

CAR DEALER

INSIDER

Profit Making Secrets for the Competitive Dealer

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Negative equity: Do it right and avoid 3 problem areas

It's up to you to make sure your F&I office is compliant

Quick test: Are your F&I managers accounting for negative equity in deals by inflating the trade-in allowance and the purchase price of the vehicle?

If so, you're running the risk of technical compliance problems with Regulation Z, the Truth in Lending Act and state laws, say dealer attorneys and compliance pros.

Here's why this method, which many stores have used for years, is now becoming problematic:

1. Federal regs now offer guidance on how to properly handle negative equity. The approaches are known as the "netting" and "non-netting" method for disclosing negative equity in retail installment contracts. Under either approach, you would account for the consequences of negative equity on Line 4 of the contract, with the amount you list resulting from whether you "net" the trade-in allowance, down payment, rebates and lien payoffs or not. Plaintiffs attorneys are increasingly likely to scrutinize how you account for negative equity. In prior years, such

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Making your CPO program more valuable for customers

What's the average premium a customer who's interested in a certified pre-owned vehicle is willing to pay?

Answer: About \$1,480 for luxury vehicle buyers and \$1,020 for non-luxury vehicle buyers, according to a recent survey from J.D. Power & Associates. The figures represent the amounts that buyers seeking certified pre-owned vehicles say they would pay to purchase those vehicles versus non-certified alternatives.

But here's the rub. Most used vehicle buyers do not value the CPO designation, says Todd Wilson, director of automotive retail research for J.D. Power. The survey shows that among buyers of CPO vehicles—which represent about 38 percent of all used vehicle buyers—only 24 percent of those who purchase a non-luxury, certified vehicle did so because of the certification. The majority wound up in a CPO vehicle because it matched the type of vehicle and price they were seeking. (The figures are slightly higher for certified luxury vehicles.)

The upshot for you: Your sales team needs to do a better job of underscoring the value that certification represents. The study shows that the majority of used vehicle buyers learn about certification programs through dealerships rather than other sources, such as advertising in online and offline settings.

Some pointers to help your CPO sales process:

- Talk up the warranty protections. Buyers say the existing factory and bumper-to-bumper warranties offered on certified vehicles are the key factors that make CPO programs valuable to them. Your salespeople—particularly those who sell both new and used vehicles—should understand the warranty coverage and demonstrate how they can help protect a buyer's investment. The study also found that luxury vehicle buyers are more likely to cite warranty coverage as a factor in their purchases. That's largely because luxury CPO programs often offer longer coverage terms than their non-luxury counterparts (four-year, 48,000 miles versus three-year, 36,000 miles), Wilson says.

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- Show the recon work you’ve conducted. You should go over the mechanical inspection report and any repairs you’ve made with customers as part of your CPO sales process. The survey shows that about 14 percent of non-luxury CPO buyers find that valuable. The stat, Wilson says, illustrates that dealers may not be presenting this information consistently.

- Treat used vehicle buyers as well as your new vehicle customers. The study shows that 40 percent of used vehicle buyers who give their sales experience a rating of 900 or better (scoring similar to sales satisfaction tallies from factory surveys) will return to the same store for another purchase. A potential roadblock: Factory satisfaction surveys on new vehicle sales, as well as related incentives, can lead salespeople to spend more time and attention on those customers at the expense of used vehicle buyers. ■

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issues cropped up as part of other claims against dealers, but dealer attorneys say the cases are cropping up as standalone claims, says dealer attorney Alex Kurkin of Pathman Lewis, LLP, Miami.

2. You may create a sales tax problem. Bumping up the purchase price of a vehicle to account for negative equity can result in customers paying more sales taxes than they should, Kurkin cautions. The issue is problematic in states that don’t have a mechanism for offsetting the add-ons to the purchase price to eliminate the tax exposure. That can also create a technical Truth in Lending Act violation because credit customers would end up paying more than cash buyers—and the added costs do not get disclosed.
3. You may run into a deceptive advertising claim. Kurkin notes he gets periodic calls from local attorneys general who are concerned when they find a retail contract with a purchase price that does not match the price a dealer advertised. Kurkin says he’s been able to diffuse the scrutiny by explaining how some dealers account for negative equity. His concern: Not all AGs may take the time to understand the reasons behind the price differences and regard it as a cause for action.

Lenders say contracts have proper disclosures

An informal poll of lenders by *Insider* reveals that what dealers say is true: It’s difficult to get a straight answer on the best way to account for negative equity in deals.

James Ryan, a spokesman for DaimlerChrysler Financial Services, says the company’s contracts carry a line item for payoffs on trade-

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Tech threat: Viruses that can disable your network and shut down operations

Dealers deploy systems to avoid thousands in lost sales and productivity

IT managers at some dealerships say it's a little like talking to a wall: They'll highlight vulnerabilities on the ever-expanding networks of computers that power most dealerships, but their overtures often fall flat as concerns about added costs and an "it won't happen here" mentality take precedence.

