

## READING AND RESPONSE

### FEBRUARY 2006

#### Dealers Face Compliance, Privacy Questions in 2006

Top attorneys in the used-car industry said compliance, Internet sales, privacy and negative equity will be some of the big legal issues in 2006.

The biggest issue will be compliance, said Keith Whann, general counsel for the National Independent Automobile Dealers Association.

Compliance keeps coming up because it's important on so many fronts, he said. Although regulations have always been a big issue, compliance and proper paperwork continue to add another dimension because of their relation to finance and insurance.

"If compliance becomes an issue in F&I," he said, "then the lenders begin to back off. They begin to look at this and decide it's just not worth the risk." Privacy requirements are also a continuing issue, but dealers are taking it more seriously and handling it better.

Many states are beginning to create their own versions of the privacy laws required at the federal level, said Tom Hudson, an attorney who specializes in automotive finance.

"We're going to end up with a somewhat crazy quilt of requirements," he said. "That's going to be a problem for people who operate in more than one state." Hudson said 'data breach' laws are another concern for dealers.

There are going to be state laws requiring companies that have a break-in or lose paper or electronic data that contains sensitive customer information to notify the customers the data has been lost.

"Those are pretty onerous laws," Hudson said.

It also means that if a dealer has a national portfolio, with hundreds or thousands of customers, there could be 50 different state requirements (plus Washington D.C.) to follow in notifying those customers.

But, protecting consumers' privacy involves another step besides just keeping their files safe, Whann said.

"Now it's not just protecting the information, or providing the privacy notice," he said, "but there's also the concern about how you dispose of the information." Dealers need to make sure they allow consumers to have the chance to opt out of certain mailings and other means of contact.

"You're also going to see in the next couple of years," Whann said, "greater enforcement activity in the privacy area."

"A lot of this is going to be spurred because there are several credit card companies which have had (hackers) break into their computer systems. Car dealerships can end up being a prime target for criminals looking to steal identities, Whann said."

"The new big issue this year is going to be the Internet," he said.

The questions include: how to sell a car away from a brick-and-mortar lot; where the paperwork is signed; and how the car is delivered, will continue to raise legal questions.

State-to-state sales bring up the issue of which state's laws have jurisdiction. Even an offer or deposit made over the Internet within the same state raises issues of deposit rules and other laws, Whann said.

Selling a vehicle via an online auction is also an issue since auctions are licensed, he said.

Hudson said dealers need to anticipate where the challenges will come from and prepare an Internet program that anticipates those challenges.

Whann said he has not seen a dealer who is able to do this.

"I'm now seeing hundreds of thousands of transactions occurring in cyberspace," Whann said, "and I don't see any one of them that is correct."

"If you look at this thing, it's a disaster. It's a house of cards." On another front, Hudson - who has encouraged dealers to have arbitration agreements in their sales contracts - said some legislators are trying to hide anti-arbitration measures in other laws.

The goal is to ban or limit the ability of dealers to use arbitration agreements.

For example, arbitration opponents have lobbied for laws to make it illegal for consumers to waive a jury trial in a consumer contract.

"That's a disguised way of getting at arbitration agreements," Hudson said, "without expressly mentioning arbitration agreements." It may not hold up in court, but it would have to be challenged first, he said.

Hudson also warned that the issue of negative equity, which came up in a California lawsuit last June, looms as a potential issue in 2006.

Negative equity is when a customer owes more on a trade-in than it's worth.

The California case came up because a dealer rolled a customer's negative equity into the cash price of a new vehicle, without telling the customer.

The court ruled the dealer also inflated the price of the trade-in in order to get the deal financed, since many lenders will not finance negative equity.

"There are several states," Hudson said, "where there is a real issue about whether or not you can finance negative equity." The problem is that a state's retail installment sales law doesn't address the issue clearly, he said.

Hudson has heard that lenders in some states will not finance negative equity because of concerns about lack of clarity in state law.

He said state attorneys general are also targeting dealer advertising, with dozens of actions across the country. Dealers need to make sure their advertising follows the required laws.

Another issue is the shadow of the California Car Buyer's Bill of Rights.

That law originally started out as legislation requiring all used-car transactions to come with a free three-day warranty.

