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FEDERAL TRADE COMMISSION
Chicago Regional Office

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Chicago, Illinois 60603
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December 22, 1988

COMMISSION AUTHORIZED

The Honorable James R. Thompson
Governor of Illinois
Office of the Governor
Springfield, Illinois 62706

Dear Governor Thompson:

The staff of the Chicago Regional Office and Bureau of Consumer Protection of the Federal Trade Commission is pleased to have the opportunity to respond to your request for comment on the need for amendatory legislation after the additions to the Illinois Vehicle Code contained in Senate Bill 1870 become effective on January 1, 1989.¹ As you have asked, we are providing comments on how Senate Bill 1870 might be amended or revised in the next legislative session to better serve its purpose of improving the welfare of the consumer and preserving the competitive environment in the car rental industry. In addition, you indicate that there may be a need for amendatory legislation to supplement the bill's disclosure requirements. We would be pleased to offer additional assistance if other amendments are offered.

Senate Bill 1870 will amend the Illinois Vehicle Code in three principal ways. First, this bill will limit the methods automobile rental companies may employ in calculating base rental charges and in advertising those prices. Second, it will dramatically alter the current methods of allocating the costs, and risks, of damage to (or theft of) a rental vehicle. Finally, it will extend the current Illinois prohibition against buying or selling motor vehicles on Sundays to include a ban on long-term leasing of motor vehicles on Sundays. We are concerned that parts of these provisions may result in increased costs to consumers who lease or rent automobiles without providing significant

¹ These comments represent the views of the Chicago Regional Office and the Bureau of Consumer Protection of the Federal Trade Commission. They are not necessarily the views of the Federal Trade Commission or any individual Commissioner. Questions or comments concerning this document may be addressed to Timothy T. Hughes, Attorney, Chicago Regional Office, (312) 353-4431.

The Honorable James R. Thompson
December 22, 1988

benefits to the majority of automobile renters or to the public at large.

The Federal Trade Commission is charged with promoting competition and protecting consumers from unfair and deceptive commercial practices.² In fulfilling this mandate, the staff of the Federal Trade Commission often submits comments, upon request, to federal, state, and local governmental bodies to help assess the competitive and consumer welfare implications of pending policy issues. In enforcing the Federal Trade Commission Act, the Commission staff has gained substantial experience in analyzing the impact of various restraints on competition (both by private action and through government intervention) and the costs and benefits to consumers of such restraints.

Pursuant to its statutory mandate, the Commission and its staff have considered other matters involving the car rental industry and Sunday closing laws. The Commission recently commented on the draft guidelines prepared by the National Association of Attorneys General's Task Force on Car Rental Industry Advertising and Practices (NAAG Guidelines).³ The advertising, pricing, and allocation of liability portions of SB 1870 are very similar to portions of these NAAG guidelines. The Commission staff has also examined, and presented its comments on, numerous Sunday closing laws.⁴

² See 15 U.S.C. § 41 et seq.

³ Letter from the Federal Trade Commission (Commissioner Strenio not joining) to Art Weiss, Deputy Attorney General, Kansas (November 4, 1988). A copy is attached. The NAAG draft guidelines were preliminarily approved with certain modifications by NAAG at its Winter meeting on December 7, 1988.

⁴ Earlier testimony on Sunday closing laws for automobile dealers was provided by the staff of the Federal Trade Commission to the Committee on Registration and Regulation, Illinois House of Representatives on April 17, 1985. A copy of that testimony is attached. See also staff comments to the Honorable Lee F. Jackson, Texas House of Representatives, May 10, 1985; and to the Honorable Lynn
(continued...)

