LEGAL: INVESTIGATORY ETIQUETTE | **F&I CONFERENCE PREVIEW** | **TRENDS:** RESIDUAL VALUES PLUNGE

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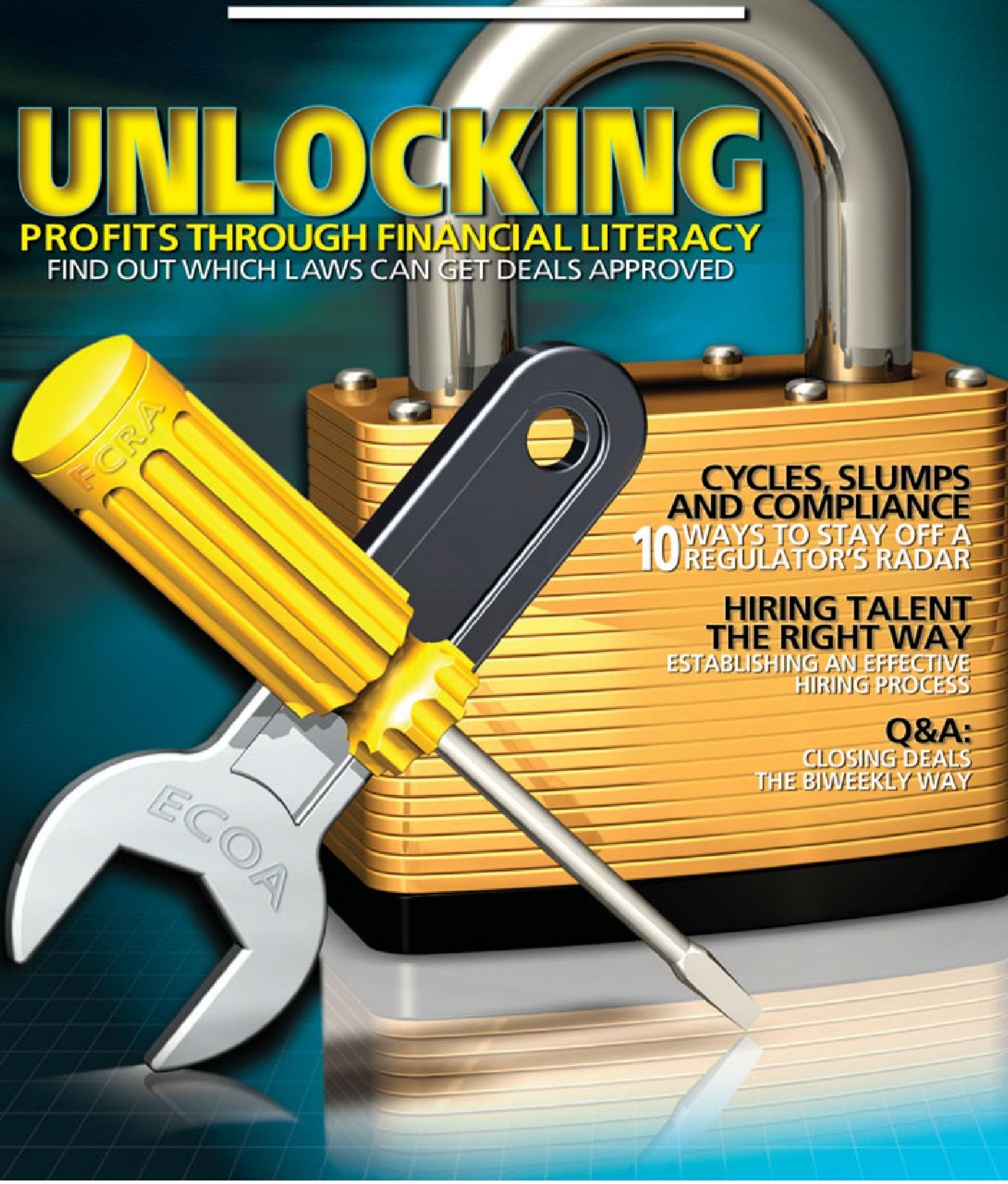
UNLOCKING
PROFITS THROUGH FINANCIAL LITERACY
FIND OUT WHICH LAWS CAN GET DEALS APPROVED



