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STEPS TO SUCCESS IN TOUGH TIMES

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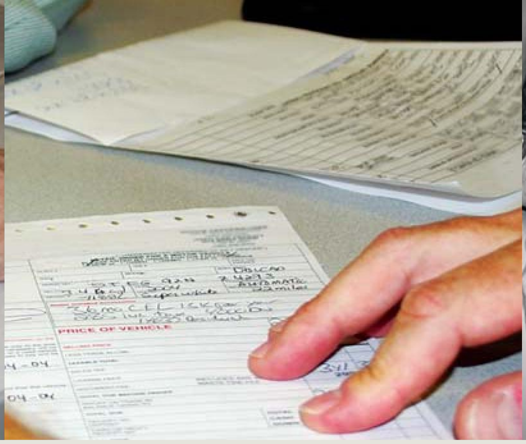

A DEALER'S ROLE IN STRUCTURED PREDATORY FINANCE

Similarities of predatory lending traits between the mortgage and auto industries were discussed in the last issue of *JM&A Today.* This article focuses on the big picture of today's complex financial markets to analyze how this system, which has been used to transfer loans, could potentially put more risk on a dealer which originates subprime retail installment sales contracts.

> Today's financial markets are no longer...simple. Complicated financial engineering often requires...intermediary entities to create a financial conduit that allows a loan to pass...

Today's financial markets are too large, complex, and opaque for legal blame of any predatory lending to be easily attributed to any one person or entity. In a predatory lending symposium held at Loyola University in fourth quarter 2008, Professor Christopher L. Peterson of the University of Utah suggested predatory lending is better defined in today's market as Predatory Structured Finance because of this market's complexity. What this could mean to an auto dealer is that it may become more scrutinized for damages in the event of a predatory lending claim.

Financial markets prior to the 1990's allowed a consumer to obtain financing from a lender which generally held the loan as an investment. This made the lender more accountable for ensuring sound lending practices. If a consumer felt victimized by predatory lending, there were only a few parties involved in the transaction that could be held accountable. Today's financial markets are no longer this simple. Complicated financial engineering often requires more than ten intermediary entities to collectively create a financial conduit that allows a loan to pass from loan originator to final-investor.

Ironically, some of these most powerful intermediary entities are often nothing more than investment trusts or corporations (known as a Special Purpose Vehicle, or SPV) which have no real assets, other than the loans, or employees. They simply hold the loans and securitize and redistribute the future profits. Over the past year, many SPVs and lenders have filed bankruptcy, leaving fewer parties which can be held legally accountable for predatory lending accusations. A dealer which originates a retail installment sales contract that becomes sold by the lender and securitized by a SPV, may find itself scrutinized for damages if the lender and SPV no longer exist.

Today's market has revealed during the lifecycle of a SPV, the loan originators (such as F&I Manager), securitizers, derivative makers, and credit raters all earned handsome commissions for their part in moving financially engineered loans, rather than for making financially sound loans. When the loans default and the profits stop, the SPV can be dissolved in a bankruptcy, eliminating any future legal responsibility.

In a retail installment sales contract, the dealer is the seller and assigns the contract to a lender. It could be possible for a dealer to be involved in a predatory lending claim if an upset consumer tries to find recourse. A dealer can try to protect itself from future claims by ensuring a Finance Manager's paperwork is complete and compliant, credit applications contain accurate information, and full consumer disclosure is documented.

Today's market includes more customers with bad credit than ever before. Auto dealers are not only feeling the effects of having fewer subprime loan options, but also trying harder than ever to make every car deal possible. It is important that a dealer maintains the highest level of legal compliance to safeguard against upset consumers who look to find fraud and sales deception to use as a loophole to rescind deals and file suits. ❖