The Honorable James R. Thompson
December 22, 1988

Pricing and Advertising Restrictions

SB 1870 contains new restrictions on the ability of automobile rental agencies to advertise, and charge for, certain items. Automobile rental agencies are specifically allowed to charge a rental fee, taxes, and a mileage charge.⁵ The bill also allows rental agencies to charge separately for other items, such as a drop-off fee or for fuel actually used, but only if "the renter can avoid incurring the charge by choosing not to obtain or utilize the optional item or service."⁶ Rental agencies may not separately charge for nondeclinable items such as "required fuel or airport surcharges" or "for transporting the renter to the location, where the rented vehicle will be delivered to the renter."⁷

SB 1870 does not prohibit automobile rental agencies from recovering their costs for mandatory additional services; it simply forbids breaking them out as charges that are added to the base rental rate in computing the total rental amount. In other words, rental agencies must "bundle" certain services into their base rental charges. The apparent rationale is to make it easier to compare advertised prices across car rental agencies, some of which impose mandatory additional charges and some of which do not.⁸

4 (...continued)
Adelman, Chairman, Wisconsin State Senate Judiciary and Consumer Affairs Committee, June 19, 1987.

5 Senate Bill 1870 § 1.

6 Id.

7 Id.

8 One effect of the bill may well be to force rental agencies that charge a flat fuel fee to incorporate that fee in the base rental rate they advertise. Car rental companies have traditionally advertised a base fee, renting automobiles with a full tank of gas and charging customers for any gasoline needed to refill the tank when the automobile is returned. At least one rental company, however, simply charges a flat fee for gasoline, regardless of the amount
(continued...)

The Honorable James R. Thompson
December 22, 1988

It is, of course, desirable that consumers have material information on rental prices before they sign a rental agreement. They can obtain that information from, among other sources, advertising, conversations when reserving a rental vehicle, and the point of sale -- the rental counter. It is not clear why additional charges need to be bundled into the base rental rate if they are adequately disclosed to consumers by such means prior to purchase. Rental advertising that deceptively omits additional charges can, and should, be subject to legal action.

It is possible that SB 1870 may make it more difficult for consumers to obtain useful information from price advertising.⁹ For example, some charges vary from location-to location.¹⁰ If the effect of the bill is to encourage rental agencies to set different base rental rates at each location, national or regional price advertising (and therefore price comparisons by consumers) may become very difficult.¹¹ One alternative available for rental companies

⁸ (...continued)
that is used. Some consumers may prefer this arrangement because it relieves them of the need to refill the tank prior to returning the automobile and allows them to determine the total cost of the rental (including fuel costs) in advance.

⁹ Short radio and television commercials advertising the existence of cheaper rates can serve a useful role in informing consumers that discounts are available and signalling that they should inquire further for details. This form of advertising is, however, by its nature incapable of providing all the information that consumers might need in making an ultimate decision on a vehicle rental.

¹⁰ Some airports charge "access" fees to off-airport rental agencies to reimburse the airport for the use of its roads and other services. These fees, which are not within the control of the rental agencies, are generally passed on to consumers.

¹¹ Indeed, the NAAG car rental task force recognized that "[b]ecause these [airport access] fees may vary from
(continued...)

The Honorable James R. Thompson
December 22, 1988

is to substitute "image" advertising that promotes recognition of the company name but may not provide the same amount of useful comparative information for consumers. Since numerous economic studies have demonstrated that price advertising enhances competition and lowers prices,¹² we suggest caution in imposing any requirements that may discourage price advertising.¹³

Lessor Liability

SB 1870 also makes significant changes in the allocation of the risks that a rental vehicle will be damaged or stolen. SB 1870 requires rental agencies to assume responsibility for losses in excess of \$200 in most

¹¹(...continued)
airport to airport, it may be difficult to build these fees into a national advertised rate." National Association of Attorneys General, Task Force of Car Rental Industry Advertising and Business Practices, Preliminary Report (June 19, 1988) at 8.

¹² See, e.g., Cleveland Regional Office and Bureau of Economics, Federal Trade Commission, Improving Consumer Access to Legal Services: The Case for Removing Restrictions on Truthful Advertising, Federal Trade Commission Staff Report (1984); Benham, The Effects of Advertising on the Price of Eyeglasses, 15 J. of L. and Econ. 337 (1972); Cady, An Estimate of the Price Effects of Restrictions on Drug Price Advertising, 14 Econ. Inquiry 493 (1976); Kwoka, Advertising and Price and Quality of Optometric Services, 74 Am. Econ. Rev. 211 (1984); and Schroeter et al., Advertising and Competition in Routine Legal Service Markets: An Empirical Investigation, 36 The J. of Indus. Econ. 49 (1987).

