F&I

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Dealer Reserve on the Endangered List

The only tattoo I have is the scar from a smallpox vaccination I received when I was ten. Everyone in school received the vaccination. Everyone has the scar tattoo to prove it.

These vaccinations were apparently mandated by a governmental agency which was working to eradicate the smallpox disease. It seemed overly invasive at the time, but it worked.

A governmental agency is at work again to eradicate something it doesn't like: dealer reserve.

The Consumer Financial Protection Bureau

A new consumer watchdog agency is in the formation stage. The Consumer Financial Protection Bureau (CFPB) is a result of the Wall Street Reform Act. According to its web site "The CFPB will set and enforce clear, consistent rules that allow banks and other consumer financial services providers to compete on a level playing field and that let the consumer *see clearly the costs and features of products and services*".

This is the same watchdog agency that franchised car dealers were successful in securing an exemption from oversight last year. At the time, it seemed like a well-deserved victory from having yet another regulatory oversight burden put on businesses that simply want to sell vehicles.

Watch out for the end around

The bureaucrats involved with the CFPB are outspoken critics of dealer reserve. These consumer advocates simply do not understand the business to business buy rate and the business to consumer right to mark up a product or service. They honestly believe that the consumer is entitled to the buy rate and that a dealer is not *entitled* to mark up the interest rate.

In other words, eradicating the yield spread premium dealers are currently able to charge is high on their wish list. Unfortunately for them, franchised dealers are exempted from their oversight.

This brings us to the end around. Many lenders are reporting that the CFPB will likely try to regulate dealers by regulating lenders. Theoretically, the agency can simply prohibit lenders from purchasing retail installment sales contracts which have a face APR higher than the buy rate on that transaction.

Voila…dealer reserve is gone.

A silver lining

I believe that dealer reserve as we know it is going away. It has been slowly evaporating for years now. The captives pay a flat fee when a deal is written at a subvened rate. Many credit unions are not paying dealer reserve on the yield spread, but rather with flat fees. Dealers have options through independent lenders and banks to sell a contract at the buy rate and receive a flat fee.

Many dealers recognize this trend as well, evidenced by their shifting of F&I compensation from reserve to product sales.

Once the CFPB imposes its will on the lenders, flats and super flats will become the way dealers are compensated for selling contracts to lenders. And this ain't gonna be so bad.

Some dealers are clamoring for a flat fee rate structure from their lenders. They have done the math. They know they are not carrying much in reserve today. Shifting to a flat fee rate structure will likely mean an increase in commission from their lenders.

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