CYCLES, SLUMPS AND COMPLIANCE
10 WAYS TO STAY OFF A REGULATOR'S RADAR

HIRING TALENT THE RIGHT WAY
ESTABLISHING AN EFFECTIVE HIRING PROCESS

Q&A:
CLOSING DEALS THE BIWEEKLY WAY

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Laws and regulations have certainly created a regulatory maze inside the F&I office, but did you know some of these laws can actually help you get a deal bought. Find out what legal tools credit management companies are using to get your customers financed.

By Steven Palmieri

F&I Manager: *Boss, I just tried to rehash this deal and the lender will not buy it. They are overly cautious because of their increasing default rate. The lender is telling me the customer's credit score is too low for them to override the system decline.*

Finance Director: *Unbelievable. We sent them a million dollars in paper last month. I guess I'm going to have to tell our GM that we have to let the customer walk since the lender won't bypass its scorecard."*

The situation described above is playing out in dealerships across the country. Finance managers are spending hours each day rehashing and restructuring deals in order to move a unit while lenders are fighting tighter lending criteria and decreased access to capital. Even if a deal is made, gross profit is often sacrificed in order to make the loan-to-value (LTV) structure match the lender approval. Even more frustrating is having an F&I manager exhaust all of his or her efforts just to have the customer turned down by every lending source.

Navigating through today's credit system not only takes persistence, but also a high level of financial literacy in order to unlock profit opportunities. This starts by understanding that credit laws can be open to interpretation, whether it is the dealer, lender, consumer, credit bureau, or a company that creates the empirical mathematical scoring model (such as Fair Isaac and Company (FICO)).

Take section 602(a)(1) of the Fair Credit Reporting Act (FCRA), which states: "The banking system is dependent upon fair and accurate credit reporting. Inaccurate credit reports directly impair the efficiency of the banking system, and unfair credit reporting methods undermine the public confidence, which is essential to the continued functioning of the banking system."

Understanding what "fair and accurate" means depends on one's interpretation. Credit is too fluid of a concept for most people to fully understand. In simple terms, credit is the granting of a loan and the creation of debt. This is where the simplicity of the credit system ends, the logical understanding of credit stops, and the analytical interpretation of credit laws begins.

Looking Beyond the Credit Report

Let's consider the empirical mathematical scoring models that are designed to equate the data in a credit report into a three-digit risk score. Few people realize that the score is not part of the customer's credit profile. A scoring model may arguably be the simplest component of credit since it is simply a mathematical formula that turns the information in a credit report into a three-digit number. However, it may lockingProfitsThrough Financial Literacy

also be arguably the most complex component of credit since the formula cannot detect mitigating factors that are erroneous, misleading or inaccurate.

Assuming an average credit scoring model with a range of 300 to 850, there are only 550 empirically derived mathematical outcomes that can be matched with each customer's individual credit report. This is a disproportionately small number range to effectively predict the risk of the more than 300 million Americans.

Troy Duhon, president of The Premier Automotive Group, fights the credit score battle every day at his six stores in New Orleans. "I understand that there are mitigating factors beyond my customer's control that affect their ability to qualify for auto financing," he says. "I have always known that my customers' credit scores are often times lower than they should be due to illegal, erroneous information reporting on the credit report."

Section 202.2(p) of The Equal Credit Opportunity Act (ECOA) does allow lenders to use empirically derived credit scoring systems to determine one's creditworthiness. However, a 2004 study by the U.S. Public Interest Research Group (USPIRG) found that 25 percent of credit reports contained errors serious enough to result in the denial of credit. Problems included false delinquencies or accounts that did not belong to the customer.

