

RENT A CENTER INC DE

Form 10-K/A

July 30, 2004

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**Form 10-K/A**  
**(Amendment No. 2)**

**FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTIONS 13 OR 15(d)**

**OF THE SECURITIES EXCHANGE ACT OF 1934**

**þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2003**

**o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**

**Commission File No. 0-25370**

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**Rent-A-Center, Inc.**

*(Exact name of registrant as specified in its charter)*

**Delaware**  
*(State or other jurisdiction of  
incorporation or organization)*

**45-0491516**  
*(I.R.S. Employer  
Identification No.)*

**5700 Tennyson Parkway**

**Third Floor**  
**Plano, Texas 75024**  
**972-801-1100**

*(Address, including zip code, and telephone number,  
including area code, of registrant's principal executive offices)*

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Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act:

**Common Stock, par value \$.01 per share**

**(Title of Class)**

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes  No

<b>Aggregate market value of the 79,704,580 shares of Common Stock held by non-affiliates of the registrant at the closing sales price on June 30, 2003</b>	<b>\$2,416,642,866</b>
<b>Number of shares of Common Stock outstanding as of the close of business on March 8, 2004:</b>	<b>81,949,634</b>

**Documents incorporated by reference:**

Portions of the definitive proxy statement relating to the 2004 Annual Meeting of Stockholders of Rent-A-Center, Inc. are incorporated by reference into Part III of this report.

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**Table of Contents****EXPLANATORY NOTE**

The registrant is filing this Amendment No. 2 on Form 10-K/A (this Form 10-K/A) to its Annual Report on Form 10-K for the year ended December 31, 2003 filed with the SEC on March 11, 2004, as amended by Amendment No. 1 on Form 10-K/A filed with the SEC on April 6, 2004 (the Form 10-K), for the purpose of deleting a reference to a third party in Note E Intangible Assets and Acquisitions of the Consolidated Financial Statements. The deletion was in response to a comment by the SEC staff to two of our registration statements on Form S-3s, which requested that we delete the reference to the third party or have the third party file a consent to be named as an expert in such registration statements. This Form 10-K/A continues to speak as of the date that the initial Form 10-K was filed with the SEC, and we have not updated the disclosures herein to reflect any information or events subsequent to the filing of the initial Form 10-K. For a discussion of events and developments thereafter, please see our reports filed with the SEC since March 11, 2004, including the Quarterly Reports on Form 10-Q/A for the quarter ended March 31, 2004 and Form 10-Q for the quarter ended June 30, 2004. Other than revisions to the signature pages as permitted by Rule 12b-15, the remainder of this Form 10-K/A is unchanged and all subsequent references to Form 10-K shall refer to the initial Form 10-K, as amended by Amendment No. 1 and this Form 10-K/A.

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**PART I**

**Item 1. Business  
Overview**

*Unless the context indicates otherwise, references to we, us and our refers to the consolidated business operations of Rent-A-Center, Inc., the parent, and all of its direct and indirect subsidiaries.*

We are the largest operator in the United States rent-to-own industry with an approximate 32% market share based on store count. At December 31, 2003, we operated 2,648 company-owned stores nationwide and in Puerto Rico, including 22 stores in Wisconsin operated by our subsidiary Get It Now, LLC under the name Get It Now. Another of our subsidiaries, ColorTyme, Inc., is a national franchisor of rent-to-own stores. At December 31, 2003, ColorTyme had 329 franchised stores in 40 states, 317 of which operated under the ColorTyme name and 12 of which operated under the Rent-A-Center name. These franchise stores represent an additional 4% market share based on store count.

Our stores generally offer high quality, durable products such as home electronics, appliances, computers and furniture and accessories under flexible rental purchase agreements that generally allow the customer to obtain ownership of the merchandise at the conclusion of an agreed upon rental period. These rental purchase agreements are designed to appeal to a wide variety of customers by allowing them to obtain merchandise that they might otherwise be unable to obtain due to insufficient cash resources or a lack of access to credit. These agreements also cater to customers who only have a temporary need or who simply desire to rent rather than purchase the merchandise. Get It Now offers our merchandise on an installment sales basis in Wisconsin. We offer well known brands such as Philips, Sony, JVC, Toshiba and Mitsubishi home electronics, Whirlpool appliances, Dell, IBM, Compaq and Hewlett-Packard computers and Ashley, England, Berkline and Standard furniture. We also offer high levels of customer service generally at no charge, including repair, pick-up and delivery. Our customers benefit from the ability to return merchandise at any time without further obligation and make payments that build toward ownership. We estimate that approximately 63% of our business is from repeat customers.

Our principal executive offices are located at 5700 Tennyson Parkway, Third Floor, Plano, Texas 75024. Our telephone number is (972) 801-1100 and our company website is [www.rentacenter.com](http://www.rentacenter.com). We do not intend for information contained on our website to be part of this Form 10-K. We make available free of charge on or through our website our annual report on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material or furnish it to the SEC. Additionally, we voluntarily will provide electronic or paper copies of our filings free of charge upon request.

