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In this Issue:

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The Vexing Problem of Erroneous Vehicle History Reports

By Kieran A. Lasater, Esq., *Fairfield and Woods, P.C.*

I. Introduction

With the rise in popularity of Vehicle History Reports ("VHRs") in used car transactions, consumers have been programmed to demand one. Carfax's Car Fox advertisements are a staple of TV and radio advertising. Experian also enjoys a large segment of the VHR market, which until recently was dominated almost exclusively by Carfax. However, many times the VHRs offered by Carfax, Experian or the other companies in the industry are false and lead to serious problems for dealers.

By way of one example only, on January 6, 2013, the industry's largest player Carfax began reporting "Total Loss" vehicle history designations on its VHRs for numerous vehicles which were, in fact, never "totaled" by an insurance company and which have clean titles. Instead, the vehicles were subject to various types of minor repairs, such as minor panel sprays or bumper repairs. For this, and without any additional apparent justification, Carfax unilaterally reported the vehicles as "Total Losses" on their VHRs. Naturally, auto dealers and individuals alike are up in arms because the practical result of these inaccurate and misleading VHRs is the immediate and drastic reduction in value of the affected vehicles.

For example, a 2010 BMW M3 coupe with 15,000 miles has an NADA estimated retail value of approximately $52,000, and is likely a prime candidate for a Certified Pre-Owned ("CPO") program. That same vehicle with a Carfax VHR indicating it as a "Total Loss" could not even be sold on most dealers' lots, would not qualify for a CPO program (many manufactures requiring that Carfax VHR be included as part of a CPO sale), and its value would be less than half. Due to the false and misleading Total Loss VHR notation, a dealer with such a vehicle would lose the future profit on such a sale—which profit would be even greater if it would have otherwise qualified for a CPO program—as well as the lost trade-in allowance provided to the previous owner on the trade which occurred before Carfax added the Total Loss notation. Today, there are likely thousands of dealers with pre-owned inventory potentially affected by erroneous VHRs, many of which are probably unaware of the problem.

This article will primarily explore the potential civil liability faced by companies for inaccurate and exaggerated VHRs. First, the article will provide a brief background on the major players in the VHR industry, including Carfax and Experian. Next, the article will examine those companies' potential civil liability for the erroneous VHRs—including a potential class action brought by dealers—by examining a similar class action litigation presently faced by Carfax in Ohio and focusing on the Total Loss VHRs as an example. Finally the article will close with suggested changes VHR providers could implement to remedy the problem and avoid potential liability.

II. Carfax, Inc.

According to its website, Carfax is "[t]he most trusted provider of vehicle history information, . . . [and] is used by millions of consumers each year.

[1] Wikipedia reports that Carfax, Inc. was founded in Columbia, Missouri in 1984, and initially focused its business on confronting odometer fraud.[2] Carfax is currently headquartered in Centerville, Virginia, with a data center in Columbia, Missouri, employing up to 750 employees company-wide.[3]

Carfax first offered its services to dealers only, but in 1996 it launched its website which offered its core product (VHRs) to consumers as well.[4] Currently, Carfax is a wholly owned subsidiary of R.L. Polk & Co.[5]

Carfax enjoys approximately a 90 percent market share of the VHR market.[6] It has exclusive agreements with 32 out of 38 manufacturers for their CPO programs, and is by far the most recognized provider of VHRs. Carfax maintains to the public that its VHRs are based on the largest available database of information and are comprehensive and accurate.

III. Experian's Autocheck

The second most prominent purveyor of VHRs is Experian's AutoCheck, with approximately 8-9 of the percent market. Experian's AutoCheck is provided by the Automotive division of Experian, which holds itself out as "a global leader in providing information, analytical and marketing services to organizations and consumers . . . ."[7] The few remaining market participants are not discussed here.

IV. Potential Civil Liability

Because of its lion's share of the market, Carfax will be examined regarding past and current civil actions. Carfax has been the subject of several lawsuits across the nation based upon its VHRs.

Sample of Current and Past Actions

West v. Carfax, Inc., et al.

