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Report to the Chairman, Subcommittee on Antitrust, Impact of Deregulation, and Privatization, Committee on Small Business, House of Representatives

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AIR TRAVEL

Effectiveness of State Consumer Protection Efforts Varies

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The Honorable Dennis E. Eckart
Chairman, Subcommittee on Antitrust,
Impact of Deregulation, and Privatization
Committee on Small Business
House of Representatives

Dear Mr. Chairman:

As requested in your letter of April 6, 1989, we surveyed the states' efforts to protect consumers from unfair and deceptive trade practices in the travel industry. As agreed with your office, we (1) examined how the states are organized to address consumer protection problems, (2) identified the most serious consumer protection problems the states have encountered in the travel area, and (3) assessed to what extent the effectiveness of state action in this area is limited by federal restrictions on the states' consumer protection role.

We looked in detail at four states—California, New York, Ohio, and Texas—chosen from those that are actively involved in travel consumer protection. We also contacted six additional states that officials of state and private organizations told us had been active on particular travel consumer protection issues we identified. Appendix III contains further details on our objectives, scope, and methodology.

Results in Brief

The four states we visited have broad statutes prohibiting unfair and deceptive trade practices; three of these also have narrower statutes prohibiting specific travel-related practices. These four states have generally assigned authority over travel-related practices to consumer protection units in the state's Office of the Attorney General, with additional authority sometimes assigned to specialized consumer protection offices.

The officials we talked to in the four states cited several problems facing travel consumers. First, financially distressed tour operators have provided some consumers with services that are less complete or inferior to what the consumer was promised—thus causing some consumers to incur substantial financial losses. Second, consumers have lost millions of dollars to travel scams—fraudulent sales of travel services. Third, airline advertising practices sometimes violate state laws against unfair and deceptive trade practices (for example, by advertising one-

way fares that are available only on a round-trip basis). And fourth, passenger rights (e.g., the right to compensation for lost baggage or denied boarding) are not always well specified.

The state agencies have successfully responded to some of these travel consumer protection problems. Their effectiveness has varied, depending in part on the adequacy of the states' authority in each area. States appear to have adequate authority to regulate tour operators, because most tour operators do a substantial portion of their business within the state in which they are located. In the case of travel scams, however, the states' efforts have been less effective because the operators typically operate by mail or telephone across state lines, thus escaping the jurisdiction of the states whose consumers are defrauded. State efforts to regulate airline advertising practices similarly have been largely ineffective because state airline advertising guidelines conflict with U.S. Department of Transportation (DOT) policies. A federal court of appeals has found state actions in regulating advertising practices to be preempted by the Federal Aviation Act, as amended by the Airline Deregulation Act of 1978. Finally, in the area of rights for airline passengers, state consumer protection officials say that airline passengers are not adequately protected by existing rules, but they saw DOT as primarily responsible for addressing these issues.

States Use Various Laws and Agencies to Address Travel Consumer Protection Problems

All 50 states have enacted general consumer protection laws that prohibit deceptive trade practices, and most prohibit unfair or unconscionable practices as well. These laws were mostly enacted during the 1960s and 1970s to supplement existing common-law prohibitions on unfair and deceptive trade practices. They apply to all consumer transactions, including the advertising and selling of travel services.

Three of the four states we visited, as well as five of the six other states we contacted, also have specific travel-related laws to protect consumers' financial interests. Such laws apply to travel agents and agencies, tour operators, and other travel promoters. They generally require either licensing or registration of tour operators or travel agents. They also generally provide some means for protecting travelers' advance payments, either by requiring deposit of such payments in a trust account or by requiring posting of bonds by the travel agent or tour operator.

In the four states that we visited, these consumer protection laws are primarily enforced by state attorneys general. Case mediators in the

attorneys general offices receive complaints from consumers and attempt to resolve problems between consumers and travel providers by contacting the airline, travel agent, or other travel provider named in the complaint to seek voluntary remedies. If mediation is not successful, officials evaluate cases to see if further investigation and litigation are warranted. The criteria for making such a determination generally include the likely public impact, number of consumers affected, number of similar complaints, and practicality of investigation.

Two of the states we visited, California and New York, have also created special consumer protection offices responsible for some consumer protection functions. These agencies focus their efforts on mediation, consumer education, and legislation rather than enforcement. While the California Department of Consumer Affairs has authority to litigate cases, it generally leaves this function to the attorney general's office. Fourteen other states have similar offices.