**Industry Overview**

According to the Association of Progressive Rental Organizations, the rent-to-own industry consists of approximately 8,300 stores, and provides approximately 6.6 million products to over 2.9 million households. We estimate the 6 largest rent-to-own industry participants account for approximately 4,800 of the total number of stores, and the majority of the remainder of the industry consists of operations with fewer than 20 stores. The rent-to-own industry is highly fragmented and, due primarily to the decreased availability of traditional financing sources, has experienced, and we believe will continue to experience, increasing consolidation. We believe this consolidation trend in the industry presents opportunities for us to continue to acquire additional stores on favorable terms.

The rent-to-own industry serves a highly diverse customer base. According to the Association of Progressive Rental Organizations, 92% of rent-to-own customers have incomes between \$15,000 and \$50,000 per year. Many of the customers served by the industry do not have access to significant amounts of credit. For these customers, the rent-to-own industry provides an alternative for them to obtain brand name products. The Association of Progressive Rental Organizations also estimates that 93% of customers have high school diplomas. According to an April 2000 Federal Trade Commission study, 75% of rent-to-own customers

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were satisfied with their experience with rent-to-own transactions. The study noted that customers gave a wide variety of reasons for their satisfaction, including the ability to obtain merchandise they otherwise could not, the low payments, the lack of a credit check, the convenience and flexibility of the transaction, the quality of the merchandise, the quality of the maintenance, delivery, and other services, the friendliness and flexibility of the store employees, and the lack of any problems or hassles.

**Strategy**

We are currently focusing our strategic efforts on:

enhancing the operations and profitability in our store locations;

opening new stores and acquiring existing rent-to-own stores both in the United States and internationally; and

building our national brand

***Enhancing Store Operations***

We continually seek to improve store performance through strategies intended to produce gains in operating efficiency and profitability. For example, we continue to focus our operational personnel on prioritizing store profit growth, including the effective pricing of rental merchandise and the management of store level operating expenses. Similarly, we instituted safety and loss prevention programs to maintain store level productivity as well as to minimize costs related to our insurance programs.

We believe we will achieve further gains in revenues and operating margins in both existing and newly acquired stores by continuing to:

use focused advertising and our new business relationships, such as our strategic alliances with McDonald's and Jackson-Hewitt, to increase store traffic;

expand the offering of upscale, higher margin products, such as Philips, Sony, JVC, Toshiba and Mitsubishi home electronics, Whirlpool appliances, Dell, IBM, Compaq and Hewlett-Packard computers and Ashley, England, Berkline and Standard furniture to increase the number of product rentals;

employ strict store-level cost control;

closely monitor each store's performance through the use of our management information system to ensure each store's adherence to established operating guidelines;

use a revenue and profit based incentive pay plan.

***Opening New Stores and Acquiring Existing Rent-To-Own Stores***

We intend to expand our business both by opening new stores in targeted markets and by acquiring existing rent-to-own stores and store account portfolios. We will focus new market penetration in adjacent areas or regions that we believe are underserved by the rent-to-own industry, which we believe represents a significant opportunity for us. In addition, we intend to pursue our acquisition strategy of targeting under-performing and under-capitalized chains of rent-to-own stores. We have gained significant experience in the acquisition and integration of other rent-to-own operators and believe the fragmented nature of the rent-to-own industry will result in ongoing consolidation opportunities. Acquired stores benefit from our administrative network, improved product mix, sophisticated management information system and purchasing power. In addition, we have potential access to our franchise locations, possessing the right of first refusal to purchase.

Since March 1993, our company-owned store base has grown from 27 to 2,648 at December 31, 2003, primarily through acquisitions. During this period, we acquired over 2,300 company-owned stores and over

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350 franchised stores in more than 140 separate transactions, including seven transactions where we acquired in excess of 50 stores. The table below summarizes the store growth activity over the last three years.

	2003	2002	2001
New store openings	101	70	76
Acquired stores	160	83	95
Stores from which we acquired accounts	220	126	90
Closed stores			
Merged with existing stores	20	23	42
Sold		4	6
Total approximate purchase price of acquisitions	\$ 126.1 million	\$ 59.5 million	\$ 49.8 million

In February 2003, we acquired substantially all of the assets of 295 stores located throughout the United States from Rent-Way, Inc. and certain of its subsidiaries for approximately \$100.4 million in cash. Of the 295 stores, 176 were merged with existing locations. Since December 31, 2003, we have acquired 12 additional stores and additional accounts from five locations for approximately \$3.9 million in cash and opened an additional 17 new stores. We also closed 18 stores, merging 11 of them with existing stores and selling seven, resulting in a total store count of 2,659 at March 8, 2004.

On February 4, 2004, we announced that we entered into a definitive agreement to acquire Rainbow Rentals, Inc., a rent-to-own operator, for \$16.00 in cash per share of Rainbow common stock. This acquisition consists of 124 rent-to-own stores in 15 states. The agreement also provides that each holder of options of Rainbow will receive an amount equal to the difference between \$16.00 and the exercise price of the option. We intend to fund the acquisition primarily with cash on hand. The acquisition, which is expected to be completed in the second quarter of 2004, is conditioned upon customary closing conditions for a transaction of this nature, including the receipt of requisite regulatory approval and approval of Rainbow's shareholders.

On March 5, 2004, we completed the purchase of five Canadian rent-to-own stores for \$3.2 million Canadian dollars (\$2.4 million U.S. dollars). The five stores are located in the cities of Edmonton and Calgary in the province of Alberta. This acquisition marks the commencement of our business operations in Canada.

