

What is the Relationship between Buying a Used Car and Consumer Protection?



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INTRODUCTION

There are industries and professions which are perceived by the public as having undesirable characteristics that make them risky for consumers. These characteristics may exhibit themselves through the circumstances surrounding the use of the good or service, or they may be exhibited in the behavior of the professionals in the industry. In many cases, consumers are hesitant to interact with these industries for fear of having a negative experience.

Lawyers, used-car salespeople, insurance salespeople, and politicians are good examples of industries or professions that consumers consider should be avoided when possible. Indeed these stereotypes are often perpetuated through television series, movies, and books. These stereotypes exist, at least in part, because consumers view these professions and industries as being risky for consumers. One particular industry stereotyped in this way and characterized by consumer mistrust is the used-car industry. Gallup's polls on the trustworthiness of professions show that Americans consistently rank car salespeople as one of the least trusted groups (Gallup, 2016, 2017, 2018).

When consumers engage in markets like the used-car market, they understand that there is uncertainty involved. This uncertainty can be framed as risk, meaning the consumer is at risk of receiving less satisfaction than they had expected when purchasing the good or service. The consumer does not know exactly how much satisfaction he or she will receive from the used car that he or she is purchasing until after the transaction has been completed. Facing such risk, consumers engage in behaviors that limit the perceived risk. Consumers may engage in search before they purchase a used car, or they may transfer the risk by buying a warranty. These behaviors exhibit consumer knowledge of the risks involved with purchasing a used car. The consumer's risk can be reduced further by his or her government's creation of consumer protection legislation.

State governments have enacted legislation that enables consumers to more easily win lawsuits against bad actors in this and other industries. These statutes are generally called Unfair and Deceptive Acts and Practices (UDAP) statutes. They were created to protect consumers from undesirable business practices. This paper examines the relationships between UDAP statutes and the decision to purchase a used car.

In the event that a consumer does purchase a used car or some other good, only to find out later that they have been taken advantage of by the salesperson, what can they do? There are essentially three paths the consumer can follow. First, the consumer could choose to do nothing, to accept the loss as the cost of purchasing a used car. Second, the consumer could engage in negotiations with the dealership to attempt to achieve their expected satisfaction. This outcome could be achieved through an agreement changing the price paid for the car, exchange, or return of the car, or both parties agreeing on some other solution. Third, the consumer can seek aid by suing the dealership through his or her state's consumer protection laws.

Imagine a consumer that wishes to purchase a car. This consumer has the choice between purchasing a used or new car. After engaging in an extensive search, the consumer decides that a used car fits his or her preferences. The consumer picks a make and model and selects a mileage range with which he or she is comfortable. The consumer finds a suitable used car and engages with a salesperson to purchase the car at a given price. The consumer asks all the right questions and inspects the car as much as he or she is able. One such question is whether or not the car had been in any accidents, to which the salesperson answers in the negative. A price is agreed upon, money and car change hands, and the transaction is completed. The consumer has the expectation that the car will be suitable for specific uses and will suit their needs for some period of time.

Months pass without event. Eventually, the consumer discovers that the car had been in a major car crash before his or her purchase (of which the salesperson was aware). This substantially diminishes its resale value. The consumer now has three courses of action. The consumer can take the loss as a consequence of purchasing a used car, engage the dealership to renegotiate the deal, or the consumer can use his or her state's consumer protection laws to sue the dealership. The probabilities of the consumer's success in the second and third options are heavily dependent on how his or her state's UDAP statute is written. Put

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another way, the consumer's risk of not being in the same or a better position after the transaction is lessened or increased, depending on the UDAP statute of the consumer's state.

This paper examines whether and how the level of protection offered by UDAP statutes is related to used-car purchases in the U.S. In order to do so, each state's UDAP statute was examined to determine how much protection the statute provides consumers. This paper examines participation in the used-car market in each state as it relates to the state's protections created under its UDAP statute. This paper finds that the differences in used-car purchases between different levels of protection provided by UDAP statutes are not explainable by chance alone.

LEGAL BACKGROUND AND LITERATURE REVIEW

Much of the previous work regarding the effects of consumer protection on consumption falls under theoretical arguments or editorialization. By cataloging each state's UDAP statute and analyzing used car purchases within the state based on UDAP statute characteristics, the relationship between the two can be estimated. This paper is meant to add to the existing literature by setting out a framework for examining the relationship between the purchasing of a good or service (used cars) and consumer-protection statutes (UDAP statutes). This paper provides a statistical analysis of how consumer choice to purchase used cars differs when levels of consumer protection differ.

Legislative Development

Before a discussion of consumer protection can begin, it is valuable to understand the current state of affairs and how it has evolved in the United States. Consumer protection from predatory, deceptive, or unfair business practices is created and administered at the state level by laws commonly referred to as UDAP statutes. These statutes are designed to protect consumers from bad actors, whether they be employees of a business or the business itself (National Consumer Law Center, 2017). These statutes may prohibit business practices that are abusive, deceptive, or even careless (National Consumer Law Center, 2017). These statutes vary widely from state to state in how they are written, causing the protections they provide to vary widely as well (National Consumer Law Center, 2017). Some states' statutes provide a great deal of protection against bad behavior, while others provide substantially less protection (National Consumer Law Center, 2017).

Before states began to enact UDAP statutes, consumers were generally only able to pursue legal action against bad actors through their state's laws against fraud (Carter, 2009). However, fraud statutes generally require that the alleged victim prove that the bad actor intentionally deceived the consumer and in most cases, only allowed the consumer to pursue the individual perpetrator rather than the business the perpetrator worked for (Carter, 2009). This left a gap in protection, allowing many abusive and unethical practices to persist (Carter, 2009). However, beginning in the 1960s, individual states started enacting UDAP statutes to close this gap (Carter, 2009). Today's UDAP statutes prohibit specific actions, outline how a judge or jury can decide whether an action is prohibited if it is not specifically named in the statute, and lay out procedures that consumers seeking recourse must follow (Carter, 2009).

