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FEDERAL TRADE COMMISSION
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December 2, 1996

The Honorable **Ron Stephens**
Chairman, Executive Committee
Illinois House of Representatives
1004 S. Lincoln, Suite 10
O'Fallon, Illinois 62269

Dear Chairman Stephens:

The staff of the Federal Trade Commission⁽¹⁾ is pleased to respond to your request for comment on House Bill No. 3285, introduced in the current session of the Illinois legislature. The bill would repeal the present ban in Illinois on car rental firms offering a "collision damage waiver" ("CDW") option, and it would impose disclosure requirements on car rental firms and a cap on CDW charges. It would also remove Illinois' ban on holding renters liable for non-intentional loss, damage or theft.

H.B. 3285 could benefit consumers in several ways. Permitting car rental firms to offer CDW might make it easier for some consumers to rent cars, especially those who are otherwise uninsured or who rent cars in high risk locations. Permitting rental firms to hold renters liable for a greater range of losses and permitting renters to purchase CDW to cover this potential liability might also lead to somewhat lower overall rental rates. Ensuring that consumers have the information they need to make choices about liability protection is likely to enhance consumer welfare more than would restricting the choices available.

I. Interest and Experience of the Federal Trade Commission.

The Federal Trade Commission is empowered to prevent unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce.⁽²⁾ Consistent with this statutory mandate, the Commission and its staff work to identify restrictions that hinder competition and increase costs without providing countervailing benefits to consumers. The Commission and its staff have commented several times about state regulation of the car rental industry.⁽³⁾

II. Description of the Proposed Legislation.

House Bill No. 3285 would eliminate the present ban in Illinois on the sale of CDW by car rental firms, require certain disclosures about CDW in contracts and advertising, and permit customers to be held responsible for non-intentional damage or loss. When the issue is considered next, the bill may include provisions that had been proposed by the Illinois Attorney General and Department of Insurance as amendments to H.B. 3285. This comment will discuss H.B. 3285 as modified by those proposed amendments.

Illinois now prohibits offering or selling CDW "or any other type of waiver or insurance as a separate charge" to cover an insurance deductible or the kinds of losses for which the law now permits customers to be held liable.⁽⁴⁾ The bill would remove that prohibition and add provisions to regulate CDW. "Damage waiver" would be defined as an agreement by the rental company not to hold the rental driver liable for damage or loss.⁽⁵⁾ A new section, titled "prohibited practices," would permit CDW clauses that meet three requirements. First, CDW must be agreed to in writing at (or before) the time the rental contract is executed.⁽⁶⁾ Second, CDW may be voided only for reasons that are specified in the law: intentional or reckless conduct, driving under the influence of alcohol or drugs, fraud, crime, and several kinds of unauthorized uses.⁽⁷⁾ Third, prices for CDW must not exceed statutory caps.⁽⁸⁾ The daily CDW rate must be no more than \$9.00 for vehicles with a dealer cost under \$30,000; for more expensive vehicles, the cap would be \$12.00.

The bill would require car rental companies to make certain disclosures about CDW in rental contracts and in advertisements and other communications about prices.⁽⁹⁾ Advertisements that state the rental cost would have to include the following information about CDW "in plain language and in conjunction with the advertised rental cost": the daily CDW rate, that CDW is an additional charge, that CDW is optional, and that renters should check their own insurance policies for rental coverage.⁽¹⁰⁾ The bill would specify how conspicuous this disclosure must be: in print, at least 10 point type; on video, at least 1/3 the size of the rental cost display; and on radio (or the audio portion of a video advertisement), immediately after the statement of the rental cost. Moreover, any written or oral statement (except by telephone) of rental cost must also include disclosure of the CDW rate and the fact that it is an additional daily charge.⁽¹¹⁾ Rental companies would have to disclose this information through signs or pamphlets posted "prominently and conspicuously" where renters may easily see them.⁽¹²⁾ These disclosures about CDW would be in addition to new requirements about disclosure of other, "mandatory" charges.⁽¹³⁾

The cap on renter responsibility for non-intentional loss would also be removed. Illinois now prohibits holding a renter responsible for more than \$200.00 of damage or loss, except when loss results from specified kinds of intentional conduct.⁽¹⁴⁾ In its place, a new section would limit the renter's liability for damage to a vehicle to the lesser of the actual repair cost or the vehicle's fair market value before the accident.⁽¹⁵⁾

III. Removing the Ban on CDW Will Likely Give Consumers More Choices.

State law banning CDW and capping renters' responsibility for losses has altered the allocation of risk, making car rental companies financially responsible for most damage. It appears that car rental companies have passed on this additional financial responsibility in the form of higher basic rental rates and refusing to rent cars in some high risk locations.

