January 31, 2012

Consumers for Auto Reliability and Safety (CARS)
Comments submitted in response to the request for comments from the Federal Trade Commission Motor Vehicle Roundtables Project Number P104811

First, thank you to the Commissioners, the Director of the Bureau of Consumer Protection, and all the FTC officials and staff who participated in and contributed to the Motor Vehicle Roundtables. We very much appreciate having been invited to participate on the panels, and also welcome the opportunity to submit further comments.

I. Scope of the problem

Data from CFA / NACCA / NACPI Annual Surveys

According to annual surveys conducted and released by the Consumer Federation of America, National Association of Consumer Agency Administrators, and North American Consumer Protection Investigators, auto sales and related complaints perennially top the list of consumer complaints filed with state and local consumer protection agencies. The most recent report, released July 27, 2011, was based on a survey of 31 state, county and city agencies in 18 states across the U.S. It does not include inquiries or requests for assistance that were not made in the form of a complaint.

That report found that once again auto complaints ranked #1 on the list of the Top Ten consumer complaints. The most common auto complaints were "misrepresentations in advertising or sales of new and used cars, lemons, faulty repairs, and leasing and towing disputes." [1]

1 2010 Consumer Survey Report, compiled and released by the Consumer Federation of America, National Association of Consumer Agency Administrators, and North American Consumer Protection Investigators, July 27, 2011, page 5.

Data from Better Business Bureau Annual Surveys

In the most recent annual consumer complaint survey published by the Better Business Bureau (BBB,) new car dealers ranked #3 and used car dealers ranked #6, in terms of complaints, by industry. Combined, they ranked #1.[2]

Year after year, the Better Business Bureau's survey finds that when complaints against both new and used car dealers are combined, more consumers complain about auto dealers than any other businesses. Part of what is so striking about the BBB's recent data is that even at a time when the home mortgage market collapsed and complaints against banks received more attention from the media and regulators, those complaints were still outstripped by complaints against auto dealerships.

While the BBB also reports that a high percentage of complaints were "resolved," it is important to note that does not necessarily mean that the consumers received any relief or were satisfied by the dealership.

Auto industry expert warns: lending fraud on the rise

Further confirming the scope and widespread nature of consumer problems regarding auto sales and lending practices, as reported in *Automotive News*, the auto industry's leading trade publication:

"... lending fraud is rising, said auto finance consultant Gil Van Over. More dealership employees and customers are falsifying credit [applications] and financing documents, Van Over said. Lenders, he added, are seeing more false income statements, phony down payments and 'power booking' -- a dealership practice of reporting nonexistent options as part of a vehicle sale to justify a bigger loan. Even large dealership groups that closely audit their finance operations are not immune."[3]

J.D. Power survey: sales lost due to dishonesty

One of the leading companies that rates customer satisfaction with products and services has surveyed car buyers and found that a significant percent of consumers who decided not to purchase vehicles at certain dealerships cited their perception that the dealer personnel were "not honest" or "would not give them a firm price." This should be an indicator for auto dealers that shady, overly aggressive sales practices can be counter-productive and actually cost them sales.

As reported in *Automotive News*:

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2 "Complaints to Better Business Bureau up ten percent nationwide," Better Business Bureau, April 1, 2011. Note: While dealers may claim that they "resolved" a large percentage of cases, that does not necessarily mean that they offered the consumers any relief or satisfied consumers who complained.

3 "Tighter credit squeezes dealers, consumers," *Automotive News*, Feb. 2, 2009. Mr. Van Over is described on his company's website as a founding member of DealerTrack's Compliance Advisory Council, which provides expertise to auto dealers regarding new laws and regulations.

