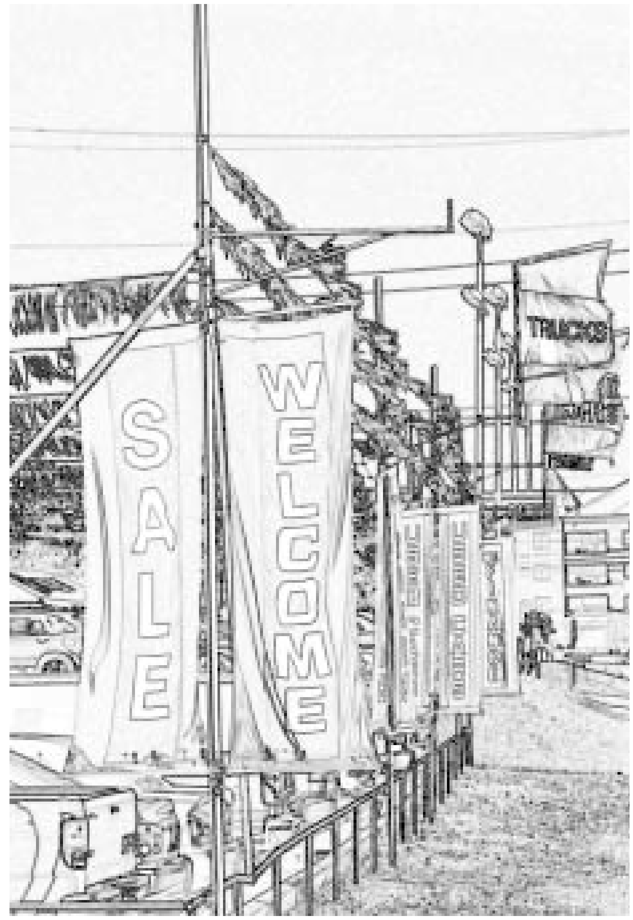
Auto Finance Add-Ons: Little Bang for the Buck



The Sky's the Limit on Price!

A report of the Southwest Regional Office of Consumers Union

by Sharon Hernandez-Darrow

Senior Staff Attorney, Rob Schneider

Edited by Kathy Mitchell, Research Director

This research was conducted thanks to the generous financial support of the FIRST Foundation.

March 2003

A new proposal filed at the Texas Legislature would unleash more expensive auto dealer add-on products onto unwary consumers—even though our research indicates that some of these products already cost consumers **$1.1 billion** too much every year.

In a high-pressure sales environment, where consumers often feel unsure about securing financing, car salesman pressure buyers into purchasing "add-on" products like extended service warranties and anti-theft coverage. These items added $99 to $5,000 per product onto the price of a new or used cars in our sample, and the fact that consumers pay interest on these products as part of the total financing package makes them even more costly.

Unfortunately, although consumers pay high prices for extended warranties and anti-theft protection, they frequently receive little value because of the products' limited coverage.

Fragmented regulation ensures that most consumers cannot find a state agency to help them solve their problems. The state of Texas splits the regulation of add-on products between two different agencies, neither of which control the product's cost to the consumer, the benefits and exclusions, nor dealers' sales tactics.

House Bill 3509 by Representative Ismael Flores would offer consumers significantly more protection by authorizing the Texas Department of Licensing and Regulation to review and approve service contracts, mandating non-negotiable sales prices, and by ensuring that consumers recieve a contract at the time of sale. HB 1380 by Representative Senfronia Thompson (D-Houston) would make matters worse by expanding the types of loans that can finance such add-on products and scaling back the already scant regulatory controls.

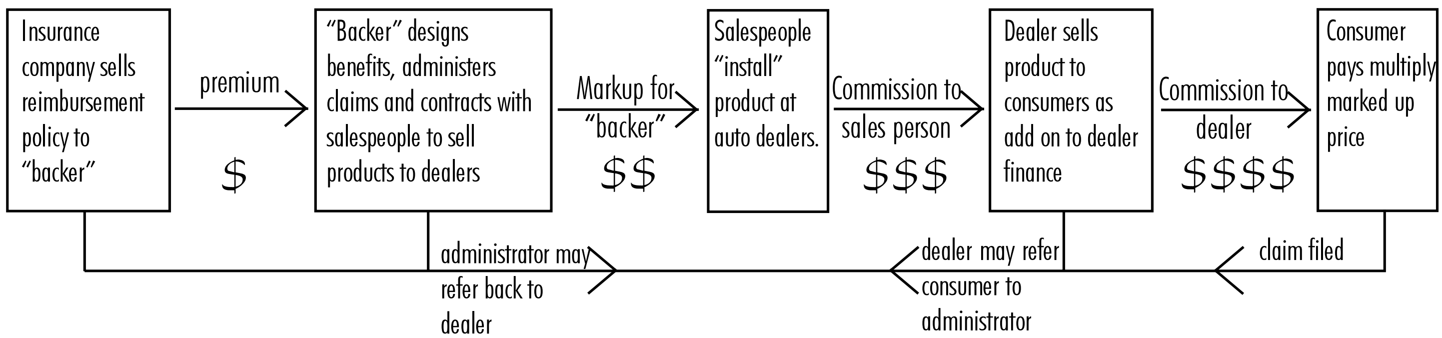
Method

Consumers Union Southwest Regional Office (CU) reviewed a random sample of 404 Attorney General complaints that were filed against auto dealerships from 2000 to 2002. We conducted an indepth review of 196 of these complaints. We also reviewed complaint information from the Office of Consumer Credit Commission and the Texas Department of Licensing and Regulation.

