AES CORP
Form DEF 14A
March 07, 2019

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
SCHEDULE 14A
Proxy Statement Pursuant to Section 14(a) of the
Securities Exchange Act of 1934
(Amendment No.)
Filed by the Registrant
Filed by a Party other than the Registrant
Check the appropriate box:
¨Preliminary Proxy Statement
¨Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
x Definitive Proxy Statement
¨Definitive Additional Materials
¨Soliciting Material Pursuant to 240.14a-12
THE AES CORPORATION

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement if other than the Registrant)
Payment of Filing Fee (Check the appropriate box):
No fee required.
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(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

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(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

NOTICE OF 2019 ANNUAL MEETING OF STOCKHOLDERS OF THE AES CORPORATION
TO BE HELD ON THURSDAY, APRIL 18, 2019
March 6, 2019
TO THE HOLDERS OF COMMON STOCK OF THE AES CORPORATION:
Notice is hereby given that the 2019 Annual Meeting of Stockholders of The AES Corporation (the "Company" or "AES") will be held on Thursday, April 18, 2019, at 9:30 a.m. EDT, at the American Trucking Association Conference Center, 950 North Glebe Road, Suite 210, Arlington, VA 22203 for the following purposes, as more fully described in the accompanying Proxy Statement:

1. To elect ten members to the Company's Board of Directors (the "Board");
2. To approve, on an advisory basis, the Company's executive compensation;
3. To ratify the appointment of Ernst & Young LLP ("EY" or the "Independent Registered Public Accounting Firm") as the independent auditors of the Company for fiscal year 2019; and
4. To transact such other business as may properly come before the Annual Meeting.

Doors to the meeting will open at 8:30 a.m. EDT. Stockholders of record at the close of business on February 26, 2019 are entitled to notice of, and to vote at, the Annual Meeting. If you plan to attend the Annual Meeting, please note that, for security reasons, before being admitted, you must present your admission ticket or proof of stock ownership and valid photo identification at the door. All hand-carried items will be subject to inspection and any bags, briefcases or packages must be checked at the registration desk prior to entering the meeting room.
IMPORTANT NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS FOR THE STOCKHOLDER MEETING TO BE HELD ON THURSDAY, APRIL 18, 2019: THE PROXY STATEMENT, ANNUAL REPORT ON FORM 10-K AND RELATED PROXY MATERIALS ARE AVAILABLE FREE OF CHARGE AT www.edocumentview.com/aes.

Paul L. Freedman
Senior Vice President, General Counsel
and Corporate Secretary

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Proxy Statement

PROXY STATEMENT

The AES Corporation
4300 Wilson Blvd.
Arlington, VA 22203, USA
www.aes.com

March 6, 2019

The Board of Directors (the "Board") of The AES Corporation (the "Company" or "AES") is soliciting proxies to be voted on the Stockholders' behalf at the 2019 Annual Meeting of Stockholders (the "Annual Meeting").

The Annual Meeting will commence at 9:30 a.m. EDT on Thursday, April 18, 2019. The Annual Meeting will be held at the American Trucking Association Conference Center, 950 North Glebe Road, Suite 210, Arlington, VA 22203.

This Proxy Statement provides information regarding the matters to be voted on at the Annual Meeting, as well as other information that may be useful to you. In accordance with rules adopted by the United States Securities and Exchange Commission (the "SEC"), instead of mailing a printed copy of our proxy materials to each Stockholder of record, we are furnishing proxy materials to our Stockholders on the Internet. If you received a Notice of Internet Availability of Proxy Materials (the "Notice") by mail, you will not receive a printed copy of the proxy materials other than as described below. Instead, the Notice will instruct you as to how you may access and review all of the important information contained in the proxy materials. The Notice also instructs you as to how you may submit your Proxy over the Internet. If you received a Notice by mail and would like to receive a printed copy of our proxy materials, you should follow the instructions for requesting such materials included in the Notice.

This Proxy Statement and accompanying Proxy Card, Annual Report on Form 10-K for the year ended December 31, 2018 (the "AES Form 10-K") and related proxy materials will first be given and/or made available to Stockholders on or about March 7, 2019. These materials will be available at www.envisionreports.com/aes for registered holders of AES stock and, at www.edocumentview.com/aes for beneficial holders of AES stock. In accordance with SEC rules, the websites, www.envisionreports.com/aes and www.edocumentview.com/aes, provide complete anonymity with respect to a Stockholder accessing the websites.

At the close of business on February 26, 2019, there were 662,404,101 shares of common stock outstanding. Each share of common stock is entitled to one vote.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Proxy Statement contains forward-looking statements as defined in the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and is subject to the safe harbors created therein. The forward-looking statements contained herein are generally identified by the words “believe,” “project,” “expect,” “anticipate,” “estimate,” “intend,” “strate “future,” “opportunity,” “plan,” “may,” “should,” “will,” “would,” “will be,” “will continue,” “will likely result,” and similar e Forward-looking statements are based on the beliefs and assumptions of our management and on currently available information. A detailed discussion of risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included in the AES Form 10-K. We undertake no responsibility to publicly update or revise any forward-looking statement.

PROXY STATEMENT SUMMARY

This summary highlights information contained elsewhere in this Proxy Statement. Please refer to the complete Proxy Statement and the AES Form 10-K before you vote.

MEETING INFORMATION

2019 Annual Meeting of Stockholders

Date and Time:	April 18, 2019	Location:	American Trucking Association Conference Center
	9:30 a.m. EDT		950 North Glebe Road, Suite 210, Arlington, VA 22203
Record Date:	February 26, 2019		* Admission Ticket required, please see page 65 of this Proxy Statement for details.

Voting Matters	Board of Directors’ Recommendations
1. Election of Ten Director Nominees	FOR all Director Nominees
2. Advisory Approval of Executive Compensation	FOR
3. Ratification of Appointment of EY as the Independent Auditors for Fiscal Year 2019	FOR

HOW TO VOTE

Your vote is important. You may vote in person at the Annual Meeting or submit a proxy over the Internet. If you received a paper copy of the proxy card (or you requested a paper copy of the materials) you may vote by telephone or by mail.

Online : www.envisionreports.com/aes	By Mail + Complete, sign, date and return your proxy card in the envelope provided
By Phone) Call the phone number located on the top of your proxy card	In Person Attend our Annual Meeting and vote by ballot

Proxy Statement Summary

CORPORATE GOVERNANCE

Our Corporate Governance Policies Reflect Best Practices

Annual Election of All Directors	98% Average Attendance of Incumbent Directors at Board and Committee Meetings
Non-Executive, Independent Chair of the Board Since 2003	Audit, Compensation and Governance Committee Members Are All Independent
Nine of Ten Director Nominees Are Independent	Directors Are Subject to Rigorous Stock Ownership Requirements
Annual Board and Committee Self-Evaluations and Review of Director Qualifications	Director Compensation Reviewed Annually
Executive Sessions of Independent Directors Held at Each Regularly Scheduled Board Meeting, and Directors Meet Periodically Throughout the Year with Individual Members of Management	Financial Audit Committee Members Are All Financially Literate and Four of Five Are Audit Committee Financial Experts
Directors Subject to Term Limits, Average Tenure of Our Directors is Less than Six Years	No Increase in Director Compensation Since 2012

Director Nominee Facts. The following charts details the qualifications of our Director nominees that are important to our business. Further discussion on the qualifications and experience of Director nominees is included in “2019 Director Nominees” section of this Proxy Statement.

Proxy Statement Summary

2018 Stockholder Engagement Program

We place great value on Stockholder outreach, and engage regularly with our investors to gain insight into the governance issues about which they care most. We seek a collaborative and mutually beneficial approach to issues of importance to investors that affect our business and aim to ensure that our corporate governance practices are informed by, and generally are in line with, our Stockholders' expectations. In 2018, we engaged with Stockholders in the fall as part of our engagement program to discuss topics, including, but not limited to, Board Composition and Evaluations, Environmental, Social and Governance ("ESG") Matters and Executive Compensation.

Environmental and Sustainability Matters

AES' efforts in Sustainability, Business Ethics and ESG practices have been recognized by third parties including, Ethisphere Instute as one of the World's Most Ethical Companies, The DowJones Sustainability Index for North America, FTSE4Good Index and the CDP Climate Change and Water Questionnaires. In 2018, AES was the first publicly-traded owner of utilites and power companies based in the US to issue a Climate Scenario Report (the "AES Climate Scenario Report") adopting the recommendations issued by the Task Force on Climate-related Financial Disclosures (TCFD). A copy of the AES Climate Scenario Report is available under the "Sustainability" tab of our website. Further information on AES' ESG practices is included in "Environmental Social and Governance" section of this Proxy Statement.

EXECUTIVE COMPENSATION SUMMARY

AES' executive compensation philosophy emphasizes pay-for-performance. Our philosophy is to provide executive compensation opportunities that approximate the 50th percentile of survey data based on our revenue size and industry. Our incentive plans are designed to reward strong performance, with greater compensation paid when performance exceeds expectations and less compensation paid when performance falls below expectations. Thus, the actual compensation realized by our Named Executive Officers ("NEOs") will be commensurate with the Company's actual performance.

AES' Compensation Committee has a practice of reviewing executive compensation program components, targets and payouts on an annual basis to ensure the strength of our pay-for-performance alignment. Our performance is evaluated against both short-term goals, which support AES' business strategy, and long-term goals, which measure the creation of sustainable Stockholder value.

Compensation and Benefits Best Practices

Target Total Compensation at 50th Percentile	Director and Executive Officer Stock Ownership Guidelines
Independent Consultant Retained by the Compensation Committee	Executive Compensation Clawback Policy
Double-Trigger Change-in-Control for Long Term Compensation Awards	No Change-in-Control Excise Tax Gross Ups
No Perquisites for our Executive Officers, Except for Relocation Benefits	No Backdating or Option Repricing
Directors and Executive Officers Prohibited from Hedging or Pledging of AES Common Stock	Annual Review of Risk Related to Compensation Programs
No Special Retirement Benefit Formulas for Executive Officers	Relative Pay-for-Performance Alignment
Mix of AES-Specific and Relative Performance Goals	

Caps on Annual and Long-Term Incentive Payouts

In 2018, AES again received strong support for its executive compensation programs, with approximately 95% of votes cast approving, on an advisory basis, our executive compensation. In 2018, as in prior years, the Compensation Committee considered input from our Stockholders and other stakeholders as part of its annual review of AES' executive compensation program.

Please see the "Compensation Discussion and Analysis" section in this Proxy Statement for a detailed description of our executive compensation programs.

Board of Directors

BOARD OF DIRECTORS
PROPOSAL 1: ELECTION OF DIRECTORS

The Board has nominated ten Directors (the “Nominees”) for election at the Annual Meeting. The table below summarizes the key qualifications, skills and attributes most relevant to the decision to nominate each candidate to service on the Board. The Nominees’ biographies describe each candidate’s background and relevant experience in more detail. The Nominees are identified and discussed in the paragraphs below for election at this year’s Annual Meeting and to each serve a one-year term expiring at the Annual Meeting in 2020.

	Davidson	Gluski	Harrington	Khanna	Koeppel	Miller	Monie	Morse	Naim	Ubben
Qualifications and Experience										
Leadership	ü	ü	ü	ü	ü	ü	ü	ü	ü	ü
Finance		ü	ü	ü	ü	ü	ü	ü		ü
Industry Knowledge		ü		ü	ü	ü		ü	ü	ü
Global Business	ü	ü	ü	ü	ü	ü	ü	ü	ü	ü
Risk Management	ü	ü	ü		ü	ü	ü	ü	ü	ü
Regulatory		ü	ü		ü	ü				ü
Corporate Strategy	ü	ü	ü	ü	ü	ü	ü	ü	ü	ü
Operations	ü	ü	ü		ü	ü	ü			ü
Human Resources & Compensation	ü	ü	ü	ü	ü	ü	ü	ü	ü	ü
Governance		ü	ü	ü	ü	ü	ü	ü	ü	ü
Engineering & Construction	ü	ü	ü		ü	ü				
Technology	ü	ü	ü	ü	ü	ü	ü	ü		ü
Environmental & Sustainability		ü	ü		ü	ü			ü	ü
Cybersecurity			ü		ü	ü				
Industry Transformation	ü	ü	ü	ü	ü	ü	ü	ü	ü	ü
Entrepreneurial		ü	ü	ü	ü		ü	ü	ü	ü
Power Distribution & Storage		ü			ü	ü				ü
Alternative Energy		ü	ü		ü	ü				ü
Additional Information										
Other Public Boards	2	1	0	1	3	2	1	1	1	0
Years of Service (1)	0	7	5	10	4	5	2	10	6	1
Age	62	61	60	52	60	70	68	72	66	57
Gender	F	M	M	M	F	M	M	M	M	M

(1) Years of Service is calculated from Annual Meeting to Annual Meeting

Board of Directors

Janet G. Davidson

Age: 62
Director Since: February 2019

Board Committees:
Financial Audit Committee
Compensation Committee

Qualifications and Experience: Ms. Davidson brings to the AES Board a deep knowledge of technology, global business operations, customer care and sales, and corporate strategy. Ms. Davidson began her career in 1979 as a member of the Technical Staff of Bell Laboratories, Lucent Technologies (as of 2006 Alcatel Lucent), and served from 1979 through her retirement in 2011 in several key positions including, most recently as Group President Internetworking Systems (2001 to 2005), Chief Strategy Officer (2005 to 2006), Chief Compliance Officer (2006 to 2008) and Executive Vice President, Quality & Customer Care (2008 to 2011). Ms. Davidson became a member of the supervisory board of ST Microelectronics in June 2013 where she is a member of the Audit and Strategic Committees.
Education: Ms. Davidson has a B.A. in Physics from Lehigh University and a M.S. in Electrical Engineering from the Georgia Institute of Technology.
Current and Former Directorships: Ms. Davidson currently serves on the Board of Directors of ST Microelectronics, N.V. (NYSE: STM) (June 2013 to the present) and Millicom International Cellular S.A., (Nasdaq: TIGO) (April 2016 to the present). She also served as a member of the board of Alcatel Lucent Foundation (2011to 2014), Lehigh University Board of Trustees (2005 to 2012), Riverside Symphonia Board of Trustees (2007), and Liberty Science Center Board of Trustees (2005 to 2006).

Andrés R. Gluski

Age: 61
Director Since: September 2011

Board Committees:

Innovation and Technology Committee

Qualifications and Experience: As the Chief Executive Officer ("CEO") of AES, Mr. Gluski provides our Board with in-depth knowledge about the Company's business, the electric industry and international markets. He has led major cost savings initiatives, a simplification of the Company's geographic footprint and global expansion of the Company's renewables and energy storage platforms. Mr. Gluski currently serves on the US-India CEO Forum and previously served on the U.S. Brazil CEO Forum from 2012 through June 2017 . Mr. Gluski also served on the President's Export Council from 2013-2016. In 2015, Mr. Gluski was also appointed Chairman of the Council of the Americas/Americas Society. Prior to his appointment as CEO in September 2011, Mr. Gluski served as Executive Vice President and Chief Operating Officer of the Company from March 2007 until that time, Regional President for Latin America from 2006 to 2007, Senior Vice President for the Caribbean and Central America from 2003 to 2006, CEO of La Electricidad de Caracas ("EDC") from 2002 to 2003 and CEO of AES Gener (Chile) in 2001. Before joining AES, Mr. Gluski held senior positions in the telecommunications and banking industry and at the International Monetary Fund and the Ministry of Finance of Venezuela.

Education: Mr. Gluski is a magna cum laude graduate of Wake Forest University and holds a M.A. and a Ph.D. in Economics from the University of Virginia.

Current and Former Directorships: Mr. Gluski currently serves on the Board of Directors of Waste Management, Inc. (NYSE: WM)(January 2015 to the present), The Council of the Americas/Americas Society (2011 to the present; Chairman since 2015), The Edison Electric Institute (2010 to the present), AES Gener (May 2005 to the present) and EnerAB (2016 to the present). He also served on the Board of Directors of Cliffs Natural Resources (NYSE: CLF) from January 2011 to August 2014 and AES Brasiliana (from March 2006 to 2016).

Board of Directors

Charles L. Harrington
Age: 60
Director Since: December 2013

Board Committees:
Financial Audit Committee, Chair
Governance Committee

Qualifications and Experience: Mr. Harrington brings to the AES Board a strong record of driving innovation and sustainable results. Since May 2008, Mr. Harrington has served as Chairman and CEO of Parsons Corporation, a leading provider of technology-driven solutions in the defense, intelligence and critical infrastructure markets (“Parsons”), and has spent over 37 years with Parsons in various operations, including in finance, as Chief Financial Officer, P&L, and business development roles. During his tenure as CEO of Parsons, Mr. Harrington has focused on transforming strategically important new technologies and business models and led Parsons to record profitability.
Education: Mr. Harrington received a B.S., magna cum laude, in Engineering from California Polytechnic State University and a M.B.A. in Finance and Marketing from the Anderson School of Management, UCLA. He also attended the Executive Education program at the Fuqua School of Business at Duke University.
Current and Former Directorships: Mr. Harrington currently serves on the Board of Directors of the J.G. Boswell Company (privately held) (2015 to the present), Parsons

Corporation (2008 to the present) and Cal Poly Foundation (2010 to the present) and was formerly a member of the boards of the following privately-held or non-profit companies: Anderson School of Management at UCLA (2008 to 2014), Blumenthal Performing Arts Center (2006 to 2012), California Science Center (2008 to 2018) and Business-Higher Education Forum (2011 to 2018).

Tarun Khanna

Age: 52
Director Since: April 2009

Board Committees:
Governance Committee
Innovation and Technology Committee, Chair

Qualifications and Experience: Dr. Khanna is the Jorge Paulo Lemann Professor at the Harvard Business School, joining the faculty in 1993. He brings substantial expertise regarding global business, emerging markets and corporate strategy to the Board. Dr. Khanna's scholarly work has been published in a range of economics, management and foreign policy journals. He has written several books on entrepreneurship in emerging markets, most recently, Trust: Creating the Foundation for

Entrepreneurship in Developing Countries (2018), and is a co-founder of several science-based startups across the developing world. He was appointed a Young Global Leader by the World Economic Forum in 2007, elected Fellow of the Academy of International Business in 2009, appointed Director of Harvard University's Lakshmi Mittal and Family South Asia Institute in 2010, appointed Chairman of the Government of India's Expert Commission on Innovation & Entrepreneurship in 2015, and honored for lifetime scholarly achievement by the Academy of Management in 2015.

Education: Dr. Khanna received a B.S.E. from Princeton University and Ph.D. from Harvard University.

Current and Former Directorships: Dr. Khanna is also a member of the boards of directors of Bharat Financial Inclusion Limited (formerly SKS Microfinance; February 2009 to the present) and Mountain Trails Foods Pvt Ltd. (2018 to the present). He is also a Director of the following privately-held companies: TVS Logistics (2008 to the present), and Axilor (2015 to the present). In addition, Dr. Khanna serves as a Director of the non-profit, Parliamentary Research Services (2015 to the present) and is a Trustee of the Museum of Fine Arts, Boston (2015 to the present).

Board of Directors

Holly K. Koeppel

Age: 60
Director
Since: April
2015

Board
Committees:
Governance
Committee,
Chair
Financial
Audit
Committee

Qualifications and Experience: Ms. Koeppel, a senior operating and financial executive, has served for over thirty years in the energy industry. Her knowledge of global energy-related commodity markets and infrastructure industries offers valuable insights to the Board. Prior to her retirement, Ms. Koeppel was Managing Director and Co-Head of Corsair Infrastructure Management (March 2015 to January 2017). From 2010 to February 2015, Ms. Koeppel was Partner and Global Co-Head of Citi Infrastructure Investors, a division of Citigroup. Prior to her service at Citi Infrastructure Investors, Ms. Koeppel served as Executive Vice President and Chief Financial Officer for American Electric Power Corporation ("AEP") from 2006 to 2009 and in several additional executive positions at AEP (from 2000 to 2006). Education: Ms. Koeppel received a B.S. in Business

Administration from Ohio State University and an M.B.A. from Ohio State University, where she was a member of Phi Beta Kappa.

Current and Former Directorships: Ms. Koeppel is a member of the boards of directors of British American Tobacco (NYSE: BTI) (July 2017 to the present), Vesuvius plc (LSE: VSVS) (April 2017 to the present) and Arch Coal, Inc. (NYSE: ARCH) (March 2019 to the present). Ms. Koeppel was a member of Reynolds American Inc. (NYSE: RAI) (2008 to July 2017) and Integrys Energy Group, Inc. (2012 to February 2015).

James H. Miller

Age: 70
Director Since: June 2013

Board Committees:
Compensation Committee, Chair
Financial Audit Committee

Qualifications and Experience: Mr. Miller brings to the AES Board his substantial experience in the energy industry both in the US and internationally, including experience in regulated utilities and competitive power markets. With more than 35 years of experience in the energy industry, Mr. Miller served as Chairman of PPL Corporation from 2006 until his retirement in March 2012. He joined PPL as President of its US generation businesses in 2001. Previously, he was Executive Vice President of USEC Inc. and President of two ABB Group subsidiaries: ABB Environmental Systems and ABB Resource Recovery Systems. He began his career at the former Delmarva Power & Light Co.

Education: Mr. Miller holds a bachelor's degree in electrical engineering from the University of Delaware and served in the US Navy nuclear

submarine program.
Current and Former Directorships: Mr. Miller is a member of the boards of directors of Crown Holdings, Incorporated (NYSE: CCK) (2010 to the present) and McDermott Inc. (NYSE:MDR) (May 2018 to the present). In addition, Mr. Miller has been a member of the boards of directors of Rayonier, Inc. (NYSE: RYN) (2011 to 2014), Rayonier Advanced Materials (NYSE: RYAM) (2014 to 2015), Lehigh Gas Partners LP (2012 to 2013) and Chicago Bridge & Iron Company N.V. (NYSE: CBI) (2014 to May 2018).

Board of Directors

Alain Monié

Age: 68
Director
Since: July
2017

Board
Committees:
Governance
Committee
Innovation
and
Technology
Committee

Qualifications and Experience: Mr. Monié has served as the chief executive officer of Ingram Micro Inc. ("Ingram Micro"), a leader in delivering the full spectrum of global technology and supply chain solutions to businesses around the world, since January 2012. Mr. Monié joined Ingram Micro in 2003 and was appointed President of the Asia Pacific region in 2004. From 2007 to 2010, he served as President and Chief Operating Officer of Ingram Micro. Following one year as Chief Executive Officer of Singapore-based Asia Pacific Resources International Limited, he returned to Ingram Micro as Chief Operating Officer in late 2011 and became Chief Executive Officer in January 2012. Prior to joining Ingram Micro, Mr. Monié held senior international leadership positions with AlliedSignal Inc. ("AlliedSignal") and, subsequently, Honeywell International ("Honeywell") after the two companies merged. Mr. Monié played a key role in AlliedSignal's 1999 merger with Honeywell and, from 2000 to 2002, he served as Honeywell's president of Latin America and head of the Industrial and Building Automation group for that region. Before joining AlliedSignal, Mr. Monié held general management positions with French aerospace company Sogitec Inc. and, prior to that time, he was a controller with Renault. He started his career as an engineer in Mexico while in military service.

Education: Mr. Monié earned a master's degree in business administration from the Institut Supérieur des Affaires in Jouy-en-Josas, France (now part of Groupe HEC). He graduated with honors in automation engineering studies at the École Nationale Supérieure d'Arts et Métiers (ENSAM), Bordeaux and Paris.

Current and Former Directorships: He currently serves on the board of directors of Ingram Micro (November 2011 to the present) and Expeditors (Nasdaq: EXPD) (May 2017 to the present), and served in the past on the boards of Amazon.com, Inc. (Nasdaq: AMZN) (2008 to 2016) and Jones Lang LaSalle Incorporated (NYSE: JLL)(2005 to 2009).

John B. Morse Jr.

Age: 72
Director Since: December 2008

Board Committees:
Chairman of the Board and Lead Independent Director

Qualifications and Experience: Mr. Morse brings substantial executive experience to the Board, including board, investment and other finance expertise. Prior to his appointment as Chairman of the Board and Lead Independent Director in April 2018, Mr. Morse served as the Chairman of the Financial Audit Committee beginning in April 2013 and was a member of the Strategy and Investment Committee of the Board. Before his retirement in December 2008, Mr. Morse served as the Senior Vice President, Finance and Chief Financial Officer of The Washington Post Company (the "Post"), now Graham Holdings Co., a diversified education and media company whose principal operations include educational services, newspaper and magazine print and online publishing, television broadcasting and cable television systems recording over $4.4 billion in annual operating revenues. During Mr. Morse's 19 year tenure, the Post's leadership made more than 100 investments in both domestic and international companies and included new endeavors in emerging markets. Prior to joining the Post, Mr. Morse was a partner at Price Waterhouse (now PricewaterhouseCoopers), where he worked with publishing/media companies and multilateral lending institutions for more than 17 years.
Education: Mr. Morse graduated with a B.A. from the University of Virginia and an M.B.A. from the Wharton School of Finance at the University of Pennsylvania. Mr. Morse is a Certified Public Accountant.
Current and Former Directorships: Mr. Morse is also a member of the boards of directors of Host Hotels & Resorts Corporation (NYSE: HST) (2005 to the present) and HSN, Inc. (Nasdaq: HSNI) (2008 to 2016). Mr. Morse also is Former Trustee and President Emeritus of the College Foundation of the University of Virginia (2002 to 2012), and completed a six-year term as a member of the Financial Accounting Standards Advisory Council (2004 to 2010).

Board of Directors

Moisés Naím

Age: 66
Director
Since: April
2013

Board
Committees:
Governance
Committee
Compensation
Committee

Qualifications and Experience:
Dr. Naím is a Distinguished Fellow at the Carnegie Endowment for International Peace and has served in that role since June 2010. For fourteen years (1996 to 2010), Dr. Naím was Editor in Chief of Foreign Policy magazine (first, at The Carnegie Endowment for International Peace and subsequently, at The Washington Post Company). He has written extensively on international economics and global politics, economic development and the consequences of globalization, and is the chief international columnist for El País and La Repubblica, which are high circulation daily newspapers in Spain and Italy, respectively. His columns are syndicated worldwide. Dr. Naím is also the host and producer of Efecto Naím, a Spanish language news and analysis weekly program that airs in the US and Latin America. Dr. Naím brings substantial international economics and political expertise to AES through his tenure as Venezuela's Minister of Industry and Trade and Director of Venezuela's Central Bank in the early 1990s and as an Executive Director of the

World Bank also in the early 1990s. He is the author of many scholarly articles and more than ten books on economics and politics and has broad experience as a consultant to corporations, governments and non-governmental organizations.
Education: Dr. Naím holds M.Sc. and Ph.D. degrees from the Massachusetts Institute of Technology.
Current and Former Directorships: Dr. Naím is a member of the board of directors of FEMSA (NYSE: FMX) (2011 to the present) and was previously a member of the board of directors of Cementos Pacasmayo (NYSE: CPAC) (2013 to 2015).

Jeffrey W. Ubben

Age: 57
Director Since: January 2018

Board Committees:
Financial Audit Committee
Compensation Committee

Qualifications and Experience: Mr. Ubben is a Founder and the Chief Executive Officer of ValueAct Capital where he is the Portfolio Manager of the ValueAct Spring Fund. Mr. Ubben served as the Chief Investment Officer of ValueAct Capital until July 2017 and is a member of the Management Committee. With more than 20 years of experience in the investment management business, Mr. Ubben has an extensive background in sophisticated financial matters and strategic planning. In addition to his investment expertise, Mr. Ubben brings to the Board strong leadership skills gained through his experience on the Boards of other public companies.
Education: He holds a B.A. from Duke University and an M.B.A. from the Kellogg Graduate School of Management at Northwestern University.
Current and Former Directorships: Mr. Ubben previously served as a director of Twenty-First Century Fox (Nasdaq: FOXA) (November 2015 to April 2018), Willis Towers Watson plc

(Nasdaq: WLTW) (2016 to 2017),Willis Group Holdings plc (2013 to 2016), Valeant Pharmaceuticals International, Inc. (NYSE: VRX) (2014 to 2015), Misys, plc (2012 to 2017), Sara Lee Corporation (2008 to 2012), and is the former Chairman and Director of Martha Stewart Living Omnimedia, Inc. (2002 to 2005), Catalina Marketing Corp, (2006 to 2007), Gartner Group, Inc., (from 2004 to 2011) and Mentor Corporation (2003 to 2006). Mr. Ubben serves on the Board of Trustees of Duke University, on the board of Trustees of Northwestern University and on the Board of Directors of E.O. Wilson Biodiversity Foundation, is a contributing member to the World Economic Forum, and formerly served as Chair of the National Board of Directors of the Posse Foundation.

THE BOARD RECOMMENDS A VOTE FOR THE ELECTION OF EACH OF THE TEN DIRECTOR NOMINEES NAMED ABOVE

Board and Committee Governance

BOARD AND COMMITTEE GOVERNANCE

Director Independence

We are required to have a majority of independent Directors serving on our Board and may only have independent Directors serving on each of our (i) Financial Audit Committee (the “Audit Committee”), (ii) Compensation Committee and (iii) Governance Committee pursuant to the rules of the New York Stock Exchange (the “NYSE”) and, with respect to our Audit Committee, the rules and regulations under the Exchange Act.