The largest such suit is an active class action suit pending in the Trumbull County Court of Common Pleas, Ohio, which was initiated in 2004, *West v. Carfax, Inc., et al.*, 2004 CV 01898. The plaintiff, Edward B. West, sued under Ohio's Consumer Sales Practices Act (and common law claims) on behalf of himself and a putative class of similarly affected consumers who purchased VHRs, asserting that Carfax's advertising failed to inform consumers that its VHRs did not contain all information about a particular vehicle's history. The plaintiff sought compensatory and punitive damages, as well as an injunction seeking to compel Carfax to disclose that it did not, in fact, have all the information relative to a vehicle. The class was defined as all persons who purchased a VHR from Carfax between 1996 and October 27, 2006.

After two years of active litigation (including Carfax's failed attempt to have the case dismissed), the parties entered into a non-monetary settlement agreement which would have primarily given class members certain vouchers for future Carfax reports and mechanical inspections of vehicles. Under the civil court rule governing class actions, the court's approval of the settlement was required, and could only be granted if it was "fair, adequate and reasonable." When the court so ruled, objections were made both to its substantive relief for the class (*i.e.*, the value, if any, of the vouchers), as well as the means by which prospective class members were to be given notice of the settlement.

The objections were appealed to the Ohio Court of Appeals, which, by an order entered on December 28, 2009, reversed the trial court and ordered that the case be remanded to determine various points of law relative to the value of the vouchers, the notice to the class members, and discovery related to the class size.[8] According to the appellate court's opinion, at the time the initial complaint was filed, Carfax faced nine similar actions in seven states. The case is presently pending before the trial court, with a hearing currently scheduled for April 8, 2013.

Off Lease Only, Inc. v. Carfax, Inc.

In this action, an independent used car dealer sued Carfax claiming that the manner in which Carfax reports "structural damage" is inconsistent and inaccurate, and that this damaged the dealer by inaccurately listing vehicles in its inventory as having "structural damage," thereby rendering the vehicles unsellable.[9] This situation is directly analogous to the Total Loss problem discussed in this article.

Carfax moved to have the complaint dismissed, arguing that the plaintiff's claims for false advertising under the federal Lanham Act, violation of Florida's Deceptive and Unfair Trade Practices Act, and common law libel claims, each failed. The plaintiff's claims were based on two examples: in one, the dealer bought a car with a clean

Carfax VHR at a Manheim auction, but thereafter, while it was on his lot, the report was changed to show structural damage where none existed; and second, where he sold a car with a clean Carfax, but the report was later changed erroneously to show structural damage leading the purchaser to return and demand rescission, which was granted to avoid a lawsuit.

Based on these allegations—as well as allegations that Carfax's advertising represents that its reports are important to any transaction and should be demanded by consumers and if a dealer does not provide one it is likely hiding something—the court refused to dismiss all but the Lanham Act claim. The Lanham Act claim was dismissed because the VHRs were themselves not advertising and so failed to meet that element of the claim.

With regards to the Florida statutory deceptive trade practices claim, Carfax argued ineffectually that the choice of law provision in the agreement between the parties required that Virginia law apply, but the court disagreed. The court held that Florida law applied because the action did not arise out of the parties' obligations under the contract, but rather "Carfax serves 'millions of consumers' and that by doing so it distributes inaccurate information about Plaintiff's inventory independently from its agreement with Plaintiff." The court further determined that a cause of action for deceptive trade practices was properly pled despite the disclaimers contained in the agreement with plaintiff which stated that its VHRs "may contain errors and omissions" and that Carfax did not guarantee the information as accurate. In discounting the disclaimers, the court noted that Carfax offers the VHRs to entities and individuals who are not parties to the agreement, which thereafter distribute reports to others not affiliated with either party. "To these individuals, the reports may be deceptive notwithstanding the disclaimers in Carfax's agreement with Plaintiff. Moreover, Plaintiff alleges that the reports are arbitrary and false and that Carfax has refused to correct the reports even after having been advised of their falsity."

The case is pending in the U.S. District Court for the Southern District of Florida. Citing undue delay and an impending trial date, on January 25, 2013, the court denied the plaintiff's attempt to amend the complaint for a second time to add a plaintiff and assert class action allegations. This case is directly relevant to the Total Loss issue and is demonstrative of the types of claims that Carfax or Experian could face despite the existence of the disclaimers discussed above.

