CFAnews

September 1996
Volume 21, No. 5
ISSN #0732-8281

Fed Releases Inadequate Auto Leasing Rules

The Federal Reserve released final rules in September spelling out the information auto leasing companies must provide to consumers at the point of sale.

While the rules will provide consumers with more information, that information is insufficient to allow them to negotiate the best deal when they lease a car, said CFA Senior Projects Director Mary Ponder.

"Consumers need a finance rate in order to compare leasing offers. A federally mandated, standardized annual lease rate would assure uniform disclosure of lease cost information," she said.

Instead, under the new rules consumers will be provided with new disclosures itemizing all costs associated with the lease, any trade-in allowance, the amount due at signing, the total of the payments, an explanation of how the up-front charges and the monthly payment were calculated, and a warning that returning the car early could result in additional charges.

Rules Fail To Include Lease Rate

"Itemizing the costs on a contract helps the consumer understand what the terms of the contract are, but it doesn't provide the necessary information to compare offers. Consumers still won't be able to tell if they have a good deal," Ponder said.

CFA and some of the state attorneys general had argued in favor of requiring a standardized lease rate in comments with the agency last year.

In choosing not to require an annual lease rate, the Federal Reserve Board argued that such a rate is too easy for dealers to manipulate by changing other components of the lease.

That reasoning should have led the Fed to adopt a standardized computation, not to "duck the issue," Ponder said. "These numbers can all be manipulated. That's a stronger argument for them to standardize how things are done," she added, noting that Canada plans to require disclosure of a standardized lease rate beginning in June 1998.

Leases have become increasingly popular in recent years, as rising prices have made it harder for many consumers to afford to buy a car.

According to the Federal Reserve Board, leases accounted for a third of all passenger car deliveries to consumers in 1995, up from 19 percent in 1989. The percentage is even higher — as high as 70 percent — among certain luxury cars.

Because the law in question applies only to leases of $25,000 or less, however, the rules may not apply to leases on many luxury cars. CFA had advocated eliminating the $25,000 cap.

While the contract disclosure rules won't become mandatory for a year, the Fed is providing a form consumers can use as a guide when they go shopping for a lease. Copies are available from the Fed's public information office and its Division of Consumer and Community Affairs.

Disclosure of Termination Costs Is Inadequate

Meanwhile, CFA is continuing to press for more complete and understandable disclosures for consumers and plans to submit additional comments to the Federal Reserve Board in November, Ponder said.

CFA is particularly concerned that the new rules do not require adequate disclosures about the potential costs of early termination, which can be substantial, she added.

According to industry sources, between 30 and 40 percent of two-year leases and between 30 and 60 percent of four-year leases are terminated early.

While the new rule requires a general warning that substantial additional charges may be imposed in cases of early termination, the dealer is not required to provide an example of the costs at the end of the first year, as CFA and other groups had requested.

CFA plans to ask the Federal Reserve Board to clarify that dealers must disclose that the consumer is entitled to a written explanation of the method of calculating early termination charges.

Meanwhile, Congress included provisions in the Omnibus Consolidated Appropriations Act of 1996 amending the Consumer Leasing Act to eliminate several advertising disclosure requirements.

Congress Weakens Advertising Rules

Specifically, lease advertisements will no longer have to disclose the total amount of the lease payments or the end-of-lease costs. As a result, consumers will no longer see important information — such as mileage allowances, cost-per-mile over that amount, and the purchase price of the car at the end of the lease — until they are handed the contract to sign, Ponder said.

Furthermore, as a result of the congressional action, the revised rules on advertising that the Federal Reserve Board issued in conjunction with the lease contract disclosure rules in mid-September will have to be revised.

"In the meantime, consumers will continue to see misleading newspaper ads with mouse-sized print and television ads with blurred disclosure information," said CFA Chairman Howard Metzenbaum.

"These delays in reforming automobile leasing ads are unpardonable. Consumers are losing millions of dollars as a result," the former senator said.