Forms of Consumer Protection

Traditionally, economic theory has viewed consumer protection as paternalistic behavior by government entities (Leland, 1979). Consumer protection statutes may be viewed as paternalistic where a government decides that its citizens are unable to choose for themselves what is best for them. If a government believes this to be true, it will enact laws designed to curtail the problem behavior by limiting consumer choice (Leland, 1979). Examples of paternalistic consumer protection would include requiring specific disclosures when selling a product or service or prohibiting the sale of a specific product or service.

This type of protection may be enacted in response to circumstances where informational asymmetries exist between the consumer and the seller, like used-car sales (Akerlof, 1970). This type of protection can be especially impactful in markets where the quality of a good is not easily ascertained, and where there are sellers willing to sell inferior goods (Akerlof, 1970). The used-car market could be labeled as such a market.

UDAP statutes are not paternalistic in nature because they do not limit consumer choice by prohibiting the sale of products or services. They do not prohibit consumers from buying used cars, nor do they force the seller to perform any action to benefit the consumer. They instead focus on providing consumers with a legal avenue to be made whole if they can show that the business entity acted dishonestly or unfairly (Carter, 2009).

Consumer Protection as Risk Mitigation

Under consumer theory, it is assumed that consumers understand that the price and quality of a good will differ from seller to seller (Stigler, 1961). This knowledge encourages consumers to engage in search, where they will seek out the good that best fits their preferences for price and quality (Stigler, 1961). As part of their search, consumers will gather and interpret information that is available in competitive markets (Stigler, 1961).

Bauer (1960) was one of the first researchers to equate consumer purchases with risk-taking. In the context of consumer purchases, risk can be defined as perceived negative outcomes from a purchasing decision (Bauer, 1960). These risks can pertain

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to differences in consumer expectations and the performance of the good or service or psychological, social, financial, and physical benefits of the good or service (Gabbot, 1991). Roselius (1971) lists an array of methods by which the risk of negative purchasing outcomes can be reduced for consumers. These include endorsements, brand image, private testing, free samples, money-back guarantees, and government testing.

Holton (1969) and Fisk (1973) recognize that consumers can mitigate the risk of a negative experience by asking for assurances of quality, but that there is little consumers can do to enforce these assurances. It is worth noting that businesses or their employees may use these techniques to encourage the transaction with no intention of actually providing these risk reduction measures. Darby and Karni (1973) illustrate that, in markets where it is difficult to determine the quality of a good before purchase, sellers may have motivation to misrepresent the good. However, in the absence of consumer-protection statutes, it is difficult to make sellers accountable for the assurances they make (Holton, 1969; Fisk, 1973).

Akerlof (1970) suggested that the used-car market poses specific problems to consumers. In particular, consumers are unable to distinguish between the quality of used cars, but sellers are more able to do so (Akerlof, 1970). This disparity gives the seller an advantage over buyers in evaluating the quality of a used car (Akerlof, 1970). Eamon and Sheldon (2009) test this hypothesis by evaluating the time between when a consumer purchases a car and then sells that same car. They hypothesize that consumers are unable to accurately determine the quality of used cars, and when the disparity between expected quality and actual quality is large, consumers will seek to replace the purchased car by selling it and purchasing another. They find that consumers who buy used cars have a high probability of reselling the same cars relatively quickly. Based on their results, they conclude that this behavior could be caused by consumers' inability to accurately determine the quality of used vehicles.

The papers in this section often point to government intervention as a way to solve these problems in markets. They state that the risk faced by consumers in some cases may be reduced by market factors or consumer behavior. The used-car market is particularly risky, and UDAP statutes serve as a way that state governments help in reducing consumer risk.

Arguments Against Consumer Protection

Arguments against consumer protection generally start with the claim that markets regulate themselves through various aspects of competition that drive out bad actors (Holton, 1969). It is argued that, by driving out these bad actors, the market itself reduces the consumer's risk of experiencing a negative ownership outcome. The argument against consumer protection receives support from the general economic theory that government intervention through regulation limits consumer choices (Holton, 1969). In some instances, regulation increases the cost of a good or service enough to make it unattainable for some consumers (Holton, 1969).

In some cases, the regulation can increase the cost so much that it will cause the good or service to be removed from the market entirely (Holton 1969). Additionally, regulation can prohibit the sale of a good or services, also making it impossible to consume the goods or services legally (Holton, 1969). Therefore, it is concluded that in many cases, government intervention in markets worsens the position of consumers.

However, Holton (1969) suggests that competition may be sufficient to protect consumers from abuse only in markets that have three attributes. First, the market must be for goods or services which are purchased frequently by consumers (Holton, 1969). Second, these markets must be for products for which the quality is determinable before the purchase is made (Holton, 1969). And third, these markets must be for products that are not rapidly changing due to technological advances (Holton, 1969). Holton (1969) holds that if a market does not have these qualities, the power of competition to drive out bad actors is significantly diminished. Fisk (1973) added that the effects of competition do not disappear in markets lacking these attributes, but that consumers use the information provided by competition differently. Rather than using the information that exists in a competitive market to find the product best matching their preferences and constraints, consumers will use the information to reduce the risk of a negative purchasing experience (Fisk, 1973).

The used-car market has none of the attributes laid out in Holton (1969) that are required for competition to serve as an adequate force to drive out bad actors. In most cases, consumers do not purchase used cars with frequency, the quality of a used car is not ascertainable before purchase, and the technology in cars is changing rapidly. In the used-car market, competition is not a sufficient source of protection for consumers, who must instead rely on their ability to gather and interpret information in order to reduce their risk of a negative ownership experience.

Used Car Consumption: Past Research

Competition may not be a sufficient protection against unfair or deceptive acts perpetrated by dishonest business people. State governments have inserted themselves as an additional barrier against consumer abuse in the form of UDAP statutes. This paper examines the relationship between consumption of used cars and consumer protection legislation, taking into account consumer preferences and constraints. It is, therefore, worthwhile to look at the methods by which researchers have measured the consumption of used cars in relation to legislation as well as consumer preferences.