We continue to believe there are attractive opportunities to expand our presence in the rent-to-own industry both nationally and internationally. We intend to increase the number of stores in which we operate by an average of approximately 5% to 10% per year over the next several years. We plan to accomplish our future growth through both selective and opportunistic acquisitions and new store development.

***Building Our National Brand***

We have implemented strategies to increase our name recognition and enhance our national brand. As part of that strategy, we utilize television and radio commercials, print, direct response and in-store signage, all of which are designed to increase our name recognition among our customers and potential customers. In 2003, we also began a sponsorship with the Woods Brothers NASCAR racing team, which we believe will further enhance our name recognition. We believe that as the Rent-A-Center name gains familiarity and national recognition through our advertising efforts, we will continue to educate the customer about the rent-to-own alternative to merchandise purchases as well as solidify our reputation as a leading provider of high quality branded merchandise.



**Table of Contents****Our Stores**

At December 31, 2003, we operated 2,648 stores nationwide and in Puerto Rico. In addition, our subsidiary ColorTyme franchised 329 stores in 40 states. This information is illustrated by the following table:

Location	Number of Stores	
	Company Owned	Franchised
Alabama	56	
Alaska	6	
Arizona	56	7
Arkansas	32	3
California	158	9
Colorado	36	4
Connecticut	30	5
Delaware	16	1
District of Columbia	4	
Florida	154	13
Georgia	101	13
Hawaii	11	3
Idaho	7	5
Illinois	124	6
Indiana	106	6
Iowa	22	
Kansas	31	19
Kentucky	41	4
Louisiana	42	5
Maine	23	10
Maryland	57	6
Massachusetts	48	7
Michigan	103	13
Minnesota	4	
Mississippi	26	2
Missouri	71	9
Montana	6	4
Nebraska	11	
Nevada	19	8
New Hampshire	14	2
New Jersey	40	8
New Mexico	13	9
New York	133	14
North Carolina	107	13
North Dakota	2	
Ohio	160	3
Oklahoma	40	15
Oregon	24	7
Pennsylvania	102	4
Puerto Rico	25	
Rhode Island	13	2
South Carolina	39	4
South Dakota	5	
Tennessee	93	4
Texas	278	60
Utah	16	3
Vermont	7	
Virginia	52	8

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Washington	41	9
West Virginia	16	2
Wisconsin	22*	
Wyoming	5	
TOTAL	2,648	329

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\* Represents stores operated by Get It Now, LLC, one of our subsidiaries.

Our stores average approximately 4,400 square feet and are located primarily in strip centers. Because we receive merchandise shipments directly from vendors, we are able to dedicate approximately 75% of the store space to showroom floor, and also eliminate warehousing costs.

### **Rent-A-Center Store Operations**

#### ***Product Selection***

Our stores offer merchandise from four basic product categories: home electronics, appliances, computers and furniture and accessories. Although we seek to ensure our stores maintain sufficient inventory to offer customers a wide variety of models, styles and brands, we generally limit inventory to prescribed levels to ensure strict inventory controls. We seek to provide a wide variety of high quality merchandise to our customers, and we emphasize high-end products from name-brand manufacturers. For the year ended December 31, 2003, home electronic products accounted for approximately 40% of our store rental revenue,

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furniture and accessories for 34%, appliances for 16% and computers for 10%. Customers may request either new merchandise or previously rented merchandise. Previously rented merchandise is offered at the same weekly or monthly rental rate as is offered for new merchandise, but with an opportunity to obtain ownership of the merchandise after fewer rental payments.

Home electronic products offered by our stores include high definition ready and wide-screen televisions, DVD players, home entertainment centers, video cassette recorders and stereos from top name-brand manufacturers such as Philips, Sony, JVC, Toshiba and Mitsubishi. We rent major appliances manufactured by Whirlpool, including refrigerators, washing machines, dryers, microwave ovens, freezers and ranges. We offer personal and laptop computers from Dell, IBM, Compaq and Hewlett-Packard. We rent a variety of furniture products, including dining room, living room and bedroom furniture featuring a number of styles, materials and colors. We offer furniture made by Ashley, England, Berkline and Standard and other top name-brand manufacturers. Accessories include pictures, lamps and tables and are typically rented as part of a package of items, such as a complete room of furniture. Showroom displays enable customers to visualize how the product will look in their homes and provide a showcase for accessories.

***Rental Purchase Agreements***

Our customers generally enter into weekly or monthly rental purchase agreements, which renew automatically upon receipt of each payment. We retain title to the merchandise during the term of the rental purchase agreement. Ownership of the merchandise generally transfers to the customer if the customer has continuously renewed the rental purchase agreement for a period of 7 to 30 months, depending upon the product type, or exercises a specified early purchase option. Although we do not conduct a formal credit investigation of each customer, a potential customer must provide store management with sufficient personal information to allow us to verify their residence and sources of income. References listed by the customer are contacted to verify the information contained in the customer's rental purchase order form. Rental payments are generally made in the store in cash, by money order or debit card. Approximately 85% of our customers pay on a weekly basis. Depending on state regulatory requirements, we charge for the reinstatement of terminated accounts or collect a delinquent account fee, and collect loss/damage waiver fees from customers desiring product protection in case of theft or certain natural disasters. These fees are standard in the industry and may be subject to government-specified limits. Please read the section entitled Government Regulation.