Using copies of extended service warranty contracts that the consumer provided, CU collected data on the specific

Consumers Union
Publisher of Consumer Reports

Consumers Pay Far More for Extended Warranty Coverage than the Insurance is Worth, Because So Many Players Can Take a Markup



At Claim Time, Consumers Report Finger Pointing Among the Players

terms of the contracts, including cost, deductible, and length of coverage. CU then compared the costs of the product to the consumer to the cost of a representative insurance plan backing the product. We also assumed that a 25% commission to the seller is reasonable. CU compared the consumer price to the reasonable estimated underlying insurance value. When the coverage was not specified in a consumers documents, CU assumed the most comprehensive and costly coverage for that car in order to give the most conservative estimate of the overcharge.

General Findings

- Half of car buyers in our complaint sample (202 people) purchased extended warranties, and paid an estimated average $755 too much for them. Assuming that half of the people who finance a car bought an extended warranty, we estimate that consumers in Texas may have paid $1 billion too much for extended warranties in 2002.
- Fewer than eight percent of consumers in our sample (32 people) purchased theft protection, but these consumers paid a huge markup. For anti-theft products, consumers typically paid $299 to $799 to buy a very low value insurance product that insurers sold to dealers for under $32 per covered car. Assuming the only 8% of people who finance their car purchased anti-theft products in 2002, we estimate consumers spent more than $100 million too much for them.

> Extended warranty is "not insurance" by Texas statute, but this statutory fiat cannot hide the fact that the product is sold and administered as insurance. One major company describes its extended warranty program as the sale of "insurance coverage at competitive prices."
>
> Interstate National Dealer Services.[5]

- The Texas agency charged with regulating these products, the Department of Licensing and Regulation (TDLR), suffers both from the lack of power and the will to protect consumers. The advisory board charged with overseeing extended warranties is composed almost entirely of industry representatives and has not met in two years,[1] and TDLR has not been able to appoint any members to the Vehicle Protection Advisory Board since its creation in 2001.[2]
- Many consumers complain of aggressive sales tactics, including adding a financing "extra" without the customer's knowledge, intimidating buyers into signing an a contract without review, and altering the contract. These consumers often felt pressured into purchasing extended warranties and anti-theft products or were told they would not receive financing otherwise.

  Consumers complained about rude salesman, overcharges, and deceptive practices—and one out of five consumers complained specifically about their extended warranty. Of 32 people who purchased anti-theft products, 18 people, over 50%, complained about their contract.
- Of the 196 files reviewed in more detail, many related to the difficulty consumers had in getting dealers to make repairs covered by the extended warranty even when those repairs were expressly provided for in the contract. Consumers also complained that they had been told their warranty covered everything, only later to find out that this was not the case.
- Consumers reported problems canceling their add-on or collecting promised cash rebates for filing no claims. Others reported receiving no copy of their contract or found out that the terms of their contracts had been altered.

The Products

Extended warranties and vehicle anti-theft products are among the profitable "add-on" products sold to consumers by auto dealers (and sometimes directly by insurers or brokers). This market has come under increasing scrutiny throughout the United States because of consumer complaints of unscrupulous sales tactics, limited coverage, and high prices.

"Extended automobile warranties" or "automobile service contracts" advertise financial protection to the automobile owner from mechanical breakdowns not covered by the manufacturer's original warranty. These contracts typically range from three months to seven years and/or 3,000 to 150,000 miles.

"Vehicle anti-theft products" or "vehicle protection products" pay a cash benefit of $2,500-$3,000 if the car is stolen within the first three years. The "plan" also includes an etched number (known as a vehicle identification number) or a decal in the automobile's window.[3]

Consumers Pay a Three Hundred Percent (or more) Markup Over the Cost of the Underlying Insurance Coverage When Buying Extended Warranty from the Dealer

Year and Make/Model		Price Paid by Consumer	Miles/ Months	American Banker Premium	Price Consumer Overpaid
2001 Mitsubishi Galant	New	$ 1,295.00	75,000/60	$ 290.00	$ 1,005.00
1998 Mitsubishi Eclipse	New	$ 795.00	75,000/60	$ 290.00	$ 505.00
1998 Toyota Corolla	Used	$ 1,786.00	75,000/72	$ 281.00	$ 1,505.00
2001 Chevrolette Silverado	New	$ 2,000.00	60,000/60	$ 276.00	$ 1,724.00
2001 Ford Mustang	New	$ 3,425.00	100,000/72	$ 737.00	$ 2,688.00
1998 Ford Expedition	New	$ 810.00	60,000/60	$ 275.00	$ 535.00
2001 Ford F150	New	$ 3,000.00	100,000/72	$ 800.00	$ 2,200.00
1995 Toyota T100	Used	$ 1,595.00	36,000/36	$ 484.00	$ 1,111.00
1996 Pontiac Bonneville	Used	$ 1,888.00	24,000/24	$ 574.00	$ 1,314.00
2001 Nissan Maxima	New	$ 1,098.00	75,000/60	$ 275.00	$ 823.00
1998 Chevrolette Malibu	New	$ 1,500.00	75,000/60	$ 275.00	$ 1,225.00

footnote 16

Automobile dealers derive an increasing share of their profit from these add-on contracts. In 2002, AutoNation, the nation's largest automobile dealer, benefited from the commission on sale of extended warranties, the liquidation of insurance reserves relating to extended warranties, and the sale of risk from a third party insurance company, resulting in an $8.1 million dollar gain.[4]