Under the NYSE rules, no Director qualifies as “independent” unless the Board affirmatively determines that the Director has no material relationship with the Company (directly, or as a partner, Stockholder, or officer of an organization that has a relationship with the Company). The Board makes independence determinations based on all relevant facts and circumstances when assessing the materiality of any relationship between the Company and a Director or a Director’s affiliation with other businesses or entities that have a relationship with the Company.

Our Board undertook an annual review of Director independence in February 2019. The purpose of this review was to determine whether any relationships or transactions involving Directors (including their family members and affiliates) were inconsistent with a determination that the Director is independent under the independence standards set forth in the NYSE rules and our Corporate Governance Guidelines and, with respect to Audit Committee members, under the Exchange Act.

In making this determination, the Board considered not only the criteria for independence set forth in the listing standards of the NYSE but also any other relevant facts and circumstances that may have come to the Board’s attention, after inquiry, relating to transactions, relationships or arrangements between a Director or any member of their immediate family (or any entity of which a Director or an immediate family member is an Executive Officer, general partner or significant equity holder) on the one hand, and AES or any of its subsidiaries or affiliates, on the other hand, that might signal potential conflicts of interest, or that might influence the Director’s relationship with AES or any of its subsidiaries. As described in the preceding sentence, the Board considered the independence issue not merely from the standpoint of the Director, but also from that of the persons or organizations with which the Director or Director nominee is affiliated.

Based on its review, our Board determined that Messrs. Harrington, Miller, Monié, Morse, Ubben, Mmes. Koeppel and Davidson, and Drs. Johnson, Khanna and Naím each qualify as independent under the independence standards existing under the NYSE rules. Our Board also determined that Messrs. Harrington, Miller, and Ubben and Mmes. Koeppel and Davidson qualify as independent under the independence standards for audit committee members under the Exchange Act.

Board Leadership Structure

Our Corporate Governance Guidelines require the separation of the offices of the Chairman of the Board (“Chairman”) and CEO. If the Chairman is independent, he or she will also serve as Lead Independent Director. Since 1993, we have separated the offices of Chairman and CEO. Since 2003, our Chairman has been an independent Director who has also acted as Lead Independent Director. In December 2018, we amended our Corporate Governance Guidelines to provide that whenever possible the Chairman shall be an independent Director.

We believe the structure described above provides strong leadership for our Board, while positioning our CEO as the leader of the Company for our investors, counterparties, employees and other stakeholders. Our current structure, which includes an independent Chairman serving as Lead Independent Director, helps ensure independent oversight over the Company. Our Corporate Governance Guidelines state that the Lead Independent Director's duties include coordinating the activities of the independent Directors, coordinating the agenda for and moderating sessions of the Board's independent Directors, and facilitating communications among the other members of the Board. This structure also allows the CEO to focus his energies on management of the Company.

Our Board currently has ten independent members. A number of our independent Board members are currently serving or have served as Directors or as members of senior management of other public companies. We have three Board Committees comprised solely of independent Directors, each with a different independent Director serving as Chair of the Committee. We believe that the number of independent experienced Directors that make up our Board, along with the independent oversight of the Board by the non-executive Chairman, benefits our Company and our Stockholders.

Pursuant to our By-Laws and our Corporate Governance Guidelines, our Board determines the best leadership structure for the Company. As part of our annual Board self-evaluation process, the Board evaluates issues such as independence of the Board, communication between Directors and Management, the relationship between the CEO and Chairman, and other matters that may be relevant to our

Board and Committee Governance

leadership structure. The Company recognizes that in the event that circumstances facing the Company change, a different leadership structure may be in the best interests of the Company and its Stockholders.

Board Committees

In 2018, the Board maintained four standing Committees:

- Compensation Committee;
- Financial Audit Committee;
- Governance Committee; and
- Innovation and Technology Committee.

The table below shows the directors who are currently members or chairs of each of the Standing Board Committees and the number of meetings each committee held in 2018.

Director	Audit	Compensation	Governance	Innovation and Technology
Andres R. Gluski				ü
Janet Davidson(2)	ü	ü		
Charles L. Harrington (1)(2)	Chair		ü	
Kristina M. Johnson		ü		ü
Tarun Khanna			ü	Chair
Holly Koeppel(1)(2)	ü		Chair	
James H. Miller (1)(2)	ü	Chair		
Alain Monié			ü	ü
John B. Morse Jr. (3)				
Moises Naim		ü	ü	
Jeffrey W. Ubben(1)(2)	ü	ü		
Number of Meetings in 2018	8	7	5	5

(1) Designated as an “audit committee financial expert” as defined by the rules and regulations of the SEC.
(2) Designated as “financially literate” as required by the NYSE rules.
(3) Chairman and Lead Independent Director, serves as an ex-officio member of each committee (with no voting authority as to such committees).

Committee Charters. Each of the four committees has a charter which can be obtained from the Company’s website (https://www.aes.com) on the “Board of Directors and Committees” page under the “About Us” tab, or by sending a request to the Office of the Corporate Secretary, The AES Corporation 4300 Wilson Boulevard, Arlington, VA 22203.

Compensation Committee. The primary functions of the Compensation Committee are to:

- review and evaluate at least annually the performance of the CEO and other executive officers of the Company, including setting goals and objectives, and to set executive compensation, including incentive awards and related performance goals;
- provide oversight of the Company’s executive compensation and benefit plans and practices;
- make recommendations to the Board to modify AES’ executive compensation and benefit programs to align with the Company’s compensation goals;
- review, discuss and make recommendations to the Board on say on pay and say on frequency matters and Stockholder engagement;

Board and Committee Governance

- assess the stock ownership guidelines for executive officers; and
- review Management's succession planning.

The Board determined that all Compensation Committee members are independent within the meaning of SEC rules and current listing standards of the NYSE. In addition, each member of the Compensation Committee is a "Non-Employee Director" as defined in Rule 16b-3 under the Exchange Act.

At the commencement of each year, AES' NEOs (other than the CEO) discuss their position-specific goals and objectives for the upcoming year with the CEO. In the first quarter of the following year, the CEO performs an assessment of each NEO's performance against his or her stated goals and, in the case of our CEO, our Compensation Committee reviews and assesses his performance against his stated goals and objectives.

Based on our CEO's performance, the Compensation Committee provides an evaluation, approves and makes a compensation recommendation to the Board as to the CEO. The Compensation Committee reviews and approves, and the Board approves, compensation recommendations submitted by the CEO on the other NEOs. The Compensation Committee then reviews these recommendations with the Board.

Additionally, the Compensation Committee makes recommendations to the Board to modify AES' compensation and benefit programs if it believes that such programs are not consistent with the Company's executive compensation goals or could otherwise be improved. Under the Compensation Committee's Charter, it may form subcommittees and delegate to such subcommittees, other Board members and Officers, such power and authority, as the Compensation Committee deems appropriate in accordance with the Charter. The Compensation Committee has also delegated to the CEO, subject to review by the Compensation Committee and the Board, the power to set compensation for non-Executive Officers. Under the 2003 Long-Term Compensation Plan, the Compensation Committee is also permitted to delegate its authority, responsibilities and powers to any person selected by it and has expressly authorized our CEO to make equity grants to non-Executive Officers in compliance with law. Under such delegation, our CEO may grant equity awards to non-Executive Officer employees up to 250,000 shares annually with a total cap of 1.25 million shares over the life of the delegation.

The Compensation Committee retains the services of its own independent outside consultant to assist it in reviewing and/or advising the amount and/or form of executive compensation. Meridian Compensation Partners, LLC ("Meridian") is the firm retained by the Compensation Committee for these purposes and is precluded from providing other non-Board related services to AES. The Compensation Committee has the sole authority to hire and dismiss its consultant. Meridian provided objective input and analysis to the Compensation Committee throughout the year with reference to market data trends, regulatory initiatives, governance best practices and emerging governance norms. For further information concerning the independent outside consultant's role in relation to NEO compensation, please refer to the "Role of the Compensation Committee Independent Consultant and Management" section in the Compensation Discussion and Analysis ("CD&A") of this Proxy Statement.

Management regularly obtains market survey data based on comparable companies from Willis Towers Watson. Meridian reviews the market survey data prior to it being shared with the Compensation Committee to ensure the data sources are appropriate for purposes of comparing our NEOs' compensation to comparable executives at similarly-sized general industry and energy industry companies.

The Compensation Committee has instructed the Senior Vice President and Chief Human Resources Officer ("CHRO") to provide information to the Compensation Committee that is required for developing compensation programs and determining executive compensation. The CHRO works directly with the Compensation Committee's independent consultant in the preparation of the background material for the Compensation Committee. For further information regarding our executive compensation practices refer to the CD&A of this Proxy Statement.

The compensation of our Directors is established by the Governance Committee. See “Director Compensation” of this Proxy Statement for a description of our Governance Committee’s processes and procedures for determining Director compensation.

Financial Audit Committee. The primary functions of the Audit Committee are to assist the Company’s Board of Directors in the oversight of:

- the integrity of the financial statements of the Company and its subsidiaries;
- the effectiveness of the Company’s internal controls over financial reporting;
- the Company’s compliance with legal and regulatory requirements;

Board and Committee Governance

- the qualifications, independence and performance of the Company's independent registered public accounting firm (the "Independent Auditor");
- the performance of the Company's internal audit function; and
- the preparation of the audit committee report included in the Company's annual Proxy Statement.

All members of the Audit Committee are independent within the meaning of the SEC rules and under the listing standards of the NYSE. The Board has also determined that each member of the Audit Committee is "financially literate" as required by the NYSE rules, and that each of Messrs. Harrington, Miller and Ubben and Ms. Koeppel are Audit Committee Financial Experts pursuant to SEC rules based on, among other things, the experience of such member, as described under the "Proposal 1: Election of Directors" section of this Proxy Statement.

Governance Committee. The principal functions of the Governance Committee are to:

- identify and provide recommendations for potential Director nominees for election to the Board;
- advise the Board with respect to Board composition, procedures and committees;
- develop and recommend to the Board corporate governance guidelines applicable to the Company;
- establish and administer programs for evaluating the performance of Board members;
- review the fees paid to outside directors for their services on the Board and its Committees;
- consider governance and social responsibility issues relating to the Company;
- review the Company's contributions to trade associations, including any amounts related to political activities and lobbying expenses, and review of other political contributions or expenditures, if any, by the Company;
- provide oversight of the Company's environmental, safety and cyber security programs and related issues; and
- provide oversight of the Company's dispute resolution, operations, construction, insurance and regulatory programs and related issues.

The Governance Committee may form subcommittees and delegate to those subcommittees such power and authority as the Committee deems appropriate and in compliance with applicable law. The Governance Committee operates under the charter of the Governance Committee adopted and approved by the Board. Consistent with the requirements of the Charter, the Board determined that all Governance Committee members are independent within the meaning of the listing standards of the NYSE.

Director Qualifications. Director nominees are selected on the basis of, among other things, experience, knowledge, skills, expertise, integrity, ability to make independent analytical inquiries, understanding the Company's global business environment and willingness to devote adequate time and effort to Board responsibilities so as to enhance the Board's ability to oversee and direct the affairs and business of the Company.

Diversity. The Company does not maintain a separate policy regarding the diversity of the Board. However, the charter of the Governance Committee requires that the Committee review the composition of the Board to ensure it has the "appropriate balance" of attributes, including, but not limited to, knowledge, experience and diversity. In addition, the Company's Corporate Governance Guidelines establish that the size of the Board shall be nine to twelve members, a range which "permits diversity of experience without hindering effective discussion or diminishing individual accountability." Consistent with these governing documents, both the Governance Committee and the full Board seek Director nominees with diverse professional backgrounds, experience and perspectives so that the Board as a whole has the range of skills and viewpoints necessary to fulfill its responsibilities. As part of our annual Board self-evaluation process, the Board evaluates whether or not the Board as a whole has the skills and backgrounds for the current issues facing the Company. The Board also evaluates its effectiveness with regard to specific areas of expertise. See also the "Proposal 1: Election of Directors" section which describes the qualifications and skills of our Directors.

Director Nomination Process. Pursuant to our Corporate Governance Guidelines, our Governance Committee reviews the qualifications of proposed Director nominees to serve on our Board and recommends Director nominees to our Board for election at the Company's Annual Meeting. The Board proposes a slate of Director nominees to the Stockholders for election to the Board, using information provided by the Governance Committee.

In certain instances, a third party may be engaged and paid a fee to assist in identifying and evaluating potential Director nominees. The Governance Committee also considers potential nominations for Director provided by Stockholders and submits any such suggested nominations, when appropriate, to the Board for approval. Stockholder nominees for Director are evaluated using the criteria described above. Stockholders wishing to recommend persons for consideration by the Governance Committee as nominees for election to the Board can do so by writing to the Office of the Corporate Secretary, The AES Corporation, 4300 Wilson Boulevard, Arlington, Virginia 22203 and providing the information and following the additional procedures set forth in the By-Laws, which are described in “Additional Governance Matters” section of this Proxy Statement.

In February 2019, Ms. Davidson was elected to our Board. Ms. Davidson was recommended through a third party search firm the Board engaged to assist in the recruitment of Directors. After the Board conducted interviews with Ms. Davidson, considered her qualifications to serve on the Board, and completed thorough conflicts and background checks, the Governance Committee recommended her nomination for election to the Board and the Board approved her election.

Innovation and Technology Committee. The Innovation and Technology Committee is responsible for the oversight and evaluation of:

- the Company’s efforts to foster growth through innovation;
- the Company’s efforts to identify and assess risks and opportunities in the power industry and adjacent industries arising from emerging or competing technologies; and
- the Company’s approach to replication of innovative solutions across businesses.

Director Attendance

Under our Corporate Governance Guidelines, Directors are expected to attend Board meetings and meetings of Committees on which they serve in person or by telephone conference, and Directors are encouraged to attend the Annual Meeting.

In 2018, our Board convened six times and our Board Committees convened for the number of meetings specified in the chart on page 14, and no Director attended less than 75% of the aggregate of all meetings of the Board and the Committees on which they then served. Non-management Directors met in executive session after each of the six in-person meetings of the Board in 2018, with Mr. Charles Rossotti presiding as Chairman and Lead Independent Director through the 2018 Annual Meeting of Stockholders and Mr. Morse presiding as Chairman and Lead Independent Director for the remaining meetings held in 2018. All Directors serving at that time attended our 2018 Annual Meeting of Stockholders on April 19, 2018.

Board and Committee Governance

Board's Role in Risk Management

Management is responsible for the management and assessment of risk at the Company, including communication of the most material risks to the Board and its Committees. The Board provides oversight over the risk management practices implemented by Management, except for the oversight of risks that have been specifically delegated to a Committee of the Board. Even when the oversight of a specific area of risk has been delegated to a Committee, the full Board maintains oversight over such risks through the receipt of reports from the Committee Chairs to the full Board at each regularly-scheduled full Board meeting. In addition, if a particular risk is material or where otherwise appropriate, the full Board may assume oversight over a particular risk, even if the risk was initially overseen by a Committee. The Board and Committee reviews occur principally through the receipt of regular reports from Management to the Board on these areas of risk, and discussions with Management regarding risk assessment and risk management as follows:

Risk Management Oversight Structure

Responsible Party	Area of Risk Oversight
Board	Oversees all operational, financial, strategic, brand and reputational risk with the oversight of specific risks undertaken within the Committee structure. The Company's Chief Financial Officer provides a report on the Company's financial performance and outlook, which may include an analysis of key external and internal drivers of performance, the Company's liquidity position, prospective sources and uses of funds, and the implications to the Company's debt covenants and credit rating, if any. Receives a report from the Company's Chief Risk Officer, which explains the Company's primary risk exposures, including currency, commodity, hydrology, and interest rate risk. In addition to the regular reports from Committee Chairs, the Board receives reports on specific areas of risk from time to time, such as regulatory, geopolitical, cyclical, or other risks.
Audit Committee	Oversees risk related to integrity of the Company's financial statements, internal controls over financial reporting and disclosure controls and procedures (including the performance of the Company's internal audit function). Oversees the performance of the independent auditor. Oversees the effectiveness of the Company's Ethics and Compliance Program.
Governance Committee	Oversees risk related to environmental compliance, safety and cyber security risks. Oversees operational and construction risks including risks related to tariffs, efficiency at our subsidiaries' plants, performance of our subsidiaries' distribution businesses, progress of construction and risks that may cause delays or increases in costs and related matters. Oversees risks related to dispute resolution and receives a privileged dispute resolution report from the General Counsel, which provides information regarding the status of the Company's litigation and related matters.
Compensation Committee	Oversees risk related to compensation practices, including practices related to hiring and retention, succession planning, and training of employees.
Innovation and Technology Committee	Oversees risk related to technologies and innovations deployed by the Company for use in its businesses.

ADDITIONAL GOVERNANCE MATTERS

Environmental, Social and Governance

AES is dedicated to improving lives and making a lasting difference in the communities in which our businesses operate. We are committed to a wide range of social, economic and environmental initiatives that will improve the lives of our employees, customers and their communities; protect the environments in which we operate; empower our people and businesses; and improve long-term returns to our investors.

We have received numerous recognitions for our environmental, social and governance practices, some of which are highlighted below:

- Ethisphere's World's Most Ethical Companies for six consecutive years;
- Since 2014, AES has been included in the DowJones Sustainability Index for North America based on RobecoSAM's analysis of financially material Environmental, Social and Governance factors;
- Since 2017, AES has been a member of the FTSE4Good Index Series. FTSE Russell is a unit of London Stock Exchange Group's information Services Division that measures the performance of companies demonstrating strong management of ESG risk.
- In 2018, AES maintained Leadership category recognition in the CDP Climate Change questionnaires with a score of "A-".

In addition to the Governance programs discussed in this Proxy Statement, the Company has a number of environmental and social initiatives described in further detail below.

Environment

The core of our corporate sustainability efforts centers on understanding the environments in which we operate and committing to the development of environmentally responsible energy solutions. Environmental stewardship and leadership are a key part of our business. Our Environmental Management System ("EMS"), environmental measurement metrics, and certificates and standards demonstrate our tangible commitment to environmental sustainability.

All our subsidiary locations are required to design, implement and manage our EMS and Environmental Policy. Our subsidiary locations are responsible for applying the EMS and Environmental Policy during their respective daily operations, when selecting or evaluating suppliers; developing new services or projects; planning logistics; managing effluents and waste; performing engineering or maintenance operations; and performing due diligence for mergers and acquisitions.

The foundation of our environmental management approach is embodied in the following four principles included in our Environmental Policy:

- Meet or exceed the requirements of environmental rules and regulations imposed by local, regional, and national governments and by participating financial institutions.
- Meet or exceed our Environmental Standards set forth in our programs and policies.
- Plan and budget for investments that achieve sustainable environmental results by taking into account the local, regional and global environment where the term "environment" is broadly defined as the external surroundings or conditions within which people live — including ecological, economic, social and all other factors that determine quality of life and standard of living.
- Strive to continually improve the environmental performance at every business.

AES is committed to a corporate strategy that aims to lower our greenhouse gas emissions and create a clean energy future by shifting our portfolio towards less carbon-intensive sources of generation with an emphasis on zero-carbon technologies like wind and solar. In 2018, we published the AES Climate Scenario Report in which we announced increasing our 2030 carbon intensity reduction target from a 50% to a 70% reduction of carbon intensity from 2016 levels. The AES Climate Scenario Report is intended to provide stakeholders with an understanding of the strength and resilience of our portfolio under various climate change scenarios applying the

Additional Governance Matters

TCFD recommendations. The AES Climate Scenario Report also includes a discussion about our strategy for managing risks and opportunities related to climate change. A copy of the AES Climate Scenario Report is available on our website under the "Sustainability" tab.

Social

Safety. Safety comes before everything at AES. We harness one of the world's most powerful forces: electricity. Our people put their lives on the line when they come to work each day. Ensuring safe operations at our facilities around the world, so each person can return home safely, is the cornerstone of our daily activities and decisions. We always put safety first, and we measure our successes by how safely we achieve our goals.

AES has built a Safety Management System ("SMS") based on the OHSAS 18001/ISOS 45001 Occupational Health and Safety Management System model. The SMS provides a consistent framework for all AES operational businesses and construction projects to set expectations, measure performance and drive improvements in our management of safety. AES' SMS include specific operational and construction safety standards that are based on global electric utility best practices and often exceed the local regulatory requirements for some of the businesses.

Stakeholder Engagement. We strive to strengthen relationships through meaningful engagement with our stakeholders. AES businesses have implemented varying levels of engagement with their local communities and focus on programs that can make a community stronger economically, socially or environmentally. We encourage our businesses to custom-tailor community engagement programs to ensure the most effective and beneficial local contribution. Additionally, we encourage AES people to get involved in volunteering programs and community activities. AES businesses also engage in partnerships with various stakeholders to maximize the benefits of the programs and make a long-term, positive impact for their communities. Partners include government agencies, development agencies, municipalities, NGOs, universities and technical institutions, business partners and subcontractors.

Human Rights. As a leader in the global power industry, we operate under a broad range of economic, political, social and cultural customs, and traditions as well as different local, regional, and international laws and regulations. We believe it is our duty and responsibility to conduct business with the highest level of integrity, ethics and compliance in all situations. AES has a Human Rights Policy that formalizes our long-standing commitment to uphold and respect human rights. While our subsidiaries have teams that manage the daily operations of our businesses, we believe AES' Human Rights Policy can foster greater awareness of human rights issues in three areas relevant to our businesses: People, Communities and Suppliers.

Our People

We recognize that our people are our energy. AES people set the foundation to achieve the Company's long-term goals. The energy our people bring to their work makes everything possible and we know we need to have the right people in the right place at the right time to meet the Company's commitments and sustain our success. Our comprehensive approach to attracting, developing and energizing our talented workforce around the world helps our people develop to their fullest potential.

Employee Development. Our global talent management strategy enables us to help people reach their potential at AES. The ACE Academy for Talent Development, our talent management framework, provides the tools and experiences needed for our employees to grow their professional skill set, evolve their leadership competencies and take their career to the next level. Every year, AES employees receive training and development related to competencies essential to the Company's business, such as leadership, compliance, safety and technical training. Training and development programs are provided through formal classroom instruction, online resources and on-the-job leaning opportunities.

Diversity. We are a diverse and inclusive Company and our employees are actively encouraged and empowered to share their perspectives. As a global company, the diversity of our employees - in race, ethnicity, culture, gender, sexual orientation, perspective and experience (among others) - is essential to our ability to continue to grow and succeed in worldwide markets.

We have a long-standing commitment to our employees to create a business working environment that fosters engagement through personal innovation, achievement, wellness, advancement and training/development opportunities, promoting health and safety, and investments in their communities. These efforts culminate in creating a business culture of achievement and loyalty that enables us to minimize turnover in our global workforce and succeed in competitive and challenging marketplaces.

Additional Governance Matters

AES Code of Business Conduct and Corporate Governance Guidelines

Our Code of Conduct and Corporate Governance Guidelines have been adopted by the Board. The Code of Conduct is intended to govern, as a requirement of employment the actions of everyone who works at AES, including employees of AES's subsidiaries and affiliates and our Directors. The Code of Conduct and the Corporate Governance Guidelines can be located in their entirety on the Company's website (https://www.aes.com). Any person may obtain a copy of the Code of Conduct or the Corporate Governance Guidelines without charge by making a written request to: Office of the Corporate Secretary, The AES Corporation, 4300 Wilson Boulevard, Arlington, VA 22203. If any amendments to, or waivers from, the Code of Conduct are made, we will disclose such amendments or waivers on our website (https://www.aes.com).

Related Person Policies and Procedures

Our Governance Committee has adopted a Related Person Transaction Policy, which sets forth the procedures for the review, approval or ratification of any transaction involving an amount in excess of $120,000 in which the Company participates and any Director or Executive Officer of the Company, any Director nominee, any person who is the beneficial owner of more than 5% of the Company's common stock, or any immediate family members of the foregoing (each, a "Related Person"), has a material interest as contemplated by Item 404(a) of Regulation S-K ("Related Person Transactions"). Under this policy, prior to entering into, or amending a potential Related Person Transaction, the Related Person or applicable business unit leader must notify the General Counsel who will assess whether the transaction is a Related Person Transaction. If the General Counsel determines that a transaction is a Related Person Transaction, the details of the transaction will be submitted to the Audit Committee for review. The Audit Committee will either approve or reject it after taking into account factors including, but not limited to, the following:

- the benefits to the Company;
- the materiality and character of the Related Person's direct or indirect interest, and the actual or apparent conflict of interest of the Related Person;
- the impact on a Director's independence in the event the Related Person is a Director or a Director nominee, an immediate family member of a Director or a Director nominee or an entity in which a Director or a Director nominee is an Executive Officer, partner, or principal;
- the commercial reasonableness of the Related Person Transaction and the availability of other sources for comparable products or services;
- the terms of the Related Person Transaction;
- the terms available to unrelated third parties or to employees generally;
- any reputational risk the Related Person Transaction may pose to the Company; and
- any other relevant information.

In the event that the General Counsel determines that the Related Person Transaction should be reviewed prior to the next Audit Committee meeting, the details of the Related Person Transaction may be submitted to a member of the Audit Committee who has been designated to act on behalf of the Audit Committee between Audit Committee meetings with respect to the review and approval of these transactions. In addition, Related Person Transactions that are not approved pursuant to the procedures set forth above may be ratified, amended or terminated by the Audit Committee or its designee. If the Audit Committee or its designee determines that the Related Person Transaction should not or cannot be ratified, the Audit Committee shall evaluate its options both with regard to the Related Person Transaction (e.g. termination, amendment, etc.) and the individuals involved in the Related Person Transaction, if necessary. At the Audit Committee's first meeting of each fiscal year, the Audit Committee shall review any previously approved or ratified Related Person Transactions that remain ongoing.

Submission of Future Stockholder Proposals and Nominations for Director

Stockholder Proposals for 2020

Proxy Statement. SEC rules permit Stockholders to submit proposals for inclusion in the Company's proxy statement if the Stockholder and proposal meet the requirements specified in Rule 14a-8 of the Exchange Act.

- Where to send Stockholder proposals. Any Stockholder proposal intended to be considered for inclusion in the Company's proxy materials for the 2020 Annual Meeting of Stockholders (the "2020 Annual Meeting") must comply with the requirements of Rule 14a-8 of the Exchange Act and be submitted in writing by notice delivered to the Office of the Corporate Secretary, located at The AES Corporation, 4300 Wilson Boulevard, Arlington, Virginia 22203.

Additional Governance Matters

- Deadline for Stockholder proposals. Stockholder proposals submitted pursuant to Rule 14a-8 must be received at our principal executive offices at least 120 days before the anniversary of the mailing of the prior year's proxy material (i.e., by November 7, 2019), unless the date of our 2020 Annual Meeting is changed by more than 30 days from April 18, 2020 (the one-year anniversary date of the 2019 Annual Meeting), in which case the proposal must be received a reasonable time before we begin to print and mail our proxy materials.
- Information to include in Stockholder proposals. Stockholder proposals must conform to and set forth the specific information required by Rule 14a-8 of the Exchange Act.

Other Proposals. Our By-Laws establish certain requirements for proposals a Stockholder wishes to present at the 2020 Annual Meeting other than pursuant to Rule 14a-8. If the proposal is not being submitted pursuant to Rule 14a-8, the proposal must be written and delivered to the Office of the Corporate Secretary at the address set forth above by the close of business not less than 90 days nor more than 120 days prior to the first anniversary of the preceding year's annual meeting (no later than January 19, 2020 and no earlier than December 20, 2019 for the 2020 Annual Meeting); provided, however, that in the event that the date of the 2020 Annual Meeting is more than 30 days before or more than 60 days after the one-year anniversary date of the 2019 Annual Meeting, or if no such meeting was held, notice by the Stockholder, to be timely, must be delivered at the address set forth above not earlier than the close of business on the 120th day prior to the 2020 Annual Meeting and not later than the close of business on the later of the 90th day prior to the 2020 Annual Meeting, or the 10th day following the day on which public announcement (as defined in Section 2.15(D) of the Company's By-Laws) of the date of such annual meeting is first made by the Company. In no event shall adjournment, recess or postponement of an annual meeting commence a new time period (or extend any time period) for the giving of a Stockholder's notice as described above. As described in Sections 2.15(B) and 2.16 of our By-Laws, the notice must contain certain information, including, without limitation, a brief description of the business desired to be brought before the meeting, the text of the proposal or business (including the text of any resolutions proposed for consideration and, in the event that such business includes a proposal to amend the By-Laws of the Company, the language of the proposed amendment) and the reasons for conducting such business at the meeting.

Director Nominations by Stockholders

Our By-Laws set forth the procedures for Stockholder nominations of Directors.