Eventually, the legislation - before it became law - was changed to make the three-day return an option that buyers can purchase for \$250 when they buy a vehicle, and requires a re-stocking fee paid by the consumer.

Whann said this is not a bad bill for dealers, since many dealers already would take back cars and do make-right work for them anyway.

However, dealers and their trade associations in other states will have to be on the lookout for similar bills which may not be as friendly to dealers as California's.

"We'll see similar forms of this adopted in other states," he said.

Hudson, however, said other states have stronger lobbies, and are not as strongly pro-consumer as California. He expects similar bills to be "dead on arrival." States are also looking at enacting their own versions of the federal relief laws that force creditors to reduce interest rates of military personnel who are called to active duty.

However, some of these newer laws would force creditors to lower rates for service members who incur the debt after they are called to active duty, unlike the federal law which only applies to service members called to active duty after they incur the debt.

Hudson said dealers in these states will have a hard time getting someone to buy their retail installment contracts.

By Jeffrey Bellant  
Used Car News Staff Writer

By: Whann & Associates, LLC

. Federal Legislative Developments

Fate of Patriot Act Provisions Remain Uncertain

The fate of a Measure that would reauthorize 16 expiring provisions of the 2001 Patriot Act remains uncertain. Republican Leaders will have to vote on whether to reauthorize the expiring provisions of the Patriot Act, despite efforts to move the Legislation before the Thanksgiving Break. House Leaders hoped to vote on H.R. 3199 on November 17th, but six Senators (three from each party) opposed to the Bill released a statement that threatened to stop the Legislation in its tracks if their concerns were not addressed, including: The legal standards for seizing business records in terrorist investigations; the standard for judicial review for national security letters; the duration of the expirations for the business records and roving wiretap provisions; and the duration of the notification period for searching a home. The current Agreement would make 14 provisions permanent, while extending until 2012 the other two governing the FBI's ability to seize business records and to use roving wiretaps to monitor more than one device. After the Senators released their statement, the Administration took a more public role in the negotiations. President Bush wants all 16 expiring provisions to be made permanent and opposes efforts to put more restrictions on law enforcement's ability to monitor the actions of suspected terrorists. Further changes in the direction of the Senate Bill would make it even less acceptable to the White House. Lawmakers will have little less than a month to settle their differences before the provisions expire on December 31, 2005.

Identity Theft Bills Remain a Priority for Congress

Committees in both Chambers have continued to advance Legislation aimed at strengthening data security. First, the Senate Commerce, Science and Transportation Committee approved a Data Security Measure in July (S. 1408). Then, on November 3rd, the House Energy and Commerce Subcommittee on Commerce, Trade and Consumer Protection approved H.R. 4127. The second Senate Bill (S. 1789) was approved by the Senate Judiciary Committee on November 17th. It would increase federal penalties for identity theft and require that consumers be notified any time the security of their personal information has been compromised. The Bill would also require any company that maintains more than 10,000 individuals' personal data, including names, Social Security Numbers, and driver's license and passport data, to develop a comprehensive data privacy program. In addition to setting notification requirements and requiring privacy programs, the Bill also would make it a crime to deliberately conceal a security breach that causes economic harm.

. Federal Regulatory Activities

NIADA Submits Comments to NHTSA Regarding Tire Safety Information Regulations

On November 18, 2002 the National Highway Traffic Safety Administration (NHTSA) issued a final Rule requiring that tire placards or labels which contain a vehicle's tire size, cold inflation pressure and cargo carrying

capacity be placed on all new vehicles with a gross vehicle weight of 10,000 pounds or less. The Rule, Federal Motor Vehicle Safety Standard No. 110, became effective on September 1, 2005. Since its implementation, there have been numerous questions raised regarding the applicability of the Rule after a vehicle's first retail sale. If the placard/labeling requirement were to apply after the first retail sale, then anyone modifying the vehicle after this point in time, including remanufacturers, distributors, dealers, and repair shops, would be required to update the placard or label. In early December, NIADA, together with other Trade Associations submitted comments and a request to NHTSA for clarification regarding that the labeling requirements under the Rule only apply prior to their first retail sale of a vehicle, thus relieving those who later modify the vehicle from the costly burden of replacarding the vehicles.