Insurance by Any Other Name

Although automobile dealers sell theft protection and extended warranty products as insurance, they are currently exempt from insurance regulation in Texas—even though they clearly meet the definition of insurance set out in the insurance code and are frequently backed by an actual insurance policy.[6] By accepting the financial risk of automobile repairs or cash payout in the event of mechanical breakdowns or car theft, the dealers in effect are acting as insurers and insurance agents but without any price controls.[7] While the Insurance Department can review the rate of an insurance policy backing these contracts, the actual contract to the consumer is not "insurance" and therefore the seller can charge any amount.

Dealers who sell extended warranties on their own cars and who cover their obligations with an reimbursement insurance policy are not subject to warranty regulations.[8] Other companies are minimally regulated by Texas Department of Licensing and Regulation (TDLR)—we'll call these unregulated insurers the "backers."

Over one hundred non-dealer "backers," who sell these products through dealers, financial institutions, via the telephone or the internet, are registered with the TDLR.[9] These companies accept risk like an insurance company, but do not have to meet insurance standards.

Instead they must show they have a certain net worth, or they must purchase an actual insurance policy to cover the risk from some regulated insurer.[10] The "backer" sometimes hires a marketing company to get their product into auto dealerships, and may also hire an administrative company to handle consumer claims.[11] For the consumer, this means that a whole "insurance" market has developed without insurance consumer protections, including any rate or policy form review or prompt payment of claim requirements.

With all these different players behind every sale, commission and sales expenses represent a high percentage of the cost of these products. One extended warranty offers a flat commission to the auto dealer of $450 - $800 or a commission rate of 50% of the selling price, which could be more than $4,400.[12] Other companies allow the dealer to mark up the price without limit and to take the mark-up as commission.[13] Interstate National Dealer Services, a TDLR licensed "backer,"reported that selling, general, and administrative expenses were 44% of revenues, and this does not include the "extra" this company allows the dealer to charge the consumer (commission).

Extended Warranty: Costs Too Much

By the time all of the companies and people selling these policies collect their mark-up, the price of an extended warranty has become extraordinarily high.

The price of extended warranties vary from model to model and from year to year. In the CU study, Texans paid an average of $1,376 for automobile extended warranties. Owners of used cars paid an average of $1,381 for extended warranties, and new car buyers paid an average of $1,371. Based on the the detailed rate filings for one large insurer backing these plans, we estimate consumers overpaid an average of $755 for their extended warranty. In addition, because the cost of this product is also added into the loan, they paid interest averaging another $499 over the life of the loan.[15]

Extended Warranty: Does Too Little

Rife with exclusions, and scheduled to largely overlap the car's standard warranty, most extended warranties cover very little.

Exclusions are lengthy. One typical extended warranty policy

Limited Benefit Products Rolled into the Car Price

Mr. G saw an advertisement in the Houston Chronicle for a 1999 Ford Explorer priced at $19,802, the same price that two people quoted to him later arrived the dealership. However, on the contract, the dealer listed the price at $21,326.

Mr. G immediately contacted the finance manger who assured him that he would receive a refund check of $1,526 plus interest and sales tax. But, the check never arrived.

"Instead, I was told that I did not receive a refund check because I had signed a form to purchase an anti-theft security system," Mr. G told the Attorney General. Included with his purchase agreement was a signed contract for "Protection Plus," an anti-theft plan consisting of "two (2) decals affixed to driver and passenger windows" along with an insurance benefit of $1,000 if the car was stolen and not recovered. The price of this "Anti-Theft Security System" was not listed separately on his vehicle purchase contract but incorporated into the vehicle price.

Current law current law does not require a theft protection plan to be separately itemized on the loan documents, nor does it require the dealer to give an actual contract to the consumer at the time of purchase.

The general manager later claimed the purchase had also included a Viper alarm system, but that Mr. G was not able to have it installed at the time of purchase. Such an alarm system was not listed as part of his "Protection Plus" plan nor was it listed on his purchase contract.

Some dealers offer service plans designed to cover only certain maintenance items like oil changes. Phil purchased a $549 Vehicle Care Program plan from an Ammarillo Nissan dealer to cover oil changes and tire rotations--but when he needed these services the dealer charged him and promised to mail a check to reimburse him for the charges. Phil never received a check, and his calls to the service department resolved nothing. When he complained to the dealer, they agreed to cancel the plan but refund him only $237.89. In the end, the dealer charged only a $75 cancellation fee, but Phil still had not received any reimbursement for his expenses at the time he filed his complaint.