***Product Turnover***

On average, a minimum rental term of 18 months is generally required to obtain ownership of new merchandise. We believe that only approximately 25% of our initial rental purchase agreements are taken to the full term of the agreement, although the average total life for each product is approximately 22 months, which includes the initial rental period, all re-rental periods and idle time in our system. Turnover varies significantly based on the type of merchandise rented, with certain consumer electronics products, such as camcorders and video cassette recorders, generally rented for shorter periods, while appliances and furniture are generally rented for longer periods. To cover the relatively high operating expenses generated by greater product turnover, rental purchase agreements require higher aggregate payments than are generally charged under other types of purchase plans, such as installment purchase or credit plans.

***Customer Service***

We generally offer same day or 24-hour delivery and installation of our merchandise at no additional cost to the customer. We provide any required service or repair without additional charge, except for damage in excess of normal wear and tear. Repair services are provided through our national network of 23 service centers, the cost of which may be reimbursed by the vendor if the item is still under factory warranty. If the product cannot be repaired at the customer's residence, we provide a temporary replacement while the product is being repaired. The customer is fully liable for damage, loss or destruction of the merchandise, unless the customer purchases an optional loss/ damage waiver covering the particular loss. Most of the products we offer

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are covered by a manufacturer's warranty for varying periods, which, subject to the terms of the warranty, is transferred to the customer in the event that the customer obtains ownership.

***Collections***

Store managers use our management information system to track collections on a daily basis. For fiscal years 2003, 2002, and 2001, the average week ending past due percentages were 6.55%, 5.95% and 5.74%, respectively. For those fiscal years, our goal was to have no more than 6.50% of our rental agreements past due one day or more each Saturday evening. For the upcoming fiscal year, our goal is to have no more than 5.99% of our rental agreements past due one day or more each Saturday evening. If a customer fails to make a rental payment when due, store personnel will attempt to contact the customer to obtain payment and reinstate the agreement, or will terminate the account and arrange to regain possession of the merchandise. We attempt to recover the rental items as soon as possible following termination or default of a rental purchase agreement, generally by the seventh day. Collection efforts are enhanced by the numerous personal and job-related references required of customers, the personal nature of the relationships between store employees and customers and the fact that, following a period in which a customer is temporarily unable to make payments on a piece of rental merchandise and must return the merchandise, that customer generally may re-rent a piece of merchandise of similar type and age on the terms the customer enjoyed prior to that period. Charge-offs due to customer stolen merchandise, expressed as a percentage of store revenues, were approximately 2.3% in 2003 and 2.5% in each of 2002 and 2001.

**Management**

We organize our network of stores geographically with multiple levels of management. At the individual store level, each store manager is responsible for customer and account relations, delivery and collection of merchandise, inventory management, staffing, training store personnel and certain marketing efforts. Three times each week, store management is required to count the store's inventory on hand and compare the count to the accounting records, with the market manager performing a similar audit at least bi-monthly. In addition, our individual store managers track their daily store performance for revenue collected as compared to the projected performance of their store. Each store manager reports to a market manager within close proximity who typically oversees six to eight stores. Typically, a market manager focuses on developing the personnel in his or her market and ensuring all stores meet our quality, cleanliness and service standards. In addition, a market manager routinely audits numerous areas of the stores' operations, including gross profit per rental agreement, petty cash and customer order forms. A significant portion of a market manager's and store manager's compensation is dependent upon store revenues and profits, which are monitored by our management reporting system and our tight control over inventory afforded by our direct shipment practice.

At December 31, 2003, we had 348 market managers who, in turn, reported to 56 regional directors. Regional directors monitor the results of their entire region, with an emphasis on developing and supervising the market managers in their region. Similar to the market managers, regional directors are responsible for ensuring store managers are following the operational guidelines, particularly those involving store presentation, collections, inventory levels and order verification. The regional directors report to eight senior vice presidents located throughout the country. The regional directors receive a significant amount of their compensation based on the profitability of the stores under their management.

Our executive management team at the home office directs and coordinates purchasing, financial planning and controls, employee training, personnel matters, acquisitions and new store initiatives. Our executive management team also evaluates the performance of each region, market and store, including the use of on-site reviews. All members of our executive management team receive a significant amount of their total compensation based on the profits generated by the entire company. As a result, our business strategy emphasizes strict cost containment.

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### **Management Information Systems**

Through a licensing agreement with High Touch, Inc., we utilize an integrated management information and control system. Each store is equipped with a computer system utilizing point of sale software developed by High Touch. This system tracks individual components of revenue, each item in idle and rented inventory, total items on rent, delinquent accounts, items in service and other account information. We electronically gather each day's activity report, which provides our executive management with access to all operating and financial information concerning any of our stores, markets or regions and generates management reports on a daily, weekly, month-to-date and year-to-date basis for each store and for every rental purchase transaction. The system enables us to track all of our merchandise and rental purchase agreements, which often include more than one unit of merchandise. In addition, our bank reconciliation system performs a daily sweep of available funds from our stores' depository accounts into our central operating account based on the balances reported by each store. Our system also includes extensive management software, report-generating capabilities and a virtual private network. The virtual private network allows us to communicate with the stores more effectively and efficiently. The reports for all stores are reviewed on a daily basis by management and unusual items are typically addressed the following business day. Utilizing the management information system, our executive management, regional directors, market managers and store managers closely monitor the productivity of stores under their supervision according to our prescribed guidelines.