States Have Identified Four Consumer Air Travel Problems

State officials identified four major types of travel consumer problems. These were also the most frequently cited problems in news accounts we surveyed on travel consumer problems and in our discussions with national organizations concerned with travel consumer problems.

The first major problem involved tour operator insolvencies that may cause financial losses to consumers when the tour operator goes bankrupt before delivering on travel paid for in advance. Consumers must often pay deposits in advance to reserve space on a tour. If the tour operator experiences financial difficulties, consumers may lose their deposits, receive travel services inferior to those promised, or get stranded outside the United States with tickets or reservations that are no longer honored.

A second major travel consumer problem involves travel scams in which fraudulent operators trick consumers into buying worthless travel club memberships or use the lure of free or low-priced travel services to make unauthorized charges on consumers' credit card accounts. These operators typically base their operations in one state and target consumers in other states using mail or telemarketing techniques. The Federal Trade Commission (FTC) estimated that travel scams in 1987 cost consumers "tens of millions of dollars."

The third major travel consumer problem is airline fare advertising practices that, according to many state attorneys general, violate the

requirements of the states' unfair and deceptive trade practices laws. Some airlines advertise one-way fares that are available only on a round-trip basis, or leave out surcharges which the traveler is required to pay. While these conditions and surcharges are required to be disclosed in the fine print of the advertisement, most state attorneys general believe consumers are deceived by these practices.

The fourth major travel consumer problem involves the lack of what are generally referred to as "passenger rights." While DOT has some regulations in force which govern compensation for lost baggage and denied boarding, the states have received many complaints about airline policies concerning lost baggage; compensation for passengers who are denied boarding (or "bumped") on flights for which they have confirmed reservations; inadequate services provided to passengers whose flights are cancelled or delayed; failure to disclose when tickets are nonrefundable; and abrupt changes in the provisions of frequent flyer plans.

State agencies lacked comprehensive data on the volume or types of travel complaints received. However, the limited data available and state officials' estimates suggested that most travel complaints concerned air carrier practices rather than practices of bus lines, railroads, or cruise ship lines.

States' Effectiveness in Protecting Consumers Varies

The state agencies have responded to some of these air travel consumer protection problems. Their effectiveness has varied, depending in part on the adequacy of the states' authority in each area. For example, states appear to have adequate authority to regulate tour operators, because most tour operators do a substantial portion of their business within a single state. Several states have enacted laws governing tour operator activities. DOT believes that most tour operator problems result from tour operator practices that violate federal law. Better coordination between state and federal officials, as recommended in our report last year on DOT's enforcement of its consumer protection responsibilities,[1] could prevent some of these practices.

In the case of travel scams, however, the states' efforts have been less effective because of limited jurisdictional boundaries. Scam operators frequently move from state to state and solicit customers in other states,

[1] Airline Competition: DOT's Implementation of Airline Regulatory Authority (GAO/RCED-89-93, June 28, 1989).

making prosecution difficult for state officials. Because travel scams are usually an interstate problem, state officials saw the need for a more active federal role to address this problem. The proposed Telemarketing Fraud Prevention Act (H.R. 1354) would require a more active federal role by mandating rulemaking by the FTC to regulate the sale of goods and services by telephone. It would also allow officials of one state to file suit against telemarketers in other states in federal district courts.

State efforts to regulate airline advertising practices similarly have been largely ineffective because state airline advertising guidelines conflict with DOT policies, and because a federal court has ruled that states are preempted from enforcing their laws in this area. Airline advertising practices are a problem that has surfaced prominently since the Civil Aeronautics Board ceased operations. Recent controversy over airline advertising has centered on whether federal statutes preempt the states from using their unfair and deceptive trade practice laws to regulate advertising. The governing decision on this issue currently is the recent decision by the Fifth Circuit Court of Appeals in TWA v. Mattox, 897 F.2d 773 (5th Cir. 1990), which ruled that state regulation of airline price advertising was preempted by Section 1305 of the Federal Aviation Act, as amended by the Airline Deregulation Act of 1978.

Finally, in the area of rights for airline passengers, federal law explicitly reserves to the federal government the authority to regulate "rates, routes, or services" of air carriers. Although consumer groups and state consumer protection officials have received numerous complaints about inconsistencies in rights afforded airline passengers, and about passengers not always being adequately informed about their rights, they saw DOT as primarily responsible for addressing these issues.