"Every year, J.D. Power and Associates issues a report card on how well auto buyers like their purchase experiences -- the consultant's Sales Satisfaction Index. But this year Power also did some digging into why sales didn't happen. 'We asked the 51% of buyers who visited more than one dealer why they didn't buy where they went first,' says John Osborn, media/marketing research director for the Westlake Village, Calif. firm. 'More than one in five walked because of something the dealer did.'...for 21 percent of lost sales, the dealer simply blew it. The study based on responses from 48,000 customers who bought or leased a new vehicle in May or June 2009, identified six no-sale sins, says Osborn. "Dealer personnel were rude, not honest, not knowledgeable, pressed customers too hard, ignored them or wouldn't give them a firm price.'"[4]

Numbers of complaints are low compared with prevalence of bad practices

In assessing the scope of the problem, it is important to keep in mind that it is a widely acknowledged rule of thumb that for every complaint that is filed, there are many more dissatisfied customers who did not bother to file a complaint. Instead, like the consumers in the J. D. Power survey, they may have simply taken their business elsewhere, or decided that next time they will purchase a vehicle from a private party, instead of a dealership. Approximately 25% of used car sales take place among private parties, an indicator that when market forces can come into play, a substantial part of the market opts to reject auto dealers altogether.

In the auto context, it is also important to recognize that it is the inherent nature of fraud, which involves concealment, deception, and misrepresentation, that its victims are often not aware they have been defrauded, and therefore are unlikely to complain. Some types of auto sales scams are extremely lucrative and widespread precisely because they are unlikely to trigger consumer complaints at all. The only way they come to light is through laborious research or legal discovery and expert analysis of documents, a very costly process. Many common auto scams do not generate complaints in proportion to how pervasive or costly the practices are, simply because the consumers generally remain unaware they have been scammed. Among the practices that fall into this category:

- Dealer markups
- Loan packing
- Power booking
- Falsified loan applications (often altered after the consumer has signed)
- Forgery
- Odometer fraud
- Salvage and rebuilt wreck / flood car fraud

In addition, many of the most pervasive scams are highly sophisticated. For example, companies sell software and offer training to dealership employees that allows dealers to increase the profit margins on finance and insurance products added on at the back end of the deal. Typically, this is the least open and transparent part of the transaction. Consumers, who may purchase a vehicle once every few years, or once in a decade or more, are at a

4"Power study finds 6 no-sale sins," Automotive News, December 14, 2009.

relative disadvantage, when faced with a trained F & I manager who may get paid $200,000 a year or more, mostly in commissions and bonuses, for inflating the profit margin in each sale.

Also, consumers are at a distinct disadvantage in assessing the condition and history of vehicles prior to purchase. Given the tremendous technological complexity of today's cars, consumers are at an even greater disadvantage than in the past. It takes expensive automotive diagnostic equipment, computers, and training in order to be able to retrieve and analyze computer "trouble codes" that are tell-tale signs to those who are in the business. Dealers are also fully aware whether they obtained a vehicle from a salvage pool, a fact that may not appear in heavily-promoted vehicle history report databases for weeks, too often giving car buyers a false sense of security when they are presented with a "clean" vehicle history report on a flood car or rebuilt wreck.

II. Why it is important for the FTC to act

Many factors make it all the more important and timely for the FTC to bring enforcement measures and promulgate rules aimed at curbing some of the worst abuses perpetrated by auto dealers, in order to protect the car buying public. Among them:

Failure of market forces

Auto dealers are uniquely positioned to be insulated from market forces. Among the reasons market forces are inadequate to address dealer scams are the below:

Dealer monopolies

Dealers are granted special monopolies under state franchise laws. All 50 states provide dealers a monopoly on new car sales. Attempts at the state level to open up the new car market to competition have been killed by auto dealers and their lobbyists. Thus, with rare exceptions (such as purchases abroad), the entire American new car market is held captive to the auto dealers. The auto dealers' monopoly on new car sales means that effective state and federal regulation is all the more appropriate and necessary.

As the *Washington Post* editorialized, "...one reason it took bankruptcy to prune the dealer network is that they have long been protected from market forces by a thick web of state franchise laws." [5]

Dealer censorship

During the roundtables convened by the FTC, auto dealers and representatives from their trade associations claimed that consumer education is adequate to address the problems in the automotive marketplace. However, those remarks are somewhat disingenuous, considering the widespread, longstanding pattern of dealer actions aimed at suppressing even the most basic consumer information about unsafe vehicles, low-value / high-price add-on products, vehicle pricing, lending practices, and negotiating tactics at auto dealerships.