Webbv. Carfax, Inc., et al.

In October 2008, the plaintiff, acting *pro se*, filed a suit in the federal court for the District of Hawaii against the former owners of a BMW he purchased, the financing institution, as well as Carfax. The claim against Carfax was described as undefined federal and state consumer protection law violations based upon the allegation that although Carfax advertised that it had information from all 50 states, it did not have the ability to check accident history information in Hawaii.[10]

Carfax was able to have the complaint dismissed based upon lack of federal subject matter jurisdiction for want of complete diversity and the lack of the threshold $75,000 amount in controversy requirement. Likewise, the court found that the plaintiff had failed to allege a federal statute upon which to find federal question jurisdiction. Therefore, the complaint was dismissed.

Carfax, Inc. v. Browning

In this case, at issue was the enforceability of a venue provision in Carfax's contracts with individual purchasers of its VHRs. The plaintiff had sued Carfax in Alabama for its failure to include an accident history in its VHR, and brought claims for fraud, misrepresentation, suppression and negligence. The plaintiff sought compensatory and punitive damages. Carfax, in turn, moved to dismiss the complaint based upon a venue provision requiring that suits be brought in Virginia. The trial court disagreed, and held that to litigate the case in Virginia was so inconvenient that it rendered the clause unenforceable. Carfax appealed the issue, and the Supreme Court of Alabama remanded the case to the trial court for a determination of whether it was "seriously inconvenient" for the plaintiff to litigate the case in Virginia, so as to render the venue provision unenforceable under Alabama law.

Accordingly, this case highlights the fact that despite purporting to require that all actions be brought in Virginia, Carfax's various contracts may not be enforced by a court to require such.

NADC Job Board

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Potential Future Liability Based on Recent "Total Loss" Practice

Carfax's recently-implemented practice of declaring vehicles a "Total Loss" when no insurance company has made such a determination is extremely troubling to dealers and individual owners alike. It therefore provides an ideal hypothetical regarding potential liability faced by purveyors of VHRs.

For dealers, just like the plaintiff in the *Off Lease Only* case discussed above—whose inventory value was reduced by the addition of erroneous "structural damage" information after he purchased the vehicle with a clean report and title—the problem has a real and immediate impact on the bottom line, as well as causes disruption to business. The vehicles affected by the Total Loss designation are unsellable on most lots, and so likely must be auctioned off at salvage prices, with significant losses of profit and trade-in allowances.

An affected dealer could bring a class action on behalf of itself and all other dealers who likewise had a Total Loss designation applied to one of their used vehicles without such a determination having been made by an insurance company. The basis for the claims would be that the report is false, deceptive and misleading, and the product of a negligent determination by Carfax, exercising independent judgment upon which consumers knowingly rely. By voluntarily assuming an obligation to accurately report vehicle histories, for a fee, Carfax assumed the duty to use reasonable care in fulfilling the duty. The false designation in turn is the direct and proximate cause of reasonably foreseeable losses and damage to the dealers. The conduct is made even more egregious where Carfax refuses to remove the designation after being confronted with its falsity.

Based on these general assertions, various causes of action could be asserted, including deceptive trade practices claims under either state statutory provisions or the common law, negligence, negligent misrepresentation, and tortious interference with business expectancy, among others. Of course the general rule is that litigants are responsible for their own attorney's fees under the American Rule; however, in many states, attorney's fees are available as a component of an award to a successful plaintiff under statutory deceptive trade practices statutes, and, if the conduct is egregious enough, double or treble damages may also be available.

In addition to potential class action suits, Carfax is equally susceptible to individual actions by affected dealers and owners alike. The limiting factor in individual suits, however, is the potential that the damages at issue will be overwhelmed by the costs of litigating the claims to a judgment. This is one benefit of class action suits; in that the costs to litigate the claims can be spread out over numerous claims, thereby making the case financially feasible.