The integration of our management information system, developed by High Touch, with our accounting system, developed by Lawson Software, Inc., facilitates the production of our financial statements. These financial statements are distributed monthly to all stores, markets, regions and our executive management team for their review.

### **Purchasing and Distribution**

Our executive management determines the general product mix in our stores based on analyses of customer rental patterns and the introduction of new products on a test basis. Individual store managers are responsible for determining the particular product selection for their store from the list of products approved by executive management. Store and market managers make specific purchasing decisions for the stores, subject to review by executive management. This is done on our new online ordering system. Additionally, we have predetermined levels of inventory allowed in each store which restrict levels of merchandise that may be purchased. All merchandise is shipped by vendors directly to each store, where it is held for rental. We do not utilize any distribution centers. These practices allow us to retain tight control over our inventory and, along with our selection of products for which consistent historical demand has been shown, reduces the number of obsolete items in our stores. The stores also have online access to determine whether other stores in their market may have merchandise available.

We purchase the majority of our merchandise from manufacturers, who ship directly to each store. Our largest suppliers include Ashley and Whirlpool, who accounted for approximately 14.9% and 13.3%, respectively, of merchandise purchased in 2003. No other supplier accounted for more than 10% of merchandise purchased during this period. We do not generally enter into written contracts with our suppliers that obligate us to meet certain minimum purchasing levels. Although we expect to continue relationships with our existing suppliers, we believe that there are numerous sources of products available, and we do not believe that the success of our operations is dependent on any one or more of our present suppliers.

### **Marketing**

We promote the products and services in our stores through direct mail advertising, radio, television and secondary print media advertisements. Our advertisements emphasize such features as product and name-brand selection, prompt delivery and the absence of initial deposits, credit investigations or long-term obligations. In 2003, we also began a sponsorship with the Woods Brothers NASCAR racing team. Advertising expense as a percentage of store revenue for the years ended December 31, 2003, 2002 and 2001 was approximately 3.1%, 3.2% and 4.0%, respectively. As we obtain new stores in our existing market areas,

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the advertising expenses of each store in the market can be reduced by listing all stores in the same market-wide advertisement.

**Competition**

The rent-to-own industry is highly competitive. According to industry sources and our estimates, the six largest industry participants account for approximately 4,800 of the 8,300 rent-to-own stores in the United States. We are the largest operator in the rent-to-own industry with 2,648 stores and 329 franchised locations as of December 31, 2003. Our stores compete with other national and regional rent-to-own businesses, as well as with rental stores that do not offer their customers a purchase option. With respect to customers desiring to purchase merchandise for cash or on credit, we also compete with department stores, credit card companies and discount stores. Competition is based primarily on store location, product selection and availability, customer service and rental rates and terms.

**ColorTyme Operations**

ColorTyme is our nationwide franchisor of rent-to-own stores. At December 31, 2003, ColorTyme franchised 329 rent-to-own stores in 40 states. These rent-to-own stores offer high quality durable products such as home electronics, appliances, computers and furniture and accessories. During 2003, 37 new locations were added, 7 were closed and 19 were sold, of which 18 were sold to us.

All but 12 of the ColorTyme franchised stores use ColorTyme's tradenames, service marks, trademarks, logos, emblems and indicia of origin. These 12 stores are franchises acquired in the Thorn Americas acquisition and continue to use the Rent-A-Center name. All stores operate under distinctive operating procedures and standards. ColorTyme's primary source of revenue is the sale of rental merchandise to its franchisees who, in turn, offer the merchandise to the general public for rent or purchase under a rent-to-own program. As franchisor, ColorTyme receives royalties of 2.0% to 5.0% of the franchisees' monthly gross revenue and, generally, an initial fee of between \$7,500 per location for existing franchisees and up to \$35,000 per location for new franchisees.

The ColorTyme franchise agreement generally requires the franchised stores to utilize specific computer hardware and software for the purpose of recording rentals, sales and other record keeping and central functions. ColorTyme retains the right to retrieve data and information from the franchised stores' computer systems. The franchise agreements also limit the ability of the franchisees to compete with other franchisees.

The franchise agreement also requires the franchised stores to exclusively offer for rent or sale only those brands, types and models of products that ColorTyme has approved. The franchised stores are required to maintain an adequate mix of inventory that consists of approved products for rent as dictated by ColorTyme policy manuals. ColorTyme negotiates purchase arrangements with various suppliers it has approved. ColorTyme's largest supplier is Whirlpool, which accounted for approximately 15% of merchandise purchased by ColorTyme in 2003.