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5 *Washington Post* Editorial, December 12, 2009.

As reported by the *American Journalism Review*:

> "Retaliatory attacks on television stations that air hard-hitting reports have also paid off for auto dealers. 'We don't even bother with most auto-related stories anymore' [wrote a consumer reporter] ...in the monthly journal published by Investigative Reporters and Editors. "'These days, even a simple consumer education story on how to buy a new car can draw the wrath of local car dealers. Trying to share such basic advice with your viewers can result in the loss of many thousands of dollars."[6]

A survey of 50 randomly chosen newspaper editors conducted by *Consumer Reports* found that " Roughly one-third of the journalists questioned said they had stopped running stories about cars and car-buying because of friction -- or anticipated friction -- from dealers. *Consumer Reports* also noted that "The dealers aren't apologetic about flexing their muscle...a spokesman for the 10,000-member National Automobile Dealers Association says it's illegal for dealers to organize a boycott of a particular news organization. 'But, he adds, 'dealers do have the right to spend their ad dollars as they see fit.'"[7]

According to a press release issued by the FTC :

> "After the *San Jose Mercury News* ran an article in May 1994 telling consumers how to analyze new car factory invoices so that they could be better negotiators when buying cars, local car dealers retaliated by conspiring to cancel their advertising in the paper, according to the Federal Trade Commission. That's illegal, the FTC charged. The car dealers could have made individual decisions to pull their advertising, but an agreement to do so restrains competition among dealers and chills the publication of important consumer information, making it more difficult for consumers to compare dealer prices and services.[8]

As the press release states, the consent agreement applied only to the trade association and not individual dealer members, who remain free to withhold advertising dollars whenever they please -- a very large hammer, especially given the precarious financial circumstances of newspapers in today's economic climate.

Since then, auto dealers have continued to exercise their market power as advertisers to either threaten news organizations or outright boycott them, in an attempt to censor the news and deprive consumers of information that is crucial for making informed decisions.

For example, auto dealers either withheld advertising or made the threat, targeting the following news organizations:

- TV news affiliates in Los Angeles -- dealers pulled ads in response to major investigative reports about allegations of widespread fraud at Gunderson Chevrolet, owned by AutoNation, and the largest GM dealership in the U.S. At the time, the dealership was under investigation by the California Department of Motor Vehicles and the Los Angeles District Attorney's High Tech Crimes Unit. Eventually, the DMV

6 "Auto dealers muscle the news room," *American Journalism Review,* September, 1991.
7 "Are automobile dealers editing your local newspaper?" *Consumer Reports*, April 1992.
8 Santa Clara County Auto Dealers Association settles charges over alleged advertising boycott. Press release issued by FTC, August 1, 1995.

suspended the dealer's license and several managers and other personnel were criminally convicted of committing fraud. [9]

- *Los Angeles Times* -- starting April 7, 2005, General Motors and some of its dealers in California reportedly pulled an estimated $10 million in advertising from the *Los Angeles Times*, in retaliation against the newspaper for reports critical of GM products, management, and certain auto dealer practices. The ad boycott lasted until August, 2005.

- ABC News affiliates -- in 2010, auto dealers openly pulled ads from ABC News affiliates in various parts of the country, in retaliation for their airing breaking news reports from the ABC network about the Toyota sudden acceleration defect and Toyota's cover-up. The cover-up led to a record fine, paid by Toyota and assessed by the U.S. Department of Transportation.

- News organizations across the U.S. -- during the debate in Congress over whether to include auto dealers under the jurisdiction of the Consumer Financial Protection Bureau, auto dealers exerted pressure against news organizations that sought to cover the debate and expose the dealers' practices.