Congress Clears Securities Bill

In one of its final acts before adjourning for the year, Congress adopted legislation to streamline regulation of securities markets.

The legislation was adopted after House and Senate negotiators reached a last-minute compromise on investment adviser oversight provisions.

CFA Director of Investor Protection Barbara Roper called the investment adviser provisions "a major disappointment, since they do absolutely nothing to rectify current inadequacies in investment adviser oversight."

"There has been nearly universal agreement for the better part of a decade that the current level of investment adviser oversight is woefully inadequate," she said. "With this legislation, Congress gave its stamp of approval to that status quo."

Roper acknowledged, however, that the compromise was an improvement over the original Senate version and that the House conferees had probably gotten the best deal they could from an intransigent Senate.

While Rep. Edward J. Markey (D-MA) led the fight on investment advisers, he received strong backing from Reps. Jack Fields (R-TX) and Thomas J. Bliley (R-VA), chairmen respectively of the Telecommunications and Finance Subcommittee and the Commerce Committee, and John Dingell (D-MI), she noted.

"Without the unified efforts of the House conferees, we would have ended up with legislation that seriously undermined the minimal protections currently in place," she said. "They deserve a vote of thanks from consumers."

Bill Divides Regulatory Jurisdiction Over Advisers

Like the original Senate version, the compromise divides regulatory jurisdiction over investment advisers between the states and the Securities and Exchange Commission, giving the SEC exclusive authority over advisers to mutual funds and advisers with $25 million or more in assets under management.

Advisers with less than $25 million in assets under management will be exempt from federal regulation so long as they are registered at the state level.

"Unless the states take dramatic steps to improve their regulatory programs, this will leave the majority of advisory firms subject neither to federal oversight nor to adequate state oversight," Roper said.

"On the other hand, because the SEC already focuses its limited resources on oversight of large advisers, this approach is unlikely to yield any dramatic improvements in oversight of large advisers unless substantial additional resources are provided," she said.

The bill does authorize $20 million for investment adviser oversight in the next two fiscal years, "but there is no guarantee that money will be appropriated," Roper said.

States Retain Authority To License Individuals

In a major improvement over the original Senate version, states will retain authority under the compromise to oversee the individual representatives of federally registered firms who do business within their borders, as well as the representatives of state-registered firms.

"This allows states to continue to conduct routine background checks and deny registration to those with a history of abusing client trust, to require testing, and to otherwise oversee the activities of these individuals," Roper said. "This is an important tool for preventing fraud."

"Since the majority of investment adviser representatives work for larger firms, the act would have seriously undermined existing investor protections without this key improvement," she said.

"Unfortunately, in their last-minute haste to throw together a compromise, the conferees drafted highly ambiguous language in this area," she added.

The bill preserves the right of states to oversee investment adviser representatives with "a place of business" in the state, whereas states currently can register any investment adviser representative who conducts business in the state, regardless of whether they actually maintain a place of business there.

Sen. Paul Sarbanes (D-MD) entered a statement in the record clarifying that no restriction of state authority in this area was intended.

"If members of the industry seek to take advantage of this ambiguity to escape state registration requirements, Congress may need to go back and clarify the language," Roper said.

The House succeeded in inserting another pro-investor provision, requiring

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Efforts Needed To Combat Insurance Fraud

Consumers and insurers have a common interest in combatting insurance fraud but tend to view the problem differently, CFA Director of Insurance J. Robert Hunter said in a speech at a September insurance fraud summit in Florida.

The fraud summit was co-sponsored by the Coalition Against Insurance Fraud, the Florida Attorney General's Office, and the Florida Insurance Commission.

"Since fraud costs are ultimately borne by consumers, it is important to understand how consumers view insurance fraud," Hunter said.

He outlined four key concerns consumers have about fraud:

Consumer Concerns About Fraud Outlined

• Consumers fear scams by insurers and agents and do not trust insurance providers.

Cutting through the "circle of distrust" between consumers and insurers "must be the centerpiece of any strategy to curtail fraud," Hunter said.

