

Moving the Metal: The Auto Finance Podcast — Driving New Standards With California's CARS Rule

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Brooke Conkle:

Welcome to *Moving the Metal*, the premier legally focused podcast for the auto finance industry. I'm Brooke Conkle, a partner in Troutman Pepper Locke's Consumer Financial Services Practice Group.

Chris Capurso:

And I'm Chris Capurso, an associate in Troutman Pepper Locke's Consumer Financial Services Practice Group.

Brooke Conkle:

Today, we'll be talking about California SB 766, or as we're calling it, the California CARS Rule. Before we jump in, let me remind you to please visit and subscribe to our blogs. We have two great ones that may be of interest to you. [TroutmanFinancialServices.com](https://www.troutmanfinancialservices.com) and [ConsumerFinancialServicesLawMonitor.com](https://www.consumerfinancialserviceslawmonitor.com). Also, we have a bevy of other podcasts that you might find interesting; [The Consumer Finance Podcast](#), which, as you might guess, is all things consumer finance related. [The Crypto Exchange](#), devoted to trends, challenges, and legal issues in Bitcoin, blockchain, fintech, and regtech. [FCRA Focus](#), a podcast dedicated to all things credit reporting. Finally, [Payments Pros](#), a great podcast focused exclusively on the payments industry. All of these insightful shows are available on your favorite podcast platform, so please check them out.

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For today, as I mentioned, we're discussing pending legislation in California that incorporates some, but not all, of the FTC's requirements in the CARS Rule. Chris, I thought we'd start off today by taking a step back and looking at where we have been with the CARS Rule. It has been quite a journey. Starting in about mid-2022, the FTC submitted a notice of proposed rulemaking. Chris, as we're going to talk about later, it was not an advanced notice of proposed rulemaking, a misstep that could have some ramifications for the FTC.

Chris Capurso:

Stay tuned.

Brooke Conkle:

That's right. Coming soon. The rule was to be cross-enforced with the FTC and the CFPB. A lot of us who were watching the CARS Rule really found it to be, essentially, another step in the war on fees. There were some major requirements of the CARS Rule that would have been, the key phrase 'would have been' required an offering price rules about how the price of vehicles would be disclosed, how they would be advertised, disclosures related to add-on products, monthly payment disclosures, and record retention requirements. Along with those requirements, there were major prohibitions that were also part of the CARS Rule, including prohibited advertising practices and prohibiting the sale of valueless add-ons. What means valueless? Who are we to say? That's right. Chris, tell us a little bit about what happened, really, with the CARS Rule.

Chris Capurso:

Yeah. I mean, you spoiled it for everybody. Over the last couple of years, there has been litigation in the Fifth Circuit over this rule. The National Automobile Dealers Association, or NADA, and the Texas Automobile Dealers Association, or TADA, challenged this rule in the Fifth Circuit and obviously, went through the procedural items that a lot of this types of litigation goes through. Then in January, we finally got our answer from the Fifth Circuit.

As Brooke spoiled, the rule was vacated by the Fifth Circuit and specifically, the thing that the Fifth Circuit really highlighted and grabbed on to was this idea of the advanced notice of proposed rulemaking. As Brooke said, there was a notice of proposed rulemaking, but there was not an advanced one. Because the FTC thought that its authority for this derived under the Dodd-Frank Act, which did not require an advanced notice of proposed rulemaking in this specific instance. The court found that authority to promulgate this rule came from the FTC Act, which did require an advanced notice of proposed rulemaking. If you're wondering why I'm saying advanced notice of proposed rulemaking, I don't think I can say NPRM consistently without stuttering over it. We're just going to use the full term.

The court essentially found that the FTC violated its own regulations by not issuing the advanced notice of proposed rulemaking and vacated the rule. We went past the period for which the FTC could file for cert with the US Supreme Court. Notably, I mean, this decision came down late January. Obviously, another thing happened in late January with the new administration coming in. As was guessed, I mean, with the new administration, new leadership of the FTC, they chose not to take up this fight. The rule is currently vacated. It's technically with the FTC for reconsideration. But we have a guess that if it hasn't been fully killed, it is on the killing floor. I mean, we talked about this in our podcast, appropriately titled Requiem for the Rules. That's where we think the federal one is. Now, we've got California coming out with their own version.