In our report last year on DOT's enforcement of its consumer protection responsibilities, we focused primarily on the adequacy of DOT's process for handling consumer complaints. We did not independently assess the significance of passenger rights problems or the adequacy of DOT's response to those problems. We did find there was a general need for DOT to draw on information from the states to help set priorities for rulemaking and enforcement at the federal level. As you know, we intend to follow up in the coming year on the extent of passenger rights problems and on DOT's implementation of our recommendation to coordinate its consumer affairs functions with state offices.

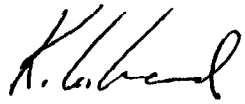
Agency Comments

DOT provided official oral comments on a draft of this report. DOT stated that we had not taken into account its view that tour operators are regulated under federal law. We have added a reference to DOT's views in the letter and a more extensive discussion of DOT's views on this matter in appendix II, where we also cite several federal court cases that support its view. We also point out that the state officials we talked to are unaware of DOT's interpretation of federal law. Better coordination between state and federal officials, in our view, could result in better protection of consumers.

DOT also believes that the question of whether states are preempted from regulating airline advertising practices has been settled by the recent decision of the Fifth Circuit Court of Appeals, which held that states are preempted.[2] We have reviewed the recent court decisions on this matter and agree that the Fifth Circuit decision is currently the governing decision on this issue. However, because the Fifth Circuit decision is expected to be appealed to the U.S. Supreme Court, the ultimate resolution of this issue is uncertain. DOT also suggested several technical changes which we incorporated as appropriate.

Additional information on the four major types of travel consumer problems we examined and on how states are addressing these problems can be found in appendixes I and II. As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies to interested parties and make copies available to others upon request. If you have any questions about this report, I can be reached at (202) 275-1000. Major contributors to this report are listed in appendix V.

Sincerely yours,



Kenneth M. Mead
Director, Transportation Issues

[2]Trans World Airlines et al. v. Mattox, 897 F.2d 773 (5th Cir. 1990).

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Abbreviations

CAB	Civil Aeronautics Board
DOT	U.S. Department of Transportation
FTC	Federal Trade Commission
GAO	General Accounting Office
IAPA	International Airline Passengers Association
NAAG	National Association of Attorneys General

States Have Identified Four Consumer Air Travel Problems

State officials identified four major types of air travel consumer problems. These problems are

- tour operator insolvencies;
- travel scams;
- airline fare advertising practices; and
- the lack of well-defined "passenger rights."

Tour Operator Bankruptcies May Cause Financial Losses to Consumers

Tour operators buy blocks of airline seats and hotel rooms at wholesale prices, assemble these components into a tour package, and retail the package to individual travelers and travel groups. Problems occur because tour operators often sell the space before they buy it. If they encounter unanticipated financial difficulties, the operators may not be able to secure the transportation or accommodations they have promised. When this happens, consumers may lose their money or receive travel services inferior to those promised.

Tour package sales are a big business. In 1988 U.S. consumers purchased $1.6 billion in tour packages from firms primarily engaged in arranging passenger transportation—a 14 percent increase over 1987. It is also largely a local business—tour operators sell a substantial portion of their tour packages to travelers located in the same state as the tour operator. Unfortunately, tour operator bankruptcies have caused consumers to lose deposits of up to $10,000 and left consumers stranded outside the United States with tickets or reservations that were not honored.

For example, in May 1987 Houston consumers encountered problems with a tour operator who sold travel certificates. The tour operator began defaulting on obligations to a travel agency that provided the air and land travel packages to be used by the certificate holders. Unable to provide travel and accommodations for many certificate holders, the tour operator offered hundreds of consumers a full refund or the opportunity to reschedule their travel arrangements. Some who rescheduled had trips cancelled a second time. Although most consumers requested refunds in full, none of the estimated 300 consumers seeking refunds have been successful in obtaining their money.

Travel Scams Cost Consumers Millions of Dollars

Travel scams are fraudulent schemes in which consumers are typically enticed, by mail or over the telephone, to buy a "bargain" vacation package. The offer may involve buying a membership in a travel club that allegedly entitles the member to free or greatly discounted travel, but that turns out to require substantial further payments not disclosed in the original offer. Alternatively, the offer may claim that the scam target has won the right to free or low-cost travel, but that the "winner" must disclose a credit card number to verify eligibility. The scam operator subsequently uses the credit card number to bill the consumer for expensive vacations without the consumer's knowledge or consent. Similar scams have been set up offering oil and gas rights, gem stones, and rare coins. In the four states we visited, state officials told us that travel scams were particularly common between 1986 and 1988. Some officials believe scam operators have now either moved on to other states or other types of scams.

