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FEDERAL TRADE COMMISSION
Chicago Regional Office

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March 21, 1989

COMMISSION AUTHORIZED

The Honorable Aldo A. DeAngelis
Assistant Minority Leader
Senate of the State of Illinois
309 State Capitol
Springfield, Illinois 62706

Dear Mr. DeAngelis:

The staff of the Federal Trade Commission's Chicago Regional Office and Bureau of Competition are pleased to have this opportunity to respond to your letter of February 21, 1989, requesting our comments on amendments to the Illinois Vehicle Code provided for in Senate Bill 1978.¹ It is our understanding that this legislation was passed on January 10, 1989, the final day of the 85th legislative session, and that these amendments were not debated either on the floor or in committee.² These amendments, if they become effective, may reduce competition and increase the prices paid by Illinois consumers for new and used cars. We believe that consumers will be best served if competition in the sale of automobiles in Illinois is not restricted unnecessarily.

This legislation makes two principal changes in the Illinois Vehicle Code, each of which is likely to prohibit innovative forms of competition in automobile sales.³ First, this legislation defines "broker" and prohibits "brokers" from selling new and used cars. Second, S.B. 1978 expands the dealer licensing provisions of the Illinois Vehicle Code

¹ These comments represent the views of the staff of the Federal Trade Commission's Chicago Regional Office and Bureau of Competition and do not necessarily represent the views of the Commission or any individual Commissioner.

² The Bill and its amendments will become law if Governor Thompson does not veto the Bill by April 6, 1989.

³ S.B. 1978 amends Sections 5-100 (Definitions), 5-101 (New Vehicle Dealer Licensing), and 5-102 (Used Vehicle Dealer Licensing) of the Illinois Vehicle Code. Ill. Rev. Stat. ch. 95 1/2.

to require a dealer's license in order to perform many of the activities (such as advertising automobile sales) that can now be performed without a license. These restrictions would end the practices of credit unions and buying clubs that currently assist consumers in locating a licensed automobile dealer willing to sell at a substantial discount.⁴ Although each of the amendments contained in S.B. 1978 operates differently in its specifics, both amendments would effectively eliminate these types of automobile marketing methods.

Since the amendments to the Illinois Vehicle Code provided for in S.B. 1978 were neither discussed nor debated prior to passage, we have little material beyond the language of the amendments themselves from which to infer their purpose. As far as we aware, the only contemporaneous statement on this question was from the Illinois New Car & Truck Dealers Association in its Legislative Bulletin of January 26, 1989, two weeks after S.B. 1978's passage. The Car Dealers Association stated that: "It appears that this language should stop the Walmarts, Buying Services, Credit Unions and other persons who attempt to broker automobiles in Illinois from acting as a licensed dealer [sic]." Our review of these amendments suggests that the Car Dealers Association's characterization accurately reflects the likely effect of this legislation.⁵

Interest and Experience of the Federal Trade Commission

Our interest in this legislation stems from the Commission's mandate to enforce the consumer protection and antitrust laws of the United States. The Federal Trade Commission is charged with promoting competition and protecting consumers from unfair competition and unfair and

⁴ In such cases the sales transaction is completely between the consumer and the car dealer, with the credit union or buying club simply acting as a broker. Credit unions that sponsor such sales allow automobile dealers to use their parking lots to display new or used cars and then invite credit union members to attend. Credit unions thus not only assist their members in the purchase of automobiles, but get an opportunity to offer financing for any automobile purchased at the sale.

⁵ We are not familiar with any automobile sales being conducted by Walmarts.

deceptive practices.⁶ 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.

During recent years, the Commission has been actively involved in issues relating to the retail automobile market. In 1984, for example, the Commission issued the Used Motor Vehicle Trade Regulation Rule ("Used Car Rule") in an effort to educate consumers about their warranty rights and to prevent the injury that can be caused by oral misrepresentations in used car transactions.⁷ The Commission has also recently ruled that automobile dealers in the Detroit area violated the antitrust laws by agreeing to limit their hours of operation.⁸ In addition, the Commission staff has conducted economic research concerning automobile marketing.⁹

⁶ See 15 U.S.C. §41 et seq.

⁷ Used Motor Vehicle Trade Regulation Rule, 16 C.F.R. Part 455. The Used Car Rule requires used car dealers to place a sticker in the window of each car that clearly states the warranty coverage being offered and that suggests consumers obtain an independent inspection of the vehicle prior to purchase. 16 C.F.R. §455.2. These stickers form part of the contract of sale for a used car. 16 C.F.R. §455.3(b).

⁸ Detroit Auto Dealers Ass'n, Inc., FTC Docket 9189 (February 22, 1989).

⁹ The Commission's Bureau of Economics recently completed a study concluding that state laws restricting the number of automobile dealers in an area increase costs to car buyers in this country by as much as \$3 billion each year. Robert P. Rogers, The Effect of State Entry Regulation on Retail Automobile Markets, Federal Trade Commission Bureau of Economics Staff Report (January 1986).