As the *West* class action case against Carfax in Ohio reflects (pending since 2004), Carfax's attempts to inject itself into the heart of every used car transaction based upon its alleged preeminence and the comprehensive nature of its VHRs—to its significant financial betterment—comes with certain risks. As more members of the public rely upon and give credence (deserved or otherwise) to the accuracy of their VHRs, the more likely it becomes that false information will be the subject of suits.

V. Potential Policy Changes to Correct Problem

Why Carfax took it upon itself to implement this new Total Loss designation change is unclear. What is clear is that the designations are many times demonstrably inaccurate, misleading, and could be the basis of civil liability for Carfax. Moreover, they do great harm to the relationship between dealers and Carfax, unnecessarily.

Carfax should immediately retract the recent Total Loss designations made since January 6, 2013, which are not based on an actual insurance determination. A true Total Loss determination by an insurance company would necessarily result in a "salvage" or similar title brand. Vehicles with a clean title should not be designated a Total Loss by Carfax. Carfax should also work with its consumers and dealers to make amends for, and pay compensation to, affected dealers and individuals for damages caused by this new policy in order to preserve its goodwill and market strength.

If Carfax has some legitimate reason for refusing to immediately retract the policy and correct the VHRs automatically, it should create a specific hotline for affected dealers and consumers to contact Carfax and rebut the Total Loss designation. Additionally, an expedited process should be instituted to minimize the amount of time it takes to correct the false VHRs.

Representatives of local automobile dealers associations and members of the National Association of Dealers Counsel ("NADC," of which the author is also a member[11]) have been in contact with Carfax on behalf of their dealer members seeking relief from the policy. Recently, on January 10, 2013, in response to one such discussion, Steve Blumenthal, who is the General Counsel for Carfax, provided the following in an email:

…. While Carfax is confident that the [Total Loss] data is accurate, Carfax appreciates the concerns raised by its dealer customers. Carfax pulled the data off its [VHRs] earlier today and is launching a process to determine ways to present the data that would better enable consumers and dealers to understand the context of the data and to weigh its importance. We will also communicate with our dealer customers before publishing the data….[12]

According to the email from Mr. Blumenthal, the erroneous data has been removed from the VHRs as of January 10, 2013. The Total Loss designations began appearing on January 6, 2013, and, therefore, numerous transactions could have been affected during this five-day period, if, in fact, the erroneous Total Loss designations were completely retracted on January 10, 2013.

Moreover, it appears that the data will eventually be re-released, however, potentially in another form. What form that proves to be may well impact Carfax's potential future liability for the Total Loss designations. The issue of inaccurate or over exaggerated VHRs goes beyond Carfax, of course, and Experian and the other market participants who tout the comprehensive and accurate nature of their VHRs are equally susceptible to such potential suits.

VI. Conclusion

VHRs are a staple of the used car industry. They will only gain in prominence going forward. However, as the Total Loss example highlights, they can suffer from serious flaws and sometimes be false and misleading, resulting in avoidable damages to dealers. These damages may be recoverable through civil action, and, potentially, class action litigation. ■

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References

1. CARFAX-About Us & What We Have To Offer When Buying a Car, available at: http://www.carfax.com/about/car_history/hcabout.cfm (last visited 1/10/2013).
2. Carfax (company), available at: http://www.en.wikipedia.org/wiki/Carfax_%28company%29 (last visited 1/10/2013).
3. *Id*.
4. *Id*.; *see also supra* note 1 ("While our [VHR] is at the heart of our business . . . .").
5. *See supra* note 2.
6. *See Experian Info. Solutions, Inc. v. Carfax, Inc.*, (No. 11-CV-8927, N.D. Ill., Dec. 16, 2011) (exhibit to complaint).
7. About AutoCheck, available at: http://www.autocheck.com/consumers/about/aboutUs.do (last visited 3/6/13).
8. *West v. Carfax, Inc., et al.*, 2009-Ohio-6857 (Oh. Ct. App. 2009); 2009 WL 5064143 (Dec. 24, 2009) (unreported decision); *see also* Michael J. Hassen, Carfax Class Acton Defense Cases—West v. Carfax: Ohio Appellate Court Reverses Trial Court Approval Of Class Action Settlement Holding Notice To Class Members Was Inadequate, available at: http://classactiondefense.jmbm.com (last visited 1/10/2013).
9. *See Off Lease Only, Inc. v. Carfax, Inc.*, 2012WL1966372 (S.D. Fl. May 31, 2012) (unreported decision).
10. *Webb v. Onizuka*, 2009WL943274 (D. Hawaii, April 8, 2009) (unreported decision).
11. This article does not reflect the opinions or beliefs of any other individual or entity, including, but not limited to, the NADC. This article has not been endorsed by the NADC.
12. Email entitled "RE: phone conversation," dated 1/10/2013 at 3:20 p.m., from Steve Blumenthal [SteveBlumenthal@carfax.com].