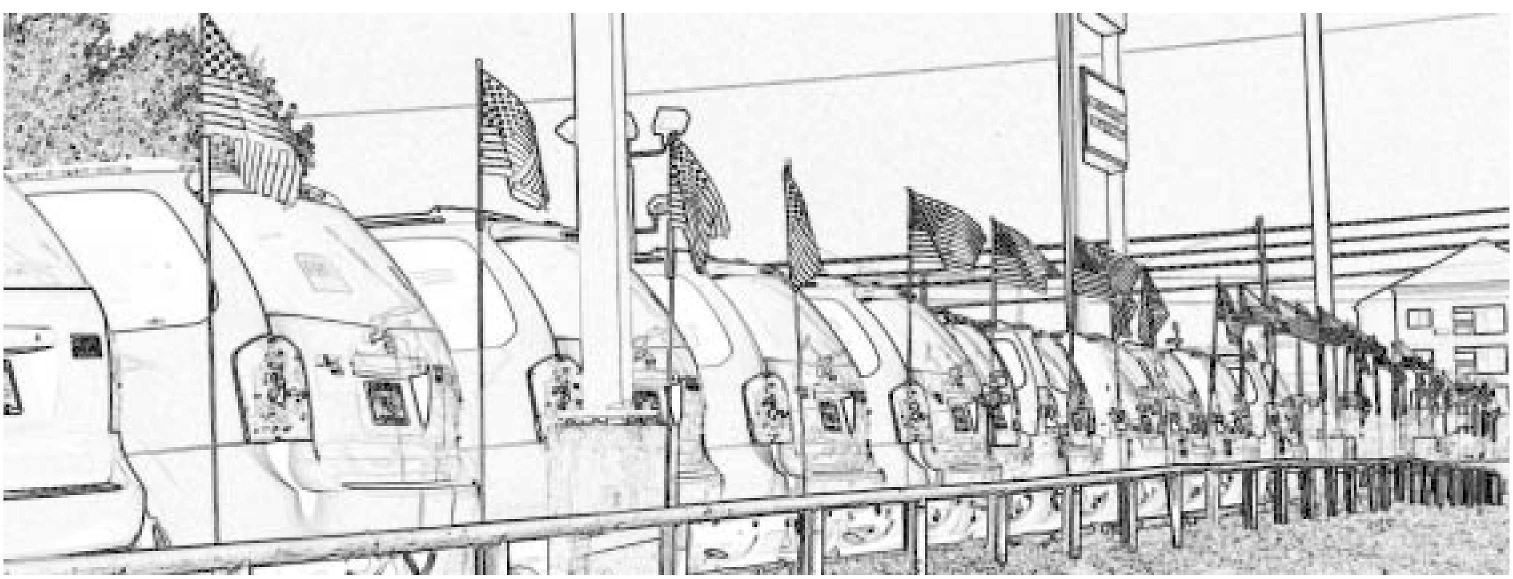
AG Consumer complaint S0003-0098, AG Consumer Complaint, No Number, Filed July 10,2000.

excludes "scheduled maintenance and wear items," "batteries, body and trim items," "noises including rattles, squeaks and wind noises," and "repair or replacement of components needed to improve operating performance due to normal wear and tear."[17]

Toyota's Extra Care states that components not covered *include but are not limited to* "engine components: transmission components, axle assembly components," "suspension components: springs, shock absorbers, Macpherson struts, shock absorber inserts, or springs," "electrical components: spark plugs, distributor caps, ignition wires, ignition lock cylinders and tumblers," "cooling system: cooling fan sensor, cooling fan relay, lines and tubes, coolant radiator reservoir tank," and "fuel system components: fuel hoses, lines and tubes, seals and gaskets, fuel tank sending unit."[18]

While extended warranties have limited coverage for regular maintenance items, they may also exclude emergency breakdowns. R. Martin O'Shea had owned his 1998 Nissan Frontier pick-up truck for slightly more than two years when, returning from a trip to a fast-food restaurant, the battery exploded, blowing the hood open, buckling it in two places, and spraying battery acid throughout the engine compartment. When Mr. O'Shea initially contacted the dealership, they assured him that the damages would be fully covered by his extended warranty. However, after some initial repairs had been made, the dealership told him that the extended warranty did not, after all, cover the repairs. He would be responsible for the charges. After much persistence, the dealership agreed not to charge him for everything, and his regular automobile insurer picked up part of the tab.[19]

Extended warranty coverage frequently expires long before it's needed. The warranty period usually starts, not from the purchase of the product, but on the day the new car initially rolled off the assembly line. Most manufacturers warranties last three year, according to www.cars.com, and most new car buyers purchase five year extended warranties. On average, consumers are only purchasing two extra years of warranty.