¹³ Besides potentially discouraging price advertising, SB 1870 may lead to consumers renting at some airports subsidizing rentals at other locations. For example, if rental agencies are forced to bundle airport access fees into their national base rental fee, customers renting automobiles near airports that have no such fees (such as O'Hare and Midway) will, in effect, subsidize those renting automobiles near airports that do.

The Honorable James R. Thompson
 December 22, 1988

situations.¹⁴ The bill thus alters the ability of rental agencies to charge separately for a Collision Damage Waiver (CDW).¹⁵ We are concerned that this could harm consumers in two ways: by limiting their ability to choose other means of covering the risk that a rental vehicle could be damaged or stolen, and by producing higher overall rental rates.

First, making rental agencies liable in the event that automobiles are damaged or stolen will eliminate the ability of consumers to choose alternative means of dealing with this risk. Renters currently have several options. They can purchase optional CDW from the rental company, which typically relieves the renter of liability for damage to or loss of the rental vehicle in case of accident or theft. Or they can decline to purchase CDW and instead: 1) assume the risk of personal liability for damage to rental vehicles,¹⁶ 2) rely on their personal automobile insurance policies for coverage,¹⁷ or 3) rely on the coverage from other providers.¹⁸ One or more of these options could be less expensive than the increased prices all customers may have to pay to cover the accident and theft losses SB 1870 shifts to the rental companies. Some renters with good driving records can currently reduce their costs by arranging third-party

¹⁴ SB 1870, § 1. Renters remain liable under SB 1870 if damage is caused intentionally, results from willful or wanton misconduct or from intoxication or drug use, occurs while engaging in a speed contest, or involves similar misconduct or criminal activity. *Id.*

¹⁵ CDW might still be sold to cover the risk of damage that is less than \$200.

¹⁶ The U.S. Government, for example, is self insured.

¹⁷ According to J. Robert Hunter, president of the National Insurance Consumer Organization, approximately 60 percent of all drivers possess automobile insurance policies that provide coverage should the insured driver experience an accident in a rental vehicle. Car rentals: How to avoid being taken for a ride, Money, April 1988, at 201.

¹⁸ For example, several credit card companies offer complete coverage for damages incurred while driving a rental car that is paid for with their card. *Id.*

The Honorable James R. Thompson
December 22, 1988

insurance rather than purchasing a CDW. Drivers who cannot, or choose not to, arrange for third-party insurance can still reduce the risk of driving a rented vehicle by purchasing a CDW.¹⁹

Second, shifting this liability to rental agencies may lead to higher basic rates. When SB 1870 goes into effect on January 1, 1989, rental car companies may have to increase the rental rate to compensate for their expanded liability for accidents and thefts. Thus, it may be more accurate to characterize the effect of this legislation not as eliminating CDW but as mandating the sale of CDW indirectly. Many consumers who would have declined purchasing CDW would be injured because they would be required, in essence, to pay for coverage twice: first for the coverage provided by their own insurance, which reflects their own driving records, and also for rental car company-provided insurance, which pools good and bad drivers.²⁰

¹⁹ In addition, making rental agencies liable for accident and theft losses could result in relatively safe drivers subsidizing relatively unsafe ones. (This is so because insurance companies are able to charge different premiums for drivers with different driving records. Rental agencies would not be able to adapt their charges to reflect these different risk levels.) It is unclear that such a subsidy would be in the public interest. Moreover, such subsidization is discouraged by the current system, which allows consumers to choose CDW protection or to decline such protection if they are (or believe themselves to be) relatively good risks.

²⁰ Moreover, it is possible that in response to this change some consumers would become less careful with rental vehicles. If this were to happen, rental companies would experience higher repair costs and an increase in the proportion of vehicles under repair at any given time. Increased costs are likely to be passed through to consumers as higher rates. For a theoretical treatment of this issue, see Brown, *Toward an Economic Theory of Liability*, 2 *J. of Legal Stud.* 323 (1973); Diamond, *Single Activity Accidents*, 3 *J. of Legal Stud.* 107 (1974); and Shavell, *Strict Liability vs. Negligence*, 9 *J. of Legal Stud.* 1 (1980).