Beginning in the late 1970s, researchers began to use disaggregate models to estimate consumer demand (Prieto & Caemmerer, 2013). These researchers were mainly focused on examining how consumer characteristics might help determine

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the kinds of cars consumers purchased (i.e. new or used, car size, style of car, etc.). These characteristics were used as proxies for consumer preferences and constraints. Lave and Train (1978) claim to be the first of these models. Using household data to control for consumer preferences, Lave and Train (1978) use a multinomial logit (MNL) model to explain how a change in energy policy, as it relates to mileage per gallon in cars, would impact consumer demand for different types of cars. Lave and Train (1978) find that income, family size, age, and education are statistically significant variables when examining consumer demand for cars.

Manski and Sherman (1980) examine how household characteristics impact the composition of households' car holdings. Focusing on several different characteristics of cars and their costs, Manski and Sherman (1980) find that income, family size, age, and education are related to purchasing cars with different characteristics. Additionally, the paper examines two aspects of car cost, purchase price and the cost of upkeep, and finds that the cost of upkeep is related to consumer preferences (Manski & Sherman, 1980). They conclude that this relationship shows that consumers do engage in and use the information they find in search to make decisions to purchase specific cars (Manski & Sherman, 1980).

Mahmassani and Mannering (1984) use similar household characteristics to examine the choice between foreign and domestic cars. They include employment status, and residential location as proxies for consumer preferences. They find that differences in these proxies are related to how consumers value domestic and foreign cars (Mahmassani and Mannering, 1984).

More recently, Miller and Mohammadian (2003) examine the demand for new and used cars, in addition to other car characteristics, using similar demographic variables as proxies for preferences and constraints. They add driver skill and sex, finding similarly that these proxies are related to consumers' decisions regarding the types of cars consumers will purchase. Choo et al. (2004) examine how personality traits relate to demand for car types, finding that purchases of certain car types are related to specific consumer personalities. Caemmerer and Prieto (2013) use similar household characteristics to examine how they relate to consumer demand for different car types and find that these demographic variables continue to serve as proxies for consumer preferences and constraints.

Using MNL methods, the literature examines how various consumer and household consumer characteristics relate to consumer demand for various types of cars. These characteristics include sex, age, household size, income, and education, and are found to be statistically significant consistently across different time periods. As such, they are used as control variables in this paper with their theoretical justification explained in the coming sections.

DATA

In order to analyze the relationship between UDAP statutes and the decision to purchase a used car, this paper uses the Consumer Expenditure Survey (CEX). The CEX is an annual study comprised of an interview survey and a diary survey and is conducted by the U.S. Bureau of the Census on behalf of the U.S. Bureau of Labor Statistics. The CEX's interview survey covers large-ticket item purchases such as cars, appliances, and construction projects in-depth, giving only cursory treatment to smaller, day-to-day purchases. The diary survey covers the smaller, day-to-day purchases in-depth, while giving almost no treatment to larger purchases. Both surveys are used by the U.S. Bureau of Labor Statistics to determine the relative changes in the importance of various goods and services in the market. The CEX also tracks the well-being of consumers in terms of wealth, income, housing, and employment. When weights are applied, the CEX is meant to be a representative survey of households in the United States.

This paper uses pooled, cross-sectional data over a ten-year period, beginning with the 2008 CEX Interview Survey, and ending with the 2017 CEX Interview Survey. These data cover both recession and expansion economies. The full CEX sample covering the ten-year period includes 525, 232 separate transactions in which a car was purchased. This initial sample is reduced to 124,657 transactions because some transactions do not have complete data on the car purchased or the individual purchasing the car. Also of note, some specific states' identifiers are suppressed, which makes regression using those states' UDAP statutes impossible. Due to the suppression of state identifiers, the sample does not include transactions from Arkansas, Montana, New Mexico, North Dakota, Rhode Island, South Dakota, Vermont, or Wyoming. However, there are only minor differences between these states' UDAP statutes and those that are represented in the analysis sample. Table 1.1 compares the full CEX sample means with the analysis sample means and illustrates the differences between the two samples. As can be seen in Table 1.1, the differences between the two samples are statistically significant. CEX survey weights are used in obtaining the results of Tables 1.1, 1.2, and 1.3 in order to make the sample representative of the U.S.

This paper does not examine or categorize the effectiveness of individual state UDAP statutes. It does not attempt to identify which states have the best or worst UDAP statutes. Rather, it examines two specific descriptors of a state statute to determine whether and how these descriptors are correlated with used-car purchases, if at all. Due to the fact that this paper examines used-car purchases, there may be multiple transactions, a single transaction, or no transaction reported for each household in any given year. The statistical analysis accounts for clustering to account for multiple transactions occurring in some households.

The dependent variable in this analysis is whether a transaction resulted in the purchase of a used car or a new car. This is represented by a dummy variable where a one (1) indicates the car purchased was used, and a zero (0) indicates the car was

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new. Using the CEX Interview data, it is possible to determine if a car was purchased in the survey year. Then the data is used to determine how many cars were purchased and whether the car was used or new. Multiple transactions can occur for an individual household if more than one car was purchased during the year.

There are two key explanatory variables in this paper. The first is the level of protection provided against unfair practices. The second is the level of protection provided against deceptive practices. These key explanatory variables are created from a dataset that the author compiled specifically for this paper. The author examined each state's UDAP statute to determine the level of protection from unfair practices and deceptive practices provided by each statute. Based on the language of the statute, the author categorized each state's UDAP statute as providing narrow, neutral, or broad protections against unfair practices and again against deceptive practices.

The key explanatory variables are categorical in nature and thus are represented as dummy variables for neutral and broad protections (with narrow being the omitted category). For example, suppose a transaction occurs in a state with neutral protections against unfair practices and broad protections against deceptive practices. If such were the case, then the category for protections against unfair practices would be represented by a one (1) in the neutral dummy and a zero (0) in the broad dummy, and the protection against deceptive practices would be represented as a one (1) in the dummy for broad protections and a zero (0) for the dummy with neutral protections. The information and system used to create these variables and reference to each state's UDAP statute can be found in Appendix 1.A.