The Fees Charged by Dealers to "Install" Theft Insurance and "Activate" a Number Etched onto the Windowshield Make These Plans Pure Junk to the Consumer

Theft Program Underwriter	Insurance Price	Theft Program Name	Price to Consumer
Western General $2,500/ 2 Years	$ 6.00	Theft Guard $ "3,000"	$ 795.00
Western General $2,500/ 3 Years	$ 8.00	SafeGuard	$ 299.00
Western General $1,000/ 4 Years	$ 6.25	Permavin	$ 379.00
Courtesy Insurance Company $5,000	$14.00	Information Unavailable	$ 1,094.00
Universal Underwriter $2,000	$ 8.33	Information Unavailable	$ 2,834.00
Universal Underwriter $4,000	$16.26	Protection Plus $1,000/3 Years	$ 1,495.00
Great American Insurance $2,500/3 years	$10.50	Theft Guard, Details Unavailable	$ 699
Great American Insurance $3,000/5 years	$14.00		

footnote 25

One consumer bought a six year extended warranty in December 1993 to cover his 1991 vehicle. When his car needed repair four years later in 1997, the dealer denied coverage because his warranty had expired. Confused, the consumer spent nine months trying to understand—no one explained to him that the extended warranty began at the car's "in-service" date in December 1990.[20]

Since the extended warranty starts along with the manufacturer warranty, it basically overlaps the original manufacturers warranty or extends only a few months/years beyond it. Car buyer Jay found this out when he spent $810 to purchase a 60 month/60,000 extended warranty for his new 1998 Ford. According to Jay, the dealer told him the extended warranty did not go into effect until after the factory warranty expired at 36,000 and would be good through 60,000 miles. When Jay traded in his car, still under factory warranty, two years later, he decided to cancel the warranty. The dealer told him that he would only get a partial refund of $350 because his warranty had been in effect for two years.[21]

Finger Pointing

Difficulties with vehicle add-on products may not end at high-pressure sales tactics or high prices. Consumers also report problems getting the dealer to honor the terms of the contract, whether they file a claim or need a refund after cancelling the policy.

The procedures to get repairs completed vary from contract to contract. In the circumstances when dealer is not the "backer," the consumer or the dealer may have to get the repairs approved by the backer or an administrative company before repairs can be made. The dealer then completes the repairs and asks the backer for reimbursement for repair costs. The consumer may have to pay for the repairs and then submit receipts to the backer for reimbursement. The backer either pays the amount, or makes a claim to an insurer with whom they hold a contractual liability reimbursement policy. This policy reimburses the company for any claims that are made by the dealer or the customer.

Sometimes consumers are caught between the dealer and the claims administrator. Ms. B paid $1,025 for an extended warranty that expressly included transmission components. When her Chrysler broke down as a result of transmission failure, the dealer assured her it was covered under her extended service contract. According to Ms. B, the dealer later notified her that the backer had denied coverage under the service contract and that she was now required to pay $3,000 to have the transmission repaired.[22]

One of consumers' top complaints is the failure of dealers to honor extended warranties. A dealer may collect a bonus if claims paid on their service contracts are less than the claims reserves maintained for such contracts.[23] When the dealer backs up its own contracts, repairs made under an extended warranty mean the dealer must provide labor and parts at no cost.

Consumers not only encounter difficulty with getting repairs made, they also have troubles getting a refund when they cancel the policies. Buyers report that dealers promise to cancel the plan, but no refund arrives, or they are told later that the plan will be cancelled for a steep administrative fee.[24]

Anti-Theft: Costs Too Much

Consumers in our sample paid anywhere from three hundred dollars to several thousand dollars for their anti-theft product. Insurance company price for the coverage backing the product? Typically from $9 - $17 for a three year product. For a five year product, costs range from $12 - $32.

Anti-Theft: Does Too Little

Vehicle anti-theft buyers end up with a product that duplicates coverage they probably already have under their regular auto policy. Anti-theft pays a modest flat benefit amount if a car is stolen. But any consumer who finances a car must buy comprehensive insurance, including theft coverage for the value of the car plus a rental car or other temporary transportation if the car is stolen.

Some anti-theft contracts actually require consumers to hold another insurance policy with theft coverage in order to receive benefits of the product. "At the time of the theft, the vehicle must be covered by comprehensive theft insurance," states the Premium Care in their contract.[26]

Theft policies may not pay a benefit for all thefts. The anti-theft product marketed by Olympicare excludes, "losses resulting from

failure to take reasonable and prudent precautions against theft… examples *include but are not limited to carjacking,* keys left in vehicle, or keys made accessible to anyone except the vehicle owner." (emphasis added). Under the same policy, owners are also not eligible for losses that are not reported to the administrator within 72 hours.[27]

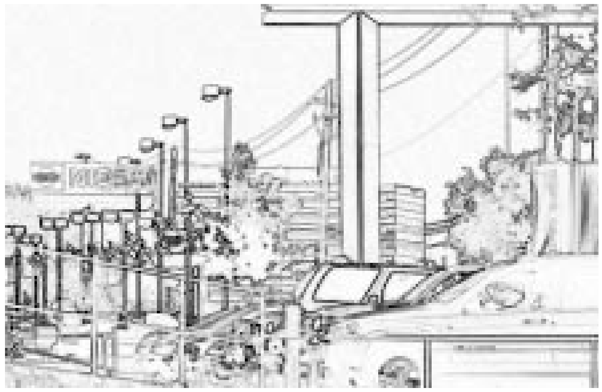
The advertised amount of anti-theft awards can also be inflated, when part of the cash award is contingent on the purchase of another vehicle from the same dealer. According to the contract's fine print, Olympicare's $5,000 anti-theft program will actually pay only $3,000 if the car is stolen. An additional $2,000 *discount* on a new car purchase will be available from the original dealer to consumers who come in within 30 days. Since car prices are not fixed, this amounts to little more than a ploy to get consumers back in the door.