The Honorable James R. Thompson
December 22, 1988

Our analysis of the CDW issue comes to a different conclusion than that reached in the NAAG Task Force Report.²¹ The task force attributes problems with the marketing of CDW to renters' ignorance of the product's features. The task force then concludes that the informational gap is such that optional CDW should simply be banned. Our view, however, is that when consumers lack the information needed to make an informed choice, the preferable approach is to provide them with the needed information, not to eliminate the choice altogether.²² We hope that the legislature will reexamine SB 1870 and explore methods of facilitating the communication of accurate information concerning optional CDW, rather than banning the CDW option altogether.

Sunday Closing

Illinois law currently prohibits automobile dealers from operating any established place of business for the purpose of selling motor vehicles on Sundays.²³ SB 1870 will extend that prohibition to preclude the leasing of automobiles on Sundays if the lease period is greater than one year.

In the spring of 1985 the staff of the Federal Trade Commission's Chicago Regional Office testified in favor of repealing the Illinois Sunday closing law for automobile dealers. As the attached testimony indicates, studies have shown that Sunday closing makes it more difficult for consumers to shop and compare, and thus may lead to increased automobile prices for consumers.²⁴ We believe that

²¹ Guideline 3.1 of the Report recommends adoption of legislation to eliminate the sale of CDW and to prohibit charging a customer for damage or theft of a vehicle.

²² See Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council, 425 U.S. 748, 770 (1975).

²³ Ill. Rev. Stat. Ch. 95 1/2, § 5-106 (1987). This section of the statute contain exceptions for some items, such as sales of mobile homes and motorcycles.

²⁴ See, e.g., Carlson and Gieseke, Price Search In a Product Market, J. of Cons. Research, March 1983, pp. 357- (continued...)

The Honorable James R. Thompson
December 22, 1988

prohibiting long-term leasing of automobiles on Sundays presents similar problems.

Consumers typically consider a range of factors in deciding the type of automobile they want to lease or purchase and where they want to obtain it. These include safety, reliability, handling, size, and price, as well as terms and conditions of the lease or purchase. Although advertising provides information that aids consumers in making informed decisions, consumers may also find it useful to engage in on site inspections of different automobiles. Sunday closing laws are likely to inhibit the ability of consumers to exercise this option.

Extending the Sunday closing law to long-term leasing raises another concern in addition to those identified above. It is our understanding that some short-term rental agencies also lease automobiles for longer periods. To the extent that both services are offered in one location, precluding long-term leasing while the location is open for short-term rental purposes may prevent the firm from realizing economies in operation and passing the attendant cost savings on to consumers.

Conclusion

In sum, it is not clear that SB 1870 will provide net benefits to consumers. We suggest additional consideration of the potential adverse effects of the requirement in SB 1870 that some charges be bundled into base automobile rental fees. We also hope you will take into account the prospect that the changes in liability for damaged or stolen rental vehicles would mean, on balance, higher rental prices for consumers. In addition, it may be desirable to review the effects of the Sunday closing law now applicable to the sale of automobiles and consider its repeal.

We hope that these comments will help you in your determination of whether SB 1870 is likely to achieve the

24 (...continued)

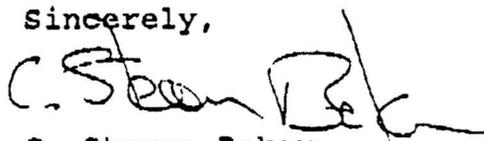
56; Morrison and Newman, Hours of Operation Restrictions and Competition Among Retail Firms, Econ. Inq., Vol. XXI, January 1983; Stigler, The Economics of Information, J. of Pol. Econ., June 1961, pp. 213-15.

The Honorable James R. Thompson
December 22, 1988

goal of protecting consumers and whether, or how, the Illinois Motor Vehicle Code could be amended or revised in the next legislative session to serve the welfare of consumers and foster a competitive environment in the car rental and leasing industries. The Commission staff will be pleased to offer any assistance that it can to your office during the next legislative session.

We appreciate the opportunity to comment.

Sincerely,

A handwritten signature in black ink, appearing to read "C. Steven Baker". The signature is written in a cursive style with a large, stylized "B" and "K".

C. Steven Baker
Director
CHICAGO REGIONAL OFFICE