Harmful impact of binding mandatory arbitration on consumers[10]

Nearly all auto dealer contracts now include one-sided clauses that impose binding mandatory arbitration (BMA) on consumers. The clauses are presented on a take-it-or-leave-it basis, as a condition for purchasing vehicles. In some cases, when consumers attempted to cross out the clauses, dealers refused to sell them a vehicle. BMA has dramatically altered the balance of power between unscrupulous dealers and their victims, who usually were already at a disadvantage. It has deprived consumers of their constitutional right to a trial by jury, and deprived them of any access to justice. It has given dealers carte blanche to engage in blatantly illegal practices, with little or no fear that their customers can protect themselves.

By inserting BMA clauses into auto sales and leasing contracts, auto dealers force wronged consumers into biased forums that are funded by the dealers themselves, where the arbitrators know that if they rule in favor of the consumer, they risk being black-balled from deciding future cases. In some cases, consumers have become trapped in a Catch -22 situation, unable to access even the biased arbitration forums because their contractual agreement calls for the dealer to pay a charge to initiate the arbitration proceeding, and the dealer refuses to do so.

Unlike judges, arbitrators are not sworn to uphold the law. In fact, they are generally trained to ignore the law. Thus, the law may be 100% on the consumer's side, but it is never applied. Consumers who are victims of even the most blatant frauds are not able to obtain relief under longstanding federal or state laws, because the arbitrators have an inherent

9 The dealership was subsequently renamed "Power Chevrolet."

10 For further information about the impact of binding mandatory arbitration on car buyers, please see testimony provided by CARS before the U.S. House of Representatives Committee on the Judiciary Subcommittee on Commercial and Administrative Law, posted at: http://carconsumers.org/HR5312_testimony.htm.

conflict of interest and have strong incentives to ignore the laws.

The imposition of arbitration also allows auto dealers to keep their practices hidden from view, from regulators and the public. The results of arbitration are usually kept secret, as are the allegations themselves. Before, the possibility of a lawsuit sometimes served as a deterrent. That deterrent effect is now gone.

As U.S. Senator Charles Grassley stated in support of legislation sought by the auto dealers, to provide them with a special exemption from the Federal Arbitration Act, freeing them from being forced into arbitration in their contracts with auto manufacturers:

> "While arbitration serves an important function as an efficient alternative to court, some trade-offs must be considered by both parties, such as limited judicial review and less formal procedures regarding discovery and rules of evidence. When mandatory binding arbitration is forced upon a party, for example when it is placed in a boiler-plate agreement, it deprives the weaker party the opportunity to elect another forum. As a proponent of arbitration I believe it is critical to ensure that the selection of arbitration is voluntary and fair…Unequal bargaining power exists in contracts between automobile and truck dealers and their manufacturers. The manufacturer drafts the contract and presents it to dealers with no opportunity to negotiate…The purpose of arbitration is to reduce costly, time-consuming litigation, not to force a party to an adhesion contract to waive access to judicial or administrative forums for the pursuit of rights under State law....This legislation will go a long way toward ensuring that parties will not be forced into binding arbitration and thereby lose important statutory rights. I am confident that given its many advantages arbitration will often be elected. But it is essential for public policy reasons and basic fairness that both parties to this type of contract have the freedom to make their own decisions based on the circumstances of the case." [11]

Although the legislation Senator Grassley championed, S 1140, did not pass, the dealers were still granted their special exemption from the Federal Arbitration Act. At the time, the National Automobile Dealers Association wrote to Congress and promised that they would not oppose restoring the same rights to consumers. However, subsequently, the dealers opposed and defeated H.R. 5312, which would have simply restored the same rights dealers enjoy, to their customers.

Under the U.S. Supreme Court's 2011 ruling in *Concepcion v. AT &T*, consumers are further disadvantaged, deprived of their ability to band together to address widespread illegal activity perpetrated by repeat offenders, through class actions.

Therefore, it is all the more important for the FTC to act, as consumers are increasingly powerless to vindicate their rights themselves.