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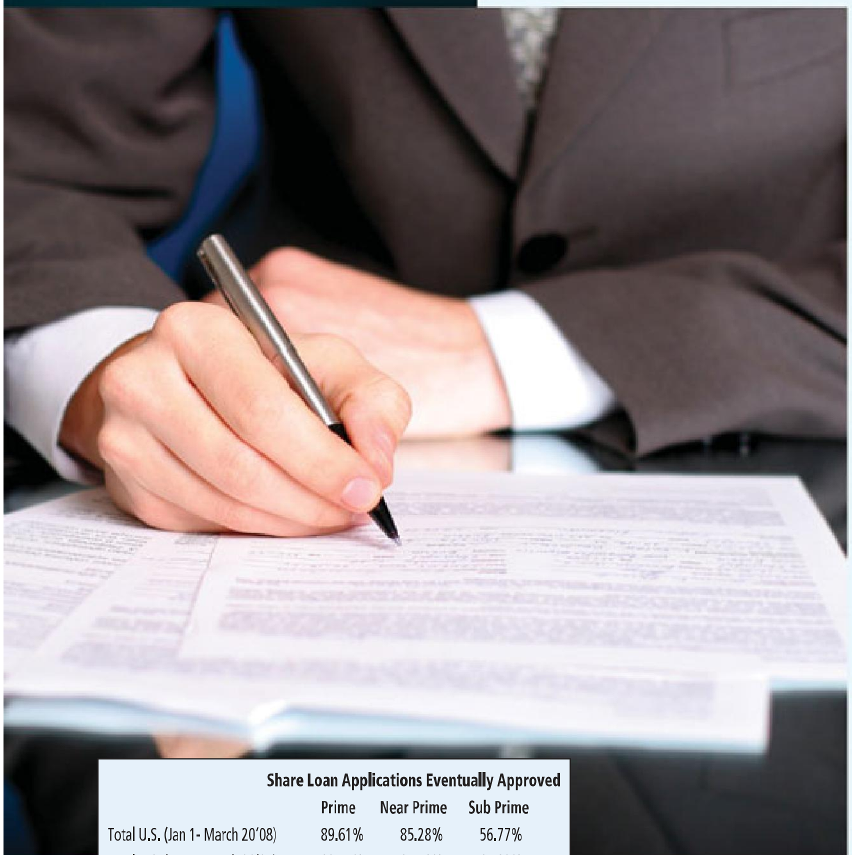
These reporting errors can be interpreted as illegal under the FCRA, which requires all information contained in a credit report to be verifiable. From a credit bureau's viewpoint, however, these errors are just that, errors. The problem is these errors lead to fewer vehicle sales at the dealership. And for those customers who are approved, those errors mean higher interest rates.

Section 202.2(p)(1)(iii) of the ECOA states that an empirical scoring system must, in part, be "developed and validated using accepted statistical principles and methodology." If the number of reporting errors is 25 percent, as the USPIRG states, then the empirical scoring system is only as good as the erroneous data it uses to calculate a score. The question is who is responsible for ensuring that a customer has a fair opportunity to acquire financing.

Section 611 of the FCRA outlines a credit bureau's responsibility to open an investigation in the event of a credit challenge by a consumer. However, the act also contains provisions that allow the credit bureau to terminate an investigation if the agency has reason to believe that a challenge is frivolous. Unfortunately, most consumer disputes end with a letter from a credit bureau stating that not enough evidence exists to open an investigation.

Using the Law to Get the Customer Financed

There are several licensed non-profit and for-profit organizations available to help consumers with their credit report disputes. Some, such as GetACar.com, also work with dealers to legally assist their customers in becoming more creditworthy. Some of the best tools employed by these companies when helping consumers with their credit are contained in the same laws governing the F&I office.



