in 1846. This concept has been used for years by music companies in cooperation with band teachers enabling beginning students to rent their instruments. If a student lost interest the rented instrument was returned and the payments ceased. If the student continued in the band and kept up the payments, eventually the instrument became his.

The "hire-purchase" or RTO merchandising method has now been extended to the sale of a wide

variety of merchandise including things such as furniture, appliances, jewelry, electronics and even office equipment. The use of the RTO concept to sell a wider variety of products has resulted in the development of a new type of retailer who targets a different kind of customer, using a different sales appeal and possibly with a different merchandising objective. RTOs have generated consumer complaints regarding the amount and clarity of rental/purchase information, high prices, severe penalties for late payments, and repossession debt collection practices. Some consumer groups want more state or federal regulation. RTOs contend they serve a group of customers rejected by other sellers and their actions are reasonable and essential for economic survival.

### REGULATORY CONCERNS

Critics say rental-purchase agreements are simply credit sales disguised as rental contracts and should be regulated as credit transactions. They contend rental purchase contracts contain a termination clause that permits the consumer to terminate the transaction at any time. They also say a customer's option to try out the product and later return it is functionally no different than a credit sale in which the buyer exercises a "satisfaction or your money back" guarantee. Essentially the only difference is that the RTO customer receives no refund whereas the credit customer does.

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The RTO industry does not recognize rental payments as equivalent to installment payments. It says customers do not pay interest because there is no debt. The industry rejects arguments that RTO transactions are a form of credit. It agrees that the RTO transactions are more costly to consumers but says the reason is because of the higher costs of services provided which are not available through credit purchases. Most RTO dealers offer free delivery, no credit checks, free repairs and a replacement or loaner while the product is being repaired. RTOs say you cannot buy a service contract from any retailer who will come out to a consumer's home and fix the product or replace it. RTO dealers must also absorb costs such as opportunity costs, depreciation, and the gamble of renting to high risk consumers.

The RTO industry claims to market over ten percent of the major appliances sold in the U.S. Yet, it remains exempt from nearly every statute regulating other retailers and financiers of consumer goods. Since the terms "lease" and "rent" are defined differently than "credit," traditional credit laws, usury ceilings and the Fair Credit Billing Act have not been applied to RTO transactions. RTO transactions are not regulated by the Consumer Leasing Act of 1976 because this Act applies only to leases that last longer than four months. RTOs contend they rent monthly, renewed each month. Also, the Federal Fair Debt Collection Practices Act does not apply to rental dealers attempting to recover their own merchandise or to collect their own debts. The statute applies only to third-party debt collection agencies.

State laws and regulations are not consistent and are varied. Florida law requires RTO dealers to state their "cash price" as well as the weekly or monthly rental fee. However, the total price of rent-to-own purchasing is not required.

### **DISCLOSURE CONCERNS**

Many consumer advocates feel RTO customers do not have the information they need available in a consistent, easy to understand form. They argue such information is needed to do price comparisons and to become aware of the total costs of potential purchases.

### **UNIQUENESS OF RTO SYSTEM**

Today's RTO transactions involve a rental agreement where payments are made at regular intervals. Most also specify that after a certain number of payments are made the merchandise belongs to the customer. As long as payments are made, the merchandise remains with the consumer. If payments stop, the agreement is considered cancelled and merchandise must be returned in good condition. This type of transaction is unique because it combines features of renting, leasing, and buying. The consumer has no equity in the merchandise until all payments under the purchase agreement have been made.

Prices are usually quoted in dollars per week or month. These sound low because they do not reflect the total amount that must be paid before the merchandise becomes the property of the customer. The cost is usually much more than the price of the same merchandise from another type of retailer.

### **CUSTOMERS**

Most RTO customers fall in the low-income range so the probability of their not being able to make payments on time is rather high. Unless required by state law, RTOs generally provide no grace period and the customer builds no equity in rented merchandise. If the renter misses a payment, the merchandise must be returned and the money already paid is jeopardized.

Most RTOs emphasize their "no credit check" to attract customers who either do not have credit or have credit problems. These are society's most vulnerable consumers. They are usually low-income, with the heads of households in the 18-34 age range. Three of each four are women. Most have limited opportunity to purchase in the traditional manner of cash retail and have limited access to credit or savings.

### **GROWTH OF RTOs**

Why the rapid growth of RTOs? There appear to be two major reasons. First, loans to marginal credit users may not be approved by banks, finance

companies or other financial institutions. Secondly, too many debts. It is estimated that about one-third of the adult population now faces credit problems. Thus, RTOs become the most easily accessible method of obtaining new merchandise.