Executive Director's Message

Erin H. Murphy
NADC Executive Director

Well folks, it is that time of year again – March Madness! 2013 is officially underway and spring is right around the corner (although some of you who live on the East Coast might find that doubtful). March is a great time to reflect on those goals that were set on January 1st and to plan ahead for the rest of the year.

NADC has some exciting events and opportunities coming up in 2013:

Attorney Directory

Please watch the mail for your 2013 NADC attorney directory. It contains the contact information for all NADC members. We've organized the directory by state to assist you when you are looking for a referral. We hope that you will find the directory a useful tool and an easy reference guide to the NADC community.

Webinars

Our next webinar, Putting the Brakes on Losses: How Auto Dealers Can Use Their Insurance Policies to Protect Profitability, is scheduled for April 9th at 2:00 PM EST. Barry Buchman with Gilbert LLP will cover four insurance coverage topics:

(1) Insurance coverage for losses arising from natural disasters like Super Storm Sandy, and related supply chain issues;
(2) Insurance coverage for consumer claims alleging errors and omissions in connection with the extension of credit, *e.g.,* Truth-In-Lending claims and claims arising from defaults/repossessions;
(3) Insurance coverage for wage and hour claims; and
(4) Insurance coverage for cyber-security risks and losses. Registration is available at www.dealercounsel.com

Are you interested in presenting a webinar for the NADC community? If so, please email me (emurphy@dealercounsel.com) your proposed topic and we will work together to schedule the webinar. All NADC members are encouraged to present webinars for your peers.

Article Submissions for The *Defender*

NADC is dedicated to providing you with invaluable resources for your auto dealer practice. We rely on the NADC community to share their expertise and knowledge through articles published in The *Defender*. Please send your contributions or proposals for articles to Editor Mike Charapp at mike.charapp@cwattorneys.com.

9th Annual NADC Member Conference

Additionally, we hope you will join us at the 9th Annual NADC Member Conference being held April 28 – 30, 2013 at the Montage Resort in Laguna Beach, CA. The conference will be a two day program designed to provide you with updates, best practices, lessons learned and other useful information. The planning committee has prepared a great agenda and you will be sure to take home valuable tools that will benefit you and your clients. Please check the website www.dealercounsel.com for a detailed agenda in the "Events" section.

2013 NADC Fall Conference

Please save the date for the 2013 NADC Fall Conference. The conference will be held October 6-8, 2013 at The Trump Hotel in Chicago, IL. For the first time this year, the program will be extended to 1 ½ days. This extra ½ day means more educational sessions and CLE credits for all! The hotel room block is now open. Hotel reservations can be made by calling 877-45-TRUMP. Please reference the NADC Fall Conference to receive our discounted rate of $299 a night.

As always, we invite you to share your ideas on how we at the NADC can support you in your dealer practice. We look forward to an exciting and successful 2013! ■

Reminder!!!

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Limitations on Manufacturers' Power to Require Exclusive Use of their Service Contracts

Feature Article

By Andrew Weill & Keith Long, *Weill & Mazer, APC*

The general manager of your client, a new car dealership, calls you to discuss a non-factory service contract program that it wants to offer its customers. "Unfortunately," the manager says, "the manufacturer told us we must sell their service contracts exclusively or we will be at risk of losing our franchise." Can the factory really do this?

The answer depends on a careful review of the law of the state in which your client is located. Over the last decade, at least five states have enacted legislation and made it unlawful to coerce a dealer into selling their service contracts by threatening injury to business or engaging in other discriminatory behavior. Other states have anti-discrimination statutes that are more general, and do not provide sections specifically relating to service contracts.