Scam operators typically set up a telephone bank in one state and make calls to consumers in other states, using carefully written telemarketing scripts; they have no intention of delivering the goods or services they promise. At July 1987 congressional hearings, the Director of Consumer Protection for the Federal Trade Commission (FTC) estimated that over the past several years the Commission had stopped over $600 million in telemarketing scams. He estimated that in 1987 alone, travel-related fraud cost consumers "tens of millions of dollars."[1]

Most States Believe Airline Advertising Practices Are Unfair and Deceptive

Prior to 1985 the Civil Aeronautics Board (CAB) adopted rules governing airline advertising practices. The CAB rules required, for example, that fare advertising show the round-trip fare for fares available only on a round-trip basis, and that required fees and charges be included in the fare.[2] Since 1985, when DOT was given the consumer protection functions of the expiring CAB, DOT has sought to enhance the operation of the market by encouraging aggressive air fare advertising. Beginning in

[1]The information on estimated losses presented during these hearings was the most recently available information on travel scams.

[2]U.S. Department of Transportation (DOT) regulations (14 CFR 399.84) state that "the Board [now Department of Transportation] considers any advertising or solicitation by a direct air carrier, indirect air carrier, or an agent of either, for passenger air transportation, a tour,...or a tour component...that states a price for such air transportation, tour, or tour component to be an unfair or deceptive trade practice, unless the price stated is the entire price to be paid by the customer to the air carrier, or agent, for such air transportation, tour, or tour component."

1985 DOT responded to inquiries from airlines and other interested parties by sending letters stating that it had reinterpreted the CAB regulations on fare advertising (which DOT was now responsible for enforcing). Even though half of a round-trip fare was less than an actual one-way fare, DOT would henceforth permit half of a round-trip fare to be advertised as a one-way fare as long as the advertisement clearly stated that a round-trip purchase was required. In 1985 and 1988 DOT also issued exemption orders permitting airlines to advertise prices that did not include government-approved charges and fees. The fare could be "unbundled," with the charges and fees listed separately in a footnote. These charges include immigration fees, security surcharges, and international departure taxes assessed on each passenger.

The states began to experience a dramatic increase in consumer complaints involving unfair and deceptive advertising practices by the airlines about a year and a half after CAB ceased operations. In 1987 attorneys general of a majority of the states voted, under the auspices of the National Association of Attorneys General, in favor of airline advertising guidelines stating that these revisions of the CAB rules allow airlines to publish advertisements that are false and misleading and deceive consumers about the true price of air travel.

Airline Practices Leave Passenger Rights Ill-Defined

Consumer complaints received by DOT increased sharply between 1985 and 1987, rising from about 8,800 to nearly 41,000. However, since 1987 complaints have receded to about the same level recorded in 1985. State officials told us consumers frequently complain about airline service problems, such as lost or damaged baggage. Travel consumer group representatives told us that passengers receive inadequate information about compensation for voluntary denied boarding and services available from airlines when flights are delayed or cancelled.

Although DOT regulations set liability limits for compensation on lost baggage, the regulations do not specify how the value of the luggage's contents will be verified. An official with the International Airline Passengers Association (IAPA) told us that airline policies on documenting proof of loss vary. Some airlines require original purchase receipts, cancelled checks, or other documentation for high-value items, while others do not. He indicated consumers are not aware of these differences.

When airline passengers are denied boarding because a flight has been oversold, DOT regulations guarantee them certain rights. When a flight is oversold, air carriers must request volunteers willing to give up their

seats to take a later flight (in return for some compensation from the airline). If an insufficient number of passengers volunteer, then the carrier may deny boarding to the remaining passengers. For involuntary denied boarding, the carrier is required to pay cash compensation of up to $400, or offer an equivalent value of free or reduced rate air transportation. In the latter instance, passengers must be informed in writing of the amount of cash that would otherwise have been offered. They must also be given a written explanation of the terms, conditions, and limitations of any compensation that is given them.

Volunteers for denied boarding may also be offered compensation for voluntarily relinquishing their confirmed seat; however, the compensation is any amount the airline offers that the passenger willingly accepts. Although DOT regulations allow the airlines to offer free air transportation as an incentive for passengers to voluntarily relinquish seats on an oversold flight, several observers, including an assistant attorney general in the New York Attorney General's Office, the Director of Consumer and Industry Affairs for IAPA, and the National Association of Attorneys General, contend that this practice is not entirely fair to consumers. They point out that, although vouchers for free air travel may seem very attractive to consumers, they sometimes carry serious restrictions on their use, such as limitations on the number of seats that are available for free use and blackout periods when no free seats are available. DOT regulations do not require the airline to disclose these restrictions; however, DOT has stated in a 1987 letter to the airline industry that it expects airlines to disclose restrictions on voluntary denied boarding compensation "before the passenger surrenders a seat or declines a check" [emphasis in original].