"Consumers distrust most insurance companies, and that's why they feel it is okay to try to get even if a claim occurs. While I reject this response, you have to understand it comes from a feeling of abuse and disrespect," he added.

If insurance companies earn the trust of their customers, they will likely have fewer problems with "soft" fraud and fewer lawsuits, he said.

• Consumers believe insurers have done too little to fight fraud.

Recent scandals involving Met Life, New York Life, and Prudential have reinforced consumers' concern that insurers are slow to combat internal fraud, he said.

Meanwhile, "fighting external fraud was lax for decades," in large part because higher costs ultimately led to higher profits, he said. "As long as costs rose within the insurer's projection of costs, called trends by the actuaries, insurers would make more money in the long run by letting costs rise," he explained. This created a "perverse disincentive for insurers to fight fraud."

Hunter credited California's Proposition 103 with changing that attitude. "Soon after Proposition 103 passed, insurers began to seriously look at all aspects of cost," including fraud, he said.

As a result, insurers have taken a number of steps to fight external fraud, including creating Special Investigative Units to investigate suspicious claims and joining with consumers to combat fraud through the Coalition Against Insurance Fraud.

• Some "normally honest consumers" will engage in soft fraud, such as trying to cover a deductible or recover their premiums.

Surveys by the Insurance Research Council have found that 28 percent of consumers say it is okay to pad a claim to cover the deductible, and 24 percent say it is okay to pad a claim to recover previously paid premiums, Hunter noted.

While this problem can be lessened by companies' treating customers better, "more must be done," he said.

Part of the answer, he said, is education. "People need to be told that this costs all of us. People need to be reminded about how wrong this is. And consumer groups must be at the forefront of saying so," he said.

• Consumers do not want fraud prevention efforts to unnecessarily delay or improperly deny their legitimate claims.

"Consumers want to join in on helping lower fraud by all parties, but when we file a legitimate claim, we want prompt and courteous action," he said. "We understand that this creates a tension between fighting fraud and paying claims."

Hunter said a "protocol" is needed that all parties can agree upon for determining when a claim is suspicious. This must include a factual basis for suspicion "and the need for early notice of suspicion to the consumer."

Coalition Takes Lead On Anti-fraud Efforts

The fraud summit brought together individuals from varied backgrounds — including prosecutors, law enforcement representatives, insurance regulators, insurers, agents, and consumer groups — to try to build consensus as the basis for working on these issues together in Florida over the long-term, said Dennis Jay, Executive Director of the Coalition Against Insurance Fraud.

It represents the first attempt to replicate the coalition's consensus-building work at the state level, he said.

As the result of the summit, three working groups were formed, and a couple of minor legislative initiatives were agreed on, he said.

CFA worked to create the Coalition Against Insurance Fraud as part of an overall effort to encourage consumer and industry cooperation to bring down insurance costs. Convened in 1993, the coalition brings together consumer groups, industry groups, and government agencies to combat all forms of insurance fraud through public information and advocacy.

Since then, the coalition has developed both a model insurance fraud act and a model fraud bureau bill. In 1996, four states enacted legislation based on the model fraud bill, and four more enacted anti-fraud legislation with assistance from the coalition.

The coalition has also developed aggressive public education and research programs to increase both knowledge about insurance fraud and the effectiveness of efforts to combat it.

"It is gratifying that the coalition has taken the lead in advancing anti-fraud initiatives throughout the country," said CFA Executive Director Stephen Brobeck.

Securities Bill

(Continued from Page 1)

the SEC to establish an 800-number investors can call for background information, including disciplinary history, of investment advisers.

"Given the inadequate level of regulatory oversight that is likely to persist under the legislation, consumers will need to take special precautions in choosing an adviser," Roper said. "This 800-number should aid them in selecting an honest adviser."

State Regulation Scaled Back

Despite the disappointing investment adviser provisions, Roper said the overall bill was a major improvement over earlier versions, which would have completely dismantled the system of state securities regulation.