This paper uses variables to control for consumer preferences and constraints across demographic and economic categories. These variables include sex, marital status, education, race, age, and income before taxes. All else being equal, consumers of different sexes, marital statuses, levels of education, race, age, and income consistently have been shown to have different preferences when it comes to the cars that they drive. The control variables for sex, marital status, education, and race have all been reduced to dummy variables, which are justified and explained below. These dummies are coded as being a one (1) where true, and a zero (0) where false. To control for differences in the transaction year and year-specific economic factors, the analysis controls for year (using dummy variables for each year with 2017 being the omitted category). To control for the prices of new and used cars within each state, the state average price of used cars and the state average price for new cars are included as continuous explanatory variables.

THEORY

This paper bases its analysis on the theory that consumers have limited resources which they allocate in order to maximize their utility. Under uncertainty, consumers will do so using expected utility (Holton, 1969). Expected utility can be raised by reducing the risk of negative outcomes through activities of the consumer (e.g., extended search or purchasing warranties) or government (e.g., enacting consumer protection) (Bauer, 1960).

This paper applies the theory discussed by Bauer (1960), assuming that consumers act to maximize utility under uncertainty. If a potential transaction involving a used car is treated as a risk-taking activity, then the risk-reducing effect of consumer protection decreasing the risk of a negative outcome can increase the probability of the transaction being completed. Fisk (1973) recognizes that, in markets lacking certain characteristics, competition does not provide the consumer with enough information regarding the quality of a good or service. This means that a consumer is less able to distinguish between the quality of goods and services across sellers. In these markets, consumers instead use information to reduce the risk of a negative purchasing outcome (Fisk, 1973). Roselius (1971) includes government action as one of the ways that consumers reduce risk in making purchasing decisions. This leads to one of Holton's (1969) conclusions, namely, that consumer protection is a way to reduce risk in markets where consumers are at a disadvantage when it comes to gathering and interpreting information. The power of this risk-reducing effect could be diminished if consumers take the increased protection as a signal that they should avoid the used car market or if consumers do not know about the added protection they are receiving.

Consumers are not the only party that takes on risk by engaging in a transaction. Car dealerships take on risk when they sell used cars. They take on the risk that the consumer will use his or her state's UDAP statute if he or she suffers a negative experience. The more protection offered by the statute, the more risk the car dealership takes on when it sells a used car. The risk-reducing effect of consumer protection could be counteracted by seller actions. Car dealerships could tighten their criteria on accepting used vehicle trade-ins in a way that limits their risk of selling a defective vehicle. Car dealerships could also incentivize their salesforces more heavily to sell new vehicles instead of used vehicles. In effect, this would lower the probability that a consumer would purchase a used car.

Another way car dealerships could handle that risk is by accepting the higher levels of risk in exchange for higher sales prices. It is commonly accepted that the added costs created by consumer protection could be passed on to the consumer, thus raising prices (Holton, 1969, p. 44). These higher prices will push some consumers out of the market for used cars. However, in some markets, the effect of higher prices may be less than others. This may be true in markets where the price is difficult to fully comprehend or know before-hand, making it more difficult to compare goods or services (i.e. home renovations or permanent

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life insurance policies). To a certain extent in the used-car market, consumers are able to identify the price and quality with some certainty.

In many cases, car dealerships not only sell used cars, but also new cars, which can be considered substitutes for one another. This makes dealerships unique, in that they have the ability to adjust the risk of lawsuit by changing not only the product creating the risk but its most common substitute as well. Car dealerships can compensate for higher risk by increasing the price for which they sell used cars, decrease their supply of used cars by taking fewer trade-ins or change their compensation mechanisms to provide greater incentives to sell new cars than used cars. Due to the control that car dealerships have over so many aspects of the car shopping experience, it may be that the risk-reducing effect of consumers is not sufficient to impact the probability of a transaction resulting in the purchase of a used car. All else being equal, it is expected that in the case of used cars, higher levels of consumer protection will result in lower probabilities that used cars will be purchased.

Sex of the consumer is included in the analysis to control for the different preferences held and constraints applying to male and female consumers. Males and females commonly have different preferences regarding cars and risk. Sex and car selection are commonly related in previous literature on the subject. McCarthy and Tay (1998), Kitmura et al. (2002), Mohammadian and Miller (2003), and Prieto and Caemmerer (2013) all find that sex has a statistically significant correlation to car selection. A dummy variable for transactions where the consumer was female is included to control for sex (male is the omitted category). Because females tend to be more risk-averse and less confident in their ability to judge the quality of cars, it is expected that females will have a lower probability of purchasing a used car than males.

The marital status of the consumer is included in the analysis to control for different preferences held and constraints experienced by consumers of different marital statuses. Individuals who are married, divorced, widowed, separated and have never married commonly have different preferences when it comes to the type of car they own and how they regard risk. Marital status also is associated with car selection in previous literature. Lave and Train (1979), Mannering and Mahmassani (1985), and Brownstone and Train (1999) find marital status to be statistically relevant when selecting a car. The effect differs between these papers, but this may be due to these papers not controlling for more types of marital status than “married” and “not married.” Therefore, dummies are created for transactions where the marital status was divorced, separated, widowed, and never married (married is the omitted category). Because of the different preferences across multiple categories of marital status, it is difficult to hypothesize the sign of the relationship before-hand.

Level of education is included in the analysis to control for different preferences held and constraints experienced by consumers with different levels of education. These preferences toward car type often manifest as differences in the utility gained from the status of owning a new car, where individuals with more education receive higher utility from the status provided. Numerous previous articles and papers tie education level to car selection. Kitmura et al. (2002), Mannering et al. (2002), Mohammadian and Miller (2003), Prieto and Caemmerer (2013) all agree that education is statistically significant in car selection. Education is separated into seven dummy categories for transactions where the consumer never attended school, only attended school through 8th grade or less, attended school between 9th and 12th grade, graduated high school, attended some college, received an associate’s degree, or received a bachelor’s degree (with those receiving a graduate degree being the omitted category). For levels of education, it is expected that the probability of a transaction resulting in the purchase of a used car will decrease as the education level decreases. This could be the result of more highly educated people considering a new car as a status symbol.

Race is included in the analysis to control for the different preferences held and constraints experienced by consumers of different races. These differences in preferences can include different cultural attitudes toward ownership or even financial institutions. While many papers include race as a control variable, very few have found it to be statistically significant in car selection. However, this may be due to the way in which previous research has identified minority races, simply selecting between “White” and “Other.” For this paper, race is categorized into five dummies representing transactions where the consumer was Black, Native American, Asian, Pacific Islanders or of mixed race (White being the omitted category). Due to race being delineated across multiple categories, it is difficult to hypothesize the sign of the relationship before-hand.

