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**COMMISSION
APPROVED**

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On Behalf Of

Dallas Regional Office And Bureaus
Of Competition, Consumer Protection,
And Economics Of The Federal Trade Commission

Before the

TEXAS MOTOR VEHICLE COMMISSION

Proposed Amendments To Chapter
105 Of The Advertising Rules Of The Texas
Motor Vehicle Commission

March 26, 1986

I am pleased to have the opportunity to comment on the proposed amendments to the advertising rules of the Texas Motor Vehicle Commission ("Commission"). These comments represent the views of the Dallas Regional Office and the Bureaus of Competition, Consumer Protection, and Economics of the Federal Trade Commission ("FTC"). They do not necessarily represent the views of the Commission or of any individual Commissioner. The Commission, however, has authorized the staff to submit these comments. Our comments are directed at the proposed modification to Section 105.12 of the Texas Motor Vehicle Commission's advertising regulations which would prohibit "invoice" advertising.¹

We cannot support the ban on invoice advertising as proposed by the Texas Motor Vehicle Commission. Restrictions on advertising have the potential to harm competition without increasing the quality of service that is provided. As a general rule, it is far more efficient and less expensive to address problems of misleading consumer information by requiring fuller disclosure of information than by attempting to ban advertising. This rule applies to the automobile industry. We are aware of no empirical studies which show that consumers have been deceived by the invoice advertising of automobiles. To the contrary, invoice advertising has been shown to be procompetitive. It provides some accurate and verifiable

¹ We have no comments with respect to the proposed amendments to Sections 105.3, 105.5, 105.8-.10, and 105.21 of the Commission's rules.

information about the cost of automobiles. It may reduce consumer search costs and it enhances comparison shopping. On balance, automobile invoice advertising is helpful to consumers. We believe, therefore, that the Commission should continue to permit invoice advertising, and if it finds some restriction on the advertising to be warranted, rather than banning all use of invoice information, it should simply prohibit advertisers from referring to invoice price without also disclosing that invoice price is not necessarily the same as dealer cost.

I. INTEREST AND EXPERIENCE OF THE FEDERAL TRADE COMMISSION

The FTC is empowered by Congress to prevent unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce. Pursuant to its statutory mandate, the FTC encourages competition among members of licensed groups, such as the learned professions, to the maximum extent compatible with other legitimate state and federal goals.

As a part of the FTC's effort to foster competition among licensed groups, it has examined the effects of public and private restrictions that limit the ability of licensed groups to

engage in nondeceptive advertising.² Studies show that prices for goods and services provided by licensed groups are lower where truthful advertising freely exists than where it is restricted or prohibited.³ Federal Trade Commission and independent studies also provide evidence that restrictions on truthful advertising are not associated with an increase in the

² See, e.g., American Medical Association, 94 F.T.C. 701 (1979), aff'd, 638 F.2d 443 (2d Cir. 1980), aff'd mem. by an equally divided Court, 455 U.S. 676 (1982). The thrust of the AMA decision -- "that broad bans on advertising and soliciting are inconsistent with the nation's public policy" (94 F.T.C. at 1011) -- is consistent with the reasoning of recent Supreme Court decisions involving professional regulations. See, e.g., Zauderer v. Office of Disciplinary Counsel of the Supreme Court of Ohio, 105 S. Ct. 2265 (1985) (holding that an attorney may not be disciplined for soliciting legal business through printed advertising containing truthful and nondeceptive information and advice regarding the legal rights of potential clients or using nondeceptive illustrations or pictures); Bates v. State Bar of Arizona, 433 U.S. 350 (1977) (holding state supreme court prohibition on advertising invalid under the First Amendment and according great importance to the role of advertising in the efficient functioning of the market for professional services); and Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748 (1976) (holding Virginia prohibition on advertising by pharmacists invalid).

³ Cleveland Regional Office and Bureau of Economics, Federal Trade Commission, Improving Consumer Access to Legal Services: The Case for Removing Restrictions on Truthful Advertising (1984); Bureau of Economics, Federal Trade Commission, Effects of Restrictions on Advertising and Commercial Practice in the Professions: The Case of Optometry (1980); Benham and Benham, Regulating Through the Professions: A Perspective on Information Control, 18 J.L. & Econ. 421 (1975); Benham, The Effects of Advertising on the Price of Eyeglasses, 15 J.L. & Econ. 337 (1972).

quality of services available in the marketplace.⁴ The FTC's goal is to identify and seek the removal of those restrictions that impede competition, increase costs, and harm consumers without providing countervailing benefits. Therefore, to the extent that truthful advertising is restricted, higher prices and a decrease in consumer welfare may result without any corresponding increase in quality.