Lack of Enforcement

One of the key points made by the state and local agencies who contributed to the annual consumer complaint survey released by the Consumer Federation of America, National Association of Consumer Agency Administrators, and North American Consumer

11 Statements on Introduced Bills and Joint Resolutions, United States Senate, June 29, 2001. Statement by Senator Grassley of Iowa in support of S 1140.

Protection Investigators was that budget cutbacks have hamstrung the ability of state and local consumer protection agencies to protect the public.

That reality also holds true for state attorneys general and district attorneys. In California, the largest auto market in the country, budget constraints have resulted in severe reductions in professional staff. Even before the economic meltdown, enforcement over auto consumer complaints was typically viewed mostly as a matter for private litigation.

In order to ascertain the level of public enforcement of state laws aimed at protecting car buyers, in September, 2007, CARS filed Public Records Act requests with the Attorney General and the District Attorneys in each of the 58 counties in the state. The requests sought information about "complaints filed, citations issued, or any other disciplinary action taken regarding the sales practices of licensed automobile dealerships under your agency's jurisdiction, involving transactions that occurred after July 1, 2006," when the state's Car Buyers Bill of Rights took effect.

Of the 58 counties, only 5 district attorneys responded that they had taken any action to discipline auto dealers during that period of time, when several million transactions occurred. Of those, 2 brought only 1 case, one brought 3 cases, and San Diego brought 9.

It is important to note that during 2007, the California District Attorneys Association was sponsoring legislation, SB 729, that was enacted to establish a Consumer Recovery Fund to provide restitution for victims of dealerships that scammed car buyers and then went out of business, leaving their customers in the lurch. The District Attorneys documented numerous examples of dealerships that closed their doors without paying off liens on traded-in vehicles or engaged in other deceptive practices, sometimes costing hundreds of consumers millions of dollars in losses, resulting in repossessions and ruining their credit.

The Attorney General responded that his office had not taken any actions. A further inquiry into whether the Attorney General had ever acted to protect military servicemembers or their families from unscrupulous auto dealerships, the Attorney General's office responded that, after looking back over approximately 30 years, they were unable to find a single case.

This is despite the fact more members of the Armed Forces are stationed in, or deployed from, California than any other state. Approximately 160,000 Servicemembers and their families reside in California. According to testimony by representatives of the Armed Forces and the Relief Societies who provide assistance to military families, the leading cause of financial readiness problems for members of the Armed Forces stationed in California is auto sales practices, particularly yo-yo financing. [12]

Before the FTC accepts any argument by auto dealers that FTC enforcement or rulemaking is not needed, we urge the FTC to request that the auto dealers provide hard data and documentation to back up their claims that they are already adequately regulated by other agencies or law enforcement officials.

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12 Quotations and excerpts from testimony presented before a legislative committee in California, the National Consumer Law Center's publication "In Harm's Way -- At Home: the Direct Targeting of America's Military and Veterans," news reports, and military sources including the U.S. Department of Defense and Secretaries of the Army and Air Force are posted on CARS' website, at: http://www.carconsumers.org/military_ripoffs.htm.

FTC action still needed on Used Car Rule

As Iowa's Special Assistant Attorney General Bill Brauch, head of the National Association of Attorneys General Working Group on Auto Issues, and Greg Grzeskiewicz, Assistant Attorney General of Illinois, stated at the FTC Roundtable in Washington, D.C., a number of other harmful practices involving auto sales continue to plague consumers, such as salvage fraud odometer fraud, unpaid liens, and other unfair and deceptive practices. As they asserted, and as documented in comments filed with the FTC by CARS, the National Consumer Law Center, and other consumer groups, regarding the Used Car Rule, used car sales pose particularly serious and widespread problems for car buyers.

CARS urges the FTC to improve the Used Car Rule, as advocated by numerous consumer groups, in the comments jointly submitted to the FTC on November 19, 2008.

Thank you again for the opportunity to participate in this important process. Should you have any questions regarding statements made at the Roundtables, or these comments, we would be most willing to provide more details upon request.

Respectfully submitted,

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