#### The IRS Clarifies New Rules for Vehicle Donations

Beginning this year, provisions in the American Jobs Creation Act of 2004 established a whole new set of Rules for determining the amount of the deduction available for charitable contributions of used vehicles. The Act added two new sections to the Internal Revenue Code. One limits the deduction to the gross proceeds realized upon the sale of a vehicle by the charity, unless the charity uses the vehicle for its exempt purposes or makes substantial improvements to it. The other creates an affirmative duty on the part of the charity to provide appropriate acknowledgment to the donor of the sales proceeds or the retention of the vehicle by the charity for a qualified use. Recently, the IRS issued Notice 2005-44 to provide further guidance on the new Rules. The Notice explains the requirements that must be met if a donor wishes to take a deduction in excess of \$500 and the contents of the acknowledgement that must be provided to the donor by the charity. Charities that issue false or fraudulent acknowledgements or knowingly fail to furnish acknowledgments can face penalties.

#### FTC Shuts Down Company's Downloading of Spyware

An organization operating a website that infected consumers' computers with spyware has been ordered to stop by a U. S. District Court. The company lured consumers to download spyware with free lyric files, browser upgrades, ring tones, and security patches. Consumers who downloaded any of the items were infected with spyware and never received any of the free offers. The FTC alleged that the spyware could then be used to track consumer's Internet surfing and home pages, to change home page settings and toolbars, and to cause pop ups and advertising on their computer screens, even when consumers' Internet browsers were not activated. The Court froze the company's assets pending a further hearing. Consumers and businesses can reduce their risk of spyware infection by updating operating system and web browser software, setting browser security high enough to detect unauthorized downloads, using anti-virus software and a firewall, downloading free software only from trusted sites and using anti-spyware software. According to a new study released by the FTC on November 28th, Internet Service Providers' anti-spam technologies can block as much as 95% of spam sent to e-mail addresses.

#### . Activities of Interest

Massachusetts Legislature Considers a Car Buyer's Bill of Rights

As we anticipated, a number of States are already working on drafting Legislation similar to the Car Buyer's Bill of Rights passed in California. Both the House and Senate in the State of Massachusetts are considering versions of a Car Buyer's Bill of Rights. The Massachusetts Independent Automobile Dealer's Association (MIADA) had an opportunity to meet with and express their concerns to Members of the House Committee in early November. The primary areas of concern included restrictions placed on independent dealers with respect to the sale of "certified" used vehicles; a proposed cap on the finance markup charge at the greater of .5 percent of the loan or \$150; the disclosures that would be required in advance of the execution of any retail installment sale, which would include the credit rating used to evaluate the buyer's credit history, the name of the company that calculated the credit rating, the lowest annual percentage rate at which a lender would accept the contract or otherwise extend credit to the buyer, the annual percentage interest rate charged to the buyer, and the total cost of arranging financing; and language that would allow purchasers of used motor vehicles to return a vehicle within three days of the date of purchase for a full refund, less a reasonable offset for mileage.

#### New Law in Louisiana Requires Destruction of Certain Flood Damaged Vehicles

On December 9th, the Governor of Louisiana signed into Law a Bill that is geared toward calming both industry and consumer fears about the sale of flood damaged vehicles following the hurricanes in the Gulf Coast. The new Law mandates that any vehicles with power trains, computers or electrical systems damaged by flooding and declared a total loss as a result of a president or governor-declared disaster be either dismantled, crushed or sold for usable parts. The only exceptions are for antique vehicles and those units weighing in excess of 20,000 pounds. Violators may be imprisoned for up to six months and/or fined up to \$5,000, in addition to performing at least 80 hours of community service. The Property Casualty Insurers Association of America opposed the Bill asserting that it is overly burdensome in that it is not limited to vehicles that are dangerous to the public and would require the destruction of thousands of vehicles that could be salvaged. Others pointed out that it will not cover uninsured vehicles, so neither consumers nor dealers will be completely protected from coming into possession of flood damaged vehicles. Lawmakers in Louisiana, maintain that it is a step in the right direction.