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Share Loan Applications Eventually Approved

	Prime	Near Prime	Sub Prime
Total U.S. (Jan 1- March 20'08)	89.61%	85.28%	56.77%
Total U.S. (Jan 1- March 20'07)	92.45%	87.18%	67.82%

Institutions Shopped before Accepted

	Prime	Near Prime	Sub Prime
Total U.S. (Jan 1- March 20'08)	3.1	3.8	5.6
Total U.S. (Jan 1- March 20'07)	1.8	2.4	4.2

Approvals for subprime loan applications fell to 57 percent between Jan. 1 and March 20, with only 1.36 percent of all loan approvals being subprime, according to CNW Market Research. For the same period last year, more than 12 percent of all loan approvals were subprime. Subprime applications were sent to more than five institutions before the loan was approved. Last year, subprime applications were sent to 4.2 institutions. Prime applications are being sent to more than three different financial institutions for approval. Last year, prime applications were sent to only 1.9 institutions.

One such tool is Section 202.6(b)(6)(ii) of the ECOA. It states that a creditor shall "consider on the applicant's request, any information the applicant may present that tends to indicate that the credit history being considered by the creditor does not accurately reflect the applicant's creditworthiness." So, if an F&I manager can gather evidence that the customer has erroneous information in his or her credit report, a creditor is obligated by law to consider the challenge.

The difficulty for a lender considering such data is to justify the manual underwriting of a deal that does not fall into the lender's scorecard criteria. The difficulty for a dealer is to make an effective attempt to get a manual underwriting exception. That's why dealerships should consider teaming up with a credit management company, one that can take up a credit dispute on behalf of the customer and the dealership.

A credit management company works by reviewing the credit and debt portfolio of the customer in order to identify and challenge information in a credit report. Companies like these have played a key role for the Premier Automotive Group.

"Knowing that there are companies providing viable credit solution options for my customers has helped me change the way my managers view declined prospects," Duhon says. "My corporate culture is not just about selling a car today, it's about building a pipeline of prospective clients to sell a car in the future."

> Not only are subprime customers more difficult to get approved, but prime customers are too. It is not unusual for us to rehash 'A' paper deals with our captive lender.
>
> *- Ricardo Rivas, finance director of Metroplex Toyota*

Changing the Dealership's Mindset

Changing the mindset from "today" to "tomorrow" is one way a dealership can strengthen its chances of overcoming the slow economy. It's what Metroplex Toyota in Dallas is doing.

"A strong F&I department is essential for any successful dealership," says Ricardo Rivas, the dealership's finance director. "In today's market, it is often a challenge for a dealer to just make it past today. Not only are subprime customers more difficult to get approved, but prime customers are too. This can be attributed to a sharp increase in negative equity caused by higher fuel prices. It is not unusual for us to rehash 'A' paper deals with our captive lender. Our captive is certainly helping us where they can."

The key to surviving today's tough economic times is financial literacy. That's part of what the Fair and Accurate Credit Transactions Act (FACTA) of 2003 attempted to do when it required that the government create the Financial Literacy and Education Commission. So why not do the same?


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"It's not easy to change the mindset of how we as dealers have sold cars in the past, but it is apparent that we must take a more proactive approach to actually help our customers. We must become more of a financial solution center. This is how we will succeed in this market."

- Troy Duhon, president of The Premier Automotive Group

Dealers are reading almost daily about lenders, mortgage companies, home builders, and title companies going bankrupt. The key is learning from companies that are overcoming today's challenges.

"The credit crunch is affecting every industry that involves finances, which is why my title company tweaked its business model to do in-house home closing wherever the client needs me to be. We've also extended our hours to include weekends in order to remain competitive," says Peter Jacoves, president of Richmond Title. "Thinking past the norm is what has helped my business remain successful. I think that solutions are available to businesses who take the time to think beyond tradition."

Duhon adds, "It's not easy to change the mindset of how we as dealers have sold cars in the past, but it is apparent that we must take a more proactive approach to actually help our customers. We must become more of a financial solution center. This is how we will succeed in this market." ■

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