Anti-theft policies also provide a much more limited payout if the vehicle is stolen and recovered, but damaged to the point of total loss. In this case, Premium Care's "$3,000" plan pays only the the *lesser* of a) $500 or b) the car owner's insurance deductible.[28]

The Hard Sell

In March 2000, Paula Claborn and her husband approached a dealer in Conroe, Texas to purchase a new vehicle. The salesman explained that the number etched on the window, an anti-theft product known as PermaVin, was included in the $800 package price (which also included a trunk mat, cargo net, and roadside assistance) and they must purchase it.

After the contract had been signed, the couple noticed a separate charge of $379.95 on the invoice for the same product. According to Ms. Claborn, the dealer told them that the product required two separate charges, one for "etching" (already included in the price of the car) and one for "activation." Furious, Paula insisted to everyone at the dealership, including the salesman and one of the managers, that she did not want PermaVin. After persistant calls and visits to the dealer, someone promised to refund the activation fee. Paula and her husband were still stuck paying interest on the charge because the dealership had included it in her financing package.[29]



"All dealerships do this," said Paula. "I've bought enough cars to know. There is always something they try to slip in to get extra money."[30]

Because automobile dealers receive commissions on the products they sell, they have an incentive to use aggressive tactics to increase their sales. As Paula Claborn found, car buyers were often told that the vehicle already had the vehicle protection product installed and could not be sold without it.[31] Consumers reported that dealers misled them—telling them that the purchase of an extended warranty or vehicle protection were necessary to secure financing, to receive a lower interest rate, or to purchase the automobile.[32]

When Julie went with her husband to purchase an SUV, the finance manager tried to convince her that, to qualify for the local credit union's low interest rate of 5.99%, they would have to purchase a $1,700 extended warranty. Otherwise, the rate would be 7.99%. Julie and her husband agreed to the purchase, but the credit union later told them that extended warranty was not required for their interest rate. Returning to the dealership, the finance manager remained adamant, she told the Attorney General, until, a phone call to the credit union and a lengthy discussion, she finally agreed to cancel the extended warranty policy. "A quote from (the finance manger) 'We are not in business to be nice,' says it all," reports Julie.[33]

Dealers also misrepresented to consumers that their car insurance would provide them with a 10% discount for the purchase of the anti-theft product,[34] that the dealer would pay for the extended warranty and interest for the first year,[35] and that the extended warranty was fully refundable if never used.[36] Dealers sometimes use a scheme, known as packing, whereby they "pre-calculate" the product or service that they wish to sell and then include it in the monthly payment they quote the customer.[37]

Other sales tactics also include failing to provide the consumer with a copy of the contract or providing a contract that has been altered. One buyer purchased a Mazda Protege for $19,125.72, insisting that she did not want an extended warranty. She was not given a contract because the salesman told her it had to be redone. After several days, the buyer contacted her lender and learned that the amount submitted by the dealership was actually $21,997.78, she told the Attorney General. The buyer returned to the dealership, and, after considerable persistence, finally reviewed the revised contract. She determined that they had added an extended warranty as well as some other items which accounted for the additional $2,872.07. The finance manager told her it was too late and that she was not a "Mazda quality" customer.[38]

Regulation

The regulation of the sale and administration of add-on products is weak and fragmented, provides only minimal oversight over product "backers," and offers no protection to the consumer from aggressive overpricing.

TDLR has no authority over many sellers in this market. Under the Texas' Service Contract Regulatory Act**,** only the companies that act as the obligor to the extended automobile warranty contract holder, i.e. the consumer, are required to register with the TDLR. Those companies who sell, market, or administer these products, and automobile dealers who sell these products on their own cars and who have a reimbursement insurance policy are exempt from TDLR rules.[39] So, although there are currently 114 automobile service contract providers registered with the TDLR, the actual number of parties offering this product, including the number of companies who escape regulation, is unknown.

Consumers looking to find information through the TDLR about the value of vehicle add-ons products would probably be disappointed. The department does not regulate either the price of the add-on product or its benefits. In fact, *the statute currently allows the dealer to negotiate the price of these products at the point of sale*. The department also does not monitor the number or amount of claims that are paid out to customers nor does it actively oversee the companies' financial status. Service contract providers are, however, required to submit the number of service contracts they sell on an annual basis in order to determine their annual registration fee. This information is defined by statute as a confidential trade secret.[40]

The Service Contract Advisory Board is virtually defunct. The board did not meet during 2001 or 2002, despite a statutory mandate that the board meet at least every six months.[41] The board is composed mainly of industry representatives; four out of six board members must be from a service contract provider or from a company that sells the product, one must be from an insurance company offering a reimbursement policy, and the last position must be filled by a consumer currently in possession of a service contract sold by a licensed provider. Unfortunately, the department has not been able to seat a consumer on the board.[42] Lack of consumer representation on the board has taken its toll; board members favored reducing the availability of TDLR's contact information to consumers[43] and proposed increasing the time period for the "backer" to provide the contract to the consumer from 21 days to 60.[44]

The regulation of vehicle anti-theft products is equally weak, and TDLR has been unable to find anyone to join the advisory board since its creation. Neither TDLR nor the advisory board have authorization to regulate rates, to control sales tactics, or to monitor and evaluate benefits.[41] Instead, the Board's powers are largely limited to advising the Commission on setting registration fees for "backers."[45]

A Nationwide Problem

State officials across the nation are cracking down on the high cost of add-ons and the sales tactics that trap customers. In Washington, New York, Minnesota, and Texas, district attorneys and attorney generals have filed lawsuits against auto dealers for deceptive sales practices of add-on products.