Other "passenger rights" are not federally protected at all. For example, consumers generally are not aware of how airline policies differ on services provided when their flights are delayed or diverted. These range from no services at all to various combinations of hotel accommodations, meals, and telephone privileges. Some airlines provide services only under certain circumstances—for example, if the passenger involved is flying first class.

Consumers have also complained that they were not informed that certain tickets were nonrefundable. While DOT regulations require that the nonrefundable nature of the ticket be disclosed on the ticket itself, they do not require that nonrefundability be disclosed when the ticket is purchased (for example, if it is purchased by telephone). However, DOT officials told us that they would regard failure to disclose nonrefundability

at the time of sale to be an unfair and deceptive trade practice, even though it is not specifically prohibited by DOT's rules.

Another area of complaint is frequent flyer programs. Complaints have centered on changes in program rules without adequate notification to members and limitations on the number of frequent flyer seats available to members when they redeem program certificates.

Finally, during the past decade dozens of airlines have ceased operations or filed for bankruptcy, costing consumers millions of dollars in lost air fares. These bankruptcy losses have continued despite efforts by DOT and state agencies to inform consumers of their rights and of possible ways to mitigate damages.

States' Effectiveness in Protecting Consumers Varies

While states have been active in protecting travelers, their ability to address specific problems varies. States appear to have adequate authority to regulate tour operators, but problems have arisen in protecting consumers against travel scams and in addressing airline advertising practices. States generally believe they lack authority to deal with "passenger rights" issues.

Tour Operators Are Subject to Both State and Federal Law

Several states have enacted consumer protection laws to deal with tour operator problems. Of the 10 states we reviewed, 8 have laws regulating tour operators. With one exception these laws require the licensing or registration of tour operators, the posting of bonds or the placing of consumers' deposits in a trust account, or a combination of these requirements.[1] Since most tour operators do a substantial portion of their business with customers within the states in which they operate, states generally believe they have adequate authority to resolve consumer problems.

State officials commonly regard tour operators, unlike charter operators, as not being regulated by the federal government.[2] DOT, however, believes that tour operators are regulated under federal law, and that the problems that consumers typically have with tour operators (e.g., passengers not receiving airline tickets because of tour operator defaults) would not occur if tour operators complied with federal law. DOT takes the position that any retailer of air transportation, including tour operators, falls within the scope of Section 401 of the Federal Aviation Act. Section 401 requires, in effect, that any operation that "holds itself out 'as ready and willing to undertake for hire the transportation of passengers or property from place to place'" have a DOT air carrier certificate.[3] DOT believes that a tour operator, as a retailer of airline services, is "holding itself out" as a source of such services. As a result, DOT takes the position that any retailer of air transportation must be either a DOT-certificated air carrier, a travel agent authorized by such an air carrier to sell air transportation on its behalf, a DOT-regulated public charter operator exempted from section 401 by DOT's public charter regulations

[1] Appendix IV shows key components of each of the eight states' laws governing tour operators.

[2] Charter operators charter all or part of the use of aircraft that are not flying on a regular schedule, while tour operators may buy space on regularly scheduled flights. Charter operators are covered by federal regulations that require them to protect consumers' payments for travel services by obtaining a bond and by depositing funds in an escrow account.

[3] Voyager 1000 v. CAB, 489 F.2d 799 (7th Cir. 1973), cert. denied, 416 U.S. 982 (1974), citing Las Vegas Hacienda, Inc. v. CAB, 298 F.2d 434 (9th Cir. 1962).

(14 C.F.R., Part 380), or a contract bulk fare operator operating under contract to a DOT-certificated air carrier under authority of CAB orders 80-11-24 (Nov. 5, 1980) and 81-7-109 (July 21, 1981).