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The Commission staff has commented on proposed Illinois legislation that would have prohibited car dealers from holding sales outside of their local markets.¹⁰ In addition, the Commission staff recently voiced concern that proposed legislation in Michigan prohibiting automobile brokering would have reduced competition and increased the prices that consumers pay for automobiles.¹¹ During the past two years, Commission staff has submitted comments to other states on issues similar to those raised by S.B. 1978.¹² In each case we concluded that these legislative initiatives could have resulted in raising the prices that consumers paid for new and used cars.

Automobile Marketing Methods

As the Car Dealers Association recognizes, several innovative methods are available to steer consumers to licensed automobile dealers willing to sell at a discount. One source is credit unions that sponsor automobile sales (by licensed dealers) on their premises. The credit unions encourage these sales because it gives them an opportunity to offer automobile financing. Since cars are sold in volume, the credit unions can obtain substantial savings for their members.

¹⁰ Letter of April 24, 1987, from John M. Peterson, Director, Chicago Regional Office of the Federal Trade Commission, to the Honorable Woods Bowman, State Representative, concerning House Bills 787 (1986) and 1173 (1987). Governor Thompson ultimately vetoed both bills.

¹¹ Comments of the Cleveland Regional Office and Bureau of Economics staffs of the Federal Trade Commission on Michigan House Bill 4390 by Mark Kindt, Director, Cleveland Regional Office (September 29, 1988).

¹² See letter from the FTC staff to the Florida Senate (March 29, 1988); letter from the FTC staff to the South Carolina House of Representatives (March 21, 1988); letter from Jeffrey I. Zuckerman, Director, FTC Bureau of Competition, to William P. TeWinkle, Wisconsin State Senate (February 19, 1988); letter from the FTC staff to the California State Assembly (January 29, 1988); letter from the FTC staff to the Governor of Texas (June 1, 1987).

Fleet dealers, such as Hertz and Avis, are a principal source of automobiles for sales conducted on credit union premises. The fleet dealers are seeking a means of selling their used rental cars. Low overhead sales offered in conjunction with credit unions enable fleet dealers to turn over their inventories efficiently. It is possible that this process will, in turn, enable rental agencies to charge consumers lower prices when renting automobiles.

The credit union fleet sales save Illinois consumers substantial amounts in their used car purchases. For example, in 1986, credit unions surveyed by the Illinois Credit Union League estimated that consumers paid an average of \$1,118 less for a used car at a credit union sponsored fleet sale than those consumers would have paid to a "conventional" used car dealer.¹³

Another marketing development that provides consumers with an opportunity to obtain substantial savings in the purchase of new cars is the emergence of automobile buying clubs and referral services. These services generally charge an annual membership fee and arrange new car purchases for members at guaranteed prices with participating dealers. An August 1988 survey of six automobile buying services by Changing Times magazine concluded that customers purchasing cars through these services would have realized substantial savings on each purchase no matter which service was picked.¹⁴

Our understanding is that Amway Corporation, for example, offers a program through which its distributors and their customers may purchase new cars from licensed dealers for a maximum of \$150 over the factory invoice price. According to Amway, these discount sales are available through independent Amway distributors to persons paying a suggested annual fee of \$24.95 and may be exercised at any of

¹³ The Illinois Credit Union League surveyed the nearly 1,000 Illinois consumers who purchased used fleet vehicles at special sales conducted by credit unions in conjunction with National Car Rental during the last six months of 1988. Of those surveyed, 80% reported that the used car price was "good or excellent" and 87.5% reported that the purchased car's performance was "good" or "excellent."

¹⁴ Taking the Hassle out of Car-Buying, Changing Times, August 1988, at 37.

67 Illinois automobile dealers who handle 128 lines of automobiles. The Amway Auto Network is currently available in thirty states, the District of Columbia and the United States Virgin Islands.¹⁵ These types of programs appear to offer consumers substantial benefits.

Prohibitions on "Brokering" Automobile Sales

S.B. 1978 would prohibit credit unions, buying clubs, or the like from acting as "brokers" in sales of new or used automobiles,¹⁶ and thus would ban the practices described above. It is difficult to see how this change will benefit consumers or competition. We have no reports of significant or extensive fraud or deception that have injured consumers who participate in these discount sales programs, and current law already provides meaningful protection to the public. Automobile sales are covered by the Illinois Consumer Fraud Act,¹⁷ and the Commission's Used Car Rule helps protect consumer's warranty rights when purchasing used cars.¹⁸ In addition, all automobile dealers must be licensed by the

¹⁵ The American Automobile Association also works with selected automobile dealers throughout the country to provide its members with opportunities to purchase new motor vehicles at substantial discounts. Changing Times, supra, at 35-38.