A continuous variable for the age of the consumer engaging in the transaction is also used to control for consumer preferences and constraints. Similarly to education level, these different preferences could result in differing levels of utility based on the status of new car ownership, where older consumers receive more utility because of the increased status. Most of the articles already cited find age to be statistically significant in car selection. It is expected that as the age of the consumer participating in the transaction increases, the probability of a used car being purchased will decrease.

A continuous variable representing the income of the consumer engaging in the transaction is included to control for differences in preferences and constraints between consumers with different levels of income. Income is listed in tens of thousands of dollars and is converted to 2017 real dollars using the U.S. Bureau of Labor Statistics’s Consumer Price Index. It is expected that the probability of a transaction resulting in the purchase of a used car will decrease for higher levels of income, where budget constraints will allow for the purchase of new cars.

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In order to control for state-specific economic factors, this paper also uses the average purchase price of used cars and the average purchase price of new cars within the state of the transaction. The actual purchase price of the transaction is an endogenous variable and thus cannot be used. As the state average price for used cars increases, it is expected that the probability of a transaction resulting in the purchase of a used car will decrease. It stands to reason that if the average price of used cars increases relative to new car average price, then the probability of a transaction resulting in the purchase of a used car will decrease. On the other hand, it is expected that as the state average price of new cars increases, relative to used car average price, the probability of a transaction resulting in the purchase of a used car will increase. These two variables are continuous variables represented in thousands of dollars and are converted to 2017 real dollars using the U.S. Bureau of Labor Statistics's Consumer Price Index.

MODEL

This paper uses a probit model to estimate the relationship between the purchase of a used car and the breadth of protection offered by UDAP statutes against unfair practices and also deceptive practices. The probit model is given here

$$Y_i^* = X_i\beta + \varepsilon_i$$

where $y_i = 1$ if $y^* > 0$ indicating that the car purchased was used, and $y_i = 0$ if $y^* \leq 0$, indicating that the car purchased was new.

In this model the subscript i represents a transaction, Y_i^* represents the unobserved net benefit of choosing a used car over a new car, y_i is the observed transaction which takes a value of 1 if a used car is purchased and 0 if a new car is purchased, X_i is a vector of all explanatory variables relevant to the i^{th} transaction (including the UDAP statutes' dummies in the state in which the i^{th} transaction occurred and the outlined control variables), β represents the vector of parameters to be estimated, and ε_i represents the error term which follows the standard normal distribution. It is expected that the probability of purchasing a used car over a new car will be lower in states with either neutral or broad protections than with narrow protections.

RESULTS

Protections Against Deceptive Acts

Table 1.2 shows the estimates of the effects of differing levels of UDAP protections against deceptive acts. The results shown are the marginal effects of a difference in consumer protection from narrow protection from deceptive acts to neutral or broad protection. Table 1.2 assumes a statute with narrow protections against deceptive acts as the base category and shows the difference in the probability of a used-car purchase under neutral and broad protections in contrast to narrow protection. A negative value represents a lower probability of purchasing a used car.

The results displayed in Table 1.2 indicate that transactions in states with neutral or broad protections against deceptive acts have a lower probability of purchasing a used car than transactions in states with narrow protections against deceptive acts. The decrease in the probability of a used car purchase could be the result of factors that would diminish the risk-reducing effect of consumer protection. As discussed above these could be due to a lack of knowledge of the protection on the part of consumers, or the protection itself could act as a signal to consumers that they should avoid the industry altogether. This result could also indicate that the risk-reducing effects of consumer protection are being counteracted by actions of car dealerships. These actions could include decreasing their used car inventories or changing the incentives of their salespeople to promote the sale of new cars over used cars. These results agree with the previously stated hypothesis.

Protections Against Unfair Acts

Table 1.3 shows the estimates of the effects of differing levels of protection against unfair acts. The results shown are the marginal effects of a difference in consumer protection from narrow protection from unfair acts to neutral or broad protection. Table 1.3 assumes a statute with narrow protections against unfair acts as the base category and shows the change in the probability of a used-car purchase under neutral and broad protections in contrast to narrow protection. A negative value represents a decrease in the probability of a transaction resulting in the purchase of a used car.

The results displayed in Table 1.3 indicate that transactions in states with neutral protections against unfair acts have a lower probability of purchasing a used car than transactions in states with narrow protections against unfair acts. The decrease in the probability of a used car purchase could be the result of factors that would diminish the risk-reducing effect of consumer protection. As discussed above, these results could indicate a lack of knowledge of the protection, or the protection itself could act as a signal to consumers that they should avoid the industry altogether. Additionally, the lower probability could be caused by any risk-reducing effect being overcome by actions taken by used car dealerships to reduce the additional risk they face because of higher levels of consumer protection. These results are consistent with the hypothesis that states with higher levels of consumer protection would correlate with a lower probability of purchasing a used car.

Control Variables

Tables 1.2 and 1.3 also display the results of the analysis regarding the consumer's sex, marital status, the highest level of education attained, race, age, the state average new-car purchase price (represented in thousands of 2017 constant dollars), the

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state average used-car purchase price (represented in thousands of 2017 constant dollars), and income before taxes (represented in tens of thousands of 2017 constant dollars).

Tables 1.2 and 1.3 indicate that, in transactions where the consumer is female, there is a lower probability that the car purchased will be a used car. This could be the result of different levels of confidence between males and females in determining the quality of used cars. Males may be more confident in their ability to determine the quality of a used car. This would result in a perceived reduction in the risk of purchasing a car (Jacobsen et al., 2013).

The results in Tables 1.2 and 1.3 indicate that transactions involving divorced or separated consumers have a higher probability of resulting in the purchase of a used car than married couples. This could be the result of a perceived change in status following a divorce or separation or from a difference in the way divorced and separated consumers perceive risk (Brownstone and Train, 1999).