#### Consumer Lawyers Suggest Dealers Justify Their Financing Profits

Plaintiffs have made a unique request to settle a lawsuit brought against Primus Financial Services, Inc. A U.S. District Judge in Tennessee ruled earlier this year that dealership markups of the finance rates charged by Primus discriminated against minority customers and ordered lawyers for the Finance Company and the Plaintiffs to propose settlement terms. Under the Plaintiffs' plan, motor vehicle dealers would have to justify any finance profit of more than \$500 on a retail sale. Similar lawsuits brought against other lenders have been settled by capping the percentage points on dealer markups of lender buy rates. The Finance Company already imposes such a limit on markups, but the Plaintiffs' Lawyer said that is not enough. Primus maintains that the proposal would add more paperwork for dealers and would adversely affect its business. Final oral arguments are scheduled for January 12, 2006.

. Case of the Month

## Circuit Courts Split on Scope of Claims Covered Under the Federal Odometer Act

Back in September, we reported on the case of *Loffe v. Skokie Motor Sales, Inc.* which was decided by the Seventh Circuit Court of Appeals. The issue in that case was whether the Federal Odometer Act creates a private right of action for a purchaser where the transferor's fraudulent intent is unrelated to a vehicle's odometer or mileage. The Court found in that case that a private right of action may only be brought under the Act where the transferor of a vehicle intended to defraud a transferee about the vehicle's mileage and its accuracy. The Eleventh Circuit Court of Appeals disagrees. In the case of *Owens v. Samkle Automotive Inc.*, the Purchaser of the vehicle did not claim that the Dealership intended to defraud her with respect to the vehicle's mileage, but rather that the Dealership failed to show her the original title to the vehicle when she purchased it in order to hide the fact that the vehicle had previously been used as a rental vehicle. The Eleventh Circuit Court overruled the lower Court's decision and found that consumers do not have to allege mileage related fraud to state a claim under the Federal Odometer Act. The Court explained that the Federal Odometer Act is meant to prevent dealers from misrepresenting not only the actual number of miles on a vehicle, but "where those miles were driven and by whom." Given the split between these Courts and the potential impact that the Eleventh Circuit Court of Appeals' decision could have on the motor vehicle industry, this issue is likely to receive more attention in the Courts. Many State Laws permit dealers to sell vehicles prior to having physical possession of a Certificate of Title. Moreover, most State UDAP Statutes provide remedies for consumers when a dealer fails to properly make disclosures unrelated to the vehicle's mileage.

## 10 Tips On Identifying Flood-Damaged Units

- 1 Check for a moldy smell inside the car.
- 2 Check for rust under the brake or gas pedals
- 3 Look for dirt or rust under the dashboard and floor mats.
- 4 Look for corrosion, water marks or a thin brown line on the exterior of a vehicle.
- 5 Ask questions about an older car with brand new interior or carpeting.
- 6 Check to see if the electrical system works.
- 7 Feel the carpet for dampness
- 8 Inspect the bolts and screws under the seats for evidence of rust.
- 9 Check the undercarriage for excessive rust.
- 10 Check the VIN with AutoCheck or Carfax to see whether a flood claim has been filed or a salvage title has been issued.

## **Safeguard your mail from con artists**

***Published: December 27, 2005***

The theft of mail from residential mailboxes is an increasing problem. Con artists use this as a means to obtain your identity information and to steal checks and other items of value.

This problem can be reduced or minimized by following these tips:

- Do not leave outgoing mail in your unlocked mailbox.
- Deposit mail in a blue collection box or inside your local post office. Don't leave mail in a collection box that is full.
- Make sure your home mailbox is in good condition. Mail that is exposed can be damaged by bad weather and is visible to thieves.
- Promptly pick up your incoming mail after it is delivered.
- Get together with neighbors and the Postal Service and arrange for the installation of locked group mailboxes for neighborhood delivery. These are known as Neighborhood Delivery & Collection Box Units (NDCBU). Each address has an individual locked unit for delivery and collection. A minimum of seven neighbors' signatures are needed on a petition requesting an NDCBU.
- Purchase a locked mailbox or convert your unlocked box to the lockable type. Make sure the mail slot is large enough for the letter carrier to insert your mail. The letter carrier cannot pick up mail from this type of box.
- Arrange for your mail to be delivered to a Post Office box for a small fee.
- Have regular income checks deposited electronically into your bank account via direct deposit.
- Promptly contact the senders if you do not receive credit cards, checks, or other valuable mail.
- Notify the post office and mailers if you change your address. When going on vacation, have the post office hold your mail or have a trusted friend or neighbor pick up your mail after delivery.
- Be observant of activities on your street, including those near your letter carrier, the postal vehicle, residential mailboxes, and collection boxes.
- If you see suspicious people or activity, call 9-1-1 while the suspects are still present.