ColorTyme is a party to an agreement with Wells Fargo Foothill, Inc., who provides \$50.0 million in aggregate financing to qualifying franchisees of ColorTyme generally of up to five times their average monthly revenues. Under the Wells Fargo agreement, upon an event of default by the franchisee under agreements governing this financing and upon the occurrence of certain other events, Wells Fargo can assign the loans and the collateral securing such loans to ColorTyme, with ColorTyme then succeeding to the rights of Wells Fargo under the debt agreements, including the right to foreclose on the collateral. An additional \$15.0 million of financing is provided by Texas Capital Bank, National Association under an agreement similar to the Wells Fargo financing. Rent-A-Center East, a wholly owned subsidiary of Rent-A-Center, Inc., guarantees the obligations of ColorTyme under each of these agreements, excluding the effects of any amounts that could be recovered under collateralization provisions, up to a maximum amount of \$65.0 million, of which \$29.0 million was outstanding as of December 31, 2003. Mark E. Speese, Rent-A-Center's Chairman of the Board and Chief Executive Officer, is a passive investor in Texas Capital Bank, owning less than 1% of its outstanding equity.

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ColorTyme has established a national advertising fund for the franchised stores, whereby ColorTyme has the right to collect up to 3% of the monthly gross revenue from each franchisee as contributions to the fund. Currently, ColorTyme has set the monthly franchisee contribution at \$250 per store per month. ColorTyme directs the advertising programs of the fund, generally consisting of advertising in print, television and radio. ColorTyme also has the right to require franchisees to expend 3% of their monthly gross revenue on local advertising.

ColorTyme licenses the use of its trademarks to the franchisees under the franchise agreement. ColorTyme owns the registered trademarks ColorTyme®, ColorTyme-What's Right for You®, and FlexTyme®, along with certain design and service marks.

Some of ColorTyme's franchisees may be in locations where they directly compete with our company-owned stores, which could negatively impact the business, financial condition and operating results of our company-owned stores.

The ColorTyme franchise agreement provides us a right of first refusal to purchase the franchise location of a ColorTyme franchisee that wishes to exit the business.

## **Get It Now Operations**

All of our Wisconsin stores are operated by our subsidiary Get It Now, LLC. Get It Now operates under a retail operation which generates installment credit sales through a retail transaction. As of December 31, 2003, we operated 22 company-owned stores within Wisconsin, all of which operate under the name Get It Now.

## **Trademarks**

We own various registered trademarks, including Rent-A-Center®, Renters Choice®, Remco® and Get It Now®. The products held for rent also bear trademarks and service marks held by their respective manufacturers.

## **Employees**

As of March 5, 2004, we had approximately 15,181 employees, of whom 290 are assigned to our headquarters and the remainder are directly involved in the management and operation of our stores and service centers. As of the same date, we had approximately 18 employees dedicated to ColorTyme, all of whom were employed full-time. The employees of the ColorTyme franchisees are not employed by us. None of our employees, including ColorTyme employees, are covered by a collective bargaining agreement. However, in June 2001, the employees of six of our stores in New York, New York elected to be represented by the Teamsters union. However, we have not entered into a collective bargaining agreement covering these employees.

We believe relationships with our employees and ColorTyme's relationships with its employees are generally good. In connection with the settlement of the *Wilfong* matter finalized in December 2002, we entered into a four-year consent decree, which can be extended by the *Wilfong* court for an additional one year upon a showing of good cause. We also agreed to augment our human resources department and our internal employee complaint procedures, enhance our gender anti-discrimination training for all employees, hire a consultant mutually acceptable to the parties for two years to advise us on employment matters, provide certain reports to the EEOC during the period of the consent decree, seek qualified female representation on our board of directors, publicize our desire to recruit, hire and promote qualified women, offer to fill job vacancies within our regional markets with qualified class members who reside in those markets and express an interest in employment by us to the extent of 10% of our job vacancies in such markets over a fifteen month period, and to take certain other steps to improve opportunities for women. We initiated many of the above programs prior to entering into the settlement of the *Wilfong* matter.

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**Government Regulation**

***State Regulation***

Currently 47 states, the District of Columbia and Puerto Rico have legislation regulating rental purchase transactions. We believe this existing legislation is generally favorable to us, as it defines and clarifies the various disclosures, procedures and transaction structures related to the rent-to-own business with which we must comply. With some variations in individual states, most related state legislation requires the lessor to make prescribed disclosures to customers about the rental purchase agreement and transaction, and provides time periods during which customers may reinstate agreements despite having failed to make a timely payment. Some state rental purchase laws prescribe grace periods for non-payment, prohibit or limit certain types of collection or other practices, and limit certain fees that may be charged. Nine states limit the total rental payments that can be charged. These limitations, however, generally do not become applicable unless the total rental payments required under an agreement exceed 2.0 times to 2.4 times of the disclosed cash price or the retail value of the rental product.

Minnesota, which has a rental purchase statute, and New Jersey and Wisconsin, which do not have rental purchase statutes, have had court decisions which treat rental purchase transactions as credit sales subject to consumer lending restrictions. In response, we have developed and utilized a separate rental agreement in Minnesota which does not provide customers with an option to purchase rented merchandise. In New Jersey, we have provided increased disclosures and longer grace periods. In Wisconsin, our Get It Now customers are provided an opportunity to purchase our merchandise through an installment sale transaction. We operate four stores in Minnesota and 40 stores in New Jersey. Our subsidiary Get It Now operates 22 stores in Wisconsin.