These tables also show that the education of the consumer involved in the transaction is associated with choosing between new and used cars. All of the educational achievement categories had a higher probability of purchasing a used car than the omitted category, households with post-baccalaureate education. This could be explained by new cars being a more desirable status symbol to individuals with more education or an increased ability to gather and interpret information regarding the quality of the car (Gabbot, 1991; Kitmura et al., 2002).

The race of the consumer involved in the transaction appears to be correlated to choice of car as well. Tables 1.2 and 1.3 indicate that transactions where the consumer identifies as Black, Native American, or Mixed Race have a higher probability of buying a used car than a white household. Transactions involving a consumer that identifies as Asian or Pacific Islander have lower probabilities of purchasing used cars than where the transaction involves a consumer identifying as white. These differences in preference based on race could be due to differences in cultural preferences.

The age of the consumer involved in the transaction also is related to the probability of purchasing a used car. For every year added in age, the probability of purchasing a used car decreases. This could be due to differences in risk perception between younger and older consumers or differences in the utility received from owning a new car.

Both state average purchase price for used cars and state average price for new cars are statistically significant in their effects on whether the transaction results in the purchase of a used car. For the state average purchase price of used vehicles, as this price decreases, the probability of purchasing a used vehicle increases, consistent with the law of demand. On the other hand, as the state average purchase price of new cars increases, the probability of a transaction resulting in the purchase of a used car increases. This is because new and used cars are substitute goods.

The income before taxes of the consumer involved in the transaction also is related to the choosing of a used car. For every \$10,000 increase in income, the probability that the car purchased is used decreases. Similar to education, this could be the result of a difference in how these consumers view new and used cars.

CONCLUSION

This paper finds that the choice between a used or new car is related to the level of consumer protection provided by the state in which the transaction occurred. In the case of protections against deceptive acts, both neutral and broad levels of protection are shown to correspond with a lower probability of a used-car purchase than where narrow levels of protection exist. In the case of protections against unfair acts, only neutral levels of protection are shown to correspond with a lower probability of a used-car purchase than where narrow levels of protection exist. All of the control variables are shown to be statistically significant in the choice between a used and new car.

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TABLES

Table 1.1: Descriptive Statistics of Dependent and Independent Variables					
Unit of Observation:		CEX Sample		Analysis Sample	
Transaction		(525,232)		(124,657)	
		Mean	Std. Err.	Mean	Std. Err.
Car Purchase	(Used)	0.609	0.0007	0.694***	0.0013
Breadth of Deception	Narrow	0.046	0.0003	0.044***	0.0004
	Neutral	0.137	0.0005	0.145***	0.0007
	Broad	0.811	0.0006	0.817***	0.0006
Breadth of Unfairness	Narrow	0.095	0.0004	0.092***	0.0006
	Neutral	0.111	0.0005	0.115***	0.0007
	Broad	0.794	0.0006	0.794	0.0008
Gender	(Female)	0.499	0.0009	0.503***	0.0014
Marital Status	Married	0.656	0.0008	0.635***	0.0014
	Widowed	0.064	0.0004	0.053***	0.0006
	Divorced	0.120	0.0006	0.123*	0.0009
	Separated	0.020	0.0002	0.024***	0.0004
	Never Married	0.140	0.0006	0.166***	0.0011
Education Received	Never Attended	0.002	0.0001	0.002	0.0001

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1st to 8th Grades	0.036	0.0003	0.0362	0.0005	
9th to 12th Grades	0.067	0.0004	0.066***	0.0007	
High School Graduate	0.245	0.0007	0.236***	0.0012	
Some College	0.207	0.0007	0.212***	0.0012	
Associate's Degree	0.106	0.0005	0.104*	0.0009	
Bachelor's Degree	0.213	0.0007	0.219***	0.0017	
Graduate Degree	0.101	0.0005	0.107***	0.0009	
Race	White	0.844	0.0007	0.831	0.0011
Black		0.089	0.0005	0.096***	0.0008
Native American		0.004	0.0001	0.004	0.0002
Asian		0.046	0.0004	0.051***	0.0006
Pacific Islander		0.004	0.0001	0.005***	0.0002
Mixed		0.0118	0.0002	0.0125*	0.0003
Age		50.680	0.0228	47.687***	0.0440
Avg. State Purchase Price (Used)₁		\$13.124	0.0030	\$14.271***	0.0038
Avg. State Purchase Price (New)₂		\$24.769	0.0047	\$27.527***	0.0043
Income Before Taxes₃		\$7.917	0.0112	\$ 8.949***	0.0219

- The analysis in this table incorporates the weights provided by the CEX

* represents a statistically significant difference across samples with a p-value of .1 to .05

** represents a statistically significant difference across samples with a p-value of .05 to .01

*** represents a statistically significant difference across samples with a p-value of less than .01

1 In 1,000s of 2017 dollars

2 In 1,000s of 2017 dollars

3 In 10,000s of 2017 dollars

Table 1.2. Marginal Effects - Breadth of Protection from Deceptive Acts

N=124,657	Used Car Purchase	
Breadth of Protection (Narrow Omitted)		
Neutral	- 0.068***	0.0096
Broad	- 0.055***	0.0087
Sex (Male Omitted)		
Female	- 0.011***	0.0034
Marital Status (Married Omitted)		
Widowed	- 0.010	0.0078
Divorced	0.065***	0.0052
Separated	0.081***	0.0118
Never Married	0.005	0.0051
Education (Post-Baccalaureate Omitted)		
Never Attended	0.191***	0.0486
Attended Grades 1-8	0.210***	0.0115
Attended Grades 9-12	0.193***	0.0086
High school Graduate	0.104***	0.0060
Some College	0.073***	0.0060
Associate degree	0.057***	0.0071
Bachelor's Degree	0.020***	0.0057
Race (White Omitted)		
Black	0.078***	0.0062
Native American	0.063**	0.0275
Asian	- 0.112***	0.0077
Pacific Islander	- 0.093***	0.0268

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Mix	0.065***	0.0166
Age	- 0.005***	0.0010
State Avg. Purchase Price (Used) ₁	- 0.020***	0.0014
State Avg. Purchase Price (New) ₂	0.003**	0.0012
Income Before Taxes ₃	- 0.007***	0.0003

