



[Back to Index](#)

Entire Issue: [HTML](#) [PDF](#)

Dealer's Edge
January 7, 2002 Vol. 8, No. 1

1249 Words

Page 1

Management matters - Lenders get tough on F&I misrepresentations - By Gil van Over

Unethical practices in the F&I office can slow cash flow... and much worse!

The F&I manager had just hit a home run... even though it was raining outside.

The gross was intact; the back-end commission paid the electric bill. Best of all, she had successfully placed her sub-prime customer through a prime lender.

How?

Maybe she successfully negotiated this deal in a package with nine great deals.

Maybe she caught the buyer in a weak moment.

Maybe she perpetrated a fraud.

"We see a growing trend of lenders who want automobile dealers to be financially accountable for defaulted loans that contain misrepresentations and/or dealer fraud," notes Bob Lazenby, president of Lazenby & Associates, Las Vegas, Nevada. "Lenders must be able to rely solely on the dealer representations and warranties when purchasing an automobile loan. If fraud or misrepresentation is identified on any loan, either performing or defaulted, the dealer should be required to repurchase the loan."

Among the various ways to defraud a lender, straw purchases, misrepresented down payments and falsified credit applications are the most common, and easiest, to detect.

Straw purchases

Here's one example of a straw purchase. John loves the shiny new truck on the showroom floor. Unfortunately, John's credit bureau score is lower than the number of channels available on his local cable system. Tim, the F&I manager will suggest that John get someone to co-sign for him. John will ask his relatives, the people next door or a co-worker.

Once John convinces his co-worker to co-sign, they head for the dealership. The F&I Manager takes a credit app and pulls the co-worker's credit report. Her bureau score is higher than a top-of-the-line BMW!

By the time John is busting bugs in his new truck, he is nowhere to be found on the loan docs. The co-worker's name is everywhere.

When John doesn't make a payment, probably within the first six months, the collector calls the co-worker. She lets the collector know right away that she only co-signed the loan so John could get his truck and does not intend to make any payments.

Contract Misrepresentations

Many F&I managers know a lender's program parameters and underwriting standards better than the buyers. This can also lead to dealer fraud.

Bob is an experienced F&I manager. He has worked with the bank's buyer for two years. He knows that the bank will approve weaker credits if the applicant has skin in the game in the form of a down payment.

Here's Bob talking to a customer with weak credit:

Bob: "Normally the bank requires a ten percent down payment and you're short about \$1,500."

Customer: "I don't have that kind of money."

Bob: "Well, I have a special deal worked out with the credit analyst at the bank who doesn't agree with the bank's policy. She'll let me rearrange the figures on the contract so that it shows a ten percent down payment."

Customer: "How do you do that?"

Bob: "You already agreed to finance \$20,000 after your \$500 rebate, right?"

Customer: "Yeah."

Bob: "We'll just show that you are buying the car for \$22,000, have a total down payment of \$2,000, and want to finance \$20,000. That will take care of the bank managers and won't cost you any money."

Customer: "And my loan will be approved?"

Bob: "No problem."

The customer really wants the car so she agrees. Bob changes the figures to fit the bank's lending guidelines, the customer drives home happy and the bank books a tainted receivable.

You can understand why most lenders have a contract verification program. The lender's employees call a random sampling of customers financed the previous month to confirm the transaction details.

Falsified Credit Applications

Another frequent method used to commit lender fraud involves falsifying one of the documents that are forwarded to the lender. This package includes the credit application, loan or lease contract, insurance verification and application for title.

Jan prefers this method to defraud the bank. She knows the bank's lending criteria as well as Bob does, but is not quite the storyteller he is. Jan prefers to change her customer's demographic information when she inputs the credit application into the bank's online credit system looking for an automatic approval.

For example, she has observed that the bank's automatic approval algorithm seems to approve ten-year homeowners with bank accounts and a 15-year job in a good profession making over \$85,000 a year.

Thanks to Jan, many college-aged burger flippers in her town now have a checking and savings account, somehow have owned a home since they were five, and seemingly have benefited from a surprising increase in the minimum wage.

Most lenders now have a "match the app to the offering screen" program in place to catch people like Jan. A discounter must compare the information on the signed credit application to the information in the finance company's computer system before she can book the contract.

"While some banks look the other way when a dealer commits contract fraud and consider fraud an operational risk, we take a very dim view of misreps." according to Joe Lipari, senior vice president for Consumer Credit for Harris Bank and Trust in Chicago.

Dealership Obligations

Aside from every one of your credit offerings taking three times longer to decide, the dealer faces potential financial ramifications.

Every dealer principal signs a Dealer Agreement with every lender the dealership does indirect lending through. While there may be slight variations between agreements, generally a dealership is required to repurchase a contract from a lender if the:

- Sold vehicle is delivered to another person not party to the contract,
- Registered owner of the vehicle is not party to the contract,
- Vehicle options represented to the lender to increase the wholesale value do not exist,
- Vehicle delivered is a different year, make or model than represented to the lender,
- Down payment stated on the contract does not agree with the actual down payment received,
- Customer's check for a down payment bounces,
- Dealer rebate is not disclosed as such,
- Down payment was borrowed,
- Dealership knowingly provided false information on the credit application or buyer's order,
- Dealership does not perfect the lender's security interest in the vehicle,
- Dealer fails to verify proper insurance coverage on the vehicle.

With the average credit loss on a repossession approaching \$6,000, it won't take many payroll deductions before the F&I manager is paying the dealership for the privilege to work.

Ramifications for the F&I manager

While the dealer has a financial obligation to right the wronged lender because of a rogue F&I manager, many problems await an unethical F&I manager, including:

- Termination,
- The lender will closely review all credit offerings, slowing call-back time to a crawl,
- Lenders will turn off the automatic approval switch and rescind any "Instant Credit" programs in place at the dealership,
- The dealer's attempt to recover the money repaid to a lender,
- Criminal prosecution could result.

Ounce of prevention

Just as lenders established controls to protect themselves against nefarious F&I managers, ethical dealer principals should establish controls within the dealership as well. For example:

- Establish a policy and deliver the message, often, that lender fraud will not be tolerated and is grounds for dismissal,
- Install audio or video taping equipment in the office where contracts are signed and randomly review the conversations,
- Periodically audit a sampling of deal jackets looking for clues to straw purchases,
- Instruct the office manager to match the journal entry in the books to the down payment listed on the contract,
- Review lenders' reports on a monthly basis looking for drastic changes in approval ratios and call back time,
- Monitor customer complaints for subtle clues in broken promises made by F&I managers,
- Include contract verification questions in your customer service follow-up call script.

Gil van Over, President of gvo3 Consulting, provides confidential lender fraud auditing for Dealer Principals, he can be reached at (312) 961-9065.

Search:

[Top of Page](#)

© 1999-2004 WD&S Publishing