Instead, it:

• restricts state regulation of certain securities, including mutual funds and securities sold on national exchanges, but it preserves state anti-fraud enforcement authority in these areas;

• preempts state requirements for broker-dealers related to capital, margin, books and records, bonding, and reports that differ from or are in addition to federal requirements; and

• requires the SEC to conduct studies in both the securities offerings and broker-dealer areas of the affect that lack of uniformity in state law has on the industry, as the possible basis for further legislation.

"While these changes are modest compared to earlier radical deregulatory proposals, it will take time to determine how they will affect the level of protection available to investors, particularly at the state level," Roper said.

"Meanwhile, since this Congress has satisfied many of the most pressing industry demands for litigation reform and regulatory relief, perhaps the next Congress will return its attention to measures that benefit investors," she said.

Consortium Releases Ten Purchase Mistakes

A little over one year into its campaign to teach consumers to make better purchase decisions, the Consumer Literacy Consortium released a list in July of ten big purchase mistakes consumers typically make.

"Consumers lose billions of dollars each year because of hasty, uninformed purchases — not just on big ticket items, but on everyday purchases as well," said CFA Executive Director and CLC Chairman Stephen Brobeck.

The CLC release featured common, repeated mistakes that needlessly cost consumers, including:

• leasing rather than buying a car in the belief that leasing costs less;

• not searching carefully for a competent, honest auto mechanic;

• assuming their insurance agent will "shop the market" to find the best auto or homeowner policy;

• not holding a cash-value life insurance policy for at least 15 years;

• not maintaining the minimum balance required to avoid checking fees;

• holding many credit cards;

• taking out a 30-year mortgage loan, rather than a 15-year loan, just because the monthly payments are lower;

• paying in full for a home improvement before the work has been completed satisfactorily;

• purchasing new appliances that are not energy efficient; and

• not comparing unit prices found on supermarket shelves.

Coalition Offers Consumer Tips

The CLC is a unique working group of representatives from consumer groups, federal and state government agencies, business organizations, and educational institutions that seeks to develop and disseminate essential consumer information.

CFA convened the consortium in 1993 after a major survey of consumer knowledge initiated by CFA found significant gaps in consumer knowledge.

In April of 1995, the CLC launched a campaign to reduce the more than $100 billion a year of wasted expenditures by publicizing money-saving tips about key consumer purchases.

The tips are contained in a free consumer guide, "66 Ways to Save Money," which offers simple, straightforward advice about purchases involving 28 essential consumer products and services.

"The 66 tips represent the best money-saving advice from America's leading consumer experts," said CLC member Robert Krughoff, President for the Center for the Study of Services, which publishes *Checkbook Magazine*. "By following the tips, the typical family can effectively give themselves a tax-free raise of more than $1,000, without changing their lifestyle."

"Only a minority of Americans consult consumer publications or other information sources before purchasing products, and the consumer information available is not always in agreement. By developing and publicizing simple tips, the Consumer Literacy Consortium is making it easier for consumers to save money and buy smart," Brobeck said.

Half A Million Brochures Distributed

Since launching the campaign, which has received extensive media attention, the consortium has distributed nearly 500,000 copies of the brochure. It recently received a grant from AT&T Universal Card Services Partners in Credit Education program to print an additional 300,000 copies for distribution to those served by consumer credit counseling services.

AT&T Universal Card Services also paid for distribution of more than 100,000 copies of the brochure with state employee payroll checks in Florida. This was arranged with assistance from Walter Dartland of the Consumer Fraud Watch and with the support of Governor Lawton Chiles.

With funding from NYNEX, the Consortium has also had the brochure translated into Spanish, and 20,000 copies of the Spanish version are currently being distributed through Consumer Action and La Raza.

The money-saving guide is available free from the CLC by sending a self-addressed, stamped business size envelope to "66 Ways to Save Money," P.O. Box 12099, Washington, D.C. 20005-0999. For a copy of the 10 Mistakes press release, send a self-addressed, stamped business size envelope to "Ten Mistakes," CFA, 1424 16th Street, N.W., Suite 604, Washington, D.C. 20036.