Several federal court cases support DOT's view that tour operators fall within the scope of Section 401 of the Federal Aviation Act. These cases state that travel agents, tour operators, and nominal "social clubs" which publicly sell tours are "indirect air carriers" for the purposes of section 401.[4] Any entities that

> "hold out to the public" that they engage in air transportation, by selling flights to the general public, by furnishing flights otherwise unserviced by regularly scheduled airlines, or by soliciting "members of the general public to purchase tickets on the flights it arranges,"

qualify as air carriers under section 401, according to these cases.[5]

By DOT's interpretation of the requirements of section 401, a tour operator must have a direct relationship, as agent or contractor, with an airline. According to DOT, by this standard most of the tour operators that are the subject of consumer complaints are operating illegally, because in general these tour operators do not have such direct contractual relations with airlines. They are buying seats from travel agents, charter operators, or other tour operators. It is the lack of this direct contractual relationship with an airline that results in consumer problems, because when the tour operator goes into default, there is no one to back up its promise of airline services, and the passenger may lose any money paid in advance for airline tickets. The laws and regulations under which agents and contractors of airlines operate provide protection for the passenger in the event that such an agent or contractor defaults. In the case of a travel agent or contract bulk fare operator, the airline is obligated to provide the transportation which the agent or contractor has sold, even if the airline has not been paid. In the case of a charter operator, the DOT-required escrow account provides some protection for the passenger.

However, the DOT rules protect travellers only from losing their airline tickets. There is no protection for the passenger from losing hotel space

[4]Arkin v. Trans International Airlines, Inc., 568 F.Supp. 11 (E.D.N.Y. 1982). See also CAB v. Carefree Travel, Inc., 513 F.2d 375 (2d Cir. 1975), and Monarch Travel Services v. ACCI, 466 F.2d 552 (9th Cir.), cert. denied, 410 U.S. 967, 93 S.Ct. 1444, 35 L.Ed.2d 701 (1973).

[5]Arkin, 568 F.Supp. at 13 (citations omitted).

and tickets for sightseeing tours, admissions to museums, etc. ("ground packages"), that tour operators also sell.

DOT staff complained to us that state officials rarely report to them tour operators who are operating illegally, while the representatives of state attorneys general told us that they were completely unaware that DOT interpreted section 401 as applying to tour operators. In our recent report, Airline Competition: DOT's Implementation of Airline Regulatory Authority (GAO/RCED-89-93, June 28, 1989), we recommended that DOT better coordinate its consumer affairs functions with state offices. We believe that this is a good example of a case where such coordination would be fruitful.

States Want More Help From Federal Authorities in Prosecuting Travel Scams

In addition to general consumer protection laws and laws applying broadly to anyone who sells travel services, 4 of the 10 states we contacted have introduced telemarketing legislation to prevent scams. In Texas and New York the legislation has not been passed. However, Tennessee and Washington enacted telemarketing legislation in 1989 that covers travel service sales. Tennessee's law became effective in June 1989, and Washington's law became effective in January 1990. These laws include provisions requiring that telemarketers register and that telephone scripts be reviewed in advance with state authorities.

The four states we visited have attempted to halt travel scam operations primarily through litigation. California and Ohio have filed several suits under their general consumer protection laws and specific travel-related laws. Texas has brought several suits against scam operators under its general consumer protection law. New York officials told us that they have mediated travel scam cases but that they have not recently filed any lawsuits against travel promoters. Tennessee's new telemarketing law has been the basis for several lawsuits since July 1989.

Texas has been the most active of the four states we visited in travel scam litigation. According to an assistant attorney general, the state has filed approximately 10 to 12 lawsuits against travel telemarketers operating in Houston since 1986. In one case, the state charged a travel telemarketer with using deceptive language in sales presentations, failing to disclose restrictions on travel services, misusing consumer credit card numbers, and failing to disclose full information about trip itineraries. The firm was enjoined from engaging in any business activity in or from the state of Texas and ordered to deposit $25,000 in an account for consumer refunds.

The federal government has attempted to halt travel scams by adopting a combination of approaches, including investigations, litigation, information sharing, and legislation. The FTC has prosecuted fraudulent travel telemarketers under Sections 5 and 13 of the Federal Trade Commission Act. In addition, the Postal Inspection Service has conducted mail fraud investigations of travel scams under Title 18 of the United States Code, Section 1341.

The FTC and the states cooperated in 1987 in setting up the Telemarketing Complaint System data base to help the nation's law enforcement agencies collect and share information on firms suspected of telemarketing fraud. The system is designed to help participating organizations identify and prosecute fraudulent telemarketers. Participating organizations include 26 states, 3 federal agencies, and 4 private organizations.