- Stockholder nomination of Directors. As described in Section 9.01 of our By-Laws, nominations of persons eligible for election to the Board may be made at any annual meeting of Stockholders or at any special meeting of Stockholders called for the purpose of electing Directors by any Stockholder of record at the time of giving of the notice and who at the time of the meeting is entitled to vote at such meeting, and who provides the required notice in accordance with Section 9.01(C) of our By-Laws.
- Timing for notice (other than proxy access procedures). The written notice required with respect to any nomination (including the completed and signed questionnaire, representation and agreement discussed below) must be given, either by personal delivery or by United States mail, postage prepaid, to the Office of the Corporate Secretary at the address set forth above (a) with respect to an election to be held at an annual meeting of Stockholders, generally not less than 90 days nor more than 120 days prior to the first anniversary of the preceding year's annual meeting (as provided above) and (b) with respect to an election to be held at a special meeting of Stockholders for the election of Directors (other than a Stockholder Requested Special Meeting, as such term is defined in the By-Laws), the close of business (as defined in the By-Laws) on the seventh day following the earlier of (i) the date on which notice of such meeting is first given to Stockholders and (ii) the date on which a public announcement (as defined in Section 2.15(D) of the Company's By-Laws) of such meeting is first made. In no event shall an adjournment, recess or postponement of an annual meeting or special meeting commence a new time period (or extend any time period) for the giving of a Stockholder's notice.

Inclusion of Stockholder Nominee in Company Proxy Statement and Form of Proxy (Proxy Access)

In December 2015, the Company amended its By-Laws to provide for "proxy access." The Company will include in its proxy statement and on its form of proxy the name of a Director nominee submitted pursuant to Section 9.02 of the By-Laws by an "Eligible Stockholder" who provides the information and satisfies the other provisions of the Company's proxy access By-Laws. To qualify as an "Eligible Stockholder," a Stockholder or a group of no more than 20 Stockholders must have continuously owned, for at least three years as of the date of the Stockholder Notice (as defined in the By-Laws), at least three percent (3%) of the outstanding shares of the Company entitled to vote in the election of directors as of the date of the Stockholder Notice (the "Required Shares") and thereafter continue to own the Required Shares through such annual meeting.

- Deadline for notice. The Stockholder notice must be delivered to the Office of the Corporate Secretary not later than the close of business on the 120th day, nor earlier than the close of business on the 150th day, prior to the first anniversary of the preceding year's annual meeting (no earlier than November 20, 2019 an no later than December 20, 2019 for the 2020 Annual Meeting).

Additional Governance Matters

In the event the annual meeting is more than 30 days before or after such anniversary date, or if no annual meeting was held in the preceding year, the Stockholder Notice must be so delivered not earlier than the close of business on the 150th day prior to such annual meeting and not later than the close of business on the later of the 120th day prior to such annual meeting, or the 10th day following the day on which public announcement of the date of such meeting is first made by the Company. In no event shall an adjournment or recess of an annual meeting, or a postponement of an annual meeting for which notice has been given or with respect to which there has been a public announcement of the date of the meeting, commence a new time period (or extend any time period) for the giving of the Stockholder notice as described above.

- Other conditions. The ability to include proxy access nominees in the Company's proxy materials is subject to a number of requirements, conditions and limitations that are set forth in the By-Laws.

The chairperson of the annual meeting may refuse to acknowledge the introduction of any Stockholder proposal or Director nomination not made in compliance with the foregoing procedures.

Other Governance Information

Section 16(a) Beneficial Ownership Reporting Compliance. Based solely on the Company's review of reports filed under Section 16(a) of the Exchange Act and certain written representations (as allowed by Item 405(b)(2)(i) of Regulation S-K), the Company believes that no person subject to Section 16(a) of the Exchange Act with respect to AES failed to file, on a timely basis, the reports required by Section 16(a) of the Exchange Act during the most recent fiscal year.

Householding Information. The SEC has adopted rules that permit companies and intermediaries such as brokers to satisfy delivery requirements for Proxy Statements with respect to two or more Stockholders sharing the same address by delivering a single Proxy Statement addressed to those Stockholders. This process, which is commonly referred to as "householding," potentially provides extra convenience for Stockholders and cost savings for companies. AES and some brokers household proxy materials, delivering a single Proxy Statement to multiple Stockholders sharing an address unless contrary instructions have been received from the affected Stockholders. Once Stockholders have received notice from their broker or us that materials will be sent in the householding manner to the Stockholder's address, householding will continue until we or the broker are otherwise notified or until the Stockholder revokes such consent. If, at any time, such Stockholders no longer wish to participate in householding and would prefer to receive a separate Proxy Statement, they should notify their broker if shares are held in a brokerage account or us if holding registered shares as provided in the next paragraph.

Any beneficial owner who has received a single copy of an Annual Report or Proxy Statement at a shared address can request to receive a separate copy of an annual report or Proxy Statement for this meeting by written or oral request and we will promptly deliver a separate copy in the format requested. To receive separate copies of those materials for this or for future meetings, please request by telephone, internet or e-mail by following the instructions found on the Notice that you have received which also contains your control number or by making your request in writing to your broker or to us, as appropriate.

Charitable Contributions. Under NYSE Listing Standard 303A.02(b)(v), the Company is required to report as to whether or not any charitable contributions were made by the Company to any charitable organization for which an AES Director served as an Executive Officer of that organization in an amount greater than $1 million or 2% of such charitable organization's consolidated gross revenues for the years 2018, 2017 or 2016. The Company did not make any such charitable contributions in 2018, nor did it make such charitable contributions in excess of those amounts in 2017 or 2016.

Communications with the Board or Its Committees. The Board offers several e-mail addresses, as set forth below, for Stockholders and interested parties to send communications through the Office of the Corporate Secretary of the Company to the non-management Directors and/or the following committees of the Board:

AES Board of Directors:	Compensation Committee:	Financial Audit Committee:

AESDirectors@aes.com	CompCommitteeChair@aes.com	AuditCommitteeChair@aes.com
Innovation and Technology Committee: InnovationCommitteeChair@aes.com	Governance Committee: NomGovCommitteeChair@aes.com	

A member of the Corporate Secretary's Office will forward to the Directors all communications that, in his or her judgment, are appropriate for consideration by the Directors. Examples of communications that would not be considered as appropriate for consideration by the Directors include commercial solicitations, requests for employment and matters not relevant to Stockholders, the functioning of the Board or the affairs of the Company.
Annual Report on Form 10-K. Any Stockholder who desires an additional copy of the AES Form 10-K (including the financial statements and financial schedules) filed on February 26, 2019 with the SEC may obtain a copy (excluding Exhibits) without charge by addressing a written request to the Office of the Corporate Secretary, The AES Corporation, 4300 Wilson Boulevard, Arlington, Virginia 22203. Exhibits also may be requested, but a charge equal to the reproduction cost thereof will be made. Stockholders may also obtain a copy of the AES Form 10-K by visiting the Company's website at https://www.aes.com.

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Director Compensation

DIRECTOR COMPENSATION

Director Compensation Program

The Governance Committee annually reviews the level and form of compensation paid to Directors, including our Director compensation program's underlying principles. Under the Corporate Governance Guidelines, a Director who is also an Officer of AES is not permitted to receive additional compensation for service as a Director. In reviewing and determining the compensation paid to Directors, the Governance Committee considers how such compensation relates and compares to that of similarly-sized general industry and energy companies and the Office of the General Counsel assists the Governance Committee with its review of our Director compensation program. The Office of the General Counsel conducts research on other companies' Director compensation practices by reviewing a broad-based Director compensation study and survey data from Willis Towers Watson's U.S. General Industry and U.S. Energy Databases, and providing the Committee with a benchmarking analysis of such companies' practices as compared to the Company's Director compensation program. Neither the Office of the General Counsel nor the Governance Committee retained an independent compensation consultant to assist with recommending or determining Director compensation in 2018. The Governance Committee has retained Meridian Compensation Partners, LLC ("Meridian") to assist with the Committee's review of Director compensation practices for 2019. Any proposed changes to the Director compensation program are recommended by the Governance Committee to the Board for consideration and approval.

Director Compensation for 2018

The Board reviews the Board compensation structure on an annual basis. In 2018, on its own initiative, the Board determined that it would not increase Board compensation for the 2018-2019 Board Year. The Board has not increased its compensation since 2012.

Board compensation is intended to meet the following goals:

- promote the recruitment of talented and experienced Directors to the AES Board;
- compensate outside Directors for the increased workload inherent in a public board Director position; and
- retain a strong financial incentive for Directors to maintain and promote the long-term health and viability of the Company.

The Governance Committee of the Board consulted various materials regarding current trends and best practices for determining compensation for boards of directors, as described above.

Annual Retainer. For 2018, Directors elected at the annual meeting of Stockholders received an $80,000 annual retainer with a requirement that at least 34% of such retainer be deferred in the form of stock units. Directors may elect (but are not required) to defer more than the mandatory 34% deferral. Any portion of the annual retainer that is deferred above the mandatory deferral was credited to the Director in stock units equivalent to 1.3 times the elected deferral amount. The Board also determined that the Chairman would receive compensation at an amount equal to 1.9 times the 2018 annual retainer of other AES Board members, and that such amount would be inclusive of all Board responsibilities.

Committee Compensation. Committee chairpersons and members received compensation for their Committee service is outlined below.

Audit Committee Chair	$30,000
Compensation Committee Chair	$25,000
Governance Committee Chair	$22,250

Innovation and Technology Committee Chair	$15,000
Audit Committee Member	$15,000
Compensation Committee Member	$15,000
Governance Committee Member	$15,000
Innovation and Technology Committee Member	$10,000

Director Compensation

Deferred Compensation Grant. Directors received an annual Deferred Incentive Compensation Grant valued at $150,000. The Board also determined that the Chairman would receive such a grant in an amount equal to 1.9 times the Deferred Incentive Compensation Grant of other AES Board members.

New Directors. Newly elected directors receive an initial grant consisting of deferred stock units and/or stock options valued at $40,000 and an Annual Retainer, Committee Fees, and Deferred Compensation Grant pro-rated for the service provided until the next annual meeting of Stockholders.

Our 2018 Board compensation structure remained consistent with past practice.

Non-Employee Director Stock Ownership Guidelines. The Board adopted stock ownership guidelines for Directors that provide for non-employee Directors to accumulate and maintain equity ownership in AES having a value of no less than five times the annual retainer within five years of the date of the Director's appointment to the Board. All stock and equity interests of a Director are taken into consideration for purposes of considering compliance with the policy, including Director stock units.

Compensation of Directors (2018)*
The following table contains information concerning the compensation of our non-Management Directors during 2018.

Name(1)	Fees Earned or Paid in Cash(2)	Stock Awards(3)	Option Awards(4)	All Other Compensation	Total
Charles L. Harrington Chair—Financial Audit Committee	$97,800	$193,040	$0	$0	$290,840
Kristina M. Johnson	$77,800	$193,040	$0	$0	$270,840
Tarun Khanna Chair—Innovation and Technology Committee	$82,800	$163,040	$30,000	$0	$275,840
Holly K. Koeppel Chair—Governance Committee	$90,050	$177,200	$0	$0	$267,250
James H. Miller Chair—Compensation Committee	$92,800	$177,200	$0	$0	$270,000
Alain Monié	$77,800	$118,040	$75,000	$0	$270,840
John B. Morse, Jr. Chairman, Lead Independent Director	$100,320	$366,776	$0	$0	$467,096
Moisés Naím	$82,800	$177,200	$0	$0	$260,000
Charles O. Rossotti (5)	$0	$0	$0	$27,000	$27,000
Jeffrey W. Ubben (6)	$103,500	$261,500	$0	$0	$365,000

* Table excludes the Non-Equity Incentive Plan Compensation, Change in Pension Value and Nonqualified Deferred Compensation Earnings, and All Other Compensation columns, which are not applicable.

NOTES:

(1) Mr. Gluski, our President and CEO, is also a member of our Board. His compensation is reported in the Summary Compensation Table and the other tables set forth in this Proxy Statement. In accordance with our Corporate Governance Guidelines, Management Directors do not receive any additional compensation in connection with service on the Board. Ms. Davidson was elected to the Board on February 22, 2019 and accordingly was not paid

any compensation in 2018.

Director Compensation

(2) Directors elected at the 2018 Annual Meeting of Stockholders received an $80,000 Annual Retainer with a requirement that at least 34% of such retainer be deferred in the form of stock units, with each Director having the right to elect to defer additional amounts as further described above. Directors may also elect to defer Committee fees in the form of stock units.

The mandatory deferral portion of the Annual Retainer is included in the “Stock Awards” column above, while the “Fees Earned or Paid in Cash” column includes amounts from the Annual Retainer and Committee fees that Directors elected to defer (above the mandatory deferral) into stock units except that the additional incremental value resulting from the 1.3 multiplier applied to elective deferrals of the Annual Retainer is included in the “Stock Awards” column, as noted in footnote 3. The elective deferral amounts were as follows:

	Annual Elective Retainer Deferred	Committee Retainer Deferred
Charles L. Harrington	$52,800	$45,000
Kristina M. Johnson	$52,800	$0
Tarun Khanna	$52,800	$0
John B. Morse, Jr.	$100,320	$0
Alain Monié	$52,800	$25,000

(3) This column includes the aggregate grant date fair value of Director stock unit awards granted in 2018 pursuant to (i) the 34% mandatory annual retainer deferral into stock units, and (ii) as further described in “Director Compensation for Year 2018” above, the additional incremental value resulting from Directors electing to defer more than 34% of their annual retainer and being credited with 1.3 or 1.9 times, as applicable, of the elective deferral amount. The aggregate grant date fair values were computed in accordance with FASB ASC Topic 718. A discussion of the relevant assumptions made in these valuations may be found in footnote 16 to the financial statements contained in the AES Form 10-K.

As of December 31, 2018, Directors had the following total number of stock units credited to their accounts under the 2003 Long Term Compensation Plan: Charles L. Harrington - 124,223; Kristina M. Johnson - 151,151; Tarun Khanna - 200,032; Holly K. Koeppel - 88,428; James H. Miller - 100,453; Alain Monié - 34,957; John B. Morse, Jr. - 227,312; Moisés Naím - 110,454; and Jeffrey Ubben - 22,945 .

(4) This column reflects aggregate grant date fair value of each Director Stock Option granted in 2018. A discussion of relevant assumptions made in this valuation may be found in footnote 16 to the financial statements contained in the AES Form 10-K.

No Directors held Options outstanding as of December 31, 2018, with the exception of Tarun Khanna - 20,000; James H. Miller - 19,280; and Alain Monié - 80,441.

(5) Mr. Rossotti’s term ended April 18, 2018. Mr. Rossotti entered into a Consulting Agreement with the company to provide consulting services to the incoming Chairman and Lead Independent Director from April 19, 2018 to December 31, 2018, which amounts are included in the “All Other Compensation” column.

(6) Mr. Ubben was elected to the Board on January 17, 2018 and accordingly was paid an initial grant of deferred stock units and an Annual Retainer, Committee Fees, and Deferred Compensation Grant pro-rated for the service provided until the April 19, 2018 Annual Meeting of Stockholders.

Executive Compensation

EXECUTIVE COMPENSATION

Compensation Discussion and Analysis ("CD&A")

Executive Summary

The following points highlight the alignment of AES' compensation plans and practices for our NEOs with performance and Stockholder value creation. Any Non-GAAP measures discussed in this CD&A are reconciled to the nearest GAAP financial measure or described how such measure is calculated from the financial statements in the section titled "Non-GAAP measures".

2018 was a good year for AES, demonstrated by strong financial results and significant progress toward achieving strategic goals. The Company delivered on all of its commitments, including financial guidance, and hit key milestones on its strategy, positioning AES for long-term, sustainable growth. As a result of these efforts, the overall performance of the Company exceeded expectations and delivered a 40% return to its Stockholders. The Company's compensation philosophy remains unchanged and the compensation earned by our NEOs demonstrates alignment between our executive compensation program design and value creation to Stockholders. In summary:

- AES' philosophy is to target total compensation opportunities at approximately the 50th percentile of companies similar in industry and size.
- With over half of NEO compensation in variable incentives, actual compensation only exceeds the 50th percentile when AES exceeds performance goals and creates commensurate Stockholder value.
- Annual incentive plan payouts were above the target opportunity based on actual performance, driven primarily by Financial and Growth goals, which were above the midpoint of our expectations for 2018.
- 2018 long-term incentive payouts reflect strong performance and Total Shareholder Return of 70% over a three-year performance period (2016-2018).
- The Compensation Committee continues to align pay practices with Stockholder interests.

What AES Does	What AES Doesn't Do
Pay-for-Performance Alignment - Annual review of AES Total Stockholder Return performance and its impact on realizable pay to ensure actual results are aligned to performance payouts	No "Single-Trigger" Vesting of Equity Awards with a Change in Control - All unvested, outstanding and future awards contain a "double-trigger" provision
Target Total Compensation at 50th Percentile - Based on similarly-sized companies' target total compensation at the size-adjusted 50th percentile	No Special Retirement Benefit Formulas for NEOs - Our non-qualified retirement plan restores benefits capped under our broad-based plan due to statutory limits
Heavy Weight on Performance Compensation - Majority of compensation is paid through annual incentive and long-term compensation plans	No Hedging or Pledging - Maintain a policy that prohibits NEOs and Directors of AES from engaging in hedging activities or pledging AES stock
Stock Ownership Guidelines - Maintain market-competitive guidelines to align NEO and Stockholder interests	No Change-In-Control Excise Tax Gross-Ups - Completely discontinued this provision

Executive Compensation

Change-In-Control Severance - Our plan is competitive with market practice and all benefits are conditioned upon "double-trigger"	No Perquisites - No perquisites are provided to any NEOs, except for relocation benefits in connection with overseas assignments
"Clawback" Policy - Policy provides for recovery of certain previously-paid incentive awards under certain circumstances	No Backdating or Option Repricings
Independent Consultant Retained by the Compensation Committee - Provides no other services to AES	No Payment of Dividends or Dividend Equivalents on Equity Awards Unless Earned and/or Vested

- The Compensation Committee annually reviews AES' performance and CEO compensation relative to power generation and utility companies from the S&P 500 Utilities Index to which investors may compare AES. The CEOs realizable compensation and AES' Total Stockholder Return are aligned with value creation to AES Stockholders as demonstrated below for the 2015-2017 period.
- At the 2018 Annual Meeting, AES received over 95% support for its NEO compensation based on the shares voted in favor of the 2018 Say on Pay proposal.

Our Executive Compensation Process

The CD&A includes compensation details for our NEOs:

Name	Title
Mr. Andrés Gluski	President & Chief Executive Officer ("CEO")
Mr. Thomas O'Flynn*	Former EVP & Chief Financial Officer ("CFO")
Mr. Bernerd Da Santos	EVP & Chief Operating Officer ("COO")
Mr. Julian Nebreda	SVP & President, South America Strategic Business Unit
Mr. Manuel Pérez Dubuc	SVP & President, New Energy Solutions

*Effective January 1, 2019, Mr. O'Flynn transitioned to a new leadership role with AES.

Our Executive Compensation Philosophy

Our philosophy is to provide compensation opportunities that approximate the 50th percentile of survey data specific to our revenue size and industry. We then design our incentive plans to pay for performance with more compensation paid when performance exceeds expectations and less compensation paid when performance does not meet expectations. Thus, the actual compensation realized by an NEO will depend on our actual performance.

In applying this philosophy, survey data is used to assess the impact of any changes on the competitiveness of target total compensation opportunities relative to the 50th percentile. Our use of survey data is described further in the section titled "How We Use Survey Data in our Executive Compensation Process."

Executive Compensation

The Compensation Committee considers additional factors in making its decisions on each NEO's target total compensation opportunity. The specific factors include:

- Individual performance against pre-set goals and objectives for the year, and Company performance;
- An individual's experience and expertise;
- Position and scope of responsibilities;
- An individual's future prospects with the Company; and
- The new total compensation that would result from any change and how the new total compensation compares to survey data.

In making its decisions, the Compensation Committee does not apply formulaic weighting to any of the above factors.

Role of the Compensation Committee, Independent Compensation Consultant, and Management

	Compensation Committee	Independent Compensation Consultant	Management (CEO & CHRO)
Provide overall oversight of the Company's compensation and benefit plans, including plans in which the NEOs participate	ü		
Annually review NEO compensation and, if appropriate, propose changes to target total compensation for Board of Directors' approval	ü		
Approve performance goals for annual and long-term incentive plans within the first three months of the performance period	ü		
Based on an assessment of performance against pre-set goals, approve payouts to NEOs under incentive plans and propose for Board of Directors' approval	ü		
Participate in all Compensation Committee meetings	ü	ü	ü
Participate in executive sessions of the Compensation Committee	ü	As requested	
Prepare and summarize detailed information on the Company's performance and, as applicable, performance of individual executives			ü
Prepare and provide (in advance whenever possible) additional materials regarding our executive compensation plans for review and discussion by the Compensation Committee in its meetings			ü
Based on business strategy, propose any changes to incentive plan designs			ü
With the Compensation Committee's knowledge, provide background information to the independent consultant required for the consultant to carry out its duties			ü
Update the Compensation Committee on market trends, regulatory matters and governance best practices related to executive compensation		ü	
Review and provide the Compensation Committee with feedback on market competitiveness of any changes to target total compensation proposed by management		ü	

Review and provide the Compensation Committee with feedback on incentive plan changes proposed by management	ü

In 2018, the Compensation Committee retained Meridian to serve as its Independent Compensation Consultant. The Compensation Committee has reviewed the independence of Meridian as required by the NYSE rules that relate to the engagement of its advisors. The Compensation Committee, after taking into consideration all relevant factors, determined Meridian to be independent, consistent with NYSE requirements. Other than services provided to the Compensation Committee, Meridian did not provide any other services to AES in 2018.

How We Use Survey Data in our Executive Compensation Process

At the time it decides target total compensation opportunities, the Compensation Committee reviews survey data from Willis Towers Watson. The data enables the Compensation Committee to compare compensation for our NEOs to compensation provided by similarly-

Executive Compensation

sized companies for executives in comparable positions to U.S.-based and internationally based NEOs. Specifically, in 2018 the Compensation Committee reviewed the following survey data:

- The U.S. General Industry Database, which consisted of other companies with international operations with a total of 507 companies;
- The U.S. Energy Industry Database, which consisted primarily of power generation and distribution companies, with a total of 124 companies; and
- Country-specific compensation databases for international data which consisted of companies similar to AES' business, with a total of 320 companies in Chile.

From the survey data regression analysis is then used to predict the compensation paid by those companies most similar to AES in size. At the time of the analysis, we used our then-current revenue estimate of $10.5B.

The survey data lag the year for which the compensation decision applies and therefore are aged at an annualized rate of 3% per year for the United States, and country-specific aging factors for international data, as provided by Willis Towers Watson. In determining companies comparable to AES in size, we use revenue because executive target total compensation more closely correlates with revenue than any other size indicator, in both general industry and the power industry.

For all U.S.-based NEOs, a blend of general industry and power industry data is appropriate based on the operational knowledge required of their positions and the international scope of their roles. For non-U.S.-based NEOs there are limitations in the survey samples and therefore market data in these countries only reflect a general industry sample.

NEO	General Industry Weighting	Power Industry Weighting
Mr. Gluski	50%	50%
Mr. O'Flynn	50%	50%
Mr. Da Santos	50%	50%
Mr. Nebreda	100%	-
Mr. Pérez Dubuc	100%	-

In the case of Messrs. Gluski and Da Santos their target total compensation was slightly below the market 50th percentile, but above the 25th percentile. In the case of Messrs. Nebreda and Pérez Dubuc, their target total compensation was between the 50th percentile and the 75th percentile, and Mr. O'Flynn was approximated at the 75th percentile. As previously described, NEOs will not realize the target level of compensation if AES does not meet performance goals and create Stockholder value, or if they terminate employment with AES prior to the vesting or payment dates of incentive awards.

The Compensation Committee views the Willis Towers Watson survey data as an appropriate benchmark of compensation practices and levels of similarly-sized companies, including companies with international operations against whom we compete for talent.

Overview of AES Total Compensation

Elements of Compensation

The following table presents each element of compensation and explains (i) the objective of each element, (ii) what the element is designed to reward, and (iii) why we choose to pay each element.

Objective	What It Rewards	Why We Pay

Base Salary Provide fixed cash compensation that reflects the individual's experience, responsibility and expertise	Accomplishment of day-to-day job responsibilities, taking into account individual performance and retention considerations	Market competitiveness; attract and retain our NEOs

Executive Compensation

Objective	What It Rewards	Why We Pay
Performance Incentive Plan (our annual incentive plan)		
Provide performance-based, short-term cash compensation relative to the achievement of pre-set objectives, and performance, based on a payout range of 0-200%	Achievement of specific pre-set performance thresholds related to safety, financial, operational and strategic objectives	Direct incentive to achieve the Company's safety, financial, operational and strategic objectives for the year
Long-Term Compensation (LTC)		
Provide awards that align the interests of our executives with those of our Stockholders over the long term	Share price growth, dividend performance and attainment of long-term financial goals	Directly links NEOs' interests with those of Stockholders and AES' long-term financial performance
Retirement and Health and Welfare Benefits		
Provide retirement and health and welfare benefits that are generally comparable to those provided to our broad-based U.S. employee population	Promote healthiness and financial readiness for retirement	Market competitiveness

CEO Compensation Relative to other NEOs

Our CEO's compensation is higher than the compensation paid to our other NEOs largely due to the scope of his position and his overall responsibility for the Company's strategy and direction, as well as his overall influence on AES' near-and long-term performance. When compared to our other NEOs, our CEO's total compensation is more heavily weighted towards incentive compensation and his stock ownership guideline is higher. The higher compensation and higher percentage of compensation in the form of performance-based incentives for our CEO are consistent with the survey data.

Mix of Cash and Equity Compensation

The Company does not target a specific allocation of cash versus equity compensation, nor does it target a specific allocation between short- and long-term compensation. The charts below indicate the mix of cash and equity compensation, as well as short-term and long-term compensation for our CEO and all other NEOs.

In making compensation decisions, the Compensation Committee does not explicitly consider prior years' awards or current equity holdings. The Compensation Committee does, however, on an ongoing basis ensure it has a detailed understanding of how its decisions

Executive Compensation

on individual compensation elements affect other compensation elements and total compensation. The Committee reviews detailed information on:

- Year-over-year changes in total compensation;
- The value of outstanding long-term compensation awards under various share price and financial performance scenarios;
- Payouts and realized gains from past long-term compensation awards; and
- The value of benefits payable upon termination and change-in-control.

A discussion of how the Compensation Committee determined each element of compensation for 2018 is provided in the next section of this CD&A.

2018 Compensation Determinations

Base Salary

As explained in the section titled "Our Executive Compensation Process," the Compensation Committee reviews the target total compensation, including base salaries, of our NEOs annually. In addition, the Compensation Committee will review the base salary of an Executive Officer if there is a promotion or in the case of a newly-hired Executive Officer.

The following table shows the 2018 base salary and the percentage increase from 2017 for each NEO. At the recommendation of the CEO, the 2018 base salaries were held flat for all of our NEOs. Mr. Pérez Dubuc only received a base salary increase upon assuming his new role. Further details on the 2018 base salaries paid to our NEOs can be found in the Summary Compensation Table of this Proxy Statement.

NEO	2018 Base Salary	Percentage Increase from 2017	Rationale for Increase
Mr. Gluski	$1,188,000	0%	No changes from 2017
Mr. O'Flynn	$690,000	0%	No changes from 2017
Mr. Da Santos	$510,000	0%	No changes from 2017
Mr. Nebreda	$396,550	0%	No changes from 2017
Mr. Pérez Dubuc	$450,000	14%	Adjustment for new role

2018 Performance Incentive Plan Payouts

2018 Company Performance Score Targets: Our NEOs are eligible for annual incentive awards under the Performance Incentive Plan, a Stockholder-approved plan. As detailed more fully below, in early 2018, the Compensation Committee established measures in three performance categories: Safety, Financial, and Strategic & Operational Objectives. In setting these performance measures, the Compensation Committee considered information provided by management about the Company's financial budget for the year as well as strategic and operational objectives. The Compensation Committee approved performance measures and objectives across all three categories that it considered to be challenging.

In early 2019, the Compensation Committee approved, and recommended to the Board of Directors to approve, the annual incentive pay-outs for 2018. The Committee's decision was based on AES' 2018 corporate performance score, which reflected actual results against pre-established performance measures shown below.

Executive Compensation

The below table reflects the measures, weights, and targets approved by the Committee, as well as the 2018 results.

Measure	Weight	Target Goal	Actual Results	Actual % of Target	2018 Score
Safety					
Serious Safety Incidents		No serious safety incidents	One or more serious safety incidents occurred	n/a	
Near Miss Reporting	10%	Reports filed timely, accurately, and mitigation plans executed	Favorable to target	n/a	60%
Proactive Safety Measures		Achieve 2018 goals	Exceeded safety walk and meeting goals	n/a	
Financial[1]					
Adjusted EPS	35%	$1.20	$1.24	103%	153%
Parent Free Cash Flow ($M)	25%	$638	$689	108%	
Strategic & Operational Objectives					
Growth Projects	20%	2,000 MW of Renewable Growth 12 tBtu of LNG Growth Strategic Capital Raising Initiatives	1,967 MW of Renewable Growth 25 tBtu of LNG Growth Strategic Capital Raising Ongoing	133%	133%
Construction Program/ Operational KPIs (Index Score)[2]	10%	Advance construction program on time / on budget 100% of Index	On time performance – 97% On budget performance – 99% 103% of Index	100%	100%

2018 AES Corporate Performance Score - 134%

[1]Assuming the threshold financial requirement for each measure is met, the score ranges from 50% to 200%: 50% score corresponds to actual results at 90% of the target goal, and a 200% score corresponds to actual results at 110% of the target goal.