CFA's PAC Endorses Congressional Candidates

In September, CFA's political action committee issued endorsements of 173 candidates in the 1996 congressional elections.

CFA endorsed 102 incumbents in the House of Representatives, six Senate incumbents, and three House members running for open Senate seats. In addition, CFA endorsed three challengers to anti-consumer incumbents in the Senate, 47 challengers to House members with poor consumer voting records, and 12 candidates for open House seats.

"The last Congress, with its unprecedented attack on consumer rights and protections, offers clear proof of how important it is to look at a candidate's position on consumer issues when choosing a representative," said CFA Executive Director Stephen Brobeck.

"An endorsement from CFA lets voters know who has stood with consumers in the past and who is most likely to stand with them when votes on important consumer issues are taken in the future," he said.

Incumbents' Voting Records Analyzed

Incumbents and House members running for Senate seats were evaluated on the basis of their career voting records on key consumer issues. Specifically, those members of Congress with a lifetime voting record of 80 percent or above, based on CFA's annual congressional voting record, were automatically awarded endorsements.

Members with lifetime records between 70 and 80 percent were given a questionnaire regarding important consumer issues. Their responses were then compared to those of their opponents, and a decision regarding endorsement was made.

Endorsements of challengers and candidates in open races were also based on an evaluation of their responses to a candidate questionnaire and their positions on key consumer issues. In assessing challengers, CFA's PAC also considered the consumer voting record of the incumbent they are challenging.

Based on their voting records while in Congress, Brobeck said, the incumbents endorsed by CFA have been:

- watchdogs of consumers pocketbooks, trying to ensure that the financial interests of corporations do not overtake the financial interests of the American family;
- defenders of the health and safety of all citizens, supporting strong new consumer protections and opposing efforts to weaken or scrap important pro-consumer programs already in place; and
- champions of "the little guy," fighting to keep a fair balance between the interest of companies in strengthening their bottom lines and the interest of all consumers in being protected from dangerous products and from unscrupulous business practices.

"These legislators have worked to make sure the American people get the most for their tax dollars. They have worked to make opportunities available for consumers while protecting them from dangerous products and unfair business practices," Brobeck said.

Non-Incumbent Endorsees Voice Strong Pro-consumer Views

As for the non-incumbents endorsed by CFA, Brobeck said, "these candidates have expressed strong pro-consumer views on important issues ranging from protecting consumers from dangerous products, insulating their pocketbooks from monopoly abuse, and securing the safety of the food we eat and the air we breath."

Brobeck noted that, for the first time in recent history, no Republican candidates earned a CFA endorsement. He attributed this to the deregulatory agenda of the new Republican majority in Congress and the overall decline in consumer voting records that accompanied it.

"In the 104th Congress, consumer protections that evolved over decades with bipartisan backing were subject to repeated attacks," he said. "The fact that many, though certainly not all, of the anti-consumer proposals put forward were either defeated or moderated is testimony to the efforts of pro-consumer members."

"If consumers are to move from defense to offense, however, then the American people must not only return to office those members who have stood with consumers in the past, but they must elect those challengers and open seat candidates who will put consumers at the top of their agenda," he said.

1996 CFA-Endorsed Congressional Candidates

Senate

DE: Sen. Joseph Biden (D)
ID: Walter Minnick (D)
IL: Rep. Richard Durbin
IA: Sen. Tom Harkin (D)
MA: Sen. John Kerry (D)
MI: Sen. Carl Levin (D)
MN: Sen. Paul Wellstone (D)
NJ: Rep. Robert Torricelli (D)
NC: Harvey Gantt (D)
RI: Rep. Jack Reed (D)
SC: Elliott Close (D)
WV: Sen. John D. Rockefeller, IV (D)