We appreciate the delicate balance that often must be struck between the desire for consumers to have access to useful information and the necessity of preventing deception. However, it is important to recognize that advertising prohibitions imposed to protect consumers can themselves be the source of consumer injury. Advertising prohibitions may reduce the dissemination of information that might potentially mislead some consumers, but prohibitions may also reduce the dissemination of accurate information that would assist many others in making purchasing decisions. For these reasons, we believe that only advertising which is false or deceptive or otherwise causes substantial consumer injury without offsetting benefits should be prohibited in the marketplace. Any other standard is likely to reduce consumers' exposure to information that is potentially useful, and may contribute to an increase in prices or a decrease

⁴ Muris and McChesney, Advertising and the Price and Quality of Legal Services: The Case for Legal Clinics, 1979 AM. B. Found. Research J. 179 (1979); Cady, Restricted Advertising and Competition: The Case of Retail Drugs (1976). See also Bureau of Economics, Federal Trade Commission, Effects of Restrictions on Advertising and Commercial Practice in the Professions: The Case of Optometry (1980).

in consumers' ability to choose effectively between competing goods and services. If consumers are shown to be misled about a particular issue, moreover, the best remedy is usually to require fuller disclosures on that specific issue, rather than to ban an entire class of advertisements.

II. THE PROPOSED AMENDMENT TO SECTION 105.12 OF THE COMMISSION'S RULES

Automobile dealers in Texas are currently permitted to engage in "invoice" or "invoice plus" advertising (e.g., "\$49 over invoice," "5% over invoice"). The proposed amendment to Section 105.12 of the Commission's rules would prohibit this type of advertising.

The reason for this proposed change appears to be a concern that consumers may equate the "invoice price" of a vehicle with the dealer's cost. As we understand it, the invoice price is the base price the manufacturer charges a dealer for an automobile. The actual dealer's cost for an automobile, however, depends upon other factors, such as manufacturers' rebates, sales incentive plans, ad allowances, and prices paid to other dealers to acquire cars that are in great demand, which are not reflected in the

invoice.⁵ There is concern therefore, that in the face of advertising based on invoice price, which does not take account of adjustments made to arrive at dealer costs, consumers will conclude that they are receiving a better bargain than they really are and will not shop aggressively for the lowest price that they could obtain.

A. Benefits from Invoice Advertising

However, invoice-based price advertising does provide valuable information which can substantially assist consumers in making automobile purchasing decisions.⁶ The invoice is a document in the dealer's possession which contains some

⁵ The proposed modification to Section 105.12 would prohibit the use of advertising which contains the terms "invoice" or "invoice price" or other terms "which refer to the cost of the vehicle to the dealer or imply that the vehicle is being offered for sale at the dealer's cost." The language of the proposed modification therefore indicates that the basis for the proposed rule change is a concern that consumers may confuse the "invoice" price with the actual "dealer cost."

⁶ Conversely, other terms, such as "dealer cost," may be significantly more misleading to consumers. Cost and profit figures may be calculated in a variety of ways, rendering them of little shopping value to consumers. Moreover, because of manufacturers' rebates, sales incentive plans, and other allowances, it is difficult for an automobile dealer to know the true cost of a vehicle at the time when it is being advertised for sale.

information about the dealer's costs in obtaining the vehicle.⁷ This information, including the total invoice price of the vehicle, can be verified by the consumer simply by viewing the invoice. The purchase of a new car differs from most other retail purchases in that the actual selling price is typically negotiated between the seller and the buyer. Consequently, information about the seller's costs can substantially aid prospective car purchasers in their negotiations by helping them to estimate what price the seller might be willing to accept. Even if this invoice information is "imperfect" in the sense that it does not reflect any rebates or other adjustments that may affect the dealer's ultimate cost, it is nonetheless quite useful to consumers. The value of invoice price information to consumers is evidenced by the fact many consumers are willing to purchase this type of information from publications such as Consumer Reports or auto purchasing guidebooks. Without this type of information, the average consumer will often be at a substantial disadvantage in identifying and negotiating the lowest possible price.

Moreover, invoice-based advertising is helpful to consumers who are comparison shopping. The invoice amount for like make and model automobiles with identical equipment does not vary

⁷ The invoice does not contain information about manufacturers' rebates, sales incentive plans, ad allowances and other factors affecting the dealer's total cost of vehicles. These figures are often unknown until long after the dealer has obtained the vehicle and sold it to the consumer. Moreover, because these payments often depend on a dealer's total sales volume, they are analogous to overhead expenses and cannot be unambiguously assigned to any individual vehicle.

among competing dealers in a given geographic market; it can provide a benchmark to which consumers can compare the offers of competing dealers. Thus, permitting dealers to advertise on an invoice basis improves the ability of consumers to compare prices of various dealers on the same make and model of automobile. In addition, invoice advertising can also help consumers focus on the dealer cost of various equipment options, since any variance between the price of two automobiles, both of which are advertised "at dealer invoice," will be attributable to the differences in equipment.