[2] Key Performance Indicators and weights for Generation businesses are as follows: Commercial Availability 32.6%, Equivalent Forced Outage Factor 25%, Equivalent Availability Factor 23.5%, Heat Rate 15.4%, and Days Sales Outstanding 3.5%. Key Performance Indicators and weights for Distribution businesses are as follows: System Average Interruption Duration Index 45.8%, System Average Interruption Frequency Index 30%, Customer Satisfaction Index 10.9%, Days Sales Outstanding 10.8%, and Non-Technical Losses 2.5%.

Both Messrs. Nebreda and Perez Dubuc served as Presidents of the South America Strategic Business Unit at different points in 2018. As leaders of the business unit their scores were based 50% on AES performance, shown above, and 50% based on the performance of the South American Strategic Business Unit. The categories are not dissimilar from the above scorecard, and the following represents the weights, targets, and performance; Safety (10%) same targets as reflected above all were exceeded resulting in a score of 100%, Adjusted Pre-Tax Contribution (22.5%) of $560.8M (target of $585M), Subsidiary Distributions (22.5%) of $303.3M (target of $291.1M), MW Growth (40%) of 470MWs (target of 670 MWs), and Talent Development (5%). Based on the aforementioned metrics, the overall South America Strategic Business Unit score was 90%.

Final 2018 Annual Incentive Payouts: The following table shows the final award for each of our NEOs under the 2018 Performance Incentive Plan. The Compensation Committee and the Board approved the annual incentive payout as a percent of the target for each of the NEOs below based on the AES Corporate Performance Scores.

NEO	2018 Base Salary	2018 Target Annual Incentive (% of base salary)	Actual 2018 Annual Incentive Award	
			Dollar Value	% of Target Annual Incentive*
Mr. Gluski	$1,188,000	150%	$2,388,000	134%
Mr. O'Flynn	$690,000	100%	$925,000	134%
Mr. Da Santos	$510,000	100%	$683,000	134%
Mr. Nebreda[1]	$396,500	85%	$378,000	112%
Mr. Pérez Dubuc[1]	$450,000	85%	$428,000	112%

*Actual percentage results above are rounded to the nearest whole number

[1] As previously described both Messrs. Nebreda and Perez Dubuc's annual incentive plan payout is based on 50% of the AES overall and 50% of the South America Business Unit. Based on an AES overall score of 134% and a South America Business Unit score of 90%, this results in a blended payout of 112%.

Long-Term Compensation

2018 Long-term Compensation Mix: In 2018, we utilized the same overall long-term compensation vehicles as in prior years. The mix was based on the following:

- Compensation philosophy which emphasizes alignment between executive compensation and Stockholder value creation;
- Long-term strategic and financial objectives;
- Goal of retaining our NEOs; and
- Review of relevant market practices.

Messrs. Gluski, O'Flynn, and Da Santos received the mix noted above as "Executive Officer as of Grant", given that they were Executive Officers as of the 2018 grant date. Messrs. Nebreda and Pérez Dubuc received a different allocation of long-term compensation vehicles as they were not Executive Officers as of the date of the 2018 grant.

Performance Stock Units Based on Proportional Free Cash Flow: Performance stock units represent the right to receive a single share of AES common stock subject to performance- and service-based vesting conditions. Performance stock units granted in 2018 are eligible to vest subject to our three-year cumulative Proportional Free Cash Flow performance. Proportional Free Cash Flow is a measure of long-term cash generation driven by increasing revenue, reducing costs, improving productivity and efficiently utilizing capital.

The Proportional Free Cash Flow target is set for the three-year performance period and is subject to pre-defined, objective adjustments during the three-year performance period based on changes to the Company's portfolio, such as an asset divestiture or sale of a portion of equity in a subsidiary.

The final value of the performance stock unit award depends upon the level of Proportional Free Cash Flow achieved over the three-year measurement period as well as our share price performance over the period since the award is stock-settled. If a threshold level of Proportional Free Cash Flow is achieved, units vest and are settled in the calendar year that immediately follows the end of the performance period.

Executive Compensation

The following table illustrates the vesting percentage at each Proportional Free Cash Flow level for targets set for the 2018-2020 performance period:

Performance Level	Vesting Percentage
75% of Performance Target or Below	0%
Equal to 87.5% of Performance Target	50%
Equal to 100% of Performance Target	100%
Equal to or Greater Than 125% of Performance Target	200%

Between the Proportional Free Cash Flow levels listed in the above table, straight-line interpolation is used to determine the vesting percentage for the award. The ability to earn performance stock units is also generally subject to the continued employment of the NEO. The Compensation Committee approved a Proportional Free Cash Flow target for the 2018 performance stock unit that will require improvement over prior performance, and is believed by the Compensation Committee to be challenging.

Performance Cash Units Based on AES Total Stockholder Return: Performance cash units represent the right to receive a cash-based payment subject to performance- and service-based vesting conditions. Performance cash units granted in 2018 are eligible to vest subject to AES' Total Stockholder Return from January 1, 2018 through December 31, 2020 relative to companies in three different indices. The indices and their weightings are as follows:

- S&P 500 Utilities Index - 50%
- S&P 500 Index - 25%
- MSCI Emerging Markets Index - 25%

We use Total Stockholder Return as a performance measure to align our NEOs' compensation with our Stockholders' interests since the ability to earn the award is linked directly to stock price and dividend performance over a period of time.

Total Stockholder Return is defined as the appreciation in stock price and dividends paid over the performance period as a percentage of the beginning stock price. To determine share price appreciation, we use a 90-day average stock price for AES, the S&P 500 Utilities Index companies, the S&P 500 Index companies, and the MSCI Emerging Markets Index companies at the beginning and end of the three-year performance period. This avoids short-term volatility impacting the calculation.

The value of each performance cash unit is equal to $1.00, and the number of performance cash units that vest depend upon AES' percentile rank against the companies in the indices. If AES' Total Stockholder Return is above the threshold percentile rank established for the performance period, a percentage of the units vest and are settled in cash in the calendar year that immediately follows the end of the performance period. The following table illustrates the vesting percentage at each percentile rank for the 2018-2020 performance period:

AES 3-Year Total Stockholder Return Percentile Rank	Vesting Percentage
Below 30th percentile	0%
Equal to 30th percentile	50%
Equal to 50th percentile	100%
Equal to 70th percentile	150%
Equal to or Greater Than 90th percentile	200%

Between the percentile ranks listed in the above table, straight-line interpolation is used to determine the vesting percentage for the award. The ability to earn these performance cash units is also generally subject to the continued employment of the NEO.

Restricted Stock Units: Restricted stock units represent the right to receive a single share of AES common stock subject to service-based vesting conditions. The Company grants restricted stock units to assist in retaining our NEOs and also to increase their ownership of AES common stock, which further aligns our NEOs' interests with those of Stockholders. Restricted stock units vest based on continued service with the Company in three equal installments beginning on the first anniversary of the grant.

Executive Compensation

2018 Long-Term Compensation Grants: In February 2018, consistent with our practice in prior years, the Company granted long-term compensation to the NEOs. The target grant values below are based upon the grant date closing stock price per share of AES common stock for performance stock units and restricted stock units, and a per unit value of $1.00 for performance cash units.

NEO	February 2018 Long-Term Compensation Target Value	
	As % of Base Salary	Dollar Amount
Mr. Gluski	535%	$6,355,800
Mr. O'Flynn	325%	$2,242,500
Mr. Da Santos	225%	$1,147,500
Mr. Nebreda	115%	$456,033
Mr. Pérez Dubuc	115%	$456,690

The values in the table above differ from the Stock Award column in the Summary Compensation Table because the performance cash units contain a market condition which results in a fair market value, for financial accounting purposes, that differs from the $1 per unit value the Company uses to determine the grant.

Prior Year Performance Stock Units Vesting in 2018: All of the NEOs received a grant of performance stock units in February 2016 for the performance period January 1, 2016 through December 31, 2018. Performance was based on the Company's Proportional Free Cash Flow performance during the three-year performance period.

The performance stock unit award paid out at 97.6% of the target number of shares based on our actual Proportional Free Cash Flow results of $4,053M, which was 99.4% of the target Proportional Free Cash Flow, and is based on the same performance scale as the 2018 performance stock units. The performance payout level is derived using straight-line interpolation: for every one percentage point performance is below the target goal, the payout is reduced by approximately four percentage points.

NEO	Target Number of Units	% of Target Vested Based on Proportional Free Cash Flow	Final Shares Vested
Mr. Gluski	264,942	97.6%	258,583
Mr. O'Flynn	94,357	97.6%	92,092
Mr. Da Santos	38,767	97.6%	37,837
Mr. Nebreda	18,821	97.6%	18,369
Mr. Pérez Dubuc	17,814	97.6%	17,386

Prior Year Performance Cash Units Vesting in 2018: All of the NEOs received a grant of performance cash units in February 2016 for the performance period January 1, 2016 through December 31, 2018. Performance was based on the Company's Total Stockholder Return relative to S&P 500 Utility Index companies (50% weight) S&P 500 Index (25% weight) and MSCI Emerging Markets Index (25% weight), and with the same performance scales for each index as the 2018 performance cash units.

Total Stockholder Return for the Company over the 2016-2018 performance period was 70%, which resulted in the Company exceeding the 80th percentile target of Total Stockholder Return for each index. The overall payout for the 2016 to 2018 Performance Cash Units was 183% of target. Actual results for each index and associated payouts are reflected below:

- S&P 500 Utilities Index - 84.0 percentile of performance, resulting payout of 185%
- S&P 500 Index - 81.4 percentile of performance, resulting payout of 178.5%
- MSCI Emerging Markets Index - 83.5 percentile of performance, resulting payout of 183.8%

Executive Compensation

NEO	Target Number of Units	% of Target Vested Based on TSR	Resulting Cash Payout
Mr. Gluski	2,493,100	183%	$4,562,373
Mr. O'Flynn	887,900	183%	$1,624,857
Mr. Da Santos	364,800	183%	$667,584
Mr. Nebreda	177,101	183%	$324,095
Mr. Pérez Dubuc	167,633	183%	$306,768

Further details on the 2016-2018 performance stock unit and performance cash unit payouts to our NEOs can be found in the Option Exercises and Stock Vested Table of this Proxy Statement.

Other Relevant Compensation Elements and Policies

Perquisites

We do not provide perquisites to any of our Executive Officers, with the exception of relocation related expenses for international assignments.

Retirement Benefits

We cover our NEOs under the Restoration Supplemental Retirement Plan ("RSRP") to restore benefits that are limited under our broad-based retirement plans due to statutory limits imposed by the Code. The RSRP's objectives are consistent with our philosophy to provide competitive levels of retirement benefits and to retain talented executives. Additionally certain internationally-based employees are eligible to participate in the International Retirement Plan ("IRP"). Neither the RSRP nor the IRP contain any enhanced or special benefit formulas for our NEOs. Contributions to the RSRP and the IRP made in 2018 are included in the All Other Compensation column of the Summary Compensation Table of this Proxy Statement. Additional information regarding the RSRP and IRP is contained in the "Narrative Disclosure Relating to the Non-Qualified Deferred Compensation Table" of this Proxy Statement.

Stock Ownership Guidelines

Our Board of Directors, based upon our management's and the Compensation Committee's recommendations, adopted stock ownership guidelines in January 2011. These guidelines promote our objective of increasing Stockholder value by encouraging our NEOs to acquire and maintain a meaningful equity stake in the Company.

The guidelines were designed to maintain stock ownership at levels high enough to assure our Stockholders of our NEOs' commitment to value creation. Under these guidelines, our NEOs are expected, over time, to acquire and hold shares of AES common stock equal in value to a multiple of their annual salaries. The Compensation Committee sets the ownership multiples based on market practice for each NEO's position. The current ownership multiple for each NEO, who was serving as of fiscal year end 2018, is as follows:

NEO	Ownership Multiple of Base Salary
Mr. Gluski	5x
Mr. O'Flynn	3x
Mr. Da Santos	3x
Mr. Nebreda	2x
Mr. Pérez Dubuc	2x

Shares owned directly and shares beneficially acquired under our retirement plans all count toward satisfying the guidelines. Unexercised stock options, unvested performance stock units and unvested restricted stock unit awards do not count towards satisfaction of the guidelines.

Executive Compensation

The Company requires that all net shares (net of option exercise price and/or withholding tax) acquired after the guideline effective date will be retained and cannot be liquidated until the guideline has been met.

Severance and Change-in-Control Arrangements

The Company maintains certain severance and change-in-control arrangements, including the Executive Severance Plan and change-in-control provisions in the long-term compensation award agreements.

Executive Severance Plan: The Compensation Committee has included all of the Company's Executive Officers in a single Executive Severance Plan, the design of which is consistent with current market practices. Newly hired or promoted executives are included in this plan beginning on the first date of their executive appointment. The Executive Severance Plan does not contain any excise tax gross-ups and, thus, none of our NEOs are eligible for an excise tax gross-up.

The Company provides severance benefits for qualifying termination both related and unrelated to a change-in-control to enable the attraction and retention of key executive talent. Also, in the case of severance benefits upon a qualifying termination related to a change-in-control, the Company believes these benefits will help to align the NEOs' interests with those of Stockholders by mitigating any uncertainties the NEOs may have about their ongoing employment if the change-in-control is pursued. The Company provides severance benefits after a change-in-control only if there is a qualifying termination of employment following the change-in-control (i.e., "double-trigger benefits").

Further details on the Executive Severance Plan and qualifying termination events can be found in the section titled "Additional Information Relating to Potential Payments upon Termination of Employment or Change-in-Control" of this Proxy Statement.

Vesting of Long-term Compensation Awards upon Change-in-Control: Upon a change-in-control, the unvested portion of all outstanding awards will vest only upon a double-trigger (at target performance levels for performance awards). The double-trigger only allows for vesting if a qualifying termination occurs in connection with the change-in-control. All unvested, outstanding awards include a double- trigger.

Clawback Policy

The Company has adopted a "clawback policy" that provides the Compensation Committee with the discretion to seek the reimbursement of any annual incentive payment or long-term compensation award, as defined under the policy, from key executives of the Company, including our NEOs, when:

- The initial payment was calculated based upon achieving certain financial results that were subsequently the subject of a material restatement of the Company's financial statements;
- The Compensation Committee, in its discretion, determines that the executive engaged in fraud or willful misconduct that caused, or substantially caused, the need for the restatement; and
- A lower payment would have been made to the executive based upon the restated financial results.

In each such instance, the Compensation Committee has the discretion to determine whether it will seek recovery from the individual executive and has discretion to determine the amount. The policy applies to annual incentive payments made in or after 2013 under the Performance Incentive Plan and performance cash unit and performance stock unit awards granted in or after 2012.

Prohibition Against Hedging and Pledging

The Board has adopted a policy that prohibits Directors and Officers required to file reports with the SEC under Section 16 of the Exchange Act of 1934, which includes our NEOs, from hedging their economic interest in AES common stock or using AES common stock as collateral in a financial transaction.

Executive Compensation

Non-GAAP Measures

In this CD&A, we reference certain Non-GAAP measures, including Adjusted EPS, which is reconciled to the nearest GAAP measure in the table below.

Reconciliation of Adjusted EPS

	Year Ended Dec. 31, 2018
Diluted earnings per share from continuing operations	$1.48
Unrealized derivative and equity security losses	$0.05
Unrealized foreign currency losses	$0.09
Disposition/ acquisition (gains)	$(1.41)
Impairment expense	$0.46
Loss on extinguishment of debt	$0.27
U.S. Tax law reform impact	$0.18
Less: Net income tax expense	$0.12
Adjusted EPS	$1.24

Additionally in this CD&A, we reference certain Proportional Free Cash Flow, Parent Free Cash Flow, Adjusted PTC, and Subsidiary Distributions.

Proportional Free Cash Flow is defined as Net Cash from Operating Activities less Maintenance and Environmental Capital Expenditures, adjusted for AES ownership percentage.

Parent Free Cash Flow is Subsidiary Distributions less cash used for interest costs, development, general and administrative activities, and tax payments by the parent company. Subsidiary Distributions should not be construed as an alternative to Net Cash Provided by Operating Activities which is determined in accordance with GAAP. Subsidiary Distributions are important to the parent company because the parent company is a holding company that does not derive any significant direct revenues from its own activities but instead relies on its subsidiaries' business activities and the resultant distributions to fund the debt service, investment and other cash needs of the holding company. The reconciliation of the difference between the Subsidiary Distributions and the Net Cash Provided by Operating Activities consists of cash generated from operating activities that is retained at the subsidiaries for a variety of reasons which are both discretionary and non-discretionary in nature. These factors include, but are not limited to, retention of cash to fund capital expenditures at the subsidiary, cash retention associated with non-recourse debt covenant restrictions and related debt service requirements at the subsidiaries, retention of cash related to sufficiency of local GAAP statutory retained earnings at the subsidiaries, retention of cash for working capital needs at the subsidiaries, and other similar timing differences between when the cash is generated at the subsidiaries and when it reaches the parent company and related holding companies.

Subsidiary Distributions are the sum of the following amounts (a) dividends paid to the Borrower by its Subsidiaries during such period; (b) consulting and management fees paid to the Borrower for such period; (c) tax sharing payments made to the Borrower during such period; (d) interest and other distributions paid to the Borrower during such period with respect to cash and other Temporary Cash Investments of the Borrower (other than with respect to amounts on deposit in the Revolving L/C Cash Collateral Account); (e) cash payments made to the Borrower in respect of foreign exchange Hedge Agreements or other foreign exchange activities entered into by the Borrower on behalf of any of its Subsidiaries; and (f) other cash payments made to the Borrower by its Subsidiaries other than (i) returns of invested capital; (ii) payments of the principal of Debt of any such Subsidiary to the Borrower and (iii) payments in an amount equal to the aggregate amount released from debt service reserve accounts upon the issuance of letters of credit for the account of the Borrower and the benefit of the beneficiaries of such accounts.

Adjusted PTC is defined as pre-tax income from continuing operations attributable to The AES Corporation excluding gains or losses of the consolidated entity due to (a) unrealized gains or losses related to derivative transactions and equity securities; (b) unrealized foreign currency gains or losses; (c) gains, losses, benefits and costs associated with dispositions and acquisitions of business interests, including early plant closures; (d) losses due to impairments; (e) gains, losses and costs due to the early retirement of debt; and (f) costs directly associated with a major restructuring program, including, but not limited to, workforce reduction efforts, relocations, and office consolidation. Adjusted PTC also includes net equity in earnings of affiliates on an after-tax basis adjusted for the same gains or losses excluded from consolidated entities.

Executive Compensation

Executive Compensation Program Alignment with Stockholders Interests

Actual compensation earned by our NEOs reflects the alignment between our executive compensation program design and value creation for Stockholders

- Based on actual performance the value of equity awards at vesting may decline, including both our AES relative Total Stockholder Return cash units and AES Proportional Free Cash Flow performance stock units.
- For the 2016-2018 performance cash units AES had a Total Stockholder Return of 70% which exceeded the 80th percentile against all three indices to which it compares itself

For the previous six performance periods where AES compared it's Total Stockholder Return to one or more indices, all payouts relating to Total Stockholder Return were forfeited in their entirety as AES did not meet the threshold performance

- As a direct result of the performance-based nature of AES' executive compensation program actual compensation earned by our NEOs has significantly varied from Summary Compensation Table reported values for the last three years.

Approximately 60% of amounts included in the Summary Compensation Table Total column have been realized by our NEOs over the preceding 3 year period.

Summary Compensation Table (2018, 2017 and 2016)[1]

Year	Salary ($)[(2)]	Bonus ($)[(3)]	Stock Awards ($)[(4)]	Non-Equity Incentive Plan Compensation ($)[(5)]	All Other Compensation ($)[(6)]	Total ($)
Andrés Gluski President & Chief Executive Officer						
2018	$1,188,000	$0	$5,900,311	$2,388,000	$283,500	$9,759,811
2017	$1,188,000	$0	$5,818,612	$2,148,000	$200,071	$9,354,683
2016	$1,165,000	$0	$5,734,136	$1,957,200	$127,750	$8,984,086
Thomas O'Flynn Former, EVP & Chief Financial Officer						
2018	$690,000	$0	$2,081,793	$925,000	$131,400	$3,828,193
2017	$690,000	$0	$2,052,965	$862,000	$107,701	$3,712,666
2016	$683,000	$0	$2,042,173	$764,960	$60,800	$3,550,933
Bernerd Da Santos EVP & Chief Operating Officer						
2018	$510,000	$69,000	$1,065,259	$683,000	$90,000	$2,417,259
2017	$510,000	$0	$1,050,505	$632,000	$69,266	$2,261,771
2016	$456,000	$0	$839,040	$485,184	$30,100	$1,810,324
Julian Nebreda [(7)] SVP & President, South America Strategic Business Unit						
2018	$396,550	$113,000	$432,267	$378,000	$803,914	$2,123,731
Manuel Pérez Dubuc [(8)] SVP & President, Global New Energy Solutions						
2018	$436,781	$0	$432,882	$428,000	$822,284	$2,119,947

* Table excludes the Options and Change in Pension Value and Non-Qualified Deferred Compensation Earnings columns, which are not applicable.

NOTES:

(1) Based on actual performance the value of equity awards may decline from reported values, including our relative Total Stockholder Return performance stock units and proportional free cash flow performance cash units. The below table reflects the aggregate value reported in the Summary Compensation Table during fiscal years 2018, 2017 and 2016, as well as income actually earned (W-2 income), during that same period.

Executive Compensation

Year	Summary Compensation Table ($)	Actual Compensation Earned	% Variance
Andrés Gluski			
2018	$9,759,811	$6,416,674	(-34%)
2017	$9,354,683	$5,358,702	(-43%)
2016	$8,984,086	$4,600,122	(-49%)
Thomas O'Flynn			
2018	$3,828,193	$2,798,219	(-27%)
2017	$3,712,666	$2,681,220	(-28%)
2016	$3,550,933	$1,853,198	(-48%)
Bernerd Da Santos			
2018	$2,417,259	$1,573,023	(-35%)
2017	$2,261,771	$1,380,263	(-39%)
2016	$1,810,324	$812,163	(-55%)

*Messrs. Nebreda and Pérez Dubuc are excluded as they were not NEOs prior to 2018.

(2) The base salary earned by each NEO during fiscal years 2018, 2017 and 2016, as applicable.

(3) In recognition of their individual performance achievements in 2018, the Compensation Committee approved the additional bonus amounts for Messrs. Da Santos and Nebreda paid under the Performance Incentive Plan.

(4) Aggregate grant date fair value of performance stock units, performance cash units, and restricted stock units granted in the year which are computed in accordance with Financial Accounting Standards Board ("FASB"), Accounting Standards Codification ("ASC") Topic 718, "Compensation-Stock Compensation" ("FASB ASC Topic 718") disregarding any estimates of forfeitures related to service-based vesting conditions. A discussion of the relevant assumptions made in the valuation may be found in our financial statements, footnotes to the financial statements (footnote 16), or Management's Discussion & Analysis, as appropriate, contained in the AES Form 10-K which also includes information for 2016 and 2017. Assuming the maximum market and financial performance conditions are achieved, and in the case of performance stock units the share price at grant, the maximum value of performance stock units and performance cash units granted in fiscal year 2018, and payable upon completion of the 2018-2020 performance period, is shown below.

Maximum Value of Performance Stock Units and Performance Cash Units
Granted in FY18 (payable after completion of 2018-2020 performance period)

Name	Performance Stock Units ($)	Performance Cash Units ($)	Total ($)
Andres Gluski	$3,813,472	$6,991,380	$10,804,852
Thomas O'Flynn	$1,345,510	$2,466,750	$3,812,260
Bernerd Da Santos	$688,501	$1,262,250	$1,950,751
Julian Nebreda	$364,821	$364,826	$729,647
Manuel Pérez Dubuc	$365,346	$365,352	$730,698

(5) The value of non-equity incentive plan awards earned during the 2018 fiscal year and paid in 2019 under our Performance Incentive Plan (our annual incentive plan).

(6) All Other Compensation includes Company contributions to both qualified and non-qualified defined contribution retirement plans. In the case of Mr. Nebreda and Mr. Pérez Dubuc, All Other Compensation also includes overseas relocation and assignment related benefits. Mr. Nebreda receives assignment related benefits as a result of his role

as SVP & President, South America Strategic Business Unit. Mr. Pérez Dubuc was on assignment as President, South America Strategic Business Unit prior to his current role of SVP, Global New Energy Solutions. Upon relocating to the United States Mr. Pérez Dubuc no longer receives any ongoing assignment allowances.

Executive Compensation

Name	AES Contributions to Qualified Defined Contribution Plans	AES Contributions to Non Qualified Defined Contribution Plans	Relocation and Assignment Benefits	Host Location Tax Payments	Total Other Compensation
Andres Gluski	$24,750	$258,750	$0	$0	$283,500
Thomas O'Flynn	$24,750	$106,650	$0	$0	$131,400
Bernerd Da Santos	$24,750	$65,250	$0	$0	$90,000
Julian Nebreda [(a)]	$24,750	$107,453	$315,172	$356,539	$803,914
Manuel Pérez Dubuc[(a)]	$22,705	$0	$702,591	$96,987	$822,283

[(a)] The Company provides various forms of compensation related to expatriate assignments that differ according to location and term of assignment, including: host housing allowances, cost of living differentials, assignment tax equalization, home leave and travel, relocation expense, and tax return and visa preparation. Among amounts included above, Mr. Nebreda received $300,542 in combined housing and cost of living allowance, and Mr. Pérez Dubuc received $655,045 in combined housing and cost of living allowance.

(7) Mr. Nebreda was not an NEO prior to 2018. Therefore, no compensation information appears for 2016 or 2017, in accordance with applicable SEC rules.

(8) Mr. Pérez Dubuc was not an NEO prior to 2018. Therefore, no compensation information appears for 2016 or 2017, in accordance with applicable SEC rules.

Sales and Lease Ownership
$
183,965

$

244,014

$
144,232

$
(60,049
)

(24.6
)%

$
99,782

69.2
%
HomeSmart
(3,428
)

(6,962
)

(7,283
)

3,534

50.8

321

4.4

RIMCO
(414
)

573

153

(987
)

(172.3
)

420

274.5

Franchise
54,171

52,672

49,577

1,499

2.8

3,095

6.2

Manufacturing
107

382

2,960

(275
)

(72.0
)

(2,578
)

(87.1
)
Other
(55,700
)

(12,910
)

119

(42,790
)

nmf

(13,029
)

nmf
Earnings Before Income Taxes for Reportable Segments
178,701

277,769

189,758

(99,068
)

(35.7
)

88,011

46.4

Elimination of Intersegment Profit
(94
)

(393
)

(2,960
)

299

76.1

2,567

86.7

Cash to Accrual and Other Adjustments
6,353

(521
)

(3,421
)

6,874

nmf

2,900

nmf
Total
$
184,960

$
276,855

$
183,377

$
(91,895
)

(33.2
)%

$
93,478

51.0
%
nmf—Calculation is not meaningful

Earnings before income taxes decreased $91.9 million, or 33.2%, due in part to a $60.0 million, or 24.6%, decrease in the Sales and Lease Ownership segment, which includes the impact of the reversal of the lawsuit accrual of $35.5 million during 2012. Earnings before income taxes were also impacted by $28.4 million in legal and regulatory expense related to a pending regulatory investigation and charges of $4.9 million due to the retirement of the Company's Chief Operating Officer and a change in the Company's vacation policies during 2013, as well as $10.4 million related to the retirement of the Company's founder and Chairman of the Board during 2012, all of which have been included in "Other" segment results.

Earnings before income taxes increased $93.5 million, or 51.0%, primarily due to a $99.8 million, or 69.2%, increase in the Sales and Lease Ownership segment, which includes the impact of the lawsuit accrual of $36.5 million during 2011 followed by the reversal of the lawsuit accrual of $35.5 million during 2012. Earnings before income taxes were also impacted by $10.4 million related to the retirement of the Company's founder and Chairman of the Board during 2012 and $3.5 million in separation costs related to the departure of the Company's former Chief Executive Officer during 2011, both of which have been included in "Other" segment results.

Income Tax Expense

Income tax expense decreased $39.5 million to $64.3 million in 2013, compared with $103.8 million in 2012, representing a 38.1% decrease due primarily to a 33.2% decrease in earnings before income taxes in 2013. In addition, our effective tax rate decreased to 34.8% in 2013 from 37.5% in 2012 due to the recognition of income tax benefits primarily related to the Company's furniture manufacturing operations and increased federal and state tax credits being applied to lower than expected earnings.

Income tax expense increased $34.2 million to $103.8 million in 2012, compared with $69.6 million in 2011, representing a 49.1% increase due to a 51.0% increase in earnings before income taxes in 2012, offset by a slightly lower tax rate in 2012. Our effective tax rate was 37.5% in 2012 and 38.0% in 2011.