House

AL: Bob Gaines (D-02)
AZ: Rep. Ed Pastor (D-02)
Alexander Schneider (D-03)
AR: Marion Berry (D-01)
Boyce Davis (D-03)
CA: Roberts Braden (D-02)
Rep. Robert Matsui (D-05)
Rep. Lynn Woolsey (D-06)
Rep. George Miller (D-07)
Rep. Nancy Pelosi (D-08)
Rep. Ronald Dellums (D-09)
Ellen Tauscher (D-10)
Jason Silva (D-11)
Rep. Tom Lantos (D-12)
Rep. Pete Stark (D-13)
Rep. Anna Eshoo (D-14)
Rep. Zoe Lofgren (D-16)
Rep. Sam Farr (D-17)
Paul Barile (D-19)
Deborah Vollmer (D-21)
Rich Sybert (R-24)
Diane Trautman (D-25)
Rep. Howard Berman (D-26)
David Levering (D-28)
Rep. Henry Waxman (D-29)
Rep. Xavier Becerra (D-30)
Rep. Matthew Martinez (D-31)
Rep. Julian Dixon (D-32)
Rep. Lucille Roybal-Allard (D-33)
Rep. Esteban Torres (D-34)
Rep. Maxine Waters (D-35)
R.O. "Bob" Davis (D-39)
Robert Conway (D-40)
Rep. George Brown (D-42)
Anita Rufus (D-44)
Sally Alexander (D-45)
Loretta Sanchez (D-46)
Tina Louise Laime (D-47)
Rep. Bob Filner (D-50)
CO: Al Gurule (D-03)
CT: Rep. Barbara Kennelly (D-01)
Rep. Sam Gejdenson (D-02)
Rep. Rosa DeLauro (D-03)
FL: Kevin Beck (D-01)
Rep. Corrine Brown (D-03)
Sandy Gordon (D-13)
Rep. Carrie Meek (D-17)
Rep. Alcee Hastings (D-23)
GA: Rep. Cynthia McKinney (D-04)
Rep. John Lewis (D-05)
HI: Rep. Neil Abercrombie (D-01)
Rep. Pastsy Mink (D-02)
IL: Rep. Bobby Rush (D-01)
Rep. Luis Gutierrez (D-04)
Rep. Sidney Yates (D-09)
Clem Balanoff (D-11)
Rep. Jerry Costello (D-12)
Catherine Lee (D-16)
Rep. Lane Evans (D-17)
IN: Rep. Peter Visclosky (D-01)
Gerald Houseman (D-04)
Julia Carson (D-10)
IA: Donna Smith (D-02)
MacDonald Smith (D-05)
KS: John Frieden (D-02)
LA: Rep. William Jefferson (D-02)
MD: Rep. Benjamin Cardin (D-03)
Rep. Albert Wynn (D-04)
Rep. Steny Hoyer (D-05)
Steve Crawford (D-06)
MA: Rep. John Olver (D-01)
Rep. Richard Neal (D-02)
Rep. Barney Frank (D-04)
Rep. Martin Meehan (D-05)
Rep. Edward Markey (D-07)
Rep. Joseph Kennedy (D-08)
Rep. John Moakley (D-09)
MI: Rep. Bart Stupak (D-01)
Dan Kruszynski (D-02)
Rep. Dale Kildee (D-09)
Rep. David Bonior (D-10)
Morris Fruman (D-11)
Rep. Sander Levin (D-12)
Rep. Lynn Rivers (D-13)
MN: Rep. Bruce Vento (D-04)
Rep. Martin O. Sabo (D-05)
Rep. James Oberstar (D-08)
MS: Rep. Bennie Thompson (D-02)
John Arthur Eaves (D-03)
MO: Joan Kelly Horn (D-02)
Ruth Bamberger (D-07)
MT: Bill Yellowtail (D-AL)
NH: Joe Keefe (D-01)
Arnie Arnesen (D-02)
NJ: Rep. Frank Pallone, Jr. (D-06)
Steve Rothman (D-09)
Rep. Donald Payne (D-10)
Chris Evangel (D-11)
Rep. Robert Menendez (D-13)
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Rep. Gary Ackerman (D-05)
Rep. Floyd Flake (D-06)
Rep. Jerrold Nadler (D-08)
Rep. Charles Schumer (D-09)
Rep. Edolphus Towns (D-10)
Rep. Major Owens (D-11)
Rep. Nydia Velazquez (D-12)
Rep. Carolyn Maloney (D-14)
Rep. Charles Rangel (D-15)
Rep. Jose Serrano (D-16)
Rep. Eliot Engel (D-17)
Rep. Nita Lowey (D-18)
Rep. Michael McNulty (D-21)
Rep. Maurice Hinchey (D-26)
Rep. Louise Slaughter (D-28)
Rep. John LaFalce (D-29)
NC: Rep. Eva Clayton (D-01)
George Parrott (D-03)
David Price (D-04)
Neil Cashion (D-05)
Ben Neill (D-10)
Rep. Melvin Watt (D-12)
OH: Mark Longabaugh (D-01)
Paul McClain (D-04)
Rep. Marcy Kaptur (D-09)
Dennis Kucinich (D-10)
Rep. Louis Stokes (D-11)
Rep. Sherrod Brown (D-13)
Rep. Thomas Sawyer (D-14)
Rep. James Traficant (D-17)
Robert Burch (D-18)
OK: Ed Crocker (D-04)
James Forsythe (D-05)
OR: Rep. Elizabeth Furse (D-01)
Mike Dugan (D-02)
Rep. Peter DeFazio (D-04)
PA: Rep. Thomas Foglietta (D-01)
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Rep. Robert Borski (D-03)
Rep. Ron Klink (D-04)
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Rep. Nick Rahall (D-03)
WI: Paul Soglin (D-02)
Rep. Gerald Kleczka (D-04)
Rep. Thomas Barrett (D-05)
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CFAnews is published eight times a year. Annual subscription rate is $25 per year.

