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Consumer Rip-offs Common in Automobile Purchases *Statement of Public Citizen President Joan Claybrook*

Today we are releasing a new report detailing the various methods that unscrupulous car dealers use to bilk consumers – even those who consider themselves sophisticated, well-informed car buyers. And you will hear from Duane Overholt, who worked in the auto sales industry for 20 years and says these techniques are used systematically throughout the industry to cheat consumers out of sometimes thousands of dollars per purchase. These scams add many, many millions of dollars each year to the profits of car dealers at the expense of consumers. And, for the most part, they get away with it.

There is ample evidence that the schemes we outline here – some of which are illegal but all of which are unethical – are not restricted to a few geographic areas or a handful of bad dealerships. In fact, customers have been robbed on both coasts and everywhere in between. Our research indicates that fraudulent practices by auto dealers may be commonplace among many of the largest auto dealership conglomerates as standard operating practice. We're talking about systemic corporate malfeasance on a massive scale.

Customers in California, Florida and in at least 37 other states have been robbed by what the Minnesota attorney general's office describes as "industry-wide practices" such as inflating the cost of warranties, contract stuffing and racial discrimination.

Our report explains these unfair practices by walking through the various steps of a purchase and the opportunities for a scam at each step. While many consumers suspect that auto dealers are not always paragons of virtue, most have no idea how vulnerable they are in a relatively large financial transaction that involves a flurry of paperwork and complicated financial relationships. Many of the basic arrangements lack transparency. For example, although consumers have a direct relationship with the lending institutions that finance vehicle purchases, the vast majority never see the paperwork maintained at the bank. Their ignorance of the details benefits dealers, because dealers receive a percentage of the loan total, and may even change key terms of the loan without consumer knowledge or consent.

Massive consolidation in the auto dealership industry has altered the relationships, and leverage, of the industry, with both financial institutions and vehicle manufacturers. While national conglomerates and franchise chains are a relatively new phenomenon, many independent dealerships may also use similar techniques to remain competitive in a marketplace awash in ill-gotten gain.

We hope that outlining the process and the techniques of deception will both educate consumers and provide law enforcement with a blueprint for investigation. I will talk briefly about just a few key tricks of the trade.

The first concept is the notion of “leg” – as in “legroom” for negotiation and profiteering. A common trick among dealers is to negotiate with the consumer for a monthly payment that is slightly above the amount required to actually purchase the car, including interest, over the life of a loan. For example, if payments to purchase the car at its actual price would be \$200 per month, a dealer will negotiate a payment of \$220 a month with the consumer.

This increases the overall size of the purchase, as well as any percentage commission the dealer may make on the loan. Yet because lending institutions will only cover the higher amount if presented with a paper trail that justifies the additional money, fraudulent dealers must invent products to “stuff” or “pack” into the contracts that fill out the payment to equal \$220 a month. The extra products or services provide a higher profit to the dealer, but little or no real value to the consumer. In the first document, the “leg” is \$7 per payment, or more than \$500 of possible hidden profit for the dealer over the life of the contract. In some cases, consumers lack any awareness that a product, such as an added warranty, has been purchased, and thus can never claim the warranty. In other cases, the warranty may duplicate the warranty that already arrives on the vehicle from the manufacturer.

A prime example of a near-useless product that is frequently stuffed into contracts without consumer knowledge is something called “etch.” You can check to see if your vehicle has etch by examining the windows or windshield of the vehicle for an acid etching of a serial or Vehicle Identification Number (VIN) that may help to track the vehicle if it was stolen. Both of these window stickers are showing “etch” was added to the vehicle in the showroom and is one of the items that increase the dealer’s starting price for the vehicle. The physical etching is typically bundled with a theft “insurance” program, which promises a very nominal reimbursement, such as \$2,500, if a car is stolen and not recovered. Etch programs cost dealers very little, but are marked up in sales contracts, as here, to as much as \$478. Consumers in the Florida class action paid as much as \$1,000.

Yet I issued the rule requiring standardization of a permanently affixed VIN visible from outside the vehicle when I was administrator of the National Highway Traffic Safety Administration, and a subsequent 1994 theft protection standard requires labeling 18 distinct parts of every American vehicle, free of charge to the owner. The key point is that etch and other extras, such as maintenance contracts that promise six oil changes for \$1,000, are not really products at all. They are mainly just placeholders for dealers to square the “leg” they’ve negotiated into the deal with the paperwork on the sale. That’s why comparisons show a wide range in prices for different consumers *on the same product or services*. These are shells in a shell game—nothing more.

There are sure to be honest and scrupulous auto dealers in America. However, many dealerships are getting away with highway robbery. By letter today Public Citizen is calling on state attorneys general across the country to launch comprehensive investigations to stop the fraud and deception that consumers face when buying a vehicle. We also believe there is a tremendous need for legislative action to close loopholes and for greater regulatory oversight of these vehicle purchases.

Public Citizen does not believe that this kind of graft is necessary for auto dealers, as an industry, to remain economically viable. The last section of our report suggests some new laws that would greatly enhance the transparency and accountability of auto dealerships, and relieve much of the trauma to consumers and their pocketbooks that now comes with buying a vehicle. These include such measures as requiring all financial and dealership documents to be contained in a single file and available to the consumer upon request; requiring disclosure of the lender’s interest rate offered before the dealer markup; and forbidding mandatory arbitration clauses in vehicle purchase contracts.