- The analysis in this table incorporates the weights provided by the CEX

* represents a statistically significant result with a p-value of .1 to .05

** represents a statistically significant result with a p-value of .05 to .01

*** represents a statistically significant result with a p-value of less than .01

1 In 1,000s of 2017 dollars

2 In 1,000s of 2017 dollars

3 In 10,000s of 2017 dollars

Table 1.3. Marginal Effects - Breadth of Protection from Unfair Acts

N=124,657	Used Car Purchase	
Breadth of Protection (Narrow Omitted)		
Neutral	- 0.014***	0.0071
Broad	- 0.004	0.0058
Sex (Male Omitted)		
Female	- 0.011***	0.0034
Marital Status (Married Omitted)		
Widowed	0.012	0.0077
Divorced	0.065***	0.0052
Separated	0.081***	0.0118
Never Married	- 0.002	0.0051
Education (Post-Baccalaureate Omitted)		
Never Attended	0.187***	0.0486
Attended Grades 1-8	0.209***	0.0114
Attended Grades 9-12	0.192***	0.0086
High school Graduate	0.103***	0.0060
Some College	0.072***	0.0060
Associate's Degree	0.057***	0.0071
Bachelor's Degree	0.020***	0.0057
Race (White Omitted)		
Black	0.077***	0.0062
Native American	0.062**	0.0276
Asian	- 0.112***	0.0077
Pacific Islander	- 0.095***	0.0268
Mix	0.067***	0.0164
Age	- 0.005***	0.0001
State Avg. Purchase Price (Used) ₁	- 0.027***	0.0014
State Avg. Purchase Price (New) ₂	0.003***	0.0013
Income Before Taxes ₃	- 0.007***	0.0030

- The analysis in this table incorporates the weights provided by the CEX

* represents a statistically significant result with a p-value of .1 to .05

** represents a statistically significant result with a p-value of .05 to .01

*** represents a statistically significant result with a p-value of less than .01

1 In 1,000s of 2017 dollars

2 In 1,000s of 2017 dollars

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3 In 10,000s of 2017 dollars

APPENDIX 1.A

Unfair Acts

In general terms, statutes define unfair practices as acts which make use of the difference between the buyer and seller in their power to gather and evaluate information regarding a good or service. In the case of the consumer in the introduction, the salesperson could use this difference to conceal or downplay the importance of certain information, like the mileage, servicing record, or accident history. Essentially, unfairness can be defined as an omission. An example of this would be if the seller knows of a defect in a vehicle that would be difficult for the buyer to discover and does not make the buyer aware of the defect.

Deceptive Acts

Statutes generally define deceptive practices as acts which are more blatant deceptions. Rather than relying on the disparity between buyer and seller, deception occurs where one party simply uses misinformation to complete the transaction. In the example from the introduction, this could be a guarantee from the salesperson that the car has never been in an accident, knowing that it had been in an accident. Essentially, deceptive can be defined as the use of misinformation. An example of this would be for the salesperson to tell the buyer that a vehicle had only had one owner when it, in fact, had several.

Breadth of Protection

In this paper, the breadth of protection refers to the range of situations in which a consumer would be able to bring a legitimate legal action against a seller for either a deceptive or unfair act. There are several factors that can impact the breadth of protections against unfair or deceptive acts or practices. As an example, a statute with a large number of instances that qualify as either unfairness or deception could only be applied under specific transactions. As an example, a statute that has a long list of prohibited acts, but those acts are only applicable to appliance sales. Under this example, the couple from the example would be unable to recoup their loss through legal action by using their state's UDAP statute. If the statute only protects against unfair or deceptive practices in insurance sales or car sales, then the breadth of protection offered would be narrow even if the number of unfair or deceptive acts is large.

As discussed above, rather than treating each state as a respondent, this paper examines the UDAP statute of each state to determine the level of protection provided by each statute. Each statute is made up of many components that determine how difficult it would be for a consumer to win a legal action. This paper simply examines the breadth of protection offered by each statute as a result of the definitions of unfair and deceptive acts within the statute. Table 2 details the statistical breakdown of these statutory definitions. The criteria used to determine whether a state provides narrow, neutral, or broad protections against unfair or deceptive acts can be seen below.

Given the qualitative nature of legislation, the independent variable measuring the breadth of protection provided by the statutory definition of unfairness is divided into three separate levels: narrow, neutral, and broad. How a statute defines unfairness or deception will broadly speaking, determine which actions are permitted and which are prohibited. A statute with a strict definition of unfairness or deception will be easily implemented by the courts but will provide narrow protection. As such, statutes that offer narrow protections through strict definitions of unfairness or deception are identified here as being narrow, statutes which provide more protection through looser definitions are identified here as neutral, and statutes providing strong protections through expansive definitions against unfairness and deception are identified here as broad.

Framework of Statute Evaluation

Due to the qualitative nature of legislation, there is no feasible way to assign continuous values to the protections provided by statutes. Instead, the author used a Likert scale, and after reading the statute assigned it a value to designate that the statute was broad (2), neutral (1), or narrow (0). By examining the Statutes of Alabama, Iowa, and Colorado, the author's scoring of state statutes can be demonstrated.

Alabama – Broad

Alabama's statute combines both unfair and deceptive under the same framework. This means that there is no difference between unfair and deceptive acts. The list of prohibited acts is extensive and is finalized by the use of language that indicates that the list is not exclusive, meaning a judge or jury could find that a situation not listed in the statute is protected against. What raises this statute to providing broad protections is the lack of knowledge by the business entity that it is in violation of the law. There were no substantive changes to Alabama's UDAP statute during the time period this paper examined.

Iowa – Neutral

The Iowa UDAP statute states that "Unfair practice" means an act or practice which causes substantial, unavoidable injury to consumers..." This is a very general statement which could allow a judge or jury to conclude that a situation is protected under the law. However, by including the terms "substantial" and "unavoidable" definition merely rises to the level of neutral

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protection. The statute defines deceptions “an act or practice which has the tendency or capacity to mislead a substantial number of consumers as to a material fact or facts.” Once again, a broad scope of circumstances could fall under this definition, but by adding the requirement that it “mislead a substantial number” limits its protective power to neutral. Iowa’s UDAP statute did not change substantively during the period examined in this paper.