In California, the law was amended in 2011 to specify that it is unlawful to discriminate against a franchise because that franchisee sells a service contract not endorsed by the manufacturer. *See,* Cal. Vehicle Code §11713.3(x)(1). The statute defines behaviors that are discriminatory including: 1) statements of any type that the dealer is obligated to exclusively sell the manufacturer's service contract; 2) statements of any type that a dealer would suffer negative consequences for selling an unapproved or unendorsed service contract; 3) measurement of a dealer's performance based on service contract sales; 4) requirements that a dealer actively promote a manufacturer endorsed service contract; 5) restrictions on access to vehicles, parts, vehicle sale or service incentives that are conditioned upon the sale of endorsed service contracts.

The California statute also sets forth what behavior is permissible for the manufacturer. There are three specific exceptions to what constitutes discrimination. First, the statute states that "[u]nfair discrimination does not include, and nothing shall prohibit a manufacturer from, offering an incentive program to vehicle dealers who voluntarily sell or offer to sell service contracts…"

Second, a dealer may also be required to provide a manufacturer approved service contract if a used vehicle is part of a manufacturer "certified vehicle" program.

Third, manufacturers may require California dealers to place a service contract disclosure on any service contracts that are not endorsed or approved by the manufacturer. The language for this disclosure is provided by statute and must read: "The service contract you are purchasing is not provided or backed by the manufacturer of the vehicle you are purchasing. The manufacturer of the vehicle is not responsible for claims or repairs under this service contract."

If the manufacturer's conduct runs afoul of subdivision (x)(1), and none of the three exceptions are applicable, a quick call or letter from you to the manufacturer may resolve the issue expeditiously.

Other states have laws that are very similar to California. For example, the Pennsylvania Professions and Occupations title forbids a manufacturer from coercing new vehicle dealers in to exclusively selling a manufacturer endorsed service contract. *See* 63 P.S. 818.12. The Pennsylvania statute defines acts of coercion in terms that are virtually identical to the California anti-discrimination statute.

Despite their similarities, the Pennsylvania and California laws have a distinguishing factor. While California lists three exceptions, Pennsylvania only defines one; in Pennsylvania, it is not coercion if a manufacturer or distributor provides an incentive program to a dealer who makes the voluntary decision to sell a manufacturer endorsed service contract exclusively. *Id.*The Pennsylvania exception to what constitutes coercion or discrimination is followed in Louisiana, Idaho, and Virginia.

On the other hand, Arizona forbids discrimination in the same way that California does –but statute does not include any statutory exceptions to the rule of what manufacturer behavior is not allowed.

Nebraska has a statute specific to service contracts, although it is less detailed. Its statute forbids manufacturers from stating or representing that a dealer is obligated to sell manufacturer sponsored service contracts. *See,* Neb.Rev.St. 60-1437. However, the Nebraska legislature does not define what type of behavior would constitute a direct or indirect representation.

In Oregon, the statute takes a very general approach and does not specifically mention service contracts. Instead, the statute forbids manufacturers from coercion or unfair competition with its franchise holders. An illustration of this general statute occurs in Oregon, where it is unlawful for a manufacturer to "Coerce or attempt to coerce a dealer to enter any agreement or sales promotion program by threatening to cancel the franchise of a dealer" or "unfairly compete with a dealer in any matters governed by the franchise". Or.St. 650.130.

Although the specificity varies, in each of the above examples the dealership is protected from coercive or threatening behavior on the part of the manufacturer. The protections afforded by each state have several different remedies which the dealer may seek to prevent further harassment. In states like California, the manufacturers' behavior is unlawful.13 California Code of Regulations 314.00. Your letter to the manufacturer should require that the manufacturer cease and desist or risk monetary penalties for each violation.*Id.* In states like Oregon where the manufacturer's actions fall under a more general umbrella, a dealer may sue for an injunction and recover damages. O.R.S. 650.170.

While several states are discussed in this article, the list of statutes may not be complete. If you have run into this type of problem in your state, please contact the authors of this article who are maintaining a database for this type of law. ■

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