By following these tips and using common sense, you can lessen your chances of being a victim of mail theft and possible identity theft.

If you have questions about postal regulations, contact your local postmaster.

By Lincoln County Sheriff

Dennis Dotson

Auto Remarketing

July 15 issue

OFAC compliance

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# No Murky Waters: Dealers Must Comply with OFAC

By Richard Greene

Editor

CHICAGO – Though separated by hundreds of miles and in different professions, Elena Lovoy and Patrick Brown are on a common educational mission. They're trying to clear the air, clarify the confusion and help more dealers comply with regulations stipulated by the Office of Foreign Assets Control.

To ensure that no business is being done with potential terrorists and to keep terrorists from purchasing motor vehicles, dealers are required by law to regularly check OFAC's "blocked persons" list. This action on the part of dealers should help guarantee that their customers do not appear on OFAC's list.

Meanwhile, on a related note, still in the pipeline are antimoney laundering rules and regulations coming from the U.S. Treasury with which dealers will also need to comply. As a part of the USA Patriot Act passed in 2001, these were due out two Septembers ago but have yet to be put in place. Lovoy still believes they are on the way, but does not know the Treasury's implementation final timetable.

However, those Patriot Act provisions are separate from the OFAC compliance regulations, and both Lovoy and Brown want to make sure that dealers grasp that differentiation and are doing everything possible to comply with OFAC.

An attorney, Lovoy is a partner in the Chicago office of Maryland-based Hudson Cook, LLP. She's a recognized speaker on auto finance legal issues. Brown is senior vice president and chief operating officer of First National Bank and Trust in Louisville, Ga. He's also president of Integra Systems Queensborough, which provides financial software and consulting services.

Both spend quite a bit of time on the road, working with dealers to help them understand their legal responsibility to comply with OFAC regulations.

## **OFAC Pre-Dates 9/11**

OFAC comes under the U.S. Department of the Treasury and “administers and enforces economic and trade sanctions based on U.S. foreign policy and national security goals against targeted foreign countries, terrorists, international narcotics traffickers, and those engaged in activities related to the proliferation of weapons of mass destruction.” According to the OFAC Web site, “OFAC itself was formally created in December 1950, following the entry of China into the Korean War, when President Truman declared a national emergency under the Trading With the Enemy Acts of 1917 and blocked all Chinese and North Korean assets subject to U.S. jurisdiction.” Over the years, the list has broadened as new categories of names have been added. This was especially true during the Cold War and the fight against Communism. Following 9/11, President Bush executed Executive Order 13224, which requires OFAC to make available to all industries a list of “blocked persons” known as “Specially Designated Nationals.” Under the order, U.S. citizens and businesses are barred from entering into “any transaction or dealing” with individuals or entities who have been linked to terrorism. With each customer, dealers must check to see if his or her name appears on OFAC’s list of “bad guys,” as it’s also been called. Penalties for non-compliance are severe. Those found guilty can be fined from \$50,000 to \$10 million, and can be imprisoned up to 30 years.

## **Clearing Up the Fog**

Confusion has arisen, say Lovoy and Brown, because some dealers have tied OFAC compliance with the ongoing tussle between President Bush and Congress to make permanent the provisions of the USA Patriot Act that are set to expire on Dec. 31.

The Patriot Act was passed after 9/11 to give law enforcement more power to pursue terrorists. Today’s national debate focuses on whether to extend and expand the law. Some of those provisions are viewed as controversial, one in particular that “allows federal agents to examine people’s book-reading habits at public libraries and bookstores as part of terrorism investigations.” On June 15, by a margin of 238-186, the House of Representatives voted to remove that specific provision.

As a result, several dealers have the misconception that if some of these Patriot Act provisions are not included, then they no longer need to comply with the OFAC regulations. That’s what a growing number have been telling Lovoy and Brown as they’ve attended various training and educational sessions, including functions sponsored by the state associations affiliated with the National Independent Automobile Dealers Association.

“That’s a common misconception, but nothing could be further

from the truth,” Lovoy stated emphatically. “These are mutually exclusive. OFAC predates the Patriot Act, and was on the books and in place long before even the terrorists dreamed up the concept of Sept. 11. Dealers have an absolute compliance obligation under OFAC.”