Net Earnings

Net earnings decreased $52.4 million to $120.7 million in 2013 from $173.0 million in 2012, representing a 30.3% decrease. As a percentage of total revenues, net earnings were 5.4% and 7.8% in 2013 and 2012, respectively.

Net earnings increased $59.3 million to $173.0 million in 2012 from $113.8 million in 2011, representing a 52.1% increase. As a percentage of total revenues, net earnings were 7.8% and 5.7% in 2012 and 2011, respectively.

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Balance Sheet

Cash and Cash Equivalents. The Company’s cash and cash equivalents balance increased to $231.1 million at December 31, 2013 from $129.5 million at December 31, 2012. For additional information related to the $101.6 million increase in cash and cash equivalents, refer to the “Liquidity and Capital Resources” section below.

Investments. The Company's investment balance increased to $112.4 million at December 31, 2013 from $85.9 million at December 31, 2012. The $26.5 million increase was primarily a result of purchases of investments, partially offset by scheduled maturities and calls of investments, during 2013.

Lease Merchandise, Net. The decrease of $94.3 million in lease merchandise, net of accumulated depreciation, to $869.7 million at December 31, 2013 from $964.1 million at December 31, 2012, is primarily the result of a net decrease of $79.1 million in the Sales and Lease Ownership segment, $7.4 million in the HomeSmart segment and $7.8 million in the RIMCO segment due to the classification of the RIMCO net assets as held for sale at December 31, 2013.

Prepaid Expenses and Other Assets. Prepaid expenses and other assets decreased $22.0 million to $55.4 million at December 31, 2013 from $77.4 million at December 31, 2012, primarily as a result of a $22.7 million decrease in the Company's income tax receivable.

Accrued Regulatory Expense. Accrued regulatory expense increased to $28.4 million at December 31, 2013 from zero at December 31, 2012 and is related to a pending regulatory investigation by the California Attorney General into the Company's leasing, marketing and privacy practices.

Deferred Income Taxes Payable. The decrease of $36.8 million in deferred income taxes payable to $227.0 million at December 31, 2013 from $263.7 million at December 31, 2012 is primarily the result of the reversal of bonus depreciation deductions on lease merchandise included in the Tax Relief, Unemployment Reauthorization and Job Creation Act of 2010.

Included in the deferred income tax payable as of December 31, 2013 are a deferred tax asset of $60.2 million and a valuation allowance of $682,000. The Company has reserved the entire value of the Canadian net operating loss as there is no expected taxable income to absorb the loss within that jurisdiction. With respect to all other deferred tax assets, the Company believes it will have sufficient taxable income in future years to realize their benefit.

Liquidity and Capital Resources

General

Cash flows from operations for the years ended December 31, 2013, 2012 and 2011 were $308.4 million, $59.8 million and $307.2 million, respectively. The $248.7 million increase in cash flows from operating activities during 2013 as compared to 2012 was due, in part, to a $41.7 million reduction in accrued litigation expense during 2012 resulting from the settlement of a lawsuit and $28.4 million in non-cash legal and regulatory expense during 2013 for loss contingencies related to the pending regulatory investigation by the California Attorney General. The increase in cash flows from operating activities also includes a net $180.9 million decrease in lease merchandise, net of the effects of acquisitions and a $45.1 million increase related to the Company's income tax receivable. The change in income tax receivable is due to The American Taxpayer Relief Act of 2012 enacted on January 2, 2013, which extended bonus depreciation on eligible inventory held during 2012 and 2013. In 2012, the Company made payments based on enacted law, resulting in an overpayment when the act was signed.

Purchases of sales and lease ownership stores had a positive impact on operating cash flows in each period presented. The positive impact on operating cash flows from purchasing stores occurs as the result of lease merchandise, other assets and intangibles acquired in these purchases being treated as an investing cash outflow. As such, the operating cash flows attributable to the newly purchased stores usually have an initial positive effect on operating cash flows that may not be indicative of the extent of their contributions in future periods. The amount of lease merchandise purchased in acquisitions and shown under investing activities, was $4.0 million in 2013, $11.9 million in 2012 and $13.4 million in 2011.

Sales of Company-operated stores are an additional source of investing cash flows in each period presented. Proceeds from such sales were $2.2 million in 2013, $2.0 million in 2012 and $7.3 million in 2011. The amount of lease merchandise sold in these sales and shown under investing activities was $882,000 in 2013, $1.4 million in 2012 and $8.9 million in 2011.

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Our primary capital requirements consist of buying lease merchandise for sales and lease ownership stores. As we continue to grow, the need for additional lease merchandise is expected to remain our major capital requirement. Other capital requirements include purchases of property, plant and equipment and expenditures for acquisitions and income tax payments. These capital requirements historically have been financed through:

- cash flow from operations;
- trade credit with vendors;
- proceeds from the sale of lease return merchandise;
- bank credit;
- private debt offerings; and
- stock offerings.

Debt Financing

At December 31, 2013, there was no outstanding balance under our revolving credit agreement. Our revolving credit facility expires December 13, 2017 and the total available credit under the facility as of December 31, 2013 is $140.0 million. As of December 31, 2013, the Company had outstanding $125.0 million in senior unsecured notes, originally issued to several insurance companies in a private placement in July 2011. The notes bear interest at the rate of 3.75% per year and mature on April 27, 2018. Payments of interest are due quarterly, commencing July 27, 2011, with principal payments of $25.0 million each due annually commencing April 27, 2014.

On October 8, 2013, the Company's revolving credit agreement, senior unsecured notes and franchise loan agreement were amended to remove or adjust certain covenants to make them less restrictive. The amendments to the Company's revolving credit agreement, senior unsecured notes and franchise loan agreement are discussed in further detail in Note 8 to the Company's consolidated financial statements.

Our revolving credit agreement and senior unsecured notes, and our franchise loan agreement discussed below, contain certain financial covenants. These covenants include requirements that we maintain ratios of: (1) EBITDA plus lease expense to fixed charges of no less than 2:1; and (2) total debt to EBITDA of no greater than 3:1; “EBITDA” in each case means consolidated net income before interest and tax expense, depreciation (other than lease merchandise depreciation) and amortization expense, and other non-cash charges. If we fail to comply with these covenants, we will be in default under these agreements, and all amounts will become due immediately. We were in compliance with all of these covenants at December 31, 2013 and believe that we will continue to be in compliance in the future.

Share Repurchases

We purchase our stock in the market from time to time as authorized by our Board of Directors. In October 2013, the Board of Directors authorized the repurchase of an additional 10,955,345 shares of common stock over the previously authorized amount of 4,044,655 shares, increasing the total number of our shares of common stock authorized for repurchase to 15,000,000.

In December 2013, the Company paid $125 million under an accelerated share repurchase program with a third party financial institution and received an initial delivery of 3,502,627 shares. In February 2014, the accelerated share repurchase program was completed and the Company received an additional 1,000,952 shares of common stock. The accelerated share repurchase program is discussed in further detail in Note 9 to the Company's consolidated financial statements.

Dividends

We have a consistent history of paying dividends, having paid dividends for 26 consecutive years. Our annual common stock dividend was $.072 per share, $.062 per share and $.054 per share in 2013, 2012 and 2011, respectively, and resulted in aggregate dividend payments of $3.9 million, $5.8 million and $4.1 million in 2013, 2012 and 2011, respectively. At its November 2013 meeting, our Board of Directors increased the quarterly dividend by 23.5%, raising it to $.021 per share. The Company also increased its quarterly dividend rate by 13.3%, to $.017 per share, in November 2012 and by 15.4%, to $.015 per share, in November 2011. Subject to sufficient operating profits, any future capital needs and other contingencies, we currently expect to continue our policy of paying dividends.

If we achieve our expected level of growth in our operations, we anticipate we will supplement our expected cash flows from operations, existing credit facilities, vendor credit and proceeds from the sale of lease return merchandise by expanding our existing credit facilities, by securing additional debt financing, or by seeking other sources of capital to ensure we will be able to fund our capital and liquidity needs for at least the next 12 to 24 months.

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Commitments

Income Taxes. During the year ended December 31, 2013, we made $54.0 million in income tax payments. Within the next twelve months, we anticipate that we will make cash payments for federal and state income taxes of approximately $183.0 million.

The American Recovery and Reinvestment Act of 2009, and the Small Business Jobs Act of 2010 provided for accelerated depreciation by allowing a bonus first-year depreciation deduction of 50% of the adjusted basis of qualified property, such as our lease merchandise, placed in service during those years. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "2010 TRA") allowed for deduction of 100% of the adjusted basis of qualified property for assets placed in service after September 8, 2010 and before December 31, 2011. The 2010 TRA also allowed for a deduction of 50% of the cost of qualified property placed in service during 2012. The American Taxpayer Relief Act of 2012 extended bonus depreciation of 50% through the end of 2013. Accordingly, our cash flow benefited from having a lower cash tax obligation, which, in turn, provided additional cash flow from operations. Because of our sales and lease ownership model, where the Company remains the owner of merchandise on lease, we benefit more from bonus depreciation, relatively, than traditional furniture, electronics and appliance retailers.

In future years, we anticipate having to make increased tax payments on our earnings as a result of expected profitability and the reversal of the accelerated depreciation deductions that were taken in 2013 and prior periods. We estimate that at December 31, 2013, the remaining tax deferral associated with the acts described above is approximately $134.0 million, of which approximately 65% is expected to reverse in 2014 and most of the remainder during 2015 and 2016.

Leases. We lease warehouse and retail store space for most of our operations under operating leases expiring at various times through 2029. Most of the leases contain renewal options for additional periods ranging from one to 20 years or provide for options to purchase the related property at predetermined purchase prices that do not represent bargain purchase options. We also lease transportation and computer equipment under operating leases expiring during the next five years. We expect that most leases will be renewed or replaced by other leases in the normal course of business. Approximate future minimum rental payments required under operating leases that have initial or remaining non-cancelable terms in excess of one year as of December 31, 2013 are shown in the below table under “Contractual Obligations and Commitments.”

As of December 31, 2013, we have 20 capital leases, 19 of which are with a limited liability company (“LLC”) whose managers and owners are seven current officers (of which six are current executive officers) and four former officers of the Company, with no individual owning more than 13.33% of the LLC. Nine of these related party leases relate to properties purchased from us in October and November of 2004 by the LLC for a total purchase price of $6.8 million. The LLC is leasing back these properties to us for a 15-year term, with a five-year renewal at our option, at an aggregate annual lease amount of $716,000. Another 10 of these related party leases relate to properties purchased from the Company in December 2002 by the LLC for a total purchase price of approximately $5.0 million. The LLC leases back these properties to the Company for a 15-year term at an aggregate annual lease of $1.2 million. We do not currently plan to enter into any similar related party lease transactions in the future.

We finance a portion of our store expansion through sale-leaseback transactions. The properties are generally sold at net book value and the resulting leases qualify and are accounted for as operating leases. We do not have any retained or contingent interests in the stores nor do we provide any guarantees, other than a corporate level guarantee of lease payments, in connection with the sale-leasebacks. The operating leases that resulted from these transactions are included in the table below under "Contractual Obligations and Commitments."

Franchise Loan Guaranty. We have guaranteed the borrowings of certain independent franchisees under a franchise loan agreement with several banks. On December 12, 2013, we entered into a seventh amendment to our second amended and restated loan facility and guaranty, dated June 18, 2010, as amended. The amendment to the franchise loan facility extended the maturity date to December 11, 2014. Pursuant to this facility, subject to certain terms and conditions, the Company's franchisees can borrow funds guaranteed by the Company. The amendment to the franchise loan agreement also (i) permit franchise borrowers to use loan proceeds for any purpose approved by the Company, in addition to merchandise purchases and related expenses, and (ii) impose certain restrictions on the indebtedness of franchisee borrowers, other than under the franchise loan facility. The Company remains subject to financial covenants under the franchise loan facility.

At December 31, 2013, the portion that we might be obligated to repay in the event franchisees defaulted was $105.0 million. However, due to franchisee borrowing limits, we believe any losses associated with any defaults would be mitigated through recovery of lease merchandise and other assets. Since its inception in 1994, we have had no significant associated losses. We believe the likelihood of any significant amounts being funded in connection with these commitments to be remote.

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Contractual Obligations and Commitments. The following table shows our approximate contractual obligations, including interest, and commitments to make future payments as of December 31, 2013:

(In Thousands)	Total	Period Less Than 1 Year	Period 1-3 Years	Period 3-5 Years	Period Over 5 Years
Debt, Excluding Capital Leases	$128,250	$25,000	$53,250	$50,000	$—
Capital Leases	14,454	2,529	5,505	4,014	2,406
Interest Obligations	22,591	5,632	10,341	6,588	30
Operating Leases	528,567	113,067	171,532	100,385	143,583
Purchase Obligations	35,448	19,197	16,251	—	—
Retirement Obligations	9,306	4,215	3,837	1,206	48
Total Contractual Cash Obligations	$738,616	$169,640	$260,716	$162,193	$146,067

The following table shows the Company's approximate commercial commitments as of December 31, 2013:

(In Thousands)	Total Amounts Committed	Period Less Than 1 Year	Period 1-3 Years	Period 3-5 Years	Period Over 5 Years
Guaranteed Borrowings of Franchisees	$105,030	$104,357	$673	$—	$—

Purchase obligations are primarily related to certain advertising and marketing programs. We have no long-term commitments to purchase merchandise nor do we have significant purchase agreements that specify minimum quantities or set prices that exceed our expected requirements for three months.

Retirement obligations primarily represent future payments associated with the retirement of the Company's founder and Chairman of the Board during the year ended December 2012 and the Chief Operating Officer during the year ended December 31, 2013.

Deferred income tax liabilities as of December 31, 2013 were approximately $227.0 million. This amount is not included in the total contractual obligations table because we believe this presentation would not be meaningful. Deferred income tax liabilities are calculated based on temporary differences between the tax basis of assets and liabilities and their respective book basis, which will result in taxable amounts in future years when the liabilities are settled at their reported financial statement amounts. The results of these calculations do not have a direct connection with the amount of cash taxes to be paid in any future periods. As a result, scheduling deferred income tax liabilities as payments due by period could be misleading, because this scheduling would not relate to liquidity needs.

Recent Accounting Pronouncements

Refer to Note 1 to the Company's consolidated financial statements for a discussion of recently issued accounting pronouncements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of December 31, 2013, we had $125.0 million of senior unsecured notes outstanding at a fixed rate of 3.75%. We had no balance outstanding under our revolving credit agreement indexed to the LIBOR ("London Interbank Offer Rate") or the prime rate, which exposes us to the risk of increased interest costs if interest rates rise. Based on our overall interest rate exposure at December 31, 2013, a hypothetical 1.0% increase or decrease in interest rates would not be material.

We do not use any significant market risk sensitive instruments to hedge commodity, foreign currency or other risks, and hold no market risk sensitive instruments for trading or speculative purposes.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Registered Public Accounting Firm

The Board of Directors of Aaron’s, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Aaron’s, Inc. and subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of earnings, comprehensive income, shareholders’ equity and cash flows for each of the three years in the period ended December 31, 2013. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Aaron’s, Inc. and subsidiaries at December 31, 2013 and 2012, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Aaron’s, Inc. and subsidiaries’ internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) and our report dated February 24, 2014 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Atlanta, Georgia

February 24, 2014

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Report of Independent Registered Public Accounting Firm on Internal Control over Financial Reporting
The Board of Directors of Aaron's, Inc. and Subsidiaries
We have audited Aaron's, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) (the COSO criteria). Aaron's, Inc. and subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.
We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.
A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.
Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.
In our opinion, Aaron's, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on the COSO criteria.
We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Aaron's, Inc. and subsidiaries as of December 31, 2013 and 2012 and the related consolidated statements of earnings, comprehensive income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2013 of Aaron's, Inc. and subsidiaries and our report dated February 24, 2014 expressed an unqualified opinion thereon.
/s/ Ernst & Young LLP
Atlanta, Georgia
February 24, 2014

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Management Report on Internal Control over Financial Reporting

Management of Aaron’s, Inc. and subsidiaries (the “Company”) is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate. Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, the risk.

The Company’s management assessed the effectiveness of the Company’s internal control over financial reporting as of December 31, 2013. In making this assessment, the Company’s management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) in Internal Control-Integrated Framework.

Based on its assessment, management believes that, as of December 31, 2013, the Company’s internal control over financial reporting was effective based on those criteria.

The Company’s internal control over financial reporting as of December 31, 2013 has been audited by Ernst & Young LLP, an independent registered public accounting firm, as stated in their report dated February 24, 2014, which expresses an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting as of December 31, 2013.

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AARON'S, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31, 2013	December 31, 2012
	(In Thousands, Except Share Data)	
ASSETS:		
Cash and Cash Equivalents	$ 231,091	$ 129,534
Investments	112,391	85,861
Accounts Receivable (net of allowances of $7,172 in 2013 and $6,001 in 2012)	68,684	74,157
Lease Merchandise (net of accumulated depreciation of $594,436 in 2013 and $575,527 in 2012)	869,725	964,067
Property, Plant and Equipment, Net	231,293	230,598
Goodwill	239,181	234,195
Other Intangibles, Net	3,535	6,026
Prepaid Expenses and Other Assets	55,436	77,387
Assets Held for Sale	15,840	11,104
Total Assets	$ 1,827,176	$ 1,812,929
LIABILITIES & SHAREHOLDERS' EQUITY:		
Accounts Payable and Accrued Expenses	$ 243,910	$ 225,532
Accrued Regulatory Expense	28,400	—
Deferred Income Taxes Payable	226,958	263,721
Customer Deposits and Advance Payments	45,241	46,022
Credit Facilities	142,704	141,528
Total Liabilities	687,213	676,803
Commitments and Contingencies (Note 8)	—	—
Shareholders' Equity:		
Common Stock: Par Value $.50 Per Share; Authorized: 225,000,000; Shares Issued: 90,752,123 at December 31, 2013 and December 31, 2012, respectively	45,376	45,376
Additional Paid-in Capital	198,182	220,362
Retained Earnings	1,202,219	1,087,032
Accumulated Other Comprehensive Loss	(64)	(69)
	1,445,713	1,352,701
Less: Treasury Shares at Cost		
Common Stock: 17,795,293 Shares at December 31, 2013 and 15,031,741 Shares at December 31, 2012	(305,750)	(216,575)
Total Shareholders' Equity	1,139,963	1,136,126
Total Liabilities & Shareholders' Equity	$ 1,827,176	$ 1,812,929

The accompanying notes are an integral part of the Consolidated Financial Statements.

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AARON'S, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS

	Year Ended December 31, 2013	Year Ended December 31, 2012	Year Ended December 31, 2011
	(In Thousands, Except Per Share Data)		
REVENUES:			
Lease Revenues and Fees	$1,748,699	$1,676,391	$1,516,508
Retail Sales	40,876	38,455	38,557
Non-Retail Sales	371,292	425,915	388,960
Franchise Royalties and Fees	68,575	66,655	63,255
Other	5,189	5,411	5,298
	2,234,631	2,212,827	2,012,578
COSTS AND EXPENSES:			
Retail Cost of Sales	24,318	21,608	22,619
Non-Retail Cost of Sales	337,581	387,362	351,887
Operating Expenses	1,022,684	952,617	866,600
Legal and Regulatory Expense/(Income)	28,400	(35,500)	36,500
Retirement and Vacation Charges	4,917	10,394	3,532
Depreciation of Lease Merchandise	628,089	601,552	547,839
Other Operating Expense (Income), Net	1,584	(2,235)	(3,550)
	2,047,573	1,935,798	1,825,427
OPERATING PROFIT	187,058	277,029	187,151
Interest Income	2,998	3,541	1,718
Interest Expense	(5,613)	(6,392)	(4,709)
Other Non-Operating Income (Expense), Net	517	2,677	(783)
EARNINGS BEFORE INCOME TAXES	184,960	276,855	183,377
INCOME TAXES	64,294	103,812	69,610
NET EARNINGS	$120,666	$173,043	$113,767
EARNINGS PER SHARE	$1.59	$2.28	$1.46
EARNINGS PER SHARE ASSUMING DILUTION	$1.58	$2.25	$1.43

The accompanying notes are an integral part of the Consolidated Financial Statements.

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AARON'S, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year End December 31,		
(In Thousands)	2013	2012	2011
Net Earnings	$120,666	$173,043	$113,767
Other Comprehensive Income (Loss):			
Foreign Currency Translation:			
Foreign Currency Translation Adjustment	5	(343)	(648)
Less: Reclassification Adjustments for Net Gains Included in Net Earnings	—	373	—
Net Change	5	30	(648)
Available-for-Sale Investments:			
Change in Net Unrealized Losses on Available-for-Sale Investments	—	—	88
Less: Reclassification Adjustment for Net Losses Included in Net Earnings	—	—	(88)
Net Change	—	—	—
Cash Flow Hedges:			
Change in Net Unrealized Gains on Derivatives Designated as Cash Flow Hedges	—	—	(12)
Less: Reclassification Adjustment for Net Gains Included in Net Earnings	—	—	12
Net Change	—	—	—
Total Other Comprehensive Income (Loss)	5	30	(648)
Comprehensive Income	$120,671	$173,073	$113,119

The accompanying notes are an integral part of the Consolidated Financial Statements.

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AARON'S, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In Thousands, Except Per Share)	Treasury Stock Shares	Treasury Stock Amount	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss)In Foreign Currency Translation	Available-for-Sale Investments	Cash Flow Hedges
Balance, January 1, 2011	(10,665)	$(77,641)	$45,376	$201,752	$809,084	$ 922	$ (88)	$ 12
Dividends, $.054 per share					(4,152)			
Stock-Based Compensation				8,385				
Reissued Shares	737	7,493		2,174				
Repurchased Shares	(5,184)	(129,958)						
Net Earnings					113,767			
Foreign Currency Translation Adjustment						(648)		
Change in Net Unrealized Losses on Available-for-Sale Investments							88	
Change in Net Unrealized Gains on Derivatives Designated as Cash Flow Hedges								(12)
Balance, December 31, 2011	(15,112)	(200,106)	45,376	212,311	918,699	274	—	—
Dividends, $.062 per share					(4,710)			
Stock-Based Compensation				6,374				
Reissued Shares	1,317	17,662		1,677				
Repurchased Shares	(1,237)	(34,131)						
Net Earnings					173,043			
Foreign Currency Translation Adjustment						(343)		
Balance, December 31, 2012	(15,032)	(216,575)	45,376	220,362	1,087,032	(69)	—	—
Dividends, $.072 per share					(5,479)			
Stock-Based Compensation				2,250				
Reissued Shares	739	10,825		570				
Repurchased Shares	(3,502)	(100,000)		(25,000)				
Net Earnings					120,666			

Foreign Currency Translation Adjustment						5		
Balance, December 31, 2013	(17,795)	$(305,750)	$45,376	$198,182	$1,202,219	$ (64)	$ —	$ —

The accompanying notes are an integral part of the Consolidated Financial Statements.

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AARON'S, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31, 2013 (In Thousands)	Year Ended December 31, 2012	Year Ended December 31, 2011
OPERATING ACTIVITIES:			
Net Earnings	$120,666	$173,043	$113,767
Adjustments to Reconcile Net Earnings to Net Cash Provided by Operating Activities:			
Depreciation of Lease Merchandise	628,089	601,552	547,839
Other Depreciation and Amortization	57,016	56,783	52,832
Bad Debt Expense	35,894	31,842	25,402
Stock-Based Compensation	2,342	6,454	8,385
Loss (Gain) on Sale of Property, Plant, and Equipment and Assets Held for Sale	613	(397)	1,172
Gain on Asset Dispositions	(705)	(265)	(3,045)
Deferred Income Taxes	(36,763)	(23,241)	59,449
Excess Tax Benefits From Stock-Based Compensation	(1,381)	(5,967)	(1,264)
Other Changes, Net	5,469	7,830	(1,693)
Changes in Operating Assets and Liabilities, Net of Effects of Acquisitions and Dispositions:			
Additions to Lease Merchandise	(964,072)	(1,162,703)	(1,024,602)
Book Value of Lease Merchandise Sold or Disposed	425,673	469,897	433,433
Accounts Receivable	(30,419)	(18,528)	(43,211)
Prepaid Expenses and Other Assets	(1,349)	(9,263)	(4,317)
Income Tax Receivable	22,688	(22,379)	79,762
Accounts Payable and Accrued Expenses	16,893	(4,635)	18,885
Accrued Litigation Expense	28,400	(41,720)	40,043
Customer Deposits and Advance Payments	(617)	1,451	4,358
Cash Provided by Operating Activities	308,437	59,754	307,195
INVESTING ACTIVITIES:			
Purchase of Investments	(74,845)	(91,000)	(100,513)
Proceeds from Maturities and Calls of Investments	47,930	102,118	1,063
Additions to Property, Plant and Equipment	(58,145)	(65,073)	(78,211)
Acquisitions of Businesses and Contracts	(10,898)	(30,799)	(32,176)
Proceeds from Dispositions of Businesses and Contracts	2,163	1,999	7,282
Proceeds from Sale of Property, Plant, and Equipment	6,841	6,790	11,481
Cash Used by Investing Activities	(86,954)	(75,965)	(191,074)
FINANCING ACTIVITIES:			
Proceeds from Credit Facilities	2,598	16,258	129,150
Repayments on Credit Facilities	(4,954)	(28,519)	(17,151)
Acquisition of Treasury Stock	(125,000)	(34,131)	(127,193)
Dividends Paid	(3,875)	(5,843)	(4,073)
Excess Tax Benefits From Stock-Based Compensation	1,381	5,967	1,264
Issuance of Stock Under Stock Option Plans	9,924	15,756	6,117
Cash Used by Financing Activities	(119,926)	(30,512)	(11,886)
Increase (Decrease) in Cash and Cash Equivalents	101,557	(46,723)	104,235

Cash and Cash Equivalents at Beginning of Year	129,534	176,257	72,022
Cash and Cash Equivalents at End of Year	$231,091	$129,534	$176,257
Cash Paid During the Year:			
Interest	$5,614	$6,498	$3,983
Income Taxes	54,027	145,370	10,991

The accompanying notes are an integral part of the Consolidated Financial Statements.

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NOTE 1: BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Aaron's, Inc. (the "Company" or "Aaron's") is a leading specialty retailer engaged in the business of leasing and selling consumer electronics, computers, furniture, appliances and household accessories throughout the United States and Canada. The Company's major operating divisions are the Sales & Lease Ownership division (established as a monthly payment concept), the HomeSmart division (established as a weekly payment concept) and the Woodhaven Furniture Industries division, which manufactures upholstered furniture and bedding predominantly for use by Company-operated and franchised stores. The Company's Sales & Lease Ownership division includes the Company's RIMCO stores, which lease automobile tires, wheels and rims under sales and lease ownership agreements. In January of 2014, we sold our 27 Company-operated RIMCO stores and the rights to five franchised RIMCO stores.

The following table presents store count by ownership type:

Stores at December 31 (Unaudited)	2013	2012	2011
Company-operated stores			
Sales and Lease Ownership	1,262	1,227	1,144
HomeSmart	81	78	71
RIMCO	27	19	16
Aaron's Office Furniture	—	—	1
Total Company-operated stores	1,370	1,324	1,232
Franchised stores[1]	781	749	713
Systemwide stores	2,151	2,073	1,945

[1] As of December 31, 2013, 2012 and 2011, 940, 929 and 943 franchises had been awarded, respectively.

Basis of Presentation

The preparation of the Company's consolidated financial statements in conformity with accounting principles generally accepted in the United States ("U.S. GAAP") requires management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Actual results could differ from those estimates. Generally, actual experience has been consistent with management's prior estimates and assumptions. Management does not believe these estimates or assumptions will change significantly in the future absent unsurfaced and unforeseen events.

Certain reclassifications have been made to the prior periods to conform to the current period presentation. In all periods presented, the Company's RIMCO operations have been reclassified from the Sales and Lease Ownership segment to the RIMCO segment in Note 11 to the consolidated financial statements.

Principles of Consolidation and Variable Interest Entities

The consolidated financial statements include the accounts of Aaron's, Inc. and its wholly owned subsidiaries. Intercompany balances and transactions between consolidated entities have been eliminated.

On October 14, 2011, the Company purchased 11.5% of newly issued shares of common stock of Perfect Home Holdings Limited ("Perfect Home"), a privately-held rent-to-own company that is primarily financed by share capital and subordinated debt. Perfect Home is based in the U.K. and operated 64 retail stores as of December 31, 2013. As part of the transaction, the Company also received notes and an option to acquire the remaining interest in Perfect Home at any time through December 31, 2013. The Company did not exercise this purchase option but is in discussions with the owners of Perfect Home to extend the notes through June 2015. The Company's investment is denominated in British Pounds.

Perfect Home is a variable interest entity ("VIE") as it does not have sufficient equity at risk; however, the Company is not the primary beneficiary and lacks the power through voting or similar rights to direct the activities of Perfect Home that most significantly affect its economic performance. As such, the VIE is not consolidated by the Company.