¹⁶ The definition of "broker" encompasses anyone who is compensated for being involved in a car sales transaction and who is not a licensed dealer or the dealer's employee, a manufacturer or manufacturer's employee, or the owner of the car being sold. Ill. Rev. Stat. ch. 95 1/2, §5-100. Other amendments prohibit brokers, as defined in the Bill, from selling new cars (Ch. 95 1/2, §5-101) and from selling used cars (Ch. 95 1/2, §5-102).

The definition of "broker" is so broad that an attorney who becomes involved in the sale of a client's car and receives legal fees for his assistance could arguably be acting illegally as a broker.

¹⁷ Illinois Consumer Fraud and Deceptive Business Practices Act, Ill. Rev. Stat. ch. 121 1/2, §262 et seq.

¹⁸ Supra note 7.

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State of Illinois.¹⁹ S.B. 1978 does not appear to provide benefits to the public that are not already available under current law.

The anti-brokering amendments provided for in S.B. 1978 appear likely to injure Illinois consumers by restricting competition in the new and used car markets. Such a restriction may in turn result in higher prices for consumers. Stopping the "Walmarts, Buying Services, Credit Unions and other persons" from offering consumers cost-saving methods of purchasing new and used automobiles does not benefit consumers. Rather, consumers would be deprived of the potentially substantial savings that they could obtain through these alternative automobile purchase programs.

Amendments to Licensing Provisions for Car Dealers

S.B. 1978 would also change the provisions for licensing new and used car dealers in a manner that could eliminate the ability of buying clubs and credit unions to participate in automobile sales. Illinois law already requires that new and used car dealers be licensed by the State. This new legislation would prohibit anyone except licensed dealers or their employees from 1)"displaying for sale [new or used] motor vehicles on a lot or showroom"; 2)"advertising for [new or used] motor vehicle [sic]; or" 3)"regularly or actively soliciting buyers for [new or used] motor vehicles."²⁰ Credit unions and buying services currently engage in these

¹⁹ Illinois Vehicle Code, Ill. Rev. Stat. ch. 95 1/2, §5-101 et seq.

²⁰ Ch. 95 1/2, §§5-101(a), 5-102(a) (as amended by S.B. 1978). This definition is so expansive it would appear to preclude a consumer from running an advertisement seeking to purchase a particular type of car. Although surely not intended, the language seems susceptible to a strong argument that newspapers and magazines would not be able to run automobile advertising -- particularly if the effect was to "regularly or actively solicit buyers for [new or used] motor vehicles."

practices but probably could not qualify for licenses because they do not actually sell automobiles themselves.²¹

These amendments to the licensing requirements have the same practical effect as S.B. 1978's prohibition of brokering. If credit unions, buying clubs or similar organizations cannot obtain licenses to display automobiles (on their own lots), advertise the existence of these sales (in newsletters or other media) or solicit the attendance of potential purchasers (such as credit union members) at automobile sales, it will be difficult or impossible for them to continue their current practices. Illinois consumers will simply lose the benefits that these organizations provide through these practices.

²¹ Although the amendments expand the types of activities that require an automobile dealer's license, the requirements for obtaining a license and the duties imposed upon license holders are not changed by the amendments. A new car dealer's license cannot be granted to someone who is not contractually authorized by a manufacturer or by a franchised distributor to sell the particular makes of cars in Illinois. Ch. 95 1/2, §5-101(d)1. Since credit unions, buying clubs and other organizers of discount new car sales do not actually sell new cars, it seems unlikely that manufacturers would contractually authorize them to do so.

In addition, both new and used car dealers are required to maintain an "established of business," as defined in the Illinois Vehicle Code, in order to qualify for a license. Ch. 95 1/2, §§5-101(d)2, 5-102(d). "Established place of business" is defined in the Code as the place owned or leased and regularly occupied by the dealer for the "primary and principal purpose" of engaging in the business of selling automobiles or automobile parts. See Ch. 95 1/2, §5-100. It is difficult to imagine how an organization such as a credit union, whose primary and principal business is extending credit and which, in fact, does not sell any cars, could have a regular or established place for the primary and principal purpose of selling cars. In order to qualify for car dealers' licenses, either the credit unions and others would have to alter their current business practices significantly or the dealer licensing provisions of the Code would have to be interpreted in a manner completely at odds with the statutory language and spirit.

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Conclusion

The proposed amendments would restrict the ability of licensed car dealers to conduct automobile sales through credit unions or buying clubs and to employ other innovative marketing techniques that result in substantial savings to consumers. We believe that the amendments to the Illinois Vehicle Code provided for in Senate Bill 1978 are not likely to benefit consumers or competition. Instead, this legislation may limit competition among automobile dealers and increase the prices that consumers pay for automobiles.

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 initial "C" and a long horizontal stroke at the end.

C. Steven Baker
Director
CHICAGO REGIONAL OFFICE