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Design & Typeset by: Dahlman/Middour Design

Bells Rake In $4.5 Billion in Excess Profits

Local monopoly telephone companies are earning $4.5 billion annually in excess profits at the expense of captive telephone ratepayers, according to a study released in September by CFA and Citizen Action.

Over the last decade, while customer service has been deteriorating and prices for local service jumped by 40 percent, local monopoly telephone companies have taken in a total of $35 billion in excess monopoly profits, according to the study, "Excess Profits and the Impact of Competition on the Baby Bells."

"These revenues should have been used to lower consumers' rates and improve service," said CFA Research Director Mark Cooper, author of the study. "Instead, most of this money has been used to enrich the companies in ventures at home and abroad."

Local monopoly phone companies have enjoyed the best of both the regulated and competitive worlds — by taking the guaranteed profits of their monopoly base and leveraging that cash flow to build up unregulated businesses, Cooper explained.

"Working in conjunction with their parent companies, the Bells have taken money from local ratepayers and channeled it into high risk, unregulated businesses, such as video, credit cards, interactive television, and even railroads," he said.

Permitting the companies to keep the excess revenues would hinder the emergence of local competition, he added.

The following are among the other major findings of the study:

- Local phone rates have increased steadily in recent years, despite the fact that the overall cost of providing service has been declining.
- The Bell companies have enjoyed profit streams and cash flows far in excess of what their historically low-risk business should have produced, and local phone service revenues are the main source of this profit.
- Per-line investment in the local network has decreased by 20 percent, indicating that the excess profits have not been used to improve service. Jobs supporting local phone service have dropped by one third.
- Dividends paid by the Bells to their parent companies have exceeded dividends paid to stockholders by almost $19 billion. The result is that most of the excess profits have been reinvested in business ventures, not paid to shareholders or passed on to ratepayers.
- The use of this "internal subsidy" created by excess profits has fueled the Bells' unfair entry into new ventures. Almost 20 percent of their revenue is derived from unregulated activities, and one in five employees works for unregulated subsidiaries.

Higher Rates, Regulatory Relief Must Be Regulated

"The companies clearly continue to milk the monopoly while at the same time claiming the new telecommunications law could harm their bottom line," Cooper said.

