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Search Articles

Topical Index

Past Issues

Print Current Issue

PDF Issue Archive

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About Us

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## Lower caps on reserve markups in new settlement

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Decision continues push toward flat-rate system for finance deals

Three large banks and Honda Financial Services struck settlement agreements last week to end class action legal cases that claim the lenders' allowing dealer markups on loans results in discrimination against black and Hispanic buyers.

Under the settlement terms, Bank of America, Bank One and U.S. Bancorp separately agreed to place a 2.5 percentage-point cap on reserve markups on all deals up to 60 months, a 2 percentage-point cap on deals between 60 and 71 months, and a 1.75 percentage-point cap for deals longer than 72 months. In addition, the lenders must provide a 10-point, bold-type disclosure on all contracts that reads:

"The annual percentage rate may be negotiable with the seller. The seller may assign this contract and retain its right to receive a part of the finance charge."

Meanwhile, Honda Financial Services went even further. The captive finance company agreed to place a 2.25 percentage-point cap on reserve markups for deals up to 60 months, and a 2 percentage-point cap on all deals that run 60 months or longer.

The company also agreed to incorporate the disclosure on its contracts and provide refinancing deals for all black and Hispanic consumers who have financed vehicles through the captive since 1990.

All the companies also agreed to invest hundreds of thousands of dollars into consumer education initiatives and provide "no markup" financing deals to 875,000 black and Hispanic customers over the next three years.

The provisions closely follow those contained in the settlement agreement Nissan Motor Acceptance Corp. struck about two years ago to end a class action case that claimed it engaged in discriminatory lending practices. In all the settlements, the lenders do not admit any wrongdoing and they stipulate that their lending practices are neutral when it comes to race and ethnicity. Spokespeople for the three banks and Honda Financial Services declined to comment on last week's settlement.

"We have continued our program here of lowering the caps to the lowest level we can achieve," says Stuart Rossman, director of litigation for the National Consumer Law Center, which has assisted plaintiffs' attorneys with filing the discrimination cases and seeking settlements. The group has also sponsored studies of lending practices that the practice of allowing reserve markups results in black and Hispanic customers paying higher interest rates than non-minority customers.



Several loan discrimination cases are still pending. The captive finance arms of Ford, Toyota and Chrysler are all contending with class action claims in various federal courts. The latest settlement may well spur those companies to seek their own settlements. "When they see the industry is starting to change it will increase pressure for them to come to the table," Rossman says.

Observers see settlement as part of move to flat rate deals

The big question for dealers: How will the settlements affect reserve income?

Indeed, some dealers will see more erosion of reserve income as a result of the deals, but little more than what most have already seen as a result of voluntary mark-up caps most lenders have put in place since the NMAC settlement and the effects of more low-interest incentive deals.

"Most deals are effectively flat rate deals anyway," says **Gil Van Over**, head of gvo3 & Associates, a Schererville, Ind.-based firm that assists dealers with implementing a legal defense strategy in F&I.

He and others believe the settlement marks the continuation of a trend that will ultimately bring an end to dealer markups, replacing the practice with flat-rate fees for finance deals.

Lenders are not likely to move to flat-rate deals voluntarily, but the cumulative effect of the settlements as well as state-sponsored pushes to limit dealer markup discretion, might compel them in that direction. Several state legislatures, including those in California, Louisiana, Illinois and others, have begun exploring ways to impose mandatory caps and pricing on finance deals.

The settlements' calls for consumer education and contract disclosures are also expected to raise more questions in F&I about the APR on deals. Van Over expects more customers to inquire whether the rate they're getting is "the best rate." n

Best practice disclosure tip: Tell consumers who ask the that what they're getting is a "fair and competitive rate" rather than the "best rate available," **Gil Van Over**, of gvo3 Consulting, advises. Its likely that customers can get a better rate elsewhere and, if you claim your offered rate is the best, you may be running afoul of the Truth in Lending Act for offering a misleading statement. n

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11300 Rockville Pike, Suite 1100, Rockville, MD 20852.

Phone: 888/287/2223 Fax: 301/816-8945 Email: [cdicustomer@ucg.com](mailto:cdicustomer@ucg.com)