Although the states we visited have had some success in prosecuting travel scams operating in their states, most state officials contacted during these visits told us federal agencies need to take a more active enforcement role if travel scams are to be eliminated. According to state officials in New York, Ohio, and Texas, scams can be most effectively prosecuted at the federal level because scam operators and targeted consumers are usually in different states, which creates jurisdictional enforcement problems for the states. The attorney general in the state whose consumers are being targeted has no authority to prosecute the fraudulent telemarketers operating out of other states. The Assistant Attorney General in Houston, Texas, pointed out that state actions are applicable only in cases where illegal action is directly related to operations within the state, or to protect consumers who reside in the state. On the other hand, federal enforcement actions, such as FTC injunctions, are enforceable in U.S. federal courts in any state. Also, the states have difficulty in obtaining restitution for consumers, whereas the FTC has the authority to freeze a firm's assets.

One approach to strengthening state authority and encouraging a more active federal enforcement role is embodied in the proposed Telemarketing Fraud Prevention Act of 1989 (H.R. 1354). This legislation would allow states to bring civil actions against fraudulent telemarketers in the U.S. district courts in the states where the telemarketers are located. Injunctions obtained as a result of the actions would be enforceable in any federal court. The bill would also mandate a more active FTC role, requiring the FTC to establish rules setting time limits on the delivery of goods and services marketed by telephone and

allowing consumers a specified period within which to cancel an order made by telephone. This legislation would resolve most of the concerns that the states have about limited state jurisdiction.

State Laws and Federal Enforcement Practice on Airline Advertising Are in Conflict

Most states believe that DOT's revisions of CAB's airline advertising rules conflict with the states' interpretations of their unfair and deceptive trade practice statutes. The states generally interpret their statutes as prohibiting the airlines from advertising half of a round-trip fare as a one-way fare when the true cost of a one-way fare is substantially more. State officials believe that such advertisements are false and misleading and deceive consumers about the true price of air travel. After the states experienced a dramatic increase in consumer complaints involving unfair and deceptive advertising practices by the airline industry, the state attorneys general, through their professional organization, the National Association of Attorneys General (NAAG), developed guidelines for airlines to follow in advertising travel. The purpose of the guidelines was to clarify for the airline industry what the states considered prohibited conduct under their laws.

A number of states have sued the airlines over airline advertising practices that in their view violate states' consumer protection laws. The airlines' defense in each of these cases has been that federal law preempts such suits. Section 105 of the Federal Aviation Act of 1958 (49 U.S.C., App. Section 1305) states that

> No state shall enact or enforce any law, rule, regulation, standard, or other provision having the force and effect of law relating to rates, routes or services of any carrier having authority under Subchapter IV of this chapter to provide air transportation.

According to the airlines, the states, by bringing suits against them on the basis of their advertising statutes, are attempting to regulate airline rates, routes, or services.

The states, on the other hand, argue that airlines can set or develop rates, routes, or services as they see fit, but they must publish or broadcast this information within a given state in a manner consistent with that state's laws. The states point to another section of the Federal Aviation Act (49 U.S.C. Section 1506) which states "Nothing in this chapter shall in any way abridge or alter the remedies now existing at common law or by statute, but the provisions of this chapter are in addition to such remedies," as preserving state remedies in this area.

In 1988, 27 states sued DOT over its 1988 airline advertising exemption orders because the orders conflicted with the states' unfair and deceptive trade practices laws. Without resolving the substantive issues, the U.S. Court of Appeals for the District of Columbia Circuit ruled in favor of the states, finding that DOT had not complied with the notice-and-comment requirements of the Administrative Procedures Act, and rescinded the two orders.

Following the court's rescission of the two airline advertising orders, DOT in July 1989 published proposed rules in the Federal Register to codify its price-advertising policy regarding one-way fares. Like the rescinded orders, the proposed rules would allow advertisers to list government-approved fees and charges separately from fares in advertisements. As of June 1990 the rules had not been adopted and DOT officials said they could not estimate when they would be.

The United States Court of Appeals for the Fifth Circuit, the highest court to rule on the matter, recently held that states are preempted from enforcing airline advertising laws.[6] The Fifth Circuit decision held that "state laws proscribing deceptive advertising are preempted by federal law when the state attempts to enforce such laws against the advertising of fares by interstate and international airlines." The court said that airline fare advertising "relates to" rates within the meaning of section 1305(a)(1) and thus any state regulation is expressly preempted. The court dismissed the states' argument that section 1506 preserved state remedies in the price advertising area, stating that "Section 1506 does not preserve state law remedies when there is express preemption under Section 1305." The court affirmed the lower court's preliminary injunction, which enjoins the Attorney General of Texas and 33 other states' attorneys general from bringing any other similar suits against the plaintiff airlines.