In 2002, Attorney General John Cornyn sued three dealerships related to the deceptive sale of auto security systems. Dealers did not disclose to customers that an $800 security system would be added to the advertised price for their automobiles. Because the dealerships had no intention of selling the automobiles at the advertised price, the Attorney General charged that the three had violated the Deceptive Trade Practices and Consumer Protection Act.[46]

In California, Los Angeles District Attorneys filed suit against Gunderson Chevrolet, owned by AutoNation, for "packing" practices. Gunderson Chevrolet agreed to pay approximately $2.5 million to settle a lawsuit alleging that the company engaged in unlawful business practices.[47] As part of the settlement, Gunderson was enjoined from quoting a price or payment amount that includes undisclosed charges. The L.A. District Attorney's Office went even further and filed criminal charges against seven former employees of the dealership for conspiring to defraud customers by including the hidden costs in sales contracts and lying about the extra charges. Six of those indicted pleaded no contest or guilty to the charges and were sentenced to jail time, probation, and a fine.[48] As a result of this investigation, the California Senate Standing Committee on Government Oversight requested to hear testimony on auto dealer "packing" practices as one of the top ten consumer complaints in 2002.[49]

The State of Florida recognizes these extended warranty products and anti-theft products as insurance, and companies offering these products must register with the department of insurance. Part of this regulation includes providing the product cost, which cannot be marked up further at the dealership.[50] The regulation also allows consumers legal recourse against price inflation by dealers.[51]

Policy Recommendations

Extended Warranties and Anti-Theft Policies as Insurance

Extended warranties and anti-theft products are insurance and should be treated as such. Amend Article 9034 and Article 9035, Texas Civil Statutes to remove the exception from insurance regulation. Texas legislators should:

- classify extended warranty and anti-theft products as insurance
- assure benefits by requiring TDI approval of policy forms
- collect basic information about premiums and losses
- assure good value by regulating prices

If the Legislature is unable to accomplish this, there must be significant measures taken to ensure the TDLR can provide strong and impartial oversight over the sale and administration of these products.

Texas Department of Licensing

In the alternative, improve TDLR oversight by granting the agency authority over benefits and prices.

- Expand the agency's authority to determine a fair price to the consumer for theft, extended warranty and any new products dealers want to introduce. Amend the law to eliminate dealer negotiated prices for add-ons.
- Expand the agency's authority by allowing the board to disapprove contracts for these products if the benefit is not reasonable in relation to the price or is deceptive, misleading, or duplicates required insurance coverage.
- Prohibit dealers from requiring consumers to pay for theft protection if they don't want it.

- Require auto dealers to provide consumers with a copy of the add-on contract upon purchase. Require the price of the product to be clearly marked on the add-on's contract and listed as a separate item on the automobile sales contract.
- Require the Board of TDLR to review annually all complaints filed against dealers or other sellers of extended warranty and theft protection products and develop a plan to address the consumer concerns.
- Information about the number of contracts sold should be made available to the public.
- Advisory Boards should actually meet, should be composed of at least half consumer representatives, and should comply with the statutory requirement to meet every 6 months.

Notes

1 Email from Tanya Gauthreaux, TDLR employee.

2 Email from Caroline Jackson, TDLR employee.

3 For the purpose of this report, anti-theft products involving the installment of complex electronics or tracking devices are not included.

4 AutoNation, Securities and Exchange Commission 10-Q filing, October 24, 2002.

5 Interstate National Dealer Services, Inc filing 10K filing with the Securities and Exchange Commission for the fiscal year 2001, pg. 4.

6 Article 9034, Texas Civil Statutes, Sec. 5(d) and Article 9035, Texas Civil Statutes, Sec. 6(e). "The marketing, sale, offering for sale, issuance, making, proposing to make, and administration of service contracts are exempt from (1) the Insurance Code and other laws of the state regulating the business of insurance." The language for vehicle protection products at Sec. 6(e) is nearly identical.

7 Texas Insurance Code, Title II, Subtitle A, Chapter 101, Sec. 101.051 defines the business of insurance as the making, proposing to make a guaranty, or receiving a premium, issuing or delivering an insurance contract, acting as an agent in the procurement of insurance, collecting commission, adjusting a claim, and more. These are all functions performed by insurers, auto dealers, broker intermediaries and others in the current system of extended warranty and theft protection. Only the Civil Statute exception makes these products anything other than insurance.

8 Article 9034, Texas Civil Statutes, Sec. 5(e)(6).

9 Texas Department of Licensing and Regulation, Registrant lists, provided in response to a Consumers Union Public Information Act request, and Vehicle Protection Product Warrantors, internet download, 8/9/02, www.license.state.tx.us/vpp/vpplist.htm.