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Because the Company is not able to exercise significant influence over the operating and financial decisions of Perfect Home, the equity portion of the investment in Perfect Home, totaling less than a thousand dollars at December 31, 2013 and 2012, respectively, is accounted for as a cost method investment and is included in prepaid expenses and other assets in the consolidated balance sheets. The notes purchased from Perfect Home totaling £12.5 million ($20.7 million) and £11.4 million ($18.4 million) at December 31, 2013 and 2012, respectively, are accounted for as held-to-maturity securities in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 320, Debt and Equity Securities, and are included in investments in the consolidated balance sheets. The increase in the Company's British pound-denominated notes during the year ended December 31, 2013 relates to accretion of the original discount on the notes with a face value of £10.0 million. Utilizing a Black-Scholes model, the options to buy the remaining interest in Perfect Home and to sell the Company's interest in Perfect Home were determined to have only nominal values.

The Company's maximum exposure to any potential losses associated with this VIE is equal to its total recorded investment which was $20.7 million at December 31, 2013.

Revenue Recognition

Lease Revenues and Fees

The Company provides merchandise, consisting of consumer electronics, computers, furniture, appliances, and household accessories, to its customers for lease under certain terms agreed to by the customer. Two primary lease models are offered to customers: one through the Company's Sales & Lease Ownership division (established as a monthly model) and the other through its HomeSmart division (established as a weekly model). The typical monthly lease model is 12, 18 or 24 months, while the typical weekly lease model is 60, 90 or 120 weeks. The Company does not require deposits upon inception of customer agreements.

In a number of states, the Company utilizes a consumer lease form as an alternative to a typical lease purchase agreement. The consumer lease differs from our state lease agreement in that it has an initial lease term in excess of four months. Generally, state laws that govern the rent-to-own industry only apply to lease agreements with an initial term of four months or less. Following satisfaction of the initial term contained in the consumer or state lease, as applicable, the customer has the right to acquire title either through a purchase option or through payment of all required lease payments.

All of the Company's customer agreements are considered operating leases under the provisions of ASC 840, Leases. As such, lease revenues are recognized as revenue in the month they are due. Lease payments received prior to the month due are recorded as deferred lease revenue, which is included in customer deposits and advance payments in the accompanying consolidated balance sheets. Until all payment obligations are satisfied under sales and lease ownership agreements, the Company maintains ownership of the lease merchandise. Initial direct costs related to the Company's customer agreements are expensed as incurred and have been classified as operating expenses in the Company's consolidated statements of earnings.

Retail and Non-Retail Sales

Revenues from the sale of merchandise to franchisees are recognized at the time of receipt of the merchandise by the franchisee based on the electronic receipt of merchandise by the franchisee within the Company's fulfillment system. Additionally, revenues from the sale of merchandise to other customers are recognized at the time of shipment, at which time title and risk of ownership are transferred to the customer.

Substantially all of the amounts reported as non-retail sales and non-retail cost of sales in the accompanying consolidated statements of earnings relate to the sale of lease merchandise to franchisees. The Company classifies the sale of merchandise to other customers as retail sales in the consolidated statements of earnings. The Company presents sales net of sales taxes.

Franchise Royalties and Fees

The Company franchises its Aaron's Sales & Lease Ownership and HomeSmart stores in markets where the Company has no immediate plans to enter. Franchisees typically pay a non-refundable initial franchise fee from $15,000 to $50,000 depending upon market size and an ongoing royalty of either 5% or 6% of gross revenues. Franchise fees and area development fees are generated from the sale of rights to develop, own and operate sales and lease ownership stores. These fees are recognized as income when substantially all of the Company's obligations per location are satisfied, generally at the date of the store opening. Franchise fees and area development fees are received before the substantial completion of the Company’s obligations and are deferred. The Company guarantees certain debt obligations of some of the franchisees and receives guarantee fees based on the outstanding debt obligations of such franchisees. The Company recognizes finance fee revenue as the guarantee obligation is satisfied. Refer to Note 8 for additional discussion of the Company’s franchise-related guarantee obligation.

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Franchise agreement fee revenue was $1.7 million, $2.4 million and $2.6 million; royalty revenue was $59.1 million, $56.5 million and $52.0 million; and finance fee revenue was $5.1 million, $4.9 million and $5.9 million for the years ended December 31, 2013, 2012 and 2011, respectively. Deferred franchise and area development agreement fees, included in accounts payable and accrued expenses in the accompanying consolidated balance sheets, were $3.4 million and $3.8 million at December 31, 2013 and 2012, respectively.

Retail and Non-Retail Cost of Sales

Included in cost of sales is the net book value of merchandise sold, primarily using specific identification. It is not practicable to allocate operating expenses between selling and lease operations.

Shipping and Handling Costs

The Company classifies shipping and handling costs as operating expenses in the accompanying consolidated statements of earnings, and these costs totaled $78.6 million, $74.9 million and $68.1 million in 2013, 2012 and 2011, respectively.

Advertising

The Company expenses advertising costs as incurred. Advertising production costs are expensed when an advertisement appears for the first time. Such advertising costs amounted to $43.0 million, $36.5 million and $38.9 million in 2013, 2012 and 2011, respectively. These advertising expenses are shown net of cooperative advertising considerations received from vendors, substantially all of which represents reimbursement of specific, identifiable and incremental costs incurred in selling those vendors' products. The amount of cooperative advertising consideration netted against advertising expense was $25.0 million, $31.1 million and $25.4 million in 2013, 2012 and 2011, respectively. The prepaid advertising asset was $2.4 million and $3.2 million at December 31, 2013 and 2012, respectively.

Stock-Based Compensation

The Company has stock-based employee compensation plans, which are more fully described in Note 10. The Company estimates the fair value for the options granted on the grant date using a Black-Scholes option-pricing model and accounts for stock-based compensation under the fair value recognition provisions codified in ASC Topic 718, Stock Compensation. The fair value of each share of restricted stock awarded is equal to the market value of a share of the Company's common stock on the grant date.

Deferred Income Taxes

Deferred income taxes represent primarily temporary differences between the amounts of assets and liabilities for financial and tax reporting purposes. The Company's largest temporary differences arise principally from the use of accelerated depreciation methods on lease merchandise for tax purposes.

Earnings per Share

Earnings per share is computed by dividing net earnings by the weighted average number of shares of common stock outstanding during the period. The computation of earnings per share assuming dilution includes the dilutive effect of stock options, restricted stock units ("RSUs") and restricted stock awards ("RSAs") as determined under the treasury stock method. The following table shows the calculation of dilutive stock awards for the years ended December 31 (shares in thousands):

	2013	2012	2011
Weighted average shares outstanding	75,747	75,820	78,101
Effect of dilutive securities:			
Stock options	421	789	998
RSUs	206	210	237
RSAs	16	7	3
Weighted average shares outstanding assuming dilution	76,390	76,826	79,339

Approximately 53,000 stock-based awards were excluded from the computations of earnings per share assuming dilution in 2012 because the awards would have been anti-dilutive for the year presented. No stock options, RSUs or RSAs were anti-dilutive during 2013 or 2011. In addition, under the terms of the Company's performance-based RSUs, approximately 175,000 RSUs may be earned based on the achievement of revenue and pre-tax profit margin targets applicable to performance periods beginning subsequent to December 31, 2013. Refer to Note 10 for additional information regarding the Company’s restricted stock arrangements.

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Lease Merchandise

The Company's lease merchandise consists primarily of consumer electronics, computers, furniture, appliances, and household accessories and is recorded at cost, which includes overhead from production facilities, shipping costs and warehousing costs. The sales and lease ownership stores depreciate merchandise over the lease agreement period, generally 12 to 24 months (monthly agreements) or 60 to 120 weeks (weekly agreements) when on lease and 36 months when not on lease, to a 0% salvage value. The Company's policies require weekly lease merchandise counts at the store, which include write-offs for unsalable, damaged, or missing merchandise inventories. Full physical inventories are generally taken at the fulfillment and manufacturing facilities two to four times a year, and appropriate provisions are made for missing, damaged and unsalable merchandise. In addition, the Company monitors lease merchandise levels and mix by division, store, and fulfillment center, as well as the average age of merchandise on hand. If unsalable lease merchandise cannot be returned to vendors, it is adjusted to its net realizable value or written off.

All lease merchandise is available for lease or sale. On a monthly basis, all damaged, lost or unsalable merchandise identified is written off. The Company records lease merchandise adjustments on the allowance method. Lease merchandise write-offs totaled $58.0 million, $54.9 million and $46.2 million during the years ended December 31, 2013, 2012 and 2011, respectively, and are included in operating expenses in the accompanying consolidated statements of earnings.

Cash and Cash Equivalents

The Company classifies highly liquid investments with maturity dates of less than three months when purchased as cash equivalents. The Company maintains its cash and cash equivalents in a limited number of banks. Bank balances typically exceed coverage provided by the Federal Deposit Insurance Corporation. However, due to the size and strength of the banks where the balances are held, such exposure to loss is considered minimal.

Investments

The Company maintains investments in various corporate debt securities, or bonds. The Company has the positive intent and ability to hold its investments in debt securities to maturity. Accordingly, the Company classifies its investments in debt securities, which mature at various dates from 2014 to 2015, as held-to-maturity securities and carries the investments at amortized cost in the consolidated balance sheets.

The Company evaluates securities for other-than-temporary impairment on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. The Company does not intend to sell the securities and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost bases.

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Accounts Receivable

Accounts receivable consist primarily of receivables due from customers of Company-operated stores, corporate receivables incurred during the normal course of business (primarily related to vendor consideration, real estate leasing activities and in-transit credit card transactions) and franchisee obligations. Accounts receivable, net of allowances, consists of the following as of December 31:

(In Thousands)	2013	2012
Customers	$8,275	$7,840
Corporate	16,730	17,215
Franchisee	43,679	49,102
	$68,684	$74,157

The Company maintains an allowance for doubtful accounts. The reserve for returns is calculated based on the historical collection experience associated with lease receivables. The Company's policy is to write off lease receivables that are 60 days or more past due on pre-determined dates occurring twice monthly. The following is a summary of the Company's allowance for doubtful accounts as of December 31:

(In Thousands)	2013	2012	2011
Beginning Balance	$6,001	$4,768	$4,544
Accounts written off	(34,723)	(30,609)	(25,178)
Bad debt expense	35,894	31,842	25,402
Ending Balance	$7,172	$6,001	$4,768

Property, Plant and Equipment

The Company records property, plant and equipment at cost. Depreciation and amortization are computed on a straight-line basis over the estimated useful lives of the respective assets, which range from five to 40 years for buildings and improvements and from one to fifteen years for other depreciable property and equipment. Costs incurred to develop software for internal use are capitalized and amortized over the estimated useful life of the software, which ranges from five to 10 years.

Gains and losses related to dispositions and retirements are recognized as incurred. Maintenance and repairs are also expensed as incurred; renewals and betterments are capitalized. Depreciation expense for property, plant and equipment is included in operating expenses in the accompanying consolidated statements of earnings and was $53.3 million, $53.1 million and $45.2 million during the years ended December 31, 2013, 2012 and 2011, respectively. Amortization of previously capitalized software development costs, which is a component of depreciation expense for property, plant and equipment, was $3.3 million, $2.6 million and $1.5 million during the years ended December 31, 2013, 2012 and 2011, respectively.

The Company assesses its long-lived assets other than goodwill for impairment whenever facts and circumstances indicate that the carrying amount may not be fully recoverable. When it is determined that the carrying values of the assets are not recoverable, the Company compares the carrying values of the assets to their fair values as estimated using discounted expected future cash flows, market values or replacement values for similar assets. The amount by which the carrying value exceeds the fair value of the asset, if any, is recognized as an impairment loss.

Assets Held for Sale

Certain properties, primarily consisting of parcels of land and commercial buildings, met the held for sale classification criteria at December 31, 2013 and 2012. After adjustment to fair value, the $15.8 million and $11.1 million carrying value of these properties has been classified as assets held for sale in the consolidated balance sheets as of December 31, 2013 and 2012, respectively. The Company estimated the fair values of these properties using market values for similar properties and these properties are considered Level 2 assets as defined in ASC Topic 820, Fair Value Measurements.

The Company recorded impairment charges of $3.8 million, $1.1 million and $453,000 in 2013, 2012 and 2011, respectively. Such impairment charges related primarily to the impairment of various land outparcels and buildings included in the Sales and Lease Ownership segment that the Company decided not to utilize for future expansion and are generally included in other operating expense (income), net within the consolidated statements of earnings. Impairment charges for the year ended December 31, 2013 included a $766,000 write-down of the net assets of the

RIMCO operating segment in connection with the Company's decision to sell the 27 Company-operated RIMCO stores and has been included in the results of the Other segment. Gains and losses on the disposal of assets held for sale amounted to net gains of $1,247,000 in 2012 and were not significant in 2013 and 2011.

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As of December 31, 2013, $9.7 million of assets held for sale are included in the RIMCO segment (principally consisting of $7.2 million of lease merchandise and $2.5 million of property, plant and equipment) and $6.2 million of assets held for sale are included in the Other segment.

Goodwill

Goodwill represents the excess of the purchase price paid over the fair value of the identifiable net tangible and intangible assets acquired in connection with business acquisitions. Impairment occurs when the carrying value of goodwill is not recoverable from future cash flows. The Company performs an assessment of goodwill for impairment at the reporting unit level annually as of September 30 and when events or circumstances indicate that impairment may have occurred. Factors which could necessitate an interim impairment assessment include a sustained decline in the Company's stock price, prolonged negative industry or economic trends and significant underperformance relative to historical or projected future operating results.

The Company has deemed its operating segments to be reporting units due to the fact that operations (stores) included in each operating segment have similar economic characteristics. As of December 31, 2013, the Company had five operating segments and reporting units: Sales and Lease Ownership, HomeSmart, RIMCO, Franchise and Manufacturing. As of December 31, 2013, the Company's Sales and Lease Ownership and HomeSmart reporting units were the only reporting units with assigned goodwill balances. The following is a summary of the Company's goodwill by reporting unit at December 31:

(In Thousands)	2013	2012
Sales and Lease Ownership	$224,523	$219,547
HomeSmart	14,658	14,648
Total	$239,181	$234,195

The goodwill impairment test consists of a two-step process, if necessary. The first step is to compare the fair value of the reporting unit to its carrying value, including goodwill. The Company uses a combination of valuation techniques to determine the fair value of its reporting units, including a multiple of gross revenue approach and discounted cash flow models that use assumptions consistent with those we believe hypothetical marketplace participants would use. The results of the market multiple and discounted cash flow models are evenly weighted in determining reporting unit fair value.

If the carrying value of the reporting unit exceeds the fair value, a second step is performed in order to determine the amount of impairment loss, if any. The second step compares the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit's goodwill exceeds its implied fair value, an impairment charge is recognized in an amount equal to that excess.

During the performance of the annual assessment of goodwill for impairment in the 2013, 2012 and 2011 fiscal years, the Company did not identify any reporting units that were not substantially in excess of their carrying values, other than the HomeSmart division for which locations were recently acquired. While no impairment was noted in our impairment test as of September 30, 2013, if profitability is delayed as a result of the significant start-up expenses associated with the HomeSmart stores, there could be a change in the valuation of the HomeSmart reporting unit that may result in the recognition of an impairment loss in future periods.

No new indications of impairment existed during the fourth quarter of 2013. As a result, no impairment testing was updated as of December 31, 2013.

Other Intangibles

Other intangibles represent the value of customer relationships, non-compete agreements and franchise development rights acquired in connection with business acquisitions and are recorded at fair value as determined by the Company. The customer relationship intangible asset is amortized on a straight-line basis over a two-year estimated useful life. The non-compete intangible asset is amortized on a straight-line basis over a three-year useful life. Acquired franchise development rights are amortized on a straight-line basis over the unexpired life of the franchisee's ten year area development agreement.

Insurance Reserves

Estimated insurance reserves are accrued primarily for group health, general liability, automobile liability and workers compensation benefits provided to the Company's employees. Estimates for these insurance reserves are made based on actual reported but unpaid claims and actuarial analyses of the projected claims run off for both reported and incurred but not reported claims.

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Asset Retirement Obligations

The Company accrues for asset retirement obligations, which relate to expected costs to remove exterior signage, in the period in which the obligations are incurred. These costs are accrued at estimated fair value. When the related liability is initially recorded, the Company capitalizes the cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its settlement value and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, the Company recognizes a gain or loss for any differences between the settlement amount and the liability recorded. Asset retirement obligations amounted to approximately $2.4 million and $2.3 million as of December 31, 2013 and 2012, respectively.

Derivative Financial Instruments

The Company utilizes derivative financial instruments, from time to time, to mitigate its exposure to certain market risks associated with its ongoing operations for a portion of the year. The primary risk it seeks to manage through the use of derivative financial instruments is commodity price risk, including the risk of increases in the market price of diesel fuel used in the Company's delivery vehicles. All derivative financial instruments are recorded at fair value on the consolidated balance sheets. The Company does not use derivative financial instruments for trading or speculative purposes. The Company is exposed to counterparty credit risk on all its derivative financial instruments. The counterparties to these contracts are high credit quality commercial banks, which the Company believes largely minimizes the risk of counterparty default. The Company did not hold any derivative financial instruments as of December 31, 2013 or 2012.

Fair Value Measurement

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. To increase the comparability of fair value measures, the following hierarchy prioritizes the inputs to valuation methodologies used to measure fair value:

Level 1—Valuations based on quoted prices for identical assets and liabilities in active markets.

Level 2—Valuations based on observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3—Valuations based on unobservable inputs reflecting our own assumptions, consistent with reasonably available assumptions made by other market participants. These valuations require significant judgment.

The Company measures assets held for sale at fair value on a nonrecurring basis and records impairment charges when they are deemed to be impaired. The Company maintains certain financial assets and liabilities, including investments and fixed-rate long term debt, that are not measured at fair value but for which fair value is disclosed.

The fair values of the Company's other current financial assets and liabilities, including cash and cash equivalents, accounts receivable and accounts payable, approximate their carrying values due to their short-term nature.

Foreign Currency

The financial statements of international subsidiaries are translated to U.S. dollars using month-end rates of exchange for assets and liabilities, and average rates of exchange for revenues, costs and expenses. Translation gains and losses of international subsidiaries are recorded in accumulated other comprehensive income as a component of shareholders' equity. Foreign currency transaction gains and losses are recorded as a component of other non-operating income (expense), net in the consolidated statements of earnings and amounted to losses of approximately $1.0 million and $465,000 during 2013 and 2011, respectively, and gains of $2.0 million during 2012.

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Recent Accounting Pronouncements

In February 2013, the FASB issued Accounting Standards Update 2013-2, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (“ASU 2013-2”). ASU 2013-2 requires preparers to report, in one place, information about reclassifications out of accumulated other comprehensive income (“AOCI”). ASU 2013-2 also requires companies to report changes in AOCI balances. For significant items reclassified out of AOCI to net income in their entirety in the same reporting period, reporting (either on the face of the statement where net income is presented or in the notes) is required about the effect of the reclassifications on the respective line items in the statement where net income is presented. For items that are not reclassified to net income in their entirety in the same reporting period, a cross reference to other disclosures currently required under US GAAP is required in the notes. The above information must be presented in one place (parenthetically on the face of the financial statements by income statement line item or in a note). ASU 2013-2 was effective for the Company beginning in 2013. The adoption of ASU 2013-2 did not have a material effect on the Company's consolidated financial statements.

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NOTE 2: ACQUISITIONS AND DISPOSITIONS

Acquisitions

The following table summarizes the Company's acquisitions of lease contracts, merchandise and the related assets of sales and lease ownership stores, none of which was individually material to the Company's consolidated financial statements, during the years ended December 31:

(In Thousands, except for store data)	2013	2012	2011
Number of stores acquired, net	10	22	52
Aggregate purchase price (primarily cash consideration)	$10,898	$31,617	$41,425
Purchase price allocation:			
Lease Merchandise	4,016	11,936	13,385
Property, Plant and Equipment	467	739	500
Other Current Assets and Current Liabilities	(228)	38	34
Identifiable Intangible Assets[1]:			
Customer Relationships	557	1,725	2,675
Non-Compete Agreements	405	1,201	1,688
Acquired Franchise Development Rights	252	764	255
Goodwill[2]	5,429	15,214	22,888

[1] The weighted-average amortization period for the Company's acquired intangible assets was 2.9 years, 3.1 years and 2.6 years in 2013, 2012 and 2011, respectively. The weighted-average amortization period by major intangible asset class for acquisitions completed during 2013, 2012 and 2011 was 2 years for customer relationships, 3 years for non-compete agreements and a range of 4.9 years to 6.9 years for acquired franchise development rights.

[2] Goodwill recognized from acquisitions primarily relates to the future strategic benefits expected to be realized upon integrating the business. All goodwill resulting from the Company's 2013, 2012 and 2011 acquisitions is expected to be deductible for tax purposes.

Acquisitions have been accounted for as business combinations, and the results of operations of the acquired businesses are included in the Company's results of operations from their dates of acquisition. The effect of these acquisitions on the 2013, 2012 and 2011 consolidated financial statements was not significant. The purchase price allocations related to current year acquisitions are tentative and preliminary.

Dispositions

The Company periodically sells sales and lease ownership stores to franchisees and third-party operators. The Company sold two, three and 25 of its Aaron's Sales and Lease Ownership stores in 2013, 2012 and 2011, respectively. The effect of these sales on the consolidated financial statements was not significant.

The Company began ceasing the operations of the Aaron's Office Furniture division in June of 2010. The Company closed 14 of its Aaron's Office Furniture stores during 2010 and sold the remaining store in August 2012. There were no significant charges related to the closure of this division in 2013, 2012 or 2011.

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NOTE 3: GOODWILL AND INTANGIBLE ASSETS

Goodwill

The following table provides information related to the carrying value of the Company's goodwill by operating segment:

(In Thousands)	Sales and Lease Ownership	HomeSmart	Total
Balance at January 1, 2012	$ 205,509	$13,833	$219,342
Additions	14,399	815	15,214
Disposals	(361)	—	(361)
Balance at December 31, 2012	219,547	14,648	234,195
Additions	5,429	—	5,429
Disposals	(499)	—	(499)
Purchase Price Adjustments	46	10	56
Balance at December 31, 2013	$ 224,523	$14,658	$239,181

Intangible Assets

The following is a summary of the Company's identifiable intangible assets by category at December 31:

	2013			2012		
(In Thousands)	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Customer Relationships	$2,282	$ (1,463)	$819	$4,377	$ (2,170)	$2,207
Non-Compete Agreements	3,265	(2,001)	1,264	3,408	(1,471)	1,937
Acquired Franchise Development Rights	3,529	(2,077)	1,452	4,566	(2,684)	1,882
Total	$9,076	$ (5,541)	$3,535	$12,351	$ (6,325)	$6,026

Total amortization expense of intangible assets, included in operating expenses in the accompanying consolidated statements of earnings, was $3.7 million, $3.7 million and $2.3 million during the years ended December 31, 2013, 2012 and 2011, respectively. As of December 31, 2013, estimated future amortization expense for the next five years related to identifiable intangible assets is as follows:

(In Thousands)	
2014	$1,983
2015	793
2016	367
2017	201
2018	98

NOTE 4: FAIR VALUE MEASUREMENT

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table summarizes financial liabilities measured at fair value on a recurring basis:

	December 31, 2013			December 31, 2012		
(In Thousands)	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Deferred Compensation Liability	$—	$(12,557)	$—	$—	$(9,518)	$—

The Company maintains a deferred compensation plan as described in Note 14 to these consolidated financial statements. The liability representing benefits accrued for plan participants is valued at the quoted market prices of the participants' investment elections, which consist of equity and debt "mirror" funds. As such, the Company has classified the deferred compensation liability as a Level 2 liability.

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Non-Financial Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

The following table summarizes non-financial assets measured at fair value on a nonrecurring basis:

	December 31, 2013			December 31, 2012		
(In Thousands)	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets Held for Sale	$—	$15,840	$—	$—	$11,104	$—

Assets held for sale includes real estate properties that consist mostly of parcels of land and commercial buildings, as well as the net assets of the RIMCO operating segment (principally consisting of lease merchandise, office furniture and leasehold improvements) in connection with the Company's decision to sell the 27 Company-operated RIMCO stores. The highest and best use of these assets is as real estate land parcels for development or real estate properties for use or lease; however, the Company has chosen not to develop or use these properties. In accordance with ASC Topic 360, Property, Plant and Equipment, assets held for sale are written down to fair value, and the adjustment is recorded in other operating expense (income), net. The Company estimated the fair values of real estate properties using the market values for similar properties. The impairment loss recorded for the RIMCO disposal group was based on our expectations of a sale price as compared to our estimation of the net assets to be sold at closing.

Certain Financial Assets and Liabilities Not Measured at Fair Value

The following table summarizes the fair value of assets (liabilities) that are not measured at fair value in the consolidated balance sheets, but for which the fair value is disclosed:

	December 31, 2013			December 31, 2012		
(In Thousands)	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Corporate Bonds [1]	$—	$91,785	$—	$—	$67,470	$—
Perfect Home Notes [2]	—	—	20,661	—	—	18,449
Fixed-Rate Long Term Debt [3]	—	(130,687)	—	—	(127,261)	—

[1] The fair value of corporate bonds is determined through the use of model-based valuation techniques for which all significant assumptions are observable in the market.

[2] The Perfect Home notes were initially valued at cost. The Company periodically reviews the valuation utilizing company-specific transactions or changes in Perfect Home's financial performance to determine if fair value adjustments are necessary.

[3] The fair value of fixed-rate long term debt is estimated using the present value of underlying cash flows discounted at a current market yield for similar instruments. The carrying value of fixed-rate long term debt was $125.0 million at December 31, 2013 and December 31, 2012.

Held-to-Maturity Securities

The Company classifies its investments in debt securities as held-to-maturity securities based on its intent and ability to hold these securities to maturity. Accordingly, the debt securities, which mature at various dates during 2014 to 2015, are recorded at amortized cost in the consolidated balance sheets. At December 31, 2013 and 2012, investments classified as held-to-maturity securities consisted of the following:

		Gross Unrealized		
(In Thousands)	Amortized Cost	Gains	Losses	Fair Value
2013				
Corporate Bonds	$ 91,730	$98	$(43)	$91,785
Perfect Home Notes	20,661	—	—	20,661
Total	$ 112,391	$98	$(43)	$112,446
2012				
Corporate Bonds	$ 67,412	$99	$(41)	$67,470
Perfect Home Notes	18,449	—	—	18,449
Total	$ 85,861	$99	$(41)	$85,919

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The amortized cost and fair value of held-to-maturity securities by contractual maturity as of December 31, 2013 are as follows:

(In Thousands)	Amortized Cost	Fair Value
Due in one year or less	$ 55,250	$55,284
Due in years one through two	57,141	57,162
Total	$ 112,391	$112,446

Information pertaining to held-to-maturity securities with gross unrealized losses is as follows.

	December 31, 2013		December 31, 2012	
(In Thousands)	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Corporate Bonds	$31,453	$(43)	$22,785	$ (41)

The unrealized losses relate principally to the increases in short-term market interest rates that occurred since the securities were purchased. As of December 31, 2013, 18 of the 48 securities are in an unrealized loss position and at December 31, 2012, 16 of the 38 securities were in an unrealized loss position. The fair value is expected to recover as the securities approach their maturities or if market yields for such investments decline. In analyzing an issuer's financial condition, management considers whether downgrades by bond rating agencies have occurred. The Company has the intent and ability to hold the investments until their amortized cost basis is recovered on the maturity date. As a result of management's analysis and review, no declines are deemed to be other than temporary.

The Company has estimated that the carrying value of its Perfect Home notes approximates fair value and, therefore, no impairment is considered to have occurred as of December 31, 2013. While no impairment was noted during 2013, if profitability is delayed as a result of the significant start-up expenses associated with Perfect Home, there could be a change in the valuation of the Perfect Home notes that may result in the recognition of an impairment loss in future periods.

NOTE 5: PROPERTY, PLANT AND EQUIPMENT

Following is a summary of the Company's property, plant, and equipment at December 31:

(In Thousands)	2013	2012
Land	$26,021	$25,285
Buildings and Improvements	84,520	81,773
Leasehold Improvements and Signs	120,702	120,883
Fixtures and Equipment[1]	172,483	152,436
Assets Under Capital Leases:		
with Related Parties	10,574	8,158
with Unrelated Parties	10,550	10,564
Construction in Progress	4,347	5,414
	429,197	404,513
Less: Accumulated Depreciation and Amortization	(197,904)	(173,915)
	$231,293	$230,598

[1] Includes internal-use software development costs of $36.3 million and $22.6 million as of December 31, 2013 and 2012, respectively. Accumulated amortization of internal-use software development costs amounted to $9.5 million and $6.6 million as of December 31, 2013 and 2012, respectively.

Amortization expense on assets recorded under capital leases is included in operating expenses and was $1.7 million, $1.2 million and $1.2 million in 2013, 2012 and 2011, respectively. Capital leases consist of buildings and improvements. Assets under capital leases with related parties included $5.8 million and $4.8 million in accumulated depreciation and amortization as of December 31, 2013 and 2012, respectively. Assets under capital leases with unrelated parties included $5.1 million and $4.4 million in accumulated depreciation and amortization as of December 31, 2013 and 2012, respectively.

