Article from Dealer magazine | June 2007

Mulligans and Other Do-overs

by : Gil Van Over

Eagle is my favorite golf term. Unfortunately, mulligan is my most frequently used golf term. I am not alone. Like most of my fellow golfers, I jump out of my car, put my clubs on the cart, get my drinks and do my best Mario Andretti imitation getting to the first tee.

Like most of my fellow golfers, my first tee shot bends to the right while my body convulses to the left trying to convince my five dollars disguised as a Titleist to come back into play. When reality sets in and the little white sphere is lost until the local diver swims to the bottom to harvest lost balls, I yell “Mulligan!” and promptly tee up another five dollars.

I get my do-over. I have a chance to start fresh and wipe out a bad memory. I may have lost five dollars, but the new beginning is worth the price.

Many dealers love mulligans. They just call it recontracting, a rewrite, or spinning a new deal.

Dealer mulligans
Dealers’ mulligans start with a spot delivery where the customer is not yet approved by a lending source. Given the sales manager’s and/or F&I manager’s experience and desire to deliver a vehicle, many transactions are spot delivered and the vast majority are placed with a finance source without any further issue.

However, my experience shows that anywhere from 1 percent to 35 percent of spot deliveries are recontracted.

The 1 percent bunch
Those dealers that recontract 1 percent typically have a great process in place to desk the deal at realistic terms given the customer’s credit background, long relationships with a limited number of preferred lenders and communication between the desk and the box about where to place the deals. These dealerships typically seem to have higher CSI scores as well. On the flip side, some peers will say that a dealer who only has to respin 1 percent of spot deliveries is not being aggressive enough.

The 35 percent bunch
At the other end of the continuum, the 35 percent mulligan company generally does not have a process for desking deals. The sales manager will either pencil every deal at state max or at 3.9 percent. There is absolutely no attention paid to standard underwriting guidelines. The deal is turned over to F&I with orders to hang the paper. If the deal can’t be hung as written, oh well. Get the customer back in and rewrite the deal after the customer has fallen in love with the vehicle and shown it to all of her friends, relatives and co-workers. CSI is a show that is filmed in Vegas, New York or Miami.

The problems with mulligans
Just because I put another five dollars on the tee does not guarantee that I will find the safe zone. I could very well pull the next shot out of bounds to the left or pop it up before reaching the forward tees.
A dealer’s recontract can go wild as well. There are times when deals end up being recontracted three, four, or five times before they are eventually unwound. Lawsuits then begin.
There are two primary recontracting issues the dark side takes umbrage with and are taking dealers to court across the country:

1. Backdating the transaction to the date of delivery instead of the date the new retail installment sales contract is signed.

2. Recontracting the contract on terms more adverse to the customer than the original transaction.

Backdating
Ironically, neither Truth in Lending Act or Regulation Z define the consummation of the financing transaction or address the dating of the RISC. This law and regulation provides the required credit disclosures, but are silent on consummation.

The courts, however, have ruled that the credit consummation occurs when the final contract is signed. The courts have further ruled that if you backdate a contract prior to the actual signing date, you are charging interest for a period of time when there was not a valid contact in place. The machinations of the finance charge and APR calculations could mean that you misstated the APR on the final contract, thus violating Truth in Lending.
Best practice advice: Date the recontracted deal the date it is signed, not the date of delivery to avoid this potential litigation risk.

Yo-yo transactions
Leave it to the dark side to find a cuter way to describe a puppy-dog close.
Regardless, it has convinced many judges and regulators that puppy-dog closes are a potentially deceptive act.

Some dealers still operate with the old school process of spotting everything at unreasonable terms, get the customer to fall in love with the vehicle, like a puppy-dog, then call the customer one to two weeks later and deliver the news that the original transaction was not approved and the customer must recontract at different terms or return the vehicle.

The dark side has gone so far as to define four red flags of potentially deceptive yo-yo transactions:
- The down payment increases
- The term decreases
- The APR increases, and/or
- The payment increases

Any recontract that has one or more of these red flags is at risk of being labeled and litigated as a yo-yo transaction.

Further, the dark side has placed a settlement value of around $50,000 per individual transaction.

Do the math. If you are recontracting 35 percent of your spot deliveries and a majority of them exhibit one of the yo-yo transaction red flags, at $50,000 per transaction, you can potentially lose more than a five dollar Titleist.

Best practice advice: Look at all recontracted deals from the last 30 days. If you have a significant percentage of potentially yo-yo transactions, train your desk personnel and change your spot delivery process. Get your F&I manager involved in the decision to spot deliver and to train the sales managers on generally accepted underwriting guidelines.

Gil Van Over is the president and founder of gvo3 & Associates, a compliance consulting firm that specializes in F&I and sales compliance. Visit www.gvo3.com for more information.