10 Article 9034, Texas Civil Statutes, Sec. 6.

11 Automobile Protection Corporation, Securities and Exchange Commissionn 10-K filing, December 31, 1998, pg 4.

12 Automobile Protection Corporation rate filing with the Florida Department of Insurance, December 15, 2001. This company is registered in Texas, but their commission rates are unavailable because they are not required to submit their rates under state law.

13 Interstate National Dealer Services, Inc filing 10K filing with the Securities and Exchange Commission for the fiscal year 2001, pg. 2.

14 Interstate National Dealer Services, Inc filing 10K filing with the Securities and Exchange Commission for the fiscal year 2001, pg. 8.

15 The overcharge is based on the difference between the dealer cost of coverage for each person's individual car (using a detailed rate filing by American Banker available from the Texas Department of Insurance) and the price paid by the consumer. The additional interest charge was calculated using each consumer's own interest rate.

16 Consumer Complaints from Attorney General's Office and Texas Department of Insurance, Property Casualty Filing Transmittal Form, Initial Rate Filing, American Bankers Insurance company of Florida, February 4, 2002.

17 Texas Department of Insurance, Property Casualty Filing Transmittal Form, Rate Filing, Lyndon Property Insurance Company Rate Filings for Vehicle Service Contract Reimbursement Insurance Policy. July 17, 2000.

18 Toyota Extra Care Vehicle Service Agreement Information for Toyota Avalon.

19Attorney General Consumer Complaint #H-0008-0375 Interview with Robert O'Shea.

20 Attorney General Consumer Complaint, no file number, filed February 28, 1999, Attorney General Consumer Complaint File S9903-0012 LKP, and Attorney General Consumer Complaint, No File Number, Filed 7-06-01.

21 Attorney General Consumer Complaint Number S0003-0048.

22 Attorney General Consumer Complaint Number H0006-0588.

23 Service Contract Providers Advisory Board Meeting Minute Notes, July 18 2000, pg. 2. Interstate National Dealer Services, Inc filing 10K filing with the Securities and Exchange Commission for the fiscal year 2001, pg. 3.

24 Attorney General Consumer complaint number D9910-0432.

25 Attorney General Consumer Complaints and Rate Filings of Universal Underwritings for 2001 and Western General Insurance Company 2002, Courtesy Insurance Company's Contractual Liability reimbursement Policy provided to the TDLR 1997, Great American Insurance Gourp Contractual Liability Reimbursement Policy.

26 "Premium Care" Theft-gard Registration Form, 2001.

27 OLYPICARE 5 Year Anti-Theft $5,000 Deductible Benefit Recovery Guarantee Contract.

28 "Premium Care" Theft-gard Registration Form, 2001.

29 Attorney General Consumer Complaint #H0003-0460, Articele 14 (a) of the Vehicle Protection Product Warrantors Law allows dealers to mandate the purchases of an theft protection product if it is already installed on the vehicle.

30 Conversation with Paula Claborn, February 3, 2003.

31 Attorney General Consumer Complaint #H0003-0460.

32 Attorney General Consumer Complaint Number D0001-0613 ESD2, Attorney General Consumer Complaint, no file number, File may 27, 1999, Attorney General Consumer Complaint # S0108-0306, Attorney General Consumer Complaint #D0105-0322.

33 Attorney General Consumer Complaint, S9906-0083.

~~34~~ Attorney General Consumer Complaint #D0011-0555 201 JEFI.

35 Attorney General Consumer Complaint dated February 2, 2001.

36 Attorney General Consumer Complaint dated July 26, 2000, Attorney General Consumer Complaint #D0008-0172.

37 Washington Attorney General News Release "AG Settles Last of Auto Packing Cases," May 22, 1998.

38 Attorney General Consumer complaint number S0106-0108.

39 Texas Civil Statutes, Article 9034, Section 5, e, 6.

40 Texas Civil Statutes, Article 9034, Section 5, c, 10 (e).

41 Texas Civil Statutes, Article 9034, Section 4, e.

42 Coversation with Chris Kadas, Texas Department of Licensing and Regulation, December 9, 2002.

43 Service Contract Providers Advisory Board Meeting Minute Notes, Nov 4, 1999, pg. 2.

44 Service Contract Providers Advisory Board Meeting Minute Notes, July 18 2000, pg. 3.

45 Texas Civil Statutes, Article 9034, Section 4, e.

46 Texas Attorney General Press Release "Attorney General's Office Files Against Three Valley Car Dealerships. June 26, 2002, New York State Attorney General Press Release, "Used Car Dealership Sued For Fraud," May 30, 2001, Washington State Attorney General's Office Press Release,"AG Settles Last of Auto Packing Cases."

47 Los Angeles District Attorney News Release, April 20, 2001. http://da.co.la.ca.us/mr/2001/042001b.htm.

48 Los Angeles District Attorney News Release, April 8, 2002. http://da.co.la.ca.us/mr/2001/042001b.htm.

49 California Select Committee on Government Oversight Briefing Paper. "The Top Ten Consumer Complaints Revisited" Thursday, November 21, 2002.

50 2002 Florida Statues 634.011 8 (a)(b), 1.a & 3. Conversation with Al Willis, Florida Department of Insurance

51 www.jameshoyer.com, reviewed October 29.2002.