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NOTE 6: CREDIT FACILITIES

Following is a summary of the Company's credit facilities at December 31:

(In Thousands)	2013	2012
Senior Unsecured Notes	$125,000	$125,000
Capital Lease Obligation:		
with Related Parties	7,412	6,122
with Unrelated Parties	7,042	7,156
Other Debt	3,250	3,250
	$142,704	$141,528

Bank Debt

On October 8, 2013, the Company entered into the fifth amendment to its revolving credit agreement dated May 23, 2008, as previously amended. The amendment changes the "Restricted Payments" negative covenant, which imposes certain restrictions on the amount of payments that can be made in respect of dividends, distributions, redemptions and stock repurchases paid in cash, to make such covenant less restrictive.

The Company's revolving credit agreement, which expires December 13, 2017, is with several banks and provides for unsecured borrowings up to $140 million (including a letter of credit and swingline loan subfacility). Amounts borrowed bear interest at the lower of the lender's prime rate or one-month LIBOR plus a margin ranging from 1.0% to 1.5% as determined by the Company's ratio of total debt to EBITDA. At December 31, 2013 and 2012, there was a zero balance under the Company's revolving credit agreement. The Company pays a commitment fee on unused balances, which ranges from 0.15% to 0.30% as determined by the Company's ratio of total debt to EBITDA.

The revolving credit agreement, senior unsecured notes discussed below and franchise loan program discussed in Note 8 contain financial covenants which, among other things, prohibit the Company from exceeding certain debt to EBITDA levels and require the maintenance of minimum fixed charge coverage ratios. If the Company fails to comply with these covenants, the Company will be in default under these agreements, and all amounts would become due immediately. Under the Company's revolving credit agreement, senior unsecured notes and franchise loan program, the Company may pay cash dividends in any year so long as, after giving pro forma effect to the dividend payment, the Company maintains compliance with its financial covenants and no event of default has occurred or would result from the payment.

At December 31, 2013, the Company was in compliance with all covenants.

Senior Unsecured Notes

On October 8, 2013, the Company entered into Amendment No. 2 to a note purchase agreement dated as of July 5, 2011 with several insurance companies. Pursuant to the note purchase agreement, the Company and certain of its subsidiaries as co-obligors, issued $125.0 million in senior unsecured notes to the purchasers in a private placement. The notes bear interest at the rate of 3.75% per year and mature on April 27, 2018. Payments of interest are due quarterly, commencing July 27, 2011, with principal payments of $25.0 million each due annually commencing April 27, 2014.

The amendment revises the note purchase agreement to, among other things, (i) remove the "Minimum Consolidated Net Worth" financial covenant which previously required that the Company maintain a certain minimum consolidated net worth and (ii) change the "Restricted Payments" negative covenant, which imposes certain restrictions on the amount of payments that can be made in respect of dividends, distributions, redemptions and stock repurchases paid in cash, to make such covenant less restrictive. The Company remains subject to other financial covenants under the note purchase agreement, including maintaining a minimum ratio of debt to earnings before interest, taxes, depreciation, and amortization and a minimum fixed charge coverage ratio.

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Capital Leases with Related Parties

As of December 31, 2013, the Company had 19 capital leases with a limited liability company ("LLC") controlled by a group of executives, including the Company's former Chairman. In October and November 2004, the Company sold 11 properties, including leasehold improvements, to the LLC. The LLC obtained borrowings collateralized by the land and buildings totaling $6.8 million. The Company occupies the land and buildings collateralizing the borrowings under a 15-year term lease, with a five-year renewal at the Company's option, at an aggregate annual rental of $716,000. The transaction has been accounted for as a financing in the accompanying consolidated financial statements. The rate of interest implicit in the leases is approximately 9.7%. Accordingly, the land and buildings, associated depreciation expense and lease obligations are recorded in the Company's consolidated financial statements. No gain or loss was recognized in this transaction.

In December 2002, the Company sold ten properties, including leasehold improvements, to the LLC. The LLC obtained borrowings collateralized by the land and buildings totaling $5.0 million. The Company occupies the land and buildings collateralizing the borrowings under a 15-year term lease at an aggregate annual rental of approximately $1,227,000. The transaction has been accounted for as a financing in the accompanying consolidated financial statements. The rate of interest implicit in the leases is approximately 10.1%. Accordingly, the land and buildings, associated depreciation expense and lease obligations are recorded in the Company's consolidated financial statements. No gain or loss was recognized in this transaction.

Sale-leasebacks

The Company finances a portion of store expansion through sale-leaseback transactions. The properties are generally sold at net book value and the resulting leases qualify and are accounted for as operating leases. The Company does not have any retained or contingent interests in the stores nor does the Company provide any guarantees, other than a corporate level guarantee of lease payments, in connection with the sale-leasebacks.

Other Debt

Other debt at December 31, 2013 and 2012 includes $3.3 million of industrial development corporation revenue bonds. The weighted-average interest rate on the outstanding bonds was .25% and .35% as of December 31, 2013 and 2012, respectively. No principal payments are due on the bonds until maturity in 2015.

Future maturities under the Company's long-term debt and capital lease obligations are as follows:

(In Thousands)	
2014	$27,529
2015	31,015
2016	27,740
2017	27,659
2018	26,355
Thereafter	2,406
	$142,704

NOTE 7: INCOME TAXES

Following is a summary of the Company's income tax expense for the years ended December 31:

(In Thousands)	2013	2012	2011
Current Income Tax Expense:			
Federal	$91,664	$116,234	$—
State	9,393	10,819	9,797
	101,057	127,053	9,797
Deferred Income Tax Expense (Benefit):			
Federal	(35,941)	(23,035)	62,015
State	(822)	(206)	(2,202)
	(36,763)	(23,241)	59,813
	$64,294	$103,812	$69,610

At December 31, 2011, the Company had a federal net operating loss ("NOL") carryforward of approximately $31.2 million available to offset future taxable income. The entire NOL carryforward was absorbed during 2012.

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As a result of the bonus depreciation provisions in the Small Business Jobs Act of 2010 and the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, the Company paid more than anticipated for the 2010 federal tax liability. The 2010 acts provided an estimated tax deferral of approximately $127.0 million. The Company filed for a refund of overpaid federal tax of approximately $80.9 million in January 2011 and received that refund in February 2011.

Significant components of the Company's deferred income tax liabilities and assets at December 31 are as follows:

(In Thousands)	2013	2012
Deferred Tax Liabilities:		
Lease Merchandise and Property, Plant and Equipment	$249,192	$279,926
Goodwill & Other Intangibles	34,512	30,754
Other, Net	2,782	3,260
Total Deferred Tax Liabilities	286,486	313,940
Deferred Tax Assets:		
Accrued Liabilities	36,778	25,365
Advance Payments	15,400	15,834
Other, Net	8,032	9,677
Total Deferred Tax Assets	60,210	50,876
Less Valuation Allowance	(682)	(657)
Net Deferred Tax Liabilities	$226,958	$263,721

The Company's effective tax rate differs from the statutory United States Federal income tax rate for the years ended December 31 as follows:

	2013	2012	2011
Statutory Rate	35.0 %	35.0 %	35.0 %
Increases in United States Federal Taxes Resulting From:			
State Income Taxes, Net of Federal Income Tax Benefit	3.1	2.5	2.7
Federal Tax Credits	(1.7)	(.1)	(.3)
Other, Net	(1.6)	.1	.6
Effective Tax Rate	34.8 %	37.5 %	38.0 %

The Company files a federal consolidated income tax return in the United States and the separate legal entities file in various states and foreign jurisdictions. With few exceptions, the Company is no longer subject to federal, state and local tax examinations by tax authorities for years before 2010.

The following table summarizes the activity related to the Company's uncertain tax positions:

(In Thousands)	2013	2012	2011
Balance at January 1,	$1,258	$1,412	$1,315
Additions based on tax positions related to the current year	454	178	178
Additions for tax positions of prior years	423	83	22
Prior year reductions	(5)	(315)	(13)
Statute expirations	(85)	(83)	(90)
Settlements	(85)	(17)	—
Balance at December 31,	$1,960	$1,258	$1,412

As of December 31, 2013 and 2012, the amount of uncertain tax benefits that, if recognized, would affect the effective tax rate is $1.5 million and $1.0 million, respectively, including interest and penalties. During the years ended December 31, 2013 and December 31, 2011, the Company recognized interest and penalties of $76,000 and $41,000. During the year ended December 31, 2012, the Company recognized a net benefit of $126,000 related to interest and penalties. The Company had $278,000 and $234,000 of accrued interest and penalties at December 31, 2013 and 2012, respectively. The Company recognizes potential interest and penalties related to uncertain tax benefits as a component of income tax expense.

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NOTE 8: COMMITMENTS AND CONTINGENCIES

Leases

The Company leases warehouse and retail store space for most of its operations under operating leases expiring at various times through 2029. The Company also leases certain properties under capital leases that are more fully described in Note 6 to these consolidated financial statements. Most of the leases contain renewal options for additional periods ranging from one to 20 years or provide for options to purchase the related property at predetermined purchase prices that do not represent bargain purchase options. In addition, certain properties occupied under operating leases contain normal purchase options. Leasehold improvements related to these leases are generally amortized over periods that do not exceed the lesser of the lease term or 15 years. While a majority of leases do not require escalating payments, for the leases which do contain such provisions, the Company records the related lease expense on a straight-line basis over the lease term. The Company also leases transportation and computer equipment under operating leases expiring during the next five years. Management expects that most leases will be renewed or replaced by other leases in the normal course of business.

Future minimum lease payments required under operating leases that have initial or remaining non-cancelable terms in excess of one year as of December 31, 2013 are as follows:

(In Thousands)	
2014	$113,067
2015	96,508
2016	75,024
2017	57,160
2018	43,225
Thereafter	143,583
	$528,567

Rental expense was $110.0 million in 2013, $102.0 million in 2012 and $93.6 million in 2011. The amount of sublease income was $2.6 million in 2013, $3.1 million in 2012 and $3.1 million in 2011. The Company has anticipated future sublease rental income of $3.5 million in 2014, $3.0 million in 2015, $2.5 million in 2016, $2.2 million in 2017, $2.1 million in 2018 and $5.6 million thereafter through 2026. Rental expense and sublease income are included in operating expenses.

Guarantees

The Company has guaranteed certain debt obligations of some of the franchisees under a franchise loan program with several banks. In the event these franchisees are unable to meet their debt service payments or otherwise experience an event of default, the Company would be unconditionally liable for the outstanding balance of the franchisees' debt obligations under the franchisee loan program, which would be due in full within 90 days of the event of default. At December 31, 2013, the maximum amount that the Company would be obligated to repay in the event franchisees defaulted was $105.0 million. The Company has recourse rights to the assets securing the debt obligations, which consist primarily of lease merchandise and fixed assets. As a result, the Company has never incurred, nor does management expect to incur, any significant losses under these guarantees. The carrying amount of the franchise-related borrowings guarantee, which is included in accounts payable and accrued expenses in the consolidated balance sheet, is approximately $2.5 million as of December 31, 2013.

On December 17, 2013, the Company entered into a seventh amendment to its second amended and restated loan facility and guaranty, dated June 18, 2010, as amended, and the Company entered into a sixth amendment as of October 8, 2013. The amendments to the franchise loan facility extended the maturity date of the franchise loan facility until December 11, 2014 and changed the “Restricted Payments” negative covenant, which imposes certain restrictions on the amount of payments that can be made in respect of dividends, distributions, redemptions and stock repurchases paid in cash, to make such covenant less restrictive.

The maximum facility commitment amount under the franchise loan program is $200.0 million, including a Canadian subfacility commitment amount for loans to franchisees that operate stores in Canada (other than in the Province of Quebec) of Cdn $50 million. We remain subject to the financial covenants under the franchise loan facility.

Legal Proceedings

From time to time, the Company is party to various legal and regulatory proceedings arising in the ordinary course of business.

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Some of the proceedings to which we are currently a party are described below. We believe we have meritorious defenses to all of the claims described below, and intend to vigorously defend against the claims. However, these proceedings are still developing and due to the inherent uncertainty in litigation, regulatory and similar adversarial proceedings, there can be no guarantee that we will ultimately be successful in these proceedings, or in others to which we are currently a party. Substantial losses from these proceedings or the costs of defending them could have a material adverse impact upon our business, financial position and results of operations.

The Company establishes an accrued liability for legal and regulatory proceedings when it determines that a loss is both probable and the amount of the loss can be reasonably estimated. The Company continually monitors its litigation and regulatory exposure, and reviews the adequacy of its legal and regulatory reserves on a quarterly basis in accordance with applicable accounting rules. The amount of any loss ultimately incurred in relation to matters for which an accrual has been established may be higher or lower than the amounts accrued for such matters.

At December 31, 2013, the Company had accrued $33.3 million for pending legal and regulatory matters for which it believes losses are probable, which is our best estimate of our exposure to loss, and mostly relates to the regulatory investigation by the California Attorney General described below. The Company estimates that the aggregate range of possible loss in excess of accrued liabilities for such probable loss contingencies is between $0 and $4.6 million.

At December 31, 2013, the Company estimated that the aggregate range of loss for all material pending legal and regulatory proceedings for which a loss is reasonably possible, but less likely than probable (i.e., excluding the contingencies described in the preceding paragraph), is between $50,000 to $8.2 million. Those matters for which a reasonable estimate is not possible are not included within estimated ranges and, therefore, the estimated ranges do not represent the Company's maximum loss exposure. Our estimates as to legal and regulatory accruals, as to aggregate probable loss amounts and as to reasonably possible loss amounts, are all subject to the uncertainties and variables described above.

Labor and Employment

In Kunstmann et al v. Aaron Rents, Inc., filed with the United States District Court, Northern District of Alabama (Case No.: 2:08-CV-01969-KOB-JEO) on October 22, 2008, plaintiffs alleged that the Company improperly classified store general managers as exempt from the overtime provisions of the Fair Labor Standards Act (“FLSA”). The case was conditionally certified as an FLSA collective action on January 25, 2010, and it now includes 227 individuals, nearly all of whom terminated from the general manager position more than two years ago. Plaintiffs seek to recover unpaid overtime compensation and other damages. On October 4, 2012, the Court denied the Company's motion for summary judgment as to the claims of Kunstmann, the named plaintiff. On January 23, 2013, the Court denied the Company's motion to decertify the class. The Company has since filed two additional motions for summary judgment, including one that seeks summary judgment in the entirety on all class members' claims, or alternatively, on matters that will reduce the size of the class or exposure arising from the class claims. Briefing on these motions began in July 2013.

The matter of Kurtis Jewell v. Aaron's, Inc. was originally filed in the United States District Court, Northern District of Ohio, Eastern Division on October 27, 2011 and was transferred on February 23, 2012 to the United States District Court for the Northern District of Georgia (Civil No.:1:12-CV-00563-AT). Plaintiff, on behalf of himself and all other non-exempt employees who worked in Company stores, alleges that the Company violated the FLSA when it automatically deducted 30 minutes from employees' time for meal breaks on days when plaintiffs allegedly did not take their meal breaks. Plaintiff claims he and other employees actually worked through meal breaks or were interrupted during the course of their meal breaks and asked to perform work. As a result of the automatic deduction, plaintiff alleges that the Company failed to account for all of his working hours when it calculated overtime, and consequently underpaid him. Plaintiffs seek to recover unpaid overtime compensation and other damages for all similarly situated employees nationwide for the applicable time period. On June 28, 2012, the Court issued an order granting conditional certification of a class consisting of all hourly store employees from June 28, 2009 to the present. The class size is approximately 1,788 opt-in plaintiffs, which is less than seven percent of the potential class members. The parties are engaging in discovery, including depositions of court-designated class members. Discovery is expected to continue until April 2014.

In Sowell, et al. v. Aaron's, Inc., United States District Court for the Northern District of Georgia (Civil No.:1:12-CV-03867-CAP-ECS), two former Company associates filed separate lawsuits on November 5, 2012;

Elizabeth Cook filed in Fulton County Georgia State Court and Brittany Sowell filed in the U.S. District Court for the Northern District of Georgia. Plaintiff Sowell then filed a First Amended Complaint in the U.S. District Court of the Northern District of Georgia on November 28, 2012. Thereafter, Plaintiff Sowell filed a Second Amended Complaint on December 21, 2012, which included Cook's claims and consolidated the cases. The case settled on October 22, 2013, and the settlement payment was substantially covered by insurance.

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Consumer

In Margaret Korrow, et al. v. Aaron's, Inc., originally filed in the Superior Court of New Jersey, Middlesex County, Law Division on October 26, 2010, plaintiff filed suit on behalf of herself and others similarly situated alleging that the Company is liable in damages to plaintiff and each class member because the Company's lease agreements issued after March 16, 2006 purportedly violated certain New Jersey state consumer statutes. Plaintiff's complaint seeks treble damages under the New Jersey Consumer Fraud Act, and statutory penalty damages of $100 per violation of all contracts issued in New Jersey, and also claim that there are multiple violations per contract. The Company removed the lawsuit to the United States District Court for the District of New Jersey on December 6, 2010 (Civil Action No.: 10-06317(JAP)(LHG)). Plaintiff on behalf of herself and others similarly situated seeks equitable relief, statutory and treble damages, pre- and post-judgment interest and attorneys' fees. Discovery on this matter is closed. On July 31, 2013, the Court certified a class comprising all persons who entered into a rent-to-own contract with the Company in New Jersey from March 16, 2006 through March 31, 2011. In August 2013, the Court of Appeals denied the Company's request for an interlocutory appeal of the class certification issue. The Company filed a motion to add counterclaims against all newly certified class members who may owe legitimate fees or damages to the Company or who failed to return merchandise prior to obtaining ownership. That motion is pending.

Privacy and Related Matters

In Crystal and Brian Byrd v. Aaron's, Inc., Aspen Way Enterprises, Inc., John Does (1-100) Aaron's Franchisees and Designerware, LLC, filed on May 16, 2011, in the United States District Court, Western District of Pennsylvania (Case No. 1:11-CV-00101-SPB), plaintiffs alleged that the Company and its independently owned and operated franchisee Aspen Way Enterprises ("Aspen Way") knowingly violated plaintiffs' privacy in violation of the Electronic Communications Privacy Act and the Computer Fraud Abuse Act and sought certification of a putative nationwide class. Plaintiffs based these claims on Aspen Way's use of a software program called "PC Rental Agent." The District Court dismissed the Company from the lawsuit on March 20, 2012. On September 14, 2012, plaintiffs filed a second amended complaint against the Company and its franchisee Aspen Way, asserting claims for violation of the Electronic Communications Privacy Act and common law invasion of privacy by intrusion upon seclusion. Plaintiffs also asserted certain vicarious liability claims against the Company based on Aspen Way's alleged conduct. On October 15, 2012, the Company filed a motion to dismiss the amended complaint, and on February 27, 2013, plaintiffs filed a motion for leave of the Court to file a third amended complaint against the Company. On May 23, 2013, the Court granted plaintiffs' motion for leave to file a third amended complaint, which asserts the same claims against the Company as the second amended complaint but also adds a request for injunction and names additional independently owned and operated Company franchisees as defendants. Plaintiffs filed the third amended complaint, and the Company has moved to dismiss that complaint on substantially the same grounds as it sought to dismiss plaintiffs' second amended complaint. That motion remains pending. Plaintiffs filed their motion for class certification on July 1, 2013, and the Company's response was filed in August 2013. On January 27, 2014, the Magistrate Judge issued recommendations on pending motions. The Judge recommended that all claims against all franchisees other than Aspen Way Enterprises, LLC be dismissed. The Judge also recommended that claims for invasion of privacy, aiding and abetting, and conspiracy be dismissed against all defendants. Finally, the Judge recommended denial of the Company's motion to dismiss the violation of Electronic Communications Privacy Act claims. In addition, on January 31, 2014, the Magistrate Judge recommended denial of the Plaintiffs' motion to certify the class. These recommendations are subject to objection by either party and will then either be adopted, in whole or in part, by the District Judge, or modified as the District Judge may determine appropriate.

In Michael Winslow and Fonda Winslow v. Sultan Financial Corporation, Aaron's, Inc., John Does (1-10), Aaron's Franchisees and Designerware, LLC, filed on March 5, 2013 in the Los Angeles Superior Court (Case No. BC502304), plaintiffs assert claims against the Company and its independently owned and operated franchisee, Sultan Financial Corporation (as well as certain John Doe franchisees), for unauthorized wiretapping, eavesdropping, electronic stalking, and violation of California's Comprehensive Computer Data Access and Fraud Act and its Unfair Competition Law. Each of these claims arises out of the alleged use of PC Rental Agent software. The plaintiffs are seeking injunctive relief and damages in connection with the allegations of the complaint. Plaintiffs are also seeking certification of a putative California class. Plaintiffs are represented by the same counsel as in the above described

Byrd litigation. In April 2013, the Company timely removed this matter to federal Court. On May 8, 2013, the Company filed a motion to stay this litigation pending resolution of the Byrd litigation, a motion to dismiss for failure to state a claim, and a motion to strike certain allegations in the complaint. The Court subsequently stayed the case. The Company's motions to dismiss and strike certain allegations remain pending.

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In Lomi Price v. Aaron's, Inc. and NW Freedom Corporation, filed on February 27, 2013, in the State Court of Fulton County, Georgia (Case No. 13-EV-016812B), an individual plaintiff asserts claims against the Company and its independently owned and operated franchisee, NW Freedom Corporation, for invasion of privacy/intrusion on seclusion, computer invasion of privacy and infliction of emotional distress. Each of these claims arises out of the alleged use of PC Rental Agent software. The plaintiff is seeking compensatory and punitive damages of not less than $250,000. On April 3, 2013, the Company filed an answer and affirmative defenses. On that same day, the Company also filed a motion to stay the litigation pending resolution of the Byrd litigation, a motion to dismiss for failure to state a claim and a motion to strike certain allegations in the complaint. All three motions remain pending.

Regulatory Investigations

Federal Trade Commission Investigation. The Federal Trade Commission (“FTC”) investigated the Company in connection with the alleged use of PC Rental Agent software by certain independently owned and operated Company franchisees, as noted above under “Privacy and Related Matters,” and the Company's alleged responsibility for that use. On October 22, 2013, the FTC published a proposed consent agreement that would close the investigation. Pursuant to FTC administrative procedure, the consent agreement was subject to public comment through November 21, 2013. The FTC is currently deciding whether to make the proposed consent agreement final.

California Attorney General Investigation. The California Attorney General has been investigating the Company's retail transactional practices, including various leasing and marketing practices, information security and privacy policies and practices related to the alleged use of PC Rental Agent software by certain independently owned and operated Company franchisees. The Company is continuing to cooperate with the investigation, including producing documents for the Attorney General's office and engaging in discussions about a possible resolution of this matter. The Company currently anticipates achieving a comprehensive resolution without litigation.

Pennsylvania Attorney General Investigation. There is a pending, active investigation by the Pennsylvania Attorney General relating to the Company's privacy practices in Pennsylvania. The privacy issues are related to the alleged use of PC Rental Agent software by certain independently owned and operated Company franchisees, and the Company's alleged responsibility for that use. The Company is continuing to cooperate in the investigation.

Other Commitments

At December 31, 2013, the Company had non-cancelable commitments primarily related to certain advertising and marketing programs of $35.4 million. Payments under these commitments are scheduled to be $19.2 million in 2014, $15.5 million in 2015 and $710,000 in 2016.

The Company maintains a 401(k) savings plan for all its full-time employees with at least one year of service and who meet certain eligibility requirements. As of December 31, 2013, the plan allows employees to contribute up to 100% of their annual compensation in accordance with federal contribution limits with 100% matching by the Company on the first 3% of compensation and 50% on the next 2% of compensation for a total of 4% matching compensation. The Company’s expense related to the plan was $3.3 million in 2013, $999,000 in 2012, and $891,000 in 2011.

The Company is a party to various claims and legal proceedings arising in the ordinary course of business. Management regularly assesses the Company’s insurance deductibles, monitors the Company's litigation and regulatory exposure with the Company’s attorneys and evaluates its loss experience. The Company also enters into various contracts in the normal course of business that may subject it to risk of financial loss if counterparties fail to perform their contractual obligations.

NOTE 9: SHAREHOLDERS’ EQUITY

The Company held 17,795,293 shares in its treasury and was authorized to purchase an additional 11,497,373 shares at December 31, 2013. The holders of common stock are entitled to receive dividends and other distributions in cash, stock or property of the Company as and when declared by its Board of Directors out of legally available funds. The Company repurchased 3,502,627 shares of its common stock through an accelerated share repurchase program in 2013 and 1,236,689 shares of its common stock on the open market in 2012.

The Company has 1,000,000 shares of preferred stock authorized. The shares are issuable in series with terms for each series fixed by and such issuance subject to approval by the Board of Directors. As of December 31, 2013, no preferred shares have been issued.

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On October 4, 2013, the Company amended its Amended and Restated Articles of Incorporation to confirm that shares of common stock the Company repurchases from time to time become treasury shares. As permitted by Georgia corporate law, the amendment was adopted by the Board of Directors of the Company without shareholder action.

Accelerated Share Repurchase Program

In December 2013, the Company entered into an accelerated share repurchase program with a third-party financial institution to purchase $125.0 million of the Company’s common stock, as part of its previously announced share repurchase program. The Company paid $125.0 million and received an initial delivery of 3,502,627 shares, estimated to be approximately 80% of the total number of shares to be repurchased under the agreement, which reduced the Company's shares outstanding at December 31, 2013. The value of the initial shares received on the date of purchase was $100.0 million, reflecting a $28.55 price per share, which was recorded as treasury shares. The Company recorded the remaining $25.0 million as a forward contract indexed to its own common stock in additional paid-in capital.

In February 2014, the accelerated share repurchase program was completed and the Company received 1,000,952 additional shares determined using a volume weighted average price of the Company's stock (inclusive of a discount) during the trading period. All amounts classified as additional paid-in capital will be reclassified to treasury shares during the first quarter of 2014 upon settlement.

NOTE 10: STOCK OPTIONS AND RESTRICTED STOCK

The Company grants stock options, restricted stock units and restricted stock awards to certain employees and directors of the Company. Total stock-based compensation expense was $2.3 million, $6.5 million and $8.4 million in 2013, 2012 and 2011, respectively, and was included as a component of operating expenses in the consolidated statements of earnings. Excess tax benefits of $1.4 million, $6.0 million and $1.3 million are included in cash provided by financing activities for the years ended 2013, 2012 and 2011, respectively.

As of December 31, 2013, there was $9.1 million of total unrecognized compensation expense related to non-vested stock-based compensation which is expected to be recognized over a period of 2.3 years.

The aggregate number of shares of common stock that may be issued or transferred under the incentive stock awards plan is 14,597,927 at December 31, 2013.

Stock Options

Under the Company’s stock option plans, options granted to date become exercisable after a period of two to five years and unexercised options lapse ten years after the date of the grant. Options are subject to forfeiture upon termination of service. The Company recognizes compensation cost for awards with graded vesting on a straight-line basis over the requisite service period for each separately vesting portion of the award. The Company determines the fair value of stock options using a Black-Scholes option pricing model that incorporates expected volatility, expected option life, estimated forfeiture rates, risk-free interest rates, and expected dividend yields.

The expected volatility is based on the historical volatility of the Company’s common stock over the most recent period generally commensurate with the expected estimated life of each respective grant. The expected lives of options are based on the Company’s historical option exercise experience. Forfeiture assumptions are based on the Company’s historical forfeiture experience. The Company believes that the historical experience method is the best estimate of future exercise and forfeiture patterns. The risk-free interest rates are determined using the implied yield available for zero-coupon United States government issues with a remaining term equal to the expected life of the grant. The expected dividend yields are based on the approved annual dividend rate in effect and market price of the underlying common stock at the time of grant. No assumption for a future dividend rate increase has been included unless there is an approved plan to increase the dividend in the near term. Shares are issued from the Company’s treasury shares upon share option exercises.

No stock options were granted in 2013, 2012 or 2011.

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The following table summarizes information about stock options outstanding at December 31, 2013:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding December 31, 2013	Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Number Exercisable December 31, 2013	Weighted Average Exercise Price
$10.01-15.00	471,250	4.13	$ 14.15	471,250	$ 14.15
15.01-19.92	215,250	6.11	19.90	57,750	19.83
$10.01-19.92	686,500	4.75	15.95	529,000	14.77

The table below summarizes option activity for the year ended December 31, 2013:

	Options (In Thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in Thousands)	Weighted Average Fair Value
Outstanding at January 1, 2013	1,513	$ 14.81			
Granted	—	—			
Exercised	(728)	13.71			
Forfeited/expired	(98)	15.29			
Outstanding at December 31, 2013	687	15.95	4.75	$ 9,233	$ 7.02
Expected to Vest at December 31, 2013	132	19.92	6.15	1,253	10.67
Exercisable at December 31, 2013	529	14.77	4.33	7,740	5.94

The aggregate intrinsic value of options exercised was $11.0 million, $20.0 million and $5.5 million in 2013, 2012 and 2011, respectively. The total fair value of options vested was $2.7 million, $2.2 million and $2.7 million in 2013, 2012 and 2011, respectively. Income tax benefits resulting from stock option exercises totaled $4.2 million, $8.4 million, and $2.1 million in 2013, 2012 and 2011, respectively.