North Carolina has no rental purchase legislation. However, the retail installment sales statute in North Carolina recognizes that rental purchase transactions which provide for more than a nominal purchase price at the end of the agreed rental period are not credit sales under such statute. We operate 107 stores in North Carolina.

There can be no assurance that new or revised rental purchase laws will not be enacted or, if enacted, that the laws would not have a material and adverse effect on us.

***Federal Legislation***

To date, no comprehensive federal legislation has been enacted regulating or otherwise impacting the rental purchase transaction. We do, however, comply with the Federal Trade Commission recommendations for disclosure in rental purchase transactions.

From time to time, we have supported legislation introduced in Congress that would regulate the rental purchase transaction. Currently, the industry has sponsored two bills that have been introduced in Congress that we support. While both beneficial and adverse legislation may be introduced in Congress in the future, any adverse federal legislation, if enacted, could have a material and adverse effect on us.



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**RISK FACTORS**

*You should carefully consider the risks described below before making an investment decision. We believe these are all the material risks currently facing our business. Our business, financial condition or results of operations could be materially adversely affected by these risks. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. You should also refer to the other information included or incorporated by reference in this report, including our financial statements and related notes.*

**We may not be able to successfully implement our growth strategy, which could cause our future earnings to grow more slowly or even decrease.**

As part of our growth strategy, we intend to increase our total number of stores in both existing markets and new markets through a combination of new store openings and store acquisitions. We increased our store base by 123 stores in 2001, 126 stores in 2002 and 241 stores in 2003. Our growth strategy could place a significant demand on our management and our financial and operational resources. This growth strategy is subject to various risks, including uncertainties regarding our ability to open new stores and our ability to acquire additional stores on favorable terms. We may not be able to continue to identify profitable new store locations or underperforming competitors as we currently anticipate. If we are unable to implement our growth strategy, our earnings may grow more slowly or even decrease.

Our continued growth also depends on our ability to increase sales in our existing stores. Our same store sales increased by 8.0%, 6.0% and 3.0% for 2001, 2002 and 2003, respectively. As a result of new store openings in existing markets and because mature stores will represent an increasing proportion of our store base over time, our same store sale increases in future periods may be lower than historical levels.

**If we fail to effectively manage our growth and integrate new stores, our financial results may be adversely affected.**

The benefits we anticipate from our growth strategy may not be realized. The addition of new stores, both through store openings and through acquisitions, requires the integration of our management philosophies and personnel, standardization of training programs, realization of operating efficiencies and effective coordination of sales and marketing and financial reporting efforts. In addition, acquisitions in general are subject to a number of special risks, including adverse short-term effects on our reported operating results, diversion of management's attention and unanticipated problems or legal liabilities. Further, a newly opened store generally does not attain positive cash flow during its first year of operations.

**There are legal proceedings pending against us seeking material damages. The costs we incur in defending ourselves or associated with settling any of these proceedings, as well as a material final judgment or decree against us, could materially adversely affect our financial condition by requiring the payment of the settlement amount, a judgment or the posting of a bond.**

Some lawsuits against us involve claims that our rental agreements constitute installment sales contracts, violate state usury laws or violate other state laws enacted to protect consumers. We are also defending a class action lawsuit alleging we violated the securities laws and lawsuits alleging we violated state wage and hour laws. Because of the uncertainties associated with litigation, we cannot estimate for you our ultimate liability for these matters, if any. The failure to pay any judgment would be a default under our senior credit facilities and the indenture governing our outstanding subordinated notes.

**Our debt agreements impose restrictions on us which may limit or prohibit us from engaging in certain transactions. If a default were to occur, our lenders could accelerate the amounts of debt outstanding, and holders of our secured indebtedness could force us to sell our assets to satisfy all or a part of what is owed.**

Covenants under our senior credit facilities and the indenture governing our outstanding subordinated notes restrict our ability to pay dividends, engage in various operational matters, as well as require us to

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maintain specified financial ratios and satisfy specified financial tests. Our ability to meet these financial ratios and tests may be affected by events beyond our control. These restrictions could limit our ability to obtain future financing, make needed capital expenditures or other investments, repurchase our outstanding debt or equity, withstand a future downturn in our business or in the economy, dispose of operations, engage in mergers, acquire additional stores or otherwise conduct necessary corporate activities. Various transactions that we may view as important opportunities, such as specified acquisitions, are also subject to the consent of lenders under the senior credit facilities, which may be withheld or granted subject to conditions specified at the time that may affect the attractiveness or viability of the transaction.

If a default were to occur, the lenders under our senior credit facilities could accelerate the amounts outstanding under the credit facilities, and our other lenders could declare immediately due and payable all amounts borrowed under other instruments that contain certain provisions for cross-acceleration or cross-default. In addition, the lenders under these agreements could terminate their commitments to lend to us. If the lenders under these agreements accelerate the repayment of borrowings, we may not have sufficient liquid assets at that time to repay the amounts then outstanding under our indebtedness or be able to find additional alternative financing. Even if we could obtain additional alternative financing, the terms of the financing may not be favorable or acceptable to us.

The existing indebtedness under our senior credit facilities is secured by substantially all of our assets. Should a default or acceleration of this indebtedness occur, the holders of this indebtedness could sell the assets to satisfy all or a part of what is owed. Our senior credit facilities also contain certain provisions prohibiting the modification of our outstanding subordinated notes, as well as limiting the ability to refinance such notes.