Brooke Conkle:

That's right, Chris. If there's anything we've talked about on this podcast in the past eight and a half months, it's as we watch the federal regulators take a big step back, we've seen state regulators really move to close that gap. Moving to the forefront, California is just one example of that, with what we're calling the California CARS Rule. There's a lot in this rule that is a significant carryover from the FTC's version. Particularly, a lot of the main hits from the CARS Rule, they're still in this California bill, including the idea of prohibitions on valueless add-ons. Again, we're still all wondering what is a valueless add-on. Value is in the eye of the beholder. But that's going to be prohibited under this version of the bill.

Additionally, the first contact price disclosures related to the offering price of a vehicle when consumers make inquiries about specific vehicles, there are requirements that the offering price be disclosed in those first contacts with consumers. Disclosures that add-ons are not required, they're entirely voluntary, the total cash price disclosure. Then finally, that two-year record retention requirement, which, Chris, is we're going to talk about, is actually a significant drop initially in the bill, the requirement for record retention with seven years. That's a really long time.

In a lot of the retail installment sales contracts, it used to be that 48 months was standard. With this record retention requirement, you could be required to hold on to any disclosures, any part of the deal jacket going back seven years. That's pretty significant. It's not to say that the California Cars Rule is really a cut and paste version of the FTC's CARS Rule, because there's new stuff in this bill, too, that's grating together initiatives from the FTC, state-level initiatives, and then also, some requirements that have been longstanding in California law.

What's new in this bill are contract cancellation options for used vehicles over \$50,000, limitations on restocking fees, prohibitions on prepayment penalties, financing requirements, and restrictions on lower dollar retail installment sales contracts, no cooling off period disclosures, disclosures for insurance charges, and then specific requirements for lease contracts. Chris, tell us a little bit about how we've gotten to where we currently are. What did we start off initially with California and how has that bill changed as time has moved on?

Chris Capurso:

Yeah. I should be clear that this is still pending as of the date of recording, which in true [*Moving the Metal*](#) fashion, it's going to be past tomorrow with flying colors. For right now, it is still pending, so there could be changes still to come. We can't see the future, unfortunately. What we can look at is the past. Since this bill was introduced in February of this year, it has been amended seven times, which is quite a bit. I've got Ferris Bueller going through my head with, he's been absent nine times, seven times this has been changed.

They're not all small changes. There are some very significant changes to the bill that have occurred. I'm going to take you on a journey. We're going to start with April. What a lovely month. April 10th, actually, my wife's birthday. We're going to talk about some of the changes that happened here. There are some big ones right off the bat. First, there was in the original bill, a requirement for express informed consent, and a definition of what express informed

consent meant, related to purchasing add-ons, things like that, that definition was removed, any references to it were removed.

Instead, it says that a dealer is not prohibited from charging for an add-on if it is “selected by” and would “benefit the purchaser,” even if they choose not to use it, which is a theme that permeates through a lot of these changes over the past couple months. Another huge one, there was a 10-day cancellation period in the original bill, that got knocked down in April to three business days. In the spirit of spoilers, that is also not to stay. We'll get to that a little bit later.

Another big one is there is a right to cancel in the original bill. This bill, or this amendment in April put a \$48,000 cap on it and made that cap adjustable annually with the consumer price index beginning in June of 2027. Another spoiler, that's not to stay. As I keep saying this, you're going to get this idea that it really looks like there was a lot of haggling when it comes to this bill, different parties getting involved, trying to get different interests in there. We understand that motor vehicle dealer groups have gotten involved in California because, I mean, another spoiler, but this looks like it's going to pass. This bill is going to be a thing. Industry wants to make sure that the things that are in there make sense and that they're not too unbelievably onerous, or maybe even don't make sense for a business trying to do business things.

As far as April 10th, the other big one is that it lowered the record retention period that Brooke mentioned, from seven years to two years, which seems much more reasonable and much easier to keep track of. Finally, and I will note here that this is not a complete list of every change. We're just trying to hit the highlights. Another one is that it alters the cooling off disclosure that's required on dealership signs to say different things about what the right to cancel actually says, in mind with this law.