But that can be a recipe for a disaster. Take Sanderson Ford, Phoenix, Ariz. Late last year, the stores' network of 500 PCs came to a halt on at least three separate occasions in a single month. That meant F&I managers couldn't use the Internet to vet deals with lenders; service advisors were unable to access the store's DMS to write ROs and look up customer records; Internet managers were unable to get new leads or follow-up on their active customer lists.

IT manager Steve Brown says the shutdown cost the store tens of thousands of dollars in lost income and productivity. The culprit? He's not certain whether the virus that ate up the network's bandwidth—essentially clogging the connections PCs use to link with the Internet and other applications—came from an e-mail someone received at the store or from a file or program someone loaded onto a PC in the store.

"There's always a way through" the firewalls and security barriers in the server networks at dealerships, Brown says.

A recent survey by DMS provider Reynolds & Reynolds shows that 44 percent of dealers list the vulnerability of their computer networks to virus attacks as a key consideration. John Darmento, a consultant with the Paul Gillrie Institute, says dealerships frequently do run into virus troubles—some of which could be avoided through a better combination of software tools and policies that govern how your employees should use the computers at your store. Here are some best practice ideas to avoid virus troubles:

- **Install a virus protection package.** Brown says he's had success using a new anti-virus

product from Reynolds and Reynolds, which recently began offering the product to dealers (see sidebar, below). Brown says the system identifies and quarantines at least one potential virus or spyware problem every day. Like other anti-virus products, the Reynolds product gives users a console that allows them to monitor potential virus activity on any PC on a network, enabling IT managers like Brown to quickly find the source of a problem and eliminate it before it can shut down a network.

Without the console, Brown would have to go to each of his store's 500 PCs to track down the source of a virus problem. The console also links daily with online services that keep tabs on known and emerging viruses and offer fixes to shut them down. Note: Virus protection software runs in conjunction with firewalls and other network security

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What's your best source for virus protection?

Dealership computer consulting expert John Darmento the Paul Gillrie Institute (www.paulgillrie.com) says the anti-virus software packages you can purchase from DMS vendors typically re-package existing technology and features you can often buy off the shelf from your local computer store. (Reynolds & Reynolds' new product, for example, runs off anti-virus tools developed by Symantec, a recognized leader in anti-virus and spyware software.)

The key is to assess functionality and price. "Sometimes the DMS vendors offer the best deal, sometimes you're better off on your own," he says. One consideration: Stores that lack their own IT staff may be better served by vendors who can handle the installations and training needed to run the software. ■

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ins. The company made the change after the feds made adjustments to Regulation Z that detail how to account for negative equity.

But an exec at a non-captive lender says that while company contracts allow for a line item disclosure for negative equity, the company leaves it up to the dealer to determine the proper way to account for it in contracts. "We don't control how the dealer writes up the deal," the exec says. In

addition, if a deal falls within the company's guidelines for financing up to 120 percent of the MSRP, and a dealer buries negative equity in the purchase price, the lender may not even know there's negative equity in the deal. Here's the upshot for you: Ask your lenders if they will approve deals using the proper approach to accounting for negative equity. Those that won't may not be your best partners to finance your deals. ■

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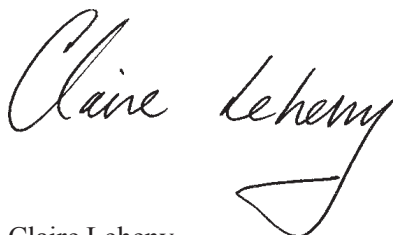
tools that your network should employ to thwart unauthorized access to your store's files and data.

- **Establish a computer user policy that has teeth.** After the network shutdown, Sanderson reiterated its user policy with store employees. The upshot: Users may not bring in files from home or download them from Internet sites without assistance from IT to ensure they're free from viruses. In addition, the store employs another software tool that blocks employees with Internet access from visiting non-work-related sites while they're at the store. A benefit: IT experts say that once employees know their Internet use is being monitored, they are less likely to spend time using the Internet for personal reasons. Sanderson's policy includes provisions for terminations if an employee repeatedly violates the policy and disregards efforts to change his/her behavior.

- **Keep your network configurations current.** Brown says it's a challenge to maintain an up-to-date listing of all active computers and their locations on a network—given personnel changes that result in people moving to different offices or new hires using a former employee's PC in a different location. Remember: The map of your network is the centerpiece of your ability to identify and quarantine viruses that may infiltrate your network. Make sure your managers work in tandem with IT as they move staff to new desks and responsibilities. ■

News Brief

Cali dealers reach compromise. The California Motor Car Dealers Association recently struck a compromise with state lawmakers interested in placing caps on dealer markups and providing contract cancellations for customers who don't like the used vehicles they purchase. The compromise, which is expected to hit Gov. Arnold Schwarzenegger's desk in the coming weeks, calls for a 2.5 percent cap on finance deals with terms of 60 months or less, and 2 percent cap on deals longer than 60 months. In addition, the legislation would give consumers a three-day cooling off period on used vehicle purchases, provided they purchase the ability to cancel contracts from dealers. Dealers can charge up to \$250 for the cancellation agreements and customers must return vehicles with no more than 250 additional miles on the odometer. Dealers would also be able to charge a restocking fee up to \$500 when customers cancel their contracts. ■



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