Colorado – Narrow

Colorado’s UDAP statute uses a list of acts to designate which practices are deemed deceptive or unfair. This list is relatively short to other states’ lists. Additionally, Colorado’s UDAP statute does not include language which would allow a judge or jury to find a situation that is not described in the statute to be protected against by the statute (like Alabama). Finally, Colorado’s list of deceptive and unfair acts functions in many regards as a simple proscription of fraud because many of the practices listed also require that the perpetrator know that they are being deceptive or unfair. Almost all of the acts require that the perpetrator knowingly mislead or deceive.

Table 1.A1: State UDAP Statute Reference and Strength

<i>State</i>	<i>State Statute</i>	<i>Protection against Unfair Acts</i>	<i>Protection Against Deceptive Acts</i>
Alabama	Ala. Code §§ 8-19-1 through 8-19-15	Broad	Broad
Alaska	Alaska Stat. §§ 45.50.471 through 45.50.561	Broad	Broad
Arizona	Ariz. Rev. Stat. Ann. §§ 44-1521 through 44-1534	Narrow	Broad
Arkansas	Ark. Code Ann. §§ 4-88-101 through 4-88-207	Broad	Broad
California	Cal. Bus. & Prof. Code §§ 17200 through 17594	Broad	Broad
Colorado	Colo. Rev. Stat. §§ 6-1-101 through 6-1-115	Narrow	Narrow
Connecticut	Conn. Gen. Stat. §§ 42-110a through 42-110q	Broad	Broad
Delaware	Del. Code Ann. tit. 6, §§ 2511 through 2527, 2580 through 2584	Narrow	Broad
District of Columbia	D.C. Code §§ 28-3901 through 28-3913	Broad	Broad
Florida	Fla. Stat. §§ 50 through 501.213	Broad	Broad
Georgia	Ga. Code Ann. §§ 10-1-390 through 10-1-407	Broad	Broad
Hawaii	Haw. Rev. Stat. §§ 480-1 through 480-24	Broad	Broad
Idaho	Idaho Code Ann. §§ 48-601 through 48-619	Broad	Broad
Illinois	815 Ill. Comp. Stat. 505/1 through 505/12	Broad	Broad
Indiana	Ind. Code §§ 24-5-0.5-1 through 24-5-0.5-12	Broad	Narrow
Iowa	Iowa Code §§ 714.16 through 714.16A	Neutral	Neutral
Kansas	Kan. Stat. Ann. §§ 50-623 through 50-640	Broad	Broad
Kentucky	Ky. Rev. Stat. Ann. §§ 367.110 through 367.990	Broad	Broad
Louisiana	La. Rev. Stat. Ann. §§ 51:1401 through 51:1420	Broad	Broad
Maine	Me. Rev. Stat. Ann. tit. 5, §§ 205A through 214	Broad	Broad
Maryland	Md. Code Ann., Com. Law §§ 13-101 through 13-501	Broad	Broad
Massachusetts	Mass. Gen. Laws Ann. ch. 93A, §§ 1 through 11	Broad	Broad
Michigan	Mich. Comp. Laws §§ 445.901 through 445.922	Broad	Broad
Minnesota	Minn. Stat. §§ 325F.68 through 325F.70	Narrow	Broad
Mississippi	Miss. Code Ann. §§ 75-24-1 through 75-24-27	Neutral	Neutral
Missouri	Mo. Rev. Stat. §§ 407.010 through 407.307	Broad	Broad
Montana	Mont. Code Ann. §§ 30-14-101 through 30-14-142	Broad	Broad
Nebraska	Neb. Rev. Stat. §§ 59-1601 through 59-1623	Broad	Broad
Nevada	Nev. Rev. Stat. §§ 598.0903 through 598.0999	Neutral	Broad
New Hampshire	N.H. Rev. Stat. Ann. §§ 358-A:1 through 358-A:13	Broad	Broad
New Jersey	N.J. Stat. Ann. §§ 56:8-1 through 56:8-91	Broad	Broad

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New Mexico	N.M. Stat. §§ 57-12-1 through 57-12-22	Broad	Broad
New York	N.Y. Exec. Law § 63(12)	Neutral	Broad
North Carolina	N.C. Gen. Stat. §§ 75-1.1 through 75-35	Broad	Broad
North Dakota	N.D. Cent. Code §§ 51-15-01 through 51-15-11	Narrow	Broad
Ohio	Ohio Rev. Code Ann. §§ 1345.01 through 1345.13	Broad	Broad
Oklahoma	Okla. Stat. tit. 15, §§ 751 through 763	Broad	Broad
Oregon	Or. Rev. Stat. §§ 646.605 through 646.656	Broad	Narrow
Pennsylvania	73 Pa. Stat. Ann. §§ 201-1 through 201-9.3	Neutral	Neutral
Rhode Island	R.I. Gen. Laws §§ 6-13.1-1 through 6-13.1-27	Broad	Broad
South Carolina	S.C. Code Ann. §§ 39-5-10 through 39-5-160	Broad	Broad
South Dakota	S.D. Codified Laws §§ 37-24-1 through 37-24-35	Narrow	Neutral
Tennessee	Tenn. Code Ann. §§ 47-18-101 through 47-18-125	Broad	Broad
Texas	Tex. Bus. & Com. Code Ann. §§ 17.41 through 17.63	Broad	Neutral
Utah	Utah Code Ann. §§ 13-11-1 through 13-11-23	Broad	Broad
Vermont	Vt. Stat. Ann. tit. 9, §§ 2451 through 2480g	Broad	Broad
Virginia	Va. Code Ann. §§ 59.1-196 through 59.1-207	Narrow	Broad
Washington	Wash. Rev. Code §§ 19.86.010 through 19.86.920	Broad	Broad
West Virginia	W. Va. Code §§ 46A-6-101 through 46A-6-110	Broad	Broad
Wisconsin	Wis. Stat. § 100.18 through 100.264	Broad	Broad
Wyoming	Wyo. Stat. Ann. §§ 40-12-101 through 40-12-114	Broad	Broad



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