We move to what? Three weeks later, May 1st, we've got removing the definition of offering price and replacing it with a total price and replacing it throughout the law, but also in definition. We've also got some new examples for what a valueless add-on might be. I mean, to Brooke's point earlier, what is it? Well, California provides some examples, including if the service contract does not cover reasonable costs of repair, oil changes for electric vehicles. Makes sense. Duplicative service contracts, where the different service contracts will cover the exact same thing and yet, the customer is being charged twice. Catalytic converter markings for vehicles that don't have a catalytic converter. Also makes sense. And a surface protection product that would void the manufacturer's warranty if it were used. That was a little different. I would have called that valueless. Definitely not a great benefit, but there's value if you're fixing the car, but if you're voiding the warranty, unintended consequences, I guess, I'll say.

Finally, with this record retention requirement we've been talking about the amount of years, but there's also specifics about what goes into that record retention requirement. What needs to be retained. The May 1st amendment altered that record retention requirement to specifically not include sales scripts and training materials. Those were in the original bill. Those got struck on May 1st.

Next, we go to May 23rd. This is a smaller one. It removed the provision that said a failure to comply with this was an unfair method of competition and subject to California's unfair competition law, which anybody who has dealt with litigation, California knows all too well. It qualified nitrogen-filled tires. Of course, there's an example in there about nitrogen filled tires as

a valueless add-on, but they do put a qualification on it that says, it's valueless if it contains less than 95% nitrogen purity. We've got a nice qualification there.

June 13th, we've got another edit. This is just to change the definition of the total price. It's to align it a little bit more with what the vehicle code says, as far as taxes, fees and charges, so we've got a nice cross reference, which is something you always want. If you change one law, we don't have these inconsistencies and California laws going on. Nice, substantive, but also clerical change, that's very helpful.

Then we go to June 26th. We've got some more big changes here. We've removed the definition of clear and conspicuous as it relates to disclosures. But it should be mentioned, the definition is gone. The reference to the term is not. There's still requirements for clearing conspicuous disclosures, but now this law does not define what clear and conspicuous means. We also got a limit on the requirement to disclose the total sale price in connection with the first communication with the consumer. That's requirement to disclose the total sale price in the first communication with the consumer. Now, as of June 26, it is the first written communication with the consumer.

Just to clarify that, it requires that certain representations about vehicles for sale or lease be given in the language primarily negotiated in. For anybody who deals in California, you know that there is a very specific law, California civil code 1632, that discusses use of different languages. There are specific disclosures. It's not just Spanish. I remember Korean is in there. It's a very broad law for contracts negotiated in other languages. Now there is an express requirement in the CARS Rule to provide certain representations about the vehicles in that language if that's the primarily negotiated language.

A big one is the CARS Rule in California would exempt auction sales. Before, it did not expressly do that. Now, we've got a definition of auction and a specific exemption for auction sales. There was a requirement that the dealer must pay the provider of an add-on within 10 days of sale. Now, it's been relaxed a little bit that it can be a little bit later. If there is an agreement in place for payment at a later date and the consumer's coverage would not be affected by that delay. That's something that dealers most certainly wanted in there to have a relaxation where there was a commercial agreement, and also the consumer isn't being affected at all.

Next, we go to July 14th. The big one here, there is now an operative date, which is October 1st, 2026. We have exceptions to the term 'motor vehicle'. Now there are car routes for wholesale, fleet sales, and commercial purchasers among other things. We have some altered record retention requirements related to marketing, specifically advertisements. There is now a definition of advertisement, that includes internet-based listings that display the vehicle's total price, and there are some other items in there related to financing advertising.

Finally, we get to July 17th. This is the last version that we have before we recorded this. This one, a big change, and I spoiled this earlier, three business days for the cancellation now becomes three days. It is important to note that three days is actually defined in the law. It specifically says now that if the third day falls on a day when the dealership is close to the public, the three-day right to cancel period extends to the next day, the dealership is actually open to the public. If dealership is closed on Sunday and that's when the cancellation period

would end, they get till Monday. The definition of three-day specifically says, that it ends at the close of business on the last day of the period, not the end of the day, which is notable.

We also have a change in the cap on cancellation. I had mentioned earlier that that was going to be changed. It was at 48,000. Now it's at 50,000. Perhaps, more interestingly, the inflation adjustment I had mentioned is now gone. We have just \$50,000 flat. There are separate right to cancel disclosure requirements. There has to be a separate written disclosure that includes items such as the components of any restocking fee, any requirements of the buyer to cancel that could include, for example, delivering the vehicle free of liens and paying those restocking fees. Some of the stuff that needs to be in the separate disclosure was already in the law, but now it's contained in a nice separate disclosure that needs to be provided.