Brown agrees. “As I’ve spoken to state conventions of the NIADA, and even recently at its national convention, I point out that dealers have to comply with the law,” he noted. “Unfortunately, I’ve met some independent dealers who are not yet complying. And I’ve spoken at a convention of rental agencies, and some rental companies have also not been complying with the OFAC regulations. This is serious. It’s the law, and the penalties of not doing so are designed to put you out of business.” Lovoy and Brown strongly urge dealers to invest time in studying OFAC’s Web site – [www.treas.gov/offices/enforcement/ofac/](http://www.treas.gov/offices/enforcement/ofac/).

### **Making Compliance Easier**

At the same time, Brown says that his firm can consult directly with dealers to make sure they’re up to speed. Integra Systems Queensborough was formed in 1994 by banking and IT professionals and is one of several companies that provide Internet-based product solutions to enable various individuals and companies, including the auto industry, to comply with the OFAC requirements.

Integra’s particular product is called OFAC IQ. It’s updated frequently, sometimes twice a day, to guarantee accuracy and to ensure immediacy.

“Our original software was written for banks, but about two years ago, an automobile company from Wisconsin approached us to help them with OFAC,” Brown explained. “As a result, they ended up helping us redesign our package for the auto industry.”

OFAC IQ has five unique search features allowing dealers to identify individuals, companies and countries with which they are not to do business. Dealers can print out their search results so they can document their compliance efforts.

Lovoy also made it clear that once a relationship is established with a customer, it’s incumbent upon the dealer to continue checking the OFAC list to discover whether that person is added to the list at a later date.

“This is not just a one point-in-time responsibility,” she said.

“It’s a real-time compliance issue. You have an on-going responsibility to make sure you know whether that person’s name has been added to the list, especially if they come back to have their car serviced. Once they drive that car off your lot, their name could be added to the OFAC list next week or at a later date. You’re supposed to know that.”

## **Anti-Money Laundering Around the Corner?**

As for the anti-money laundering rules, Lovoy said she believes they are still coming and dealers will need to adhere to them.

“I don’t have any reason to believe that the U.S. Treasury does not intend to implement the statutory requirements by regulations,” Lovoy said. “But as of today, although the statute says that all financial institutions will have to have a formal anti-money laundering program in place, we don’t have any regulations on the books yet that tell dealers what they need to do.”

So far, Lovoy said, under the Patriot Act, dealers already are required to fill out the currency transaction reporting form. She said its name has been changed but dealers still need to complete and submit it. “Though only the form’s name has changed, this form now has law enforcement value and not just IRS value,” Lovoy explained.

According to Lovoy, a regulation was published three years ago that would have required all financial institutions – and that term was broadly defined – to put into place an anti-money laundering compliance program. Banks already did, she said, but now dealers would now be included. Dealers were given a reprieve, though, in October 2002, when the regulations were to have kicked in.

Included in this program would be the need for formal written procedures and policies, training, an anti-money laundering compliance officer, and audits.

At the same time, Lovoy said, a third provision of the Patriot Act would require an exchange of information between dealers and federal law enforcement.

“Except for the currency transaction reporting requirement, these other Patriot Act provisions that apply to dealers have not been implemented by regulations yet,” she stated.

Lovoy urges dealers to be on the lookout and once these regulations come down the pike, they will need to be just as diligent to comply with these as they are with the OFAC rules.

**READING & RESPONSE FORM**  
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**February 2006**

<b>ARTICLE:</b>	<b>QUESTION</b>
Used Car News	One of the biggest legal issues surrounding the auto industry this year will be the internet. <p style="text-align: right;">True _____ False _____</p>
Legal & Legislative	One new rule for vehicle donations creates an affirmative duty on the part of the charity to provide appropriate acknowledgement to the donor of the sales proceeds or the retention of the vehicle by the charity for a qualified use. <p style="text-align: right;">True _____ False _____</p>
OFAC	Dealers have an absolute compliance obligation under OFAC. <p style="text-align: right;">True _____ False _____</p>
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Safeguard Your Mail	Identity theft is commonly obtained through checks and other items stolen from your mail box. <p style="text-align: right;">True _____ False _____</p>
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