"As state and federal regulators work to fulfill the promise of the new telecommunications law, they must reject Bell claims for regulatory relief or higher local rates. Instead, fair competition should be implemented to lower consumer rates and return local phone company profits to reasonable levels," he said.

"Real competition will put an end to the overpricing of basic service and the leveraging of excessive profits from telephone service for entry into unregulated businesses," Cooper added. "The key is for policy makers to resist the claims of the Baby Bells to be made whole in the face of competition."

In September testimony before the Federal-State Joint Board on Universal Service on recovery of interstate loop costs, Cooper praised the Federal Communications Commission for having taken "several bold and important steps in recent weeks to set the telecommunications industry on the path to vigorous, consumer friendly competition."

In particular, he noted the agency's decisions to set the price of unbundled network elements "at levels that recover the costs of a forward looking, least cost telecommunications network" and to allocate costs to enhanced services "on a reasonable cost causal basis."

"No decision is more important to consumers, however, than to recognize the shared nature of loop facilities," Cooper said. "Instead of having a misguided debate about subsidies between local and long distance in the recovery of a cost that is shared between them, we can now move on to the important question of the efficient and equitable recovery of shared costs," he said.

"As we stand at the dawn of the information age, we all expect and hope that the number and type of services that fill the telecommunications network will expand dramatically," he explained. "So long as we spread the shared costs of the network across all services that use it, we should have little difficulty in preserving universal service for all Americans. The costs of basic service should plummet as all the enhanced services fill its immense capacity."

Plan For Recovering Loop Costs Proposed

Cooper also noted that loop costs are falling dramatically.

"With the cost of the loop plummeting and the uses of the loop expanding, keeping basic service affordable requires only that we ensure that all services share the responsibility for the recovery of the efficient costs of providing those services," he said.

Cooper argued that both the Carrier Common Line Charge and the Subscriber Line Charge are too high and should be reduced. He further suggested "carefully transforming" the Common Carrier Line Charge from a usage charge to channel charge placed on the provider of the service.

"The interstate costs of loop could be recovered through either a reduced per-minute charge or a channel charge" assessed on the long distance carrier selected by each customer, he said.

Committee Rejects Civil Procedure Rules Changes

The Committee on Rules of Practice and Procedure of the Judicial Conference of the United States announced in June that it would not proceed at this time with proposed changes to the Federal Rule of Civil Procedure governing protective orders during the discovery process. CFA, Consumers Union, and the Coalition Against Misuse of Pesticides had submitted comments earlier this year arguing that the proposed changes were not in the public interest and should be rejected.

"If the proposed changes had been approved, protective orders would have been both more prevalent and more conclusive," said CFA General Counsel Mary Ellen Fise. "This would have denied consumers and government agencies access to a valuable source of information and would have permitted harmful products to remain in the marketplace."

It is unclear what the future of the proposed changes will be. In deciding not to proceed, the committee said it would consider proposed changes related to protective orders as part of a new project on the scope of discovery.

At the same time, the committee was considering changes to the rules for certifying class actions which would have severely limited access to the courts for ordinary individuals. Writing to the committee in June, CFA Chairman Howard Metzenbaum singled out three aspects of the proposal for criticism: its requirement that the court make a preliminary evaluation of the merits of the claim in determining whether to certify the class; its requirement that the court review whether "public values" are served by class certification; and its requirement that a class action be, not only superior to other means of proceeding, but also necessary.

"These proposed changes are of enormous concern, in that they are clearly designed to limit access of the ordinary citizen and consumer to the courts, have been proposed without any consideration to judicial expediency, and offer unjustifiable protection to defendants who have committed legal wrongs which have resulted in widespread and far-reaching injury," the former senator wrote.

When the committee released a revised set of proposed changes for public comment in August, all three of these provisions had been eliminated. The proposal retained other troubling provisions, however, including a requirement that judges determine whether the benefits to individual plaintiffs outweigh the costs to the court system and to the defendant of proceeding with a class action. The deadline for comments is February 15.

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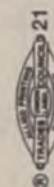

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