**A change of control could accelerate our obligation to pay our outstanding indebtedness, and we may not have sufficient liquid assets to repay these amounts.**

Under our senior credit facilities, an event of default would result if a third party became the beneficial owner of 35.0% or more of our voting stock or upon certain changes in the constitution of our Board of Directors. As of December 31, 2003, we were required to make principal payments under our senior credit facilities of \$4.0 million in 2004, \$4.0 million in 2005, \$4.0 million in 2006, \$4.0 million in 2007, and \$382.0 million after 2007. These payments reduce our cash flow. If the lenders under our debt instruments accelerate these obligations, we may not have sufficient liquid assets to repay amounts outstanding under these agreements.

Under the indenture governing our outstanding subordinated notes, in the event that a change in control occurs, we may be required to offer to purchase all of our outstanding subordinated notes at 101% of their original aggregate principal amount, plus accrued interest to the date of repurchase. A change in control also would result in an event of default under our senior credit facilities, which would allow our lenders to accelerate indebtedness owed to them.

**Rent-to-own transactions are regulated by law in most states. Any adverse change in these laws or the passage of adverse new laws could expose us to litigation or require us to alter our business practices.**

As is the case with most businesses, we are subject to various governmental regulations, including specifically in our case regulations regarding rent-to-own transactions. There are currently 47 states that have passed laws regulating rental purchase transactions and another state that has a retail installment sales statute that excludes rent-to-own transactions from its coverage if certain criteria are met. These laws generally require certain contractual and advertising disclosures. They also provide varying levels of substantive consumer protection, such as requiring a grace period for late fees and contract reinstatement rights in the event the rental purchase agreement is terminated. The rental purchase laws of nine states limit the total amount of rentals that may be charged over the life of a rental purchase agreement. Several states also effectively regulate rental purchase transactions under other consumer protection statutes. We are currently subject to outstanding judgments and other litigation alleging that we have violated some of these statutory provisions.

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Although there is no comprehensive federal legislation regulating rental-purchase transactions, adverse federal legislation may be enacted in the future. From time to time, legislation has been introduced in Congress seeking to regulate our business. In addition, various legislatures in the states where we currently do business may adopt new legislation or amend existing legislation that could require us to alter our business practices.

### **Our business depends on a limited number of key personnel, with whom we do not have employment agreements. The loss of any one of these individuals could disrupt our business.**

Our continued success is highly dependent upon the personal efforts and abilities of our senior management, including Mark E. Speese, our Chairman of the Board and Chief Executive Officer and Mitchell E. Fadel, our President and Chief Operating Officer. We do not have employment contracts with or maintain key-person insurance on the lives of any of these officers and the loss of any one of them could disrupt our business.

### **A small group of our directors and their affiliates have influence over the outcome of certain corporate transactions affecting us, including potential mergers or acquisitions, the constitution of our board of directors and sales or changes in control.**

Affiliates of Apollo Management IV, L.P. hold all of our outstanding Series C preferred stock. Pursuant to the terms of a stockholders agreement entered into among us, Apollo, Mark E. Speese and certain other parties, Apollo has the right to designate two persons to be nominated to our board of directors. The terms of our Series C preferred stock as well as the stockholders agreement also contain provisions requiring Apollo's approval to effect certain transactions involving us, including repurchasing shares of our common stock, declaring or paying any dividend on our common stock, increasing the size of our board of directors to more than eight persons, selling all or substantially all of our assets and entering into any merger or consolidation or other business combination.

These documents also provide that one member of each of our board committees must be a director who was designated for nomination by Apollo. In addition, the terms of our Series C preferred stock and the stockholders agreement restrict our ability to issue debt or equity securities with a value in excess of \$10 million without the majority affirmative vote of our finance committee, and in most cases, require the unanimous vote of our finance committee for the issuance of our equity securities with a value in excess of \$10 million.

### **Our organizational documents, Series C preferred stock and debt instruments contain provisions that may prevent or deter another group from paying a premium over the market price to our stockholders to acquire our stock.**

Our organizational documents contain provisions that classify our board of directors, authorize our board of directors to issue blank check preferred stock and establish advance notice requirements on our stockholders for director nominations and actions to be taken at annual meetings of the stockholders. In addition, as a Delaware corporation, we are subject to Section 203 of the Delaware General Corporation Law relating to business combinations. Our senior credit facilities, the indenture governing our subordinated notes and our Series C preferred stock certificate of designations each contain various change of control provisions which, in the event of a change of control, would cause a default under those provisions. These provisions and arrangements could delay, deter or prevent a merger, consolidation, tender offer or other business combination or change of control involving us that could include a premium over the market price of our common stock that some or a majority of our stockholders might consider to be in their best interests.

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**Our stock price is volatile, and you may not be able to recover your investment if our stock price declines.**

The stock price of our common stock has been volatile and can be expected to be significantly affected by factors such as:

quarterly variations in our results of operations, which may be impacted by, among other things, changes in same store sales and when and how many stores we acquire or open;

quarterly variations in our competitors' results of operations;

changes in earnings estimates or buy/sell recommendations by financial analysts;