A ban on invoice advertising would increase consumers' "search costs," making it more difficult for consumers to obtain the useful information found on the invoice. These costs--the time, effort, expense and inconvenience incurred by consumers in obtaining purchasing information--are difficult to measure, but they are real.⁸ As Judge (then Professor) Robert Bork noted, increasing the inconvenience of shopping for automobiles is no different from raising automobile prices.⁹

Further, economic research has established that when search costs for shoppers decrease, the prices of the products they are looking for will also decrease.¹⁰ The explanation for this effect is that shopping is not much different from other

⁸ Stigler, "The Economics of Information," Journal of Political Economy, June 1961, pp. 213-25.

⁹ Bork, The Antitrust Paradox, Basic Books, pp. 85-86 (1978).

¹⁰ See, e.g., Carlson & Gieseke, "Price Search in a Product Market," Journal of Consumer Research, March 1983, pp. 357-65; Stigler, supra.

activities that involve sacrifices: when shopping costs less (i.e., is made less difficult), people do it more.¹¹ If consumers shop more, they are likely to learn more about competing goods and prices. This increased knowledge of pricing information enhances consumers' ability to obtain the best bargains available, thereby increasing competition among sellers to sell higher quality products at the lowest possible prices. The fact that a decrease in search costs will lead to a decrease in prices has been documented in such diverse economic sectors as groceries,¹² eyeglasses,¹³ and legal services.¹⁴

Lastly, we note that in a market like autos, where almost all prices are negotiable, it may be difficult for a dealer to undertake effective price advertising. Invoice ads can be an effective means of informing the public that the dealer sells cars at a "low markup," and thus can provide valuable information to potential purchasers.

In light of these reasons, we feel that a prohibition on invoice-related advertising could result in injury to consumers, as well as reduced competition among dealers. The question is whether the ban would provide consumer benefits that outweigh these costs.

¹¹ Morrison & Newman, in "Hours of Operation Restrictions and Competition Among Retail Firms," Economic Inquiry, Vol. XXI, January 1983, observed that shoppers were less likely to take extended shopping trips when stores were closed on Sundays.

¹² Carlson and Gieseke, supra.

¹³ See note 3, supra.

¹⁴ Id.

B. Injury from Invoice Advertising

The apparent reason for a ban on invoice-related advertising is the concern that some consumers will confuse references to the dealer's "invoice" price with references to the dealer's actual cost. It is unclear to what extent such confusion exists. Indeed, we are not aware of any empirical studies that indicate consumers generally confuse the term "invoice amount" with the dealer's actual cost.

Moreover, consumers shopping for an automobile are seeking the best combination of a low purchase price and the vehicle characteristics they desire. Since any rebates or allowances would not directly alter that combination of consumer price and characteristics, it is unclear whether consumers would modify their purchasing decisions if they were aware that the dealer might receive a rebate or other payment from the manufacturer. A consumer could conceivably purchase a car in the belief that by purchasing "at invoice," he had received the lowest possible price, and the consumer might thereby forego the opportunity to seek an even lower price. But advertising and competition among dealers offering even lower prices should assure that consumers will learn of the availability of lower prices.

In addition, the invoice price may be below the actual dealer cost for dealers who pay premiums to other dealers to acquire popular models. In these instances, consumers who confuse invoice price with ultimate dealer cost would not appear to be injured.

Accordingly, we believe that the possibility of consumer injury from invoice-related advertising does not outweigh the apparent information-enhancing and competitive benefits that such advertising can provide. Thus, we believe there is insufficient justification for a total ban on such advertising.

C. An Alternative Approach

Although we do not support a ban on a ban on invoice-related advertising, if the Motor Vehicle Commission believes some restriction on invoice-based advertising is needed, it could take some action short of a ban to minimize the possibility that references to an automobile's invoice price might confuse consumers. It could amend its rule to require that dealers who advertise on an invoice basis disclose in their ads that the invoice price may not equal the dealer's actual cost. Such a disclosure would certainly be less costly to consumers than an outright ban on invoice-based advertising, because it would preserve the benefits that consumers and competition derive from invoice-based advertising. This disclosure would also substantially reduce any confusion associated with invoice advertising and thereby prevent any injury that might flow from the confusion. Accordingly, if the Motor Vehicle Commission concludes that the risk of consumer harm from invoice-based advertising is great enough to necessitate any regulatory intervention, we believe a disclosure requirement is clearly preferable to an outright prohibition on truthful claims.

III. CONCLUSION

We do not support the ban on invoice advertising to be imposed by the proposed amendment to Section 105.12 of the Commission's rules. Given the procompetitive benefits which may be associated with invoice advertising, and in the absence of evidence indicating that such advertising is likely to injure consumers, we believe that automobile dealers in Texas should be permitted to continue this advertising practice. If the Commission determines, nonetheless, that some limitation on invoice-based advertising is warranted we support the addition of a disclosure requirement to accompany advertising referring to invoice price.

We thank you for your willingness to consider our comments. We have referred to a number of studies in these comments. We will be happy to supply a copy of any of these if you so desire.

I now stand ready to answer any questions that the Texas Motor Vehicle Commission may have.