States Generally Lack Authority to Address Passenger Rights Problems

State officials we visited do not generally view solutions to passenger rights complaints as within their jurisdiction. They believe that these airline practices fall within the "rates, routes or services" whose regulation is reserved to the federal government. With a few exceptions, they said passenger rights complaints were referred to the airlines or DOT. In the four states we visited, officials in the offices of attorneys general and other consumer protection offices received complaints about lost luggage and other airline services and generally referred them to the

[6]Trans World Airlines et al. v. Mattox, 897 F.2d 773 (5th Cir. 1990).

airline or DOT for resolution. In those cases where states tried to resolve these types of complaints, for example, by contacting the airlines, they believed their success was limited by their lack of authority over the airlines.

One area where states have tried to be active is in requiring disclosure of airline policies. In December 1987 NAAG adopted a guideline on the disclosure of restrictions in compensation for passengers voluntarily denied boarding on overbooked flights. This guideline calls for full disclosure by the airlines of all restrictions on offers for future air travel before consumers volunteer to give up their seats. NAAG believes that it is unfair and deceptive to promise free air travel without disclosing the restrictions on the travel offered. Like NAAG's advertising guidelines, this guideline is intended to clarify what the states consider prohibited conduct under their laws. Since federal regulations require passengers involuntarily denied boarding to receive a full explanation of any restrictions on the free air travel provided as compensation, the NAAG guideline would make the policy on voluntary denied boarding more consistent with the policies on involuntarily denied boardings. We did not determine the effectiveness of this guideline.

Objectives, Scope, and Methodology

At the request of the Chairman, Subcommittee on Antitrust, Impact of Deregulation, and Privatization, House Committee on Small Business, we assessed state efforts to protect consumers from unfair and deceptive travel industry practices. As agreed with the Subcommittee office, we focused on the air travel industry. Our objectives were to (1) examine how the states are organized to address consumer protection problems, (2) identify the most serious consumer protection problems the states have encountered in the air travel area, and (3) assess how the effectiveness of state action in this area is limited by federal restrictions on the states' consumer protection role.

To address these issues, we visited the states of California, New York, Ohio, and Texas. We selected these four states because they are large and because each had enacted a travel-related consumer protection law. We also contacted consumer protection agencies in the states of Florida, Hawaii, Illinois, Rhode Island, Tennessee, and Washington because officials of state and private organizations indicated these six states were also active in the area of travel-related consumer protection. In addition to state agencies, we contacted several private organizations that are concerned with the provision of transportation services to consumers—the American Society of Travel Agents, Consumer Reports Travel Letter, the International Airline Passenger Association, and the National Association of Consumer Agency Administrators.

We reviewed federal and state laws and regulations applicable to air travel-related consumer protection as well as other laws used to protect consumers from unfair and deceptive trade practices. We also reviewed the limited amount of data state agencies had developed on their consumer protection efforts to find out where the most serious problems were. Finally, we conducted a literature search to identify potential travel issues and to identify which states were active in protecting consumers from travel-related problems.

Our audit work was carried out between February and November 1989 in accordance with generally accepted government auditing standards.

State Travel Laws for Tour Operators

State	Requirements to License	Requirements to Register	Payment protection for consumers: Trust account[a] (percent)		Bond		Other
California	-	X	90	OR	Equal to amount of contract with carrier		-
Florida	X	-	-		$10,000-$25,000		-
Hawaii	X	-	-		-		Travel Agency Recovery Fund: funding from travel agency/license fees; $8,000 per consumer
Illinois	-	-	90		-		-
New York	-	-	-		-		-
Ohio	-	X	-		$20,000 intrastate; $50,000 interstate & international	OR	Statement from licensed financial institution guaranteeing performance ($50,000 +)
Rhode Island	X	-	-		$10,000		-
Washington	-	-	90	OR	$50,000 + or 10 percent of 2 months revenue	OR	Maintain written agreement with carriers

Note: Although each law uses a different term to describe to whom it applies, the definitions of travel promoter, tour operator, and travel consultant are synonymous. All refer to an individual who sells or arranges for the sale of air, sea, or land transportation separately or in conjunction with other travel services. Although the Hawaii and Rhode Island laws specify travel agents, state officials told us these laws could also be applied to tour operators.

[a]A trust account is an account in which a percentage of the consumer's payment for travel services is deposited to ensure that, in the event of cancellation of the tour for any reason, the consumer is repaid the amount deposited. The percentage shown represents the percent of the consumer's payment for travel services that tour operators must deposit.

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