The staff believes that permitting CDW and removing the caps on renter responsibility is a step in the right direction. It would make another option available to consumers, an option which might make it easier for some consumers to rent cars. To cover the risk of loss or damage to a rented car due to non-intentional accident or theft, a consumer might assume the risk personally, rely on personal automobile insurance, or rely on coverage from a credit card or other source. Where it is available, the consumer could also buy CDW from the rental company, which would relieve the consumer from having to pay the cost of loss or damage to the rented car. For many consumers, the first three options could be preferable to, and less expensive than, CDW. Renters with good driving records can reduce their costs by arranging third-party insurance rather than purchasing CDW. But for others, who cannot or do not arrange for third-party insurance or protection to cover rentals, the availability of CDW could make it possible for them to rent a car. In fact, we understand that some rental car companies generally do not rent to consumers that are otherwise uninsured and that this situation might change if those consumers had the option of purchasing CDW.

Even if average car rental rates are not substantially different where CDW is banned, the ban may still have adversely affected many consumers. When CDW is banned the rental companies would typically include their overall risk of loss in the basic rental rate, which would be the same for both good and bad drivers. Including the cost of the risk of loss in the rental rate could, in effect, injure those consumers who have personal auto insurance that also covers rentals by requiring them to pay for coverage twice. In addition, it requires consumers with good driving

records whose personal policy rates reflect their own driving records to pay the higher costs of being placed in the same risk pool as drivers with poor records. Thus even drivers who have their own insurance would pay, indirectly, for the protection that the rental company provides itself against renters with both good and bad driving records. Therefore consumers who already have auto insurance that covers their risk would pay an additional sum in an increased basic rental fee.

As noted, with traditional auto insurance safer drivers pay less than drivers that pose a greater risk.⁽¹⁶⁾ When this risk is instead recovered through a higher rental rate, however, there is no way to adjust price between drivers posing different levels of risk. Thus when optional CDW is banned, relatively safe drivers may subsidize relatively unsafe ones because the costs of losses must be bundled into the rental price that applies for everyone.⁽¹⁷⁾

Banning optional CDW may have led to higher basic rental rates in Illinois, if car rental companies raised rates to recover the costs of accident and theft. There is some evidence that rates are higher in Illinois and New York, two states that have banned CDW and capped renters' liability, than in other states. The difference in rates may be due to many causes, and not just the difference in treatment of renters' liability. Moreover, the increase in apparent average rates in those states is smaller than the average CDW charge, so the average total costs of renting in those states may not be out of line with the average total costs actually experienced in other states.⁽¹⁸⁾ In general, though, it would be expected that permitting greater flexibility in how rental firms can handle these liabilities, including permitting the firms to shift liabilities to renters, could lead to lower costs and thus to lower rates.

There have been allegations over the years that marketing of CDW has taken advantage of renters' ignorance about CDW. In general, when consumers lack the information needed to make an informed choice, the better approach is to provide the information, rather than prevent the choice.⁽¹⁹⁾ H.B. 3285 includes several provisions intended to ensure that consumers are informed about CDW and some of the other options available to them. Thus, the bill moves in a desirable direction. By tying disclosures about CDW to statements about price, the bill recognizes one of the problems that have been alleged: advertisements of seemingly low prices may have misled consumers by failing to disclose substantial additional charges like CDW.⁽²⁰⁾

IV. Conclusion.

On balance, allowing CDW to be offered in Illinois could benefit consumers by giving them an additional way to cover the risk of unintentional loss. Normally giving consumers enough information to make informed choices would be better than eliminating a choice altogether. Thus, requiring some disclosures, as this bill would do, would be preferable to prohibiting CDW altogether.

I hope that these views are helpful in your consideration of these issues. If you have any questions, please do not hesitate to call.

Sincerely yours,

C. Steven Baker
Director

1. These comments are the views of the staff of the Federal Trade Commission, and do not necessarily represent the views of the Commission or any individual Commissioner.

2. 15 U.S.C. 41 et seq.

3. See, e.g., Letters from the Federal Trade Commission (Commissioner Strenio not joining) to Art Weiss, Deputy Attorney General, Kansas Judicial Center (November 4, 1988) commenting on National Association of Attorneys General ("NAAG"), Draft Guidelines of the Task Force on Car Rental Industry, Advertising and Practices (1988) and to The Honorable Robert T. Stephan, Attorney General of Kansas (February 24, 1989), commenting on NAAG, Final

Guidelines of the Task Force on Car Rental Industry Advertising and Practices (1988); and letters from Commission Staff to The Honorable James R. Thompson, Governor of Illinois (December 22, 1988) and The Honorable Thomas F. Allgood, Georgia State Senate (November 20, 1989) commenting on pending state legislation governing the sale of CDW.