Cancellation and refund must be done by the dealer within 48 hours of the consumer exercising the right. That's a pretty tight turnaround. The cancellation section requirements do not apply if it's the sale of a leased vehicle to the lessee and they had possession prior to the sale. It does not apply to used vehicles sold at auction. Those are some of the big changes. Thank you for taking that journey with me. Who knows if we're going to get earlier, mid-September edit. Obviously, we'll probably be coming back to this when we have a final version. Right now, those are the big changes that we've seen over the last six months.

Brooke Conkle:

A lot of changes, Chris. I mean, a lot of moving parts in this bill. What does it all mean for litigation? California is already a, one, a significant jurisdiction for both dealers and for auto finance companies. To go back, frankly, to the FTC's version of the CARS Rule, the FTC's position was that all of these requirements and prohibitions were part of UDAP Law. frankly, were bedrock parts of UDAP Law that this was existing requirements and prohibitions that the agency was just codifying in a singular unified place.

For California, you take that logic. Chris, as you mentioned, they have struck the portion of the law that says that this is a per se violation of the UCL. Frankly, many plaintiff's lawyers would argue that that logic still extends for California law, that any violation of the California CARS Rule would be also a violation of California UDAP Law. Why is that so important for auto finance companies? As we've discussed, it's because of the Holder Rule. California has the *Pulliam* decision, which has found that plaintiffs are able to recover attorney's fees above and beyond what they have paid under the Holder Rule. The UDAP Laws provide for attorney's fees. This bill really could, one, provide a lot of new requirements and restrictions on dealers. Those requirements and restrictions can be enforced against the holder of a retail installment sales contract through a UDAP Law. Chris, what does this mean for compliance?

Chris Capurso:

Well, for dealers, it means quite a bit. I mean, there's a lot of new requirements coming in. It's nice that there's now an October 1st deadline, but even that's likely not going to be enough, because there is so much going on. I mean, I guess, we should be thankful that it's not January 1st. There's a lot going on in a lot of different ways. There's disclosures, there's operational items that need to be changed, like getting this cancellation period if you don't already have one in California, and making sure that the right caps are on and with the add-ons, reviewing your add-

on program and making sure that nothing could potentially run afoul of any of the requirements here.

Some of it's, as I mentioned, not down to the specific type of add-on, but for example, duplicative service contracts. Either service contract could technically be okay. But if they covered the same thing, would that be something that a consumer plaintiff lawyer would go after? These are all things to consider. There's obviously the base lift of just having to comply with all of the things that this is going to do.

Again, I should mention that this is still pending. So, who knows what the actual final could say? We've probably got an idea that we're whittling down to the actual meat of what this is going to say, but there could be another change to come. Who knows? There's also the operational considerations and how one change here, what's that going to mean for over here? Different areas of the operation. Then as Brooke said, for finance companies, if the claim could be made against you for a dealer's violation, then you've got to have your dealer oversight up to snuff, especially in California and make sure that dealers, I mean, if they're not representing that they're complying with this, making sure that you're working with reputable dealers who haven't been sued under this. It's just more lift for both dealers and finance companies.

The other thing, obviously, overhanging everything is, okay, this is California. This sounds eerily similar to privacy. California was the first one there. Now look at us, we've got this patchwork of state privacy laws all over the nation. Does this mean we're going to get a patchwork of FTC CARS Rule laws all over the nation? Are they going to be a little bit different? Is Colorado going to come in and say, "Hey, we should have a five-day cancellation period?" Then our beloved Commonwealth of Virginia, are they going to come in and say, "Well, actually, the cap on cancellation should be \$100,000." Then, we all of a sudden, get a patchwork of compliance efforts. Then you're, I don't want to say you're wishing for the FTC CARS Rule, but maybe you're hoping for a national solution that's at least consistent and that you can at least implement nationwide with a little fear of running afoul of an individual state requirement.

It's going to be interesting what happens here, because this is the forefront. This is the beginning. We're going to see what happens. I think, both Brooke and I agree that this is likely coming. This is going to happen. It's just what happens from here, as far as compliance California and what the other states have to say about it. With that happy note, we'll wrap it up for today's podcast.

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