### PROBLEM AREAS

Most consumer complaints or merchant/consumer disagreements revolve around the following concerns.

**Total cost of RTO transactions.** Many consumers complain that the total cost of RTO purchases were from 100 to 300 percent more than the cost of comparable products sold by other methods.

**Reinstatement rights.** When a late payment or a missed payment results in the loss of merchandise which is almost paid off, hard feelings are likely. Some RTO dealers will assess a penalty and reinstate the agreement. In other instances the customer loses his/her total investment.

**Used goods.** Many consumers have complained they were supposed to receive a new product but received a used one instead.

**Service.** Servicing the product at no cost is a big selling feature of RTO, however a major area of complaints relate to delays encountered when trying to get appliances repaired. Some people complained about receiving appliances that were not operating properly. Others received loaners that were not satisfactory or were of lower quality.

RTOs also have experienced frustrations. Even though only about two percent of their customers skip or steal the merchandise (remove rented merchandise without notifying the company) these do represent a loss.

### WHY SHOP WITH RTOs?

When questioned about why they shopped with RTO companies customers gave four reasons:

1. To get the item "right away."
2. No credit check is required.
3. Were denied credit at other places, or credit is overextended.

4. Thought it was a neighborhood business because it was located in the neighborhood.

When surveyed regarding their opinions of RTO dealers, one group of customers reported they were aware that RTO costs were higher. More than two of each five said RTO was "OK, but not great." About one third were not satisfied with the RTO programs (Swagler & Wheeler, 1989).

### AVAILABILITY

In some locations such as college towns and areas near large medical centers, acceptable furnished residences for short term occupancy may be scarce or unavailable. In these situations it may be more advantageous to rent than to buy furniture and/or appliances for the short period it is needed. Most locations have few places to rent furniture and appliances. Also, the condition of the rental furniture may not be very good. RTO companies usually offer a choice of new or minimum wear used furniture and appliances. Thus, they can fulfill the need for those who wish to rent furniture for a short time and do not consider this to be a method of purchasing.

### RTO CAUTIONS

There are certain precautions that any consumer should consider before buying from a rent-to-own (RTO) retailer.

- The total cost of ownership through RTO should be compared with the cost of merchandise sold outright. Try to locate conventional credit. Consider lay-away plans. Or, buy used merchandise from a retailer, garage sale, classified ad or a thrift shop. RTO is a very costly method of ownership.
- Realize that although RTO dealers do not use credit reporting agencies, they do obtain and check information about you. They will ask for information about your employment, such as, who you work for, how long, income, and location. This information will be checked. Also, dealers will ask for the name and address of several relatives and friends. (The company will have enough information to locate you.)
- Make sure any contract you are considering signing contains all of the important financial information. This includes things such as cash selling price of the merchandise; if it is new or

used; the amount and timing of rental payments; a list of and the amount of any other charges, such as deposits, delivery or reinstatement charges, late fees and fees to be paid at the end of the contract before ownership; and the total cost of the agreement.

- Be aware that you will not own the merchandise until the total amount on the contract is paid. Realize that although you are making payments, you are not building any ownership in the merchandise, and you have no equity in it.
- Learn what will happen if your payments are late and the merchandise is repossessed. If there is no grace period, what will happen if a payment is late?
- Be sure the contract carries an accurate description of the merchandise and if it is new or used. Do not accept substitute merchandise with the promise that it will be replaced later.
- Find out who pays for repairs. Also, find out if you will receive a loaner, or if payment stops while the item is being repaired.
- Make sure the contract describes conditions under which you may end the rental purchase agreement. Are their penalties for cancelling the agreement?
- Find out if there is an early purchase option where you may buy the merchandise without waiting until the end of the contract.
- Find out if your payment records will be reported to a credit reporting agency (credit bureau).
- Before signing, make sure you understand everything in the contract. Ask questions and, if needed, either take a copy of the contract to someone who can help you to understand it or bring this person with you.

- Do not sign a contract with blanks. Either mark through them or have them filled in. Get a copy of what you sign at the time that you sign it.
- If you do not know the reputation of the company with whom you will be dealing, call your local Better Business Bureau, Chamber of Commerce or Consumer Protection Agency. Find out how long the company has been in business and if there are unresolved complaints against the company.
- Comparison shop between different type sellers of the merchandise you are considering. If a RTO company is your choice, comparison shop more than one company if there are more in your area.

### CONCLUSION

There are advantages and disadvantages to rent-to-own companies. The most important question is whether the advantages outweigh the disadvantages. Consumers need to make informed decisions, not decisions made out of apathy or lack of understanding. Consumers do have buying options.

### REFERENCES

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