4. ILCS Sec. 6-305(f).

5. H.B. 3285, Sec. 10.

6. H.B. 3285, Sec. 15(a).

7. H.B. 3285, Sec. 15(b).

8. H.B. 3285, Sec. 15(c).

9. H.B. 3285, Sec. 20(a) and (b) (proposed amendments). Contracts would have to include a specified disclosure statement, set apart in boldface type no smaller than 10 point. The disclosure, in 10 point boldface type, is:

NOTICE: This contract offers, for an additional charge, a collision damage waiver to cover your financial responsibility for damage to the rental vehicle. The purchase of a collision damage waiver is optional and may be declined. You are advised to carefully consider whether to sign this waiver if you have rental vehicle collision coverage provided by your credit card or collision insurance on your own vehicle. Before deciding whether to purchase the collision damage waiver, you may wish to determine whether your own vehicle insurance affords you coverage for damage to the rental vehicle and the amount of deductible under your own insurance coverage.

10. H.B. 3285, Sec. 20(c).

11. H.B. 3285, Sec. 20(d).

12. H.B. 3285, Sec. 20(e).

13. H.B. 3285, Sec. 25, would require that any mandatory charge be fully disclosed and prominently displayed on the face of the rental agreement and in all price advertisements, displays, quotes, or offers (including computer reservation systems). A "mandatory charge" is defined as "any charge, surcharge, or fee in addition to the base rental rate for an item or service provided in connection with the rental transaction that the renter does not have the option of avoiding or declining and that is not otherwise imposed by law."

14. ILCS Sec. 6-305(b). The list of causes for which a renter may now be held liable is the same as the list of causes for which a rental company might void a CDW under H.B. 3285; see text at n. 7, supra.

15. H.B. 3285, Sec. 30. If a rental car is stolen and the renter failed to exercise due care (or committed or abetted the theft), the rental company could recover for the costs due to the loss, up to the vehicle's fair market value. The rental company could not collect multiple recoveries, would be required to obtain and submit appraisals or estimates before recovering, and would be required to mitigate its damages. The rental company would be prohibited from requiring a deposit or advance charge against a credit card to cover prospective damage, and from requiring any payment for damage when a vehicle is returned until after the cost is agreed to or determined by law. And if a renter has personal insurance, the renter could require the rental company to deal with the renter's insurance company directly.

16. When renters know they will not be liable for negligent damage, they may be less careful and suffer more accidents. The losses would fall on the rental companies, increasing their costs to repair and replace vehicles. Those increased costs would likely be passed through to consumers as higher rental rates. For theoretical treatment of the

relationship between liability standard and accident rates, see Brown, *Toward an Economic Theory of Liability*, 2 J. Legal Stud. 323 (1973); Diamond, *Single Activity Accidents*, 3 J. Legal Stud. 107 (1974); and Shavell, *Strict Liability vs. Negligence*, 9 J. Legal Stud. 1 (1980). For an effort to measure how accident rates and costs vary under different liability and insurance regimes, see Sloan et al., *Tort Liability Versus Other Approaches for Deterring Careless Driving*, 14 Int'l Rev. L. & Econ. 53 (1994).

17. Potential renters may opt not to rent rather than pay the higher bundled price. This results in a reduction in output in the car rental industry.

18. A telephone survey by the US Public Interest Research Group in 1994 found that average rental rates in Illinois and New York were about 10 percent higher than the national average (about \$27.50, compared to about \$25.00). The same survey found the average CDW rate quoted nationally was about \$11.00, more than four times the difference in average basic rental rates. Based on these data, if only about a quarter of renters actually buy CDW, then the total rental costs in the banning states would be about the same as the national average total. The report of this survey does not indicate clearly how the survey sample was selected, and other surveys might reach different results about the extent or reasons for discrepancies in rates.

19. For a statement of this principle, see *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 770 (1975):

There is, of course, an alternative to this highly paternalistic approach. That alternative is to assume that this information is not in itself harmful, that people will perceive their own best interest if only they are well enough informed, and that the best means to that end is to open the channels of communication rather than to close them.

20. We should note, however, that the disclosures about CDW that would be required under H. B. 3285 have some potential to create problems in advertising, such as 15 or 30 second radio or television spots. These disclosures could cause advertisers to avoid referring to the rental price, resulting in less price advertising and less price competition.