Restricted Stock

Shares of restricted stock or restricted stock units (collectively, “restricted stock”) may be granted to employees and directors and typically vest over approximately two to five year periods. Restricted stock grants may be subject to one or more objective employment, performance or other forfeiture conditions as established at the time of grant. Restricted shares granted with performance conditions are typically granted to eligible participants upon achievement of certain pre-tax profit and revenue levels by the employees' operating units or the overall Company. Plan participants include certain vice presidents, director level employees and other key personnel in the Company’s home office, divisional vice presidents and regional managers.

In addition, the Company grants time-based restricted stock to certain executive officers, as well as performance-based restricted stock that will be eligible to vest at the completion of a three-year period assuming certain performance conditions are achieved over three annual performance periods. The Company recognizes compensation cost for its performance-based restricted stock over the vesting period based on the probability that the performance condition will be satisfied.

Any shares of restricted stock that are forfeited may again become available for issuance. Compensation cost for restricted stock is equal to the fair market value of the shares at the date of the award and is amortized to compensation expense on a straight-line basis over the vesting period. The Company granted 307,000, 368,000 and 266,000 shares of restricted stock at weighted-average fair values of $29.23, $26.08 and $23.57 in 2013, 2012 and 2011, respectively.

The following table summarizes information about restricted stock activity:

	Restricted Stock (In Thousands)	Weighted Average Fair Value
Non-vested at January 1, 2013	696	$ 23.28
Granted	307	29.23
Vested	(6)	28.22

Forfeited	(315)	23.60
Non-vested at December 31, 2013	682	25.77

The total fair value of restricted stock vesting during the year was $722,000, $4.4 million and $5.7 million in 2013, 2012 and 2011, respectively.

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Retirement and Separation-Related Modifications

In connection with the retirement of the Company’s founder and Chairman of the Board, the Company recorded a $10.4 million charge to operating expenses, of which $1.7 million related to the accelerated vesting of 75,000 shares of restricted stock and 25,000 stock options in 2012. During 2011, the Company recorded a $3.5 million charge for separation costs primarily related to the immediate vest modification of 150,000 shares of restricted stock and 50,000 stock options related to the separation of the Company’s Chief Executive Officer. The total incremental cost resulting from the modifications, due primarily to increases in the Company’s stock price as of the modification date compared to the grant date, was $1.2 million and $1.3 million in 2012 and 2011, respectively. There were no similar modification charges in 2013.

NOTE 11: SEGMENTS

Description of Products and Services of Reportable Segments

As of December 31, 2013, the Company had five operating and reportable segments: Sales and Lease Ownership, HomeSmart, RIMCO, Franchise and Manufacturing. In the first quarter of 2013, the Company determined that the RIMCO segment no longer met the aggregation criteria in ASC 280, Segment Reporting. Accordingly, for all periods presented, RIMCO has been reclassified from the Sales and Lease Ownership segment to the RIMCO segment. In January of 2014, the Company sold the 27 Company-operated RIMCO stores and the rights to five franchised RIMCO stores.

The Aaron’s Sales & Lease Ownership division offers electronics, furniture, appliances and computers to consumers primarily on a monthly payment basis with no credit requirements. The HomeSmart division was established to offer electronics, furniture, appliances and computers to consumers on a weekly payment basis with no credit requirements. The Company's RIMCO stores leased automobile tires, wheels and rims to customers under sales and lease ownership agreements. The Company’s Franchise operation awards franchises and supports franchisees of its sales and lease ownership concept. The Manufacturing segment manufactures upholstered furniture and bedding predominantly for use by Company-operated and franchised stores. Therefore, the Manufacturing segment's revenues and earnings before income taxes are primarily the result of intercompany transactions, substantially all of which revenues and earnings are eliminated through the elimination of intersegment revenues and intersegment profit.

Measurement of Segment Profit or Loss and Segment Assets

The Company evaluates performance and allocates resources based on revenue growth and pre-tax profit or loss from operations. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies except that the sales and lease ownership division revenues and certain other items are presented on a cash basis. Intersegment sales are completed at internally negotiated amounts. Since the intersegment profit affect inventory valuation, depreciation and cost of goods sold are adjusted when intersegment profit is eliminated in consolidation.

Factors Used by Management to Identify the Reportable Segments

The Company’s reportable segments are based on the operations of the Company that the chief operating decision maker regularly reviews to analyze performance and allocate resources among business units of the Company.

Information on segments and a reconciliation to earnings before income taxes are as follows for the years ended December 31:

(In Thousands)	2013	2012	2011
Revenues From External Customers:			
Sales and Lease Ownership	$2,076,269	$2,068,124	$1,920,372
HomeSmart	62,840	55,226	15,624
RIMCO	20,596	16,674	11,317
Franchise	68,575	66,655	63,255
Manufacturing	106,523	95,693	89,430
Other	1,562	3,014	5,539
Revenues of Reportable Segments	2,336,365	2,305,386	2,105,537
Elimination of Intersegment Revenues	(103,834)	(95,150)	(89,430)
Cash to Accrual Adjustments	2,100	2,591	(3,529)

Total Revenues from External Customers	$2,234,631	$2,212,827	$2,012,578
Earnings (Loss) Before Income Taxes:			
Sales and Lease Ownership	$183,965	$244,014	$144,232

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(In Thousands)	2013	2012	2011
HomeSmart	(3,428)	(6,962)	(7,283)
RIMCO	(414)	573	153
Franchise	54,171	52,672	49,577
Manufacturing	107	382	2,960
Other	(55,700)	(12,910)	119
Earnings Before Income Taxes for Reportable Segments	178,701	277,769	189,758
Elimination of Intersegment Profit	(94)	(393)	(2,960)
Cash to Accrual and Other Adjustments	6,353	(521)	(3,421)
Total Earnings Before Income Taxes	$184,960	$276,855	$183,377
Assets:			
Sales and Lease Ownership	$1,431,720	$1,410,075	$1,285,807
HomeSmart	47,970	58,347	50,600
RIMCO	13,195	11,737	7,344
Franchise	47,788	53,820	56,131
Manufacturing[1]	24,305	24,787	21,691
Other	262,198	254,163	310,326
Total Assets	$1,827,176	$1,812,929	$1,731,899

1 Includes inventory (principally raw materials and work-in-process) that has been classified within lease merchandise in the consolidated balance sheets of $14.0 million, $14.1 million and $11.2 million as of December 31, 2013, 2012 and 2011, respectively.

Depreciation and Amortization:			
Sales and Lease Ownership	$641,576	$620,774	$581,945
HomeSmart	23,977	20,482	5,933
RIMCO	6,703	5,247	3,198
Franchise	156	146	41
Manufacturing	2,081	4,430	1,294
Other	10,612	7,256	8,260
Total Depreciation and Amortization	$685,105	$658,335	$600,671

Interest Expense:			
Sales and Lease Ownership	$4,470	$5,345	$4,348
HomeSmart	916	846	201
RIMCO	227	186	125
Franchise	—	—	—
Manufacturing	80	106	142
Other	(80)	(91)	(107)
Total Interest Expense	$5,613	$6,392	$4,709

Capital Expenditures:			
Sales and Lease Ownership	$30,831	$33,460	$51,639
HomeSmart	994	4,121	10,950
RIMCO	1,650	2,020	1,763
Franchise	—	—	—
Manufacturing	1,531	4,493	2,107
Other	23,139	20,979	11,752
Total Capital Expenditures	$58,145	$65,073	$78,211

Revenues From Canadian Operations (included in totals above):			
Sales and Lease Ownership	$300	$308	$3,258
Assets From Canadian Operations (included in totals above):			
Sales and Lease Ownership	$1,021	$1,391	$1,527

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Revenues in the "Other" category are primarily revenues from leasing space to unrelated third parties in the corporate headquarters building, revenues of the Aaron's Office Furniture division through the date of sale in August 2012 and revenues from several minor unrelated activities. The pre-tax losses or earnings in the "Other" category are the net result of the activity mentioned above, net of the portion of corporate overhead not allocated to the reportable segments for management purposes.

For the year ended December 31, 2013, the pre-tax losses of the "Other" category included $28.4 million related to an accrual for loss contingencies for a pending regulatory investigation and $4.9 million related to retirement expense and a change in vacation policies. For the year ended December 31, 2012, the pre-tax losses of the "Other" category included $10.4 million in retirement charges associated with the retirement of the Company's founder and Chairman of the Board. Earnings (Loss) Before Income Taxes above for the Sales and Lease Ownership segment include the $36.5 million accrual of a lawsuit for 2011 and the reversal of the lawsuit accrual of $35.5 million in 2012. In addition, during 2011, the Company incurred $3.5 million in separation costs related to the departure of the Company's former Chief Executive Officer, which are reflected in the pre-tax earnings of the "Other" category.

NOTE 12: RELATED PARTY TRANSACTIONS

The Company leases certain properties under capital leases with certain related parties that are more fully described in Note 6 above.

In the fourth quarter of 2011, the Company purchased an airplane for $2.8 million and sold it to R. Charles Loudermilk, Sr., the Company's founder and former Chairman of the Board, for the same amount. The Company paid approximately $80,000 in brokerage fees in connection with the transaction, for which Mr. Loudermilk, Sr., reimbursed the Company. In the fourth quarter of 2011, the Company transferred a Company-owned vehicle to Mr. Loudermilk, Sr., valued at $21,000.

NOTE 13: QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Certain reclassifications have been made to prior quarters to conform to the current period presentation.

(In Thousands, Except Per Share Data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Year Ended December 31, 2013				
Revenues	$593,010	$ 550,545	$537,224	$ 553,852
Gross Profit *	302,439	282,276	265,056	263,080
Earnings Before Income Taxes	81,042	40,387	29,420	34,111
Net Earnings	51,000	25,854	21,138	22,674
Earnings Per Share	.67	.34	.28	.30
Earnings Per Share Assuming Dilution	.67	.34	.28	.30
Year Ended December 31, 2012				
Revenues	$583,299	$ 537,279	$526,883	$ 565,366
Gross Profit *	284,083	266,913	259,957	264,396
Earnings Before Income Taxes	115,029	58,590	46,044	57,192
Net Earnings	71,226	36,244	28,941	36,632
Earnings Per Share	.94	.48	.38	.48
Earnings Per Share Assuming Dilution	.92	.47	.38	.48

* Gross profit is the sum of lease revenues and fees, retail sales, and non-retail sales less retail cost of sales, non-retail cost of sales, depreciation of lease merchandise and write-offs of lease merchandise.

The second quarter of 2013 included a pre-tax $15.0 million charge related to an accrual for loss contingencies for a pending regulatory investigation by the California Attorney General and a $4.9 million charge related to retirement expenses and a change in vacation policies. The third quarter of 2013 included an additional pre-tax $13.4 million charge related to the pending regulatory investigation.

The first quarter of 2012 included a pre-tax $35.5 million reversal of a lawsuit accrual, and the third quarter of 2012 included a pre-tax $10.4 million retirement charge associated with the retirement of the Company's founder and Chairman of the Board.

NOTE 14: DEFERRED COMPENSATION PLAN

Effective July 1, 2009, the Company implemented the Aaron's, Inc. Deferred Compensation Plan, an unfunded, nonqualified deferred compensation plan for a select group of management, highly compensated employees and non-employee directors. On a pre-tax basis, eligible employees can defer receipt of up to 75% of their base compensation and up to 100% of their incentive pay compensation, and eligible non-employee directors can defer receipt of up to 100% of both their cash and stock director fees.

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Compensation deferred under the plan is credited to each participant's deferral account and a deferred compensation liability is recorded in accounts payable and accrued expenses in the consolidated balance sheets. The deferred compensation plan liability was approximately $12.6 million and $9.5 million as of December 31, 2013 and 2012, respectively. Liabilities under the plan are recorded at amounts due to participants, based on the fair value of participants' selected investments. The Company has established a rabbi trust to fund obligations under the plan with Company-owned life insurance. The obligations are unsecured general obligations of the Company and the participants have no right, interest or claim in the assets of the Company, except as unsecured general creditors. The cash surrender value of these policies totaled $14.1 million and $10.4 million as of December 31, 2013 and 2012, respectively, and is included in prepaid expenses and other assets in the consolidated balance sheets.
Deferred compensation expense charged to operations for the Company's matching contributions totaled $139,000, $285,000 and $306,000 in 2013, 2012, and 2011, respectively. Benefits of $1.3 million, $616,000 and $77,000 were paid during the years ended December 31, 2013, 2012 and 2011, respectively.

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NOTE 15: SUBSEQUENT EVENTS

As previously discussed, in January 2014, the Company sold the 27 Company-operated RIMCO stores and the rights to five franchised RIMCO stores, which leased automobile tires, wheels and rims under sales and lease ownership agreements. The Company received total cash consideration of $10.0 million from a third party. During the year ended December 31, 2013, the Company recognized impairment charges of $766,000 related to the write-down of the net assets of the RIMCO operating segment (principally consisting of lease merchandise, office furniture and leasehold improvements) to fair value less cost to sell. The Company expects any additional charges associated with the disposal of the RIMCO segment to be immaterial to future results of operations.

In addition, in February 2014, the accelerated share repurchase program with a third-party financial institution was completed and the Company received an additional 1.0 million shares of common stock.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

An evaluation of Aaron’s disclosure controls and procedures, as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, was carried out by management, with the participation of the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), as of the end of the period covered by this Annual Report on Form 10-K. Based on management’s evaluation, the CEO and CFO concluded that the Company’s disclosure controls and procedures were effective as of December 31, 2013 to provide reasonable assurance that the objectives of disclosure controls and procedures are met.

Reports of Management and Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting

Management has assessed, and the Company’s independent registered public accounting firm, Ernst & Young LLP, has audited, the Company’s internal control over financial reporting as of December 31, 2013. The unqualified reports of management and Ernst & Young LLP thereon are included in Item 8 of this Annual Report on Form 10-K and are incorporated by reference herein.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company’s internal control over financial reporting, as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, during the Company’s fourth fiscal quarter of 2013 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

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PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS OF THE REGISTRANT AND CORPORATE GOVERNANCE

The information required in response to this Item is contained under the captions “Election of Directors (Item 1),” “Committees of the Board of Directors” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Proxy Statement to be filed with the SEC pursuant to Regulation 14A. These portions of the Proxy Statement are hereby incorporated by reference.

We have adopted a written code of ethics that applies to all our directors, officers and employees, including our principal executive officer, principal financial officer, principal accounting officer or controller and other executive officers identified pursuant to this Item 10 who perform similar functions, which we refer to as the Selected Officers. The code is posted on our website at http://www.aarons.com. We will disclose any material changes in or waivers from our code of ethics applicable to any Selected Officer on our website at http://www.aarons.com or by filing a Form 8-K.

ITEM 11. EXECUTIVE COMPENSATION

The information required in response to this Item is contained under the captions “Compensation Discussion and Analysis,” “Summary Compensation Table,” “Grants of Plan Based Awards in Fiscal Year 2013,” “Outstanding Equity Awards at 2013 Fiscal Year-End,” “Option Exercises and Stock Vested in Fiscal Year 2013,” “Non-Qualified Deferred Compensation December 31, 2013,” “Potential Payments Upon Termination or Change in Control,” “Non-Management Director Compensation in 2013,” “Employment Agreements with Named Executive Officers,” “Executive Bonus Plan,” “Restated and Amended 2001 Stock Option and Incentive Award Plan,” “Compensation Committee Interlocks and Insider Participation” and “Compensation Committee Report” in the Proxy Statement. These portions of the Proxy Statement are hereby incorporated by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required in response to this Item is contained under the captions “Beneficial Ownership of Common Stock” and “Equity Compensation Plans” in the Proxy Statement. These portions of the Proxy Statement are hereby incorporated by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required in response to this Item is contained under the captions “Related Party Transactions” and “”Election of Directors (Item 1)” in the Proxy Statement. These portions of the Proxy Statement are hereby incorporated by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required in response to this Item is contained under the caption “Audit Matters” in the Proxy Statement. This portion of the Proxy Statement is hereby incorporated by reference.

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PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENTS and SCHEDULES

a) 1. FINANCIAL STATEMENTS

The following financial statements and notes thereto of Aaron's, Inc. and Subsidiaries, and the related Reports of Independent Registered Public Accounting Firm are set forth in Item 8 and Item 9A.

Consolidated Balance Sheets—December 31, 2013 and 2012
Consolidated Statements of Earnings—Years ended December 31, 2013, 2012 and 2011
Consolidated Statement of Comprehensive Income—Years ended December 31, 2013, 2012 and 2011
Consolidated Statements of Shareholders' Equity—Years ended December 31, 2013, 2012 and 2011
Consolidated Statements of Cash Flows—Years ended December 31, 2013, 2012 and 2011
Notes to Consolidated Financial Statements
Report of Independent Registered Public Accounting Firm
Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting

2. FINANCIAL STATEMENT SCHEDULES

All schedules for which provision is made in the applicable accounting regulations of the SEC have been omitted because they are not applicable or the required information is included in the financial statements or notes thereto.

3. EXHIBITS

EXHIBIT NO.	DESCRIPTION OF EXHIBIT
3(i)	Amended and Restated Articles of Incorporation of Aaron's, Inc.
3(ii)	Amended and Restated By-laws of Aaron's, Inc. (incorporated by reference to Exhibit 3(i) of the Registrant's Current Report on Form 8-K filed with the SEC on February 21, 2014).
4	Specimen of Form of Stock Certificate Representing Shares of Common Stock of the Registrant, par value \$0.50 per share (incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form 8-A/A filed with the SEC on December 10, 2010).
10.1	Loan Agreement between Fort Bend County Industrial Development Corporation and Aaron Rents, Inc. relating to the Industrial Development Revenue Bonds (Aaron Rents, Inc. Project), Series 2000 dated October 1, 2000 (incorporated by reference to Exhibit 10(m) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2000 filed with the SEC on March 30, 2001).
10.2	Letter of Credit and Reimbursement Agreement between the Registrant and First Union National Bank dated as of October 1, 2000 (incorporated by reference to Exhibit 10(n) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2000 filed with the SEC on March 30, 2001).
10.3	First Omnibus Amendment dated as of August 21, 2002, but effective as of October 31, 2001 to the Amended and Restated Master Agreement and Amended and Restated Lease Agreement dated as of October 31, 2001, as amended, among Aaron Rents, Inc. as lessee, SunTrust Banks, Inc. as lessor, Wachovia Bank, National Association, as lender, and SunTrust Bank as lease participant and agent (incorporated by reference to Exhibit 10(kk) to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2005 filed with the SEC on November 8, 2005).
10.4	First Amendment dated as of July 27, 2005 to Amended and Restated Master Agreement and Amended and Restated Lease Agreement dated as of October 31, 2001, as amended, among Aaron Rents, Inc. as lessee, SunTrust Banks, Inc. as lessor, Wachovia Bank, National Association, as lender, and SunTrust Bank as lease participant and agent (incorporated by reference to Exhibit 10(jj) of the Registrant's Current Report on Form 8-K filed with the SEC on August 2, 2005).
10.5	Note Purchase Agreement by and among Aaron's, Inc. and certain other obligors and the purchasers dated as of July 5, 2011 and Form of Senior Note (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on July 8, 2011).

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10.6	Amendment No. 1 to Note Purchase Agreement by and among Aaron’s, Inc. and certain other obligors and the purchasers, dated as of December 19, 2012 (incorporated by reference to Exhibit 10 of the Registrant’s Current Report on Form 8-K filed with the SEC on December 26, 2012).
10.7	Amendment No. 2 to Note Purchase Agreement by and among Aaron’s, Inc. and certain other obligors and the purchasers, dated as of October 8, 2013 (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on October 15, 2013).
10.8	Revolving Credit Agreement, dated as of May 23, 2008, among Aaron Rents, Inc., as borrower, the lenders from time to time party thereto, and SunTrust Bank, as administrative agent (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on May 30, 2008).
10.9	First Amendment made and entered into on March 31, 2011 to the Revolving Credit Agreement, dated as of May 23, 2008, by and among Aaron’s, Inc., each of the other lending institutions party thereto as participants, and SunTrust Bank as administrative agent for the lenders (incorporated by reference to Exhibit 10.2 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 31, 2001 filed with the SEC on May 4, 2011).
10.10	Second Amendment to Revolving Credit Agreement, by and among Aaron’s, Inc., as borrower, SunTrust Bank, as administrative agent, and each of the other financial institutions party thereto as lenders, dated as of May 18, 2011 (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K, filed with the SEC on May 24, 2011).
10.11	Third Amendment made and entered into as of July 1, 2011 to Revolving Credit Agreement dated as of May 23, 2008 by and among Aaron’s, Inc., the several banks and other financial institutions from time to time party thereto and SunTrust Bank as administrative agent (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K filed with the SEC on July 8, 2011).
10.12	Fourth Amendment to Revolving Credit Agreement, by and among Aaron’s, Inc., as borrower, SunTrust Bank, as administrative agent, and each of the lending institutions party thereto as lenders, dated as of December 13, 2012 (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K filed with the SEC on December 19, 2012).
10.13	Fifth Amendment to Revolving Credit Agreement, by and among Aaron’s, Inc., as borrower, SunTrust Bank, as administrative agent, and each of the lending institutions party thereto as lenders, dated as of October 8, 2013 (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K filed with the SEC on October 15, 2013).
10.14	Second Amended and Restated Loan Facility Agreement and Guaranty, by and among Aaron's, Inc., SunTrust Bank, as servicer, and the other financial institutions party thereto as participants, dated as of June 18, 2010 (incorporated by reference to Exhibit 10.1 of the Registrant’s Current Report on Form 8-K, filed with the SEC on June 24, 2010).
10.15	First Amendment made and entered into as of March 31, 2011 to the Second Amended and Restated Loan Facility Agreement and Guaranty, dated as of June 18, 2010, by and among Aarons, Inc. as sponsor, each of the other lending institutions party thereto as participants, and SunTrust Bank as servicer (incorporated by reference to Exhibit 10.1 of the Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 31, 2011 filed with the SEC on May 4, 2011).
10.16	Second Amendment to Second Amended and Restated Loan Facility Agreement and Guaranty, by and among Aaron’s, Inc., as sponsor, SunTrust Bank, as servicer, and each of the other financial institutions party thereto as participants, dated as of May 18, 2011 (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K filed with the SEC on May 24, 2011).
10.17	Third Amendment made and entered into as of July 1, 2011 to Second Amended and Restated Loan Facility Agreement and Guaranty dated as of June 18, 2010 by and among Aaron’s, Inc. as sponsor, SunTrust Bank and each of the other lending institutions party thereto as participants, and SunTrust Bank as servicer (incorporated by reference to Exhibit 10.4 of the Registrant’s Current Report on From 8-K filed with July 8, 2011).
10.18	

	Fourth Amendment made and entered into as of May 16, 2012 to Second Amended and Restated Loan Facility Agreement and Guarantee dated as of June 18, 2010 by and among Aaron’s, Inc. as sponsor, SunTrust Bank and each of the other lending institutions party thereto as participants, and SunTrust Bank as servicer (incorporated by reference to Exhibit 10.41 of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2012 filed with the SEC on February 22, 2013).
10.19	Fifth Amendment to Second Amended and Restated Loan Facility Agreement and Guaranty, by and among Aaron’s, Inc., as sponsor, SunTrust Bank, as servicer, and each of the other financial institutions party thereto as participants, dated as of December 13, 2012 (incorporated by reference to Exhibit 10.2 of the Registrant’s Current Report on Form 8-K filed with the SEC on December 19, 2012).
10.20	Sixth Amendment to Second Amended and Restated Loan Facility Agreement and Guaranty, by and among Aaron’s, Inc., as sponsor, SunTrust Bank, as servicer, and each of the other financial institutions party thereto as participants, dated as of October 8, 2013 (incorporated by reference to Exhibit 10.3 of the Registrant’s Current Report on Form 8-K filed with the SEC on October 15, 2013).
10.21	Seventh Amendment to Second Amended and Restated Loan Facility Agreement and Guaranty, by and among Aaron's, Inc. as sponsor, SunTrust Bank, as servicer, and each of the other financial institutions party thereto as participants, dated as of December 12, 2013 (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on December 18, 2013).

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10.22	Aaron's, Inc. Employees Retirement Plan and Trust, as amended and restated (incorporated by reference to Exhibit 99.3 of the Registrant's Registration Statement on Form S-8 (333-171113) filed with the SEC on December 10, 2010).
10.23	Amendment No. 1 to the Aaron's Inc. Employees Retirement Plan and Trust, as amended and restated, dated as of December 1, 2011 (incorporated by reference to Exhibit 10.1 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 filed with the SEC on August 2, 2013).
10.24	Amendment No. 2 to the Aaron's Inc. Employees Retirement Plan and Trust, as amended and restated, dated as of December 29, 2011 (incorporated by reference to Exhibit 10.2 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 filed with the SEC on August 2, 2013).
10.25	Amendment No. 3 to the Aaron's Inc. Employees Retirement Plan and Trust, as amended and restated, dated as of December 31, 2012 (incorporated by reference to Exhibit 10.3 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 filed with the SEC on August 2, 2013).
10.26	Amended and Restated Aaron Rents, Inc. 2001 Stock Option and Incentive Award Plan (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on April 10, 2009).
10.27	Form of Restricted Stock Unit Award Agreement for awards made prior to February 2014 (incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on From 10-Q for the quarter ended March 31, 2012 filed with the SEC on May 8, 2012).
10.28	Form of Option Award Agreement for awards made prior to February 2014.
10.29	Form of Restricted Stock Unit Award for awards made in or after February 2014.
10.30	Form of Option Award Agreement for awards made in or after February 2014.
10.31	Form of Performance Share Award Agreement for awards made in or after February 2014.
10.32	Aaron's Management Performance Plan (Summary of terms for Home Office Vice Presidents) (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on August 5, 2011).
10.33	Aaron's, Inc. 2001 Stock Option and Incentive Award Plan Master Restricted Stock Unit Agreement (Aaron's Management Performance Plan) (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed with the SEC on August 5, 2011).
10.34	Aaron's, Inc. Deferred Compensation Plan Master Plan Document, Effective July 1, 2009 (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on June 12, 2009).
10.35	Employment Agreement, dated as of April 18, 2012, by and between Aaron's, Inc. and Ronald W. Allen (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on April 24, 2012).
10.36	Employment Agreement, dated as of April 18, 2012, by and between Aaron's, Inc. and Gilbert L. Danielson (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on April 24, 2012).
10.37	Executive Severance Pay Plan of Aaron's, Inc. (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on January 31, 2014).
10.38	Separation Agreement, dated as of May 1, 2013, by and between Aaron's, Inc. and William K. Butler (incorporated by reference to Exhibit 10.4 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 filed with the SEC on August 2, 2013).
10.39	Retirement Agreement between Aaron's, Inc. and R. Charles Loudermilk, Sr., dated August 24, 2012 (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the SEC on August 30, 2012).
10.40	Fixed Dollar Discounted Accelerated Share Repurchase Agreement, dated December 3, 2013, by and between Aaron's, Inc. and Wells Fargo Securities, LLC.
21	Subsidiaries of the Registrant.
23	Consent of Ernst & Young LLP.

31.1	Certification of the Chief Executive Officer of Aaron’s, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Chief Financial Officer of Aaron’s, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer of Aaron’s, Inc. furnished herewith pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of the Chief Financial Officer of Aaron’s, Inc. furnished herewith pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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101	The following financial information from Aaron's, Inc. Annual Report on Form 10-K for the year ended December 31, 2013, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets as of December 31, 2013 and December 31, 2012, (ii) Consolidated Statements of Earnings for the Years ended December 31, 2013, 2012 and 2011, (iii) Consolidated Statements of Comprehensive Income for the Years ended December 31, 31, 2013, 2012 and 2011, (iv) Consolidated Statements of Cash Flows for the years ended December 31, 2013, 2012 and 2011, (v) Consolidated Statements of Shareholder's Equity for the Years ended December 31, 2013, 2012 and 2011 and (v) the Notes to Consolidated Financial Statements.

(b) EXHIBITS

The exhibits listed in Item 15(a)(3) are included elsewhere in this Report.

(c) FINANCIAL STATEMENTS AND SCHEDULES

The financial statements listed in Item 15(a)(1) are included in Item 8 in this Report.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on February 24, 2014.

AARON'S, INC.

By: /s/ GILBERT L. DANIELSON
Gilbert L. Danielson
Executive Vice President, Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on February 24, 2014.

SIGNATURE	TITLE
/s/ RONALD W. ALLEN Ronald W. Allen	Chairman of the Board of Directors, President and Chief Executive Officer and Director (Principal Executive Officer)
/s/ GILBERT L. DANIELSON Gilbert L. Danielson	Executive Vice President, Chief Financial Officer and Director (Principal Financial Officer)
/s/ ROBERT P. SINCLAIR, JR. Robert P. Sinclair, Jr.	Vice President, Corporate Controller (Principal Accounting Officer)
/s/ DAVID L. BUCK David L. Buck	Chief Operating Officer
/s/ LEO BENATAR Leo Benatar	Director
/s/ KATHY T. BETTY Kathy T. Betty	Director
/s/ CYNTHIA N. DAY Cynthia N. Day	Director
/s/ HUBERT L. HARRIS, JR. Hubert L. Harris, Jr.	Director
/s/ DAVID L. KOLB David L. Kolb	Director
/s/ RAY M. ROBINSON Ray M. Robinson	Director