Lender Leverage Equals More Approvals

Figure out exactly what your lenders consider creditworthy and show them how your customers fit the bill.

By Ronald J. Reahard

As an F&I professional, you have a responsibility to your dealership and sales force to obtain approvals for as many deals as possible. Your primary consideration must be to develop a long-term, mutually beneficial relationship between your dealership and its finance sources.

Lenders really do want to approve every qualified deal they receive. Your responsibility is to take the time and make the effort to know what's important to each of your paper buyers. This way, you'll be able to get an unqualified approval on as many deals as possible.

When you do your job honestly and effectively, you become an integral part of the credit evaluation process.

Structure the Deal

The first thing every lender considers is the deal structure itself. Based on the lender's stated guidelines—maximum advance, debt-to-income ratio and so on—does this deal meet the lender's requirements?

It's critical that you know what's important to your paper buyer and what guidelines he or she uses to evaluate a deal. Then you can structure the deal in advance to ensure an approval. Nothing irritates paper buyers more than receiving deals that don't even remotely meet their guidelines. To increase your chances of getting customers approved, you should evaluate their credit reports to assist the sales department (and the customer!) in structuring the deal.

Learn the Lender's Portfolio Mix

All lenders have a portfolio mix—the percentage of paper they want to achieve in each tier level. In addition, each paper buyer has his or her own portfolio and each dealership also has a loan portfolio. It's absolutely critical that you determine what percentage of paper your lender wants in each tier and how your dealership stacks up in comparison. Your lender needs—and expects—a mix of paper. While it might be tempting to always give your best paper to the source with the best buy rate, doing so will adversely affect your portfolio mix with those lenders buying your tier-two, tier-three and tier-four customers.

Consider Look-to-Book Ratio

Lenders also evaluate a dealership's performance by the look-to-book ratio. Compared to the number of deals they looked at from your dealership, how many did they actually book? Say a lender looks at 60 deals from you in a given month and approves 30. If the lender receives 15 of those deals, they're being compensated for only a fraction of their efforts. Why would lenders work a deal they might not receive, especially if they knew the dealer sent it only after everyone else rejected it? The lender who approves a deal should get the deal, unless the tier is unrealistic based on the lender's stated guidelines.

Interview the Customer

Interviewing the customer before submitting the deal to a lender is essential. You need to provide your paper buyer with sufficient reasons to justify an approval.

The credit bureau report, when properly used during the interview, can help increase your chances of obtaining an approval. A credit report reveals many aspects of the consumer's borrowing activities. The lender considers all these aspects to some degree when evaluating the deal. Knowing what your paper buyer is looking for is key to analyzing a credit report (see the related sidebar).

Although Regulation Z says that discussing customers' credit bureau information with them isn't illegal, always ask for the customer's permission before doing so. Do not, under any circumstances, give the customer a copy of his or her credit bureau report. Customers who are denied loans are entitled to a free copy of their report from the credit bureau.

Paint a Good Picture

In addition to FICO scores, most lenders consider certain characteristics of the customer to determine creditworthiness. Many lenders use an internal computerized scoring system that assigns numerical point values to these characteristics. Virtually all these factors are on the credit application, credit bureau report, or the buyer's order or deal sheet.

No matter what scoring system a lender uses, paper buyers base their decisions on three basic elements:

1. Capacity—The customer's ability to pay based on income, net worth, investments, other indebtedness and credit score guide. Insufficient capacity is the number one reason most deals are rejected!

2. Character—The customer's likelihood of paying based on previous credit experience, occupation, stability, education, references, family and paying habits.

3. Collateral—The customer's willingness to pay based on the type of collateral, down payment, equity and the ability to locate the collateral.

Because a paper buyer never sees the customer, you must paint a picture of the customer that lets the paper buyer justify an approval. Before submitting the application,

Credit Reports: Factors Lenders Consider

• *Payment history.* Previous delinquencies, charge-offs and defaults are the strongest indicators of whether or not this loan is a good risk. Delinquencies are evaluated in terms of severity, recency and frequency. A 30-day late payment isn't as serious as a 90-day late payment. A 30-day late payment made one month ago indicates higher risk than a 30-day late payment made four years ago. The older, smaller and less frequent the customer's delinquency is, the better that customer will typically score.

• *Outstanding debt.* A credit record with many outstanding balances and a high ratio of balances to the customer's credit limits generally indicate greater risk and a lower tier level. Lenders also look at how many credit cards have balances.

• *Credit history*. The trade lines in a credit report indicate how long the customer's credit has been established and the types of credit they've obtained. The lender typically associates a short credit history with greater risk, but—depending on other factors—even customers with short credit histories could still meet their guidelines.

• *Inquiries and new account openings.* Inquiry references show if the consumer has been actively seeking additional credit and, if so, what type. Numerous inquiries and new account openings typically indicate greater risk but in the context of the overall credit picture.

• *Types of credit in use.* The type of credit a customer is currently using can also affect lender decisions. Loans from a personal finance company might indicate the consumer's inability to secure credit from less expensive sources. A consumer with no bankcards—or too many—is seen as a higher risk. The worst credit risk would have no bankcards and several finance company loans.

learn the circumstances surrounding any adverse credit information disclosed by the customer or in the credit report. Find reasons why this customer is now a good risk and document them to help your paper buyer justify an approval or change a tier level. You only get one chance to convince the paper buyer!

BUILD YOUR CASE

To build your customer's case for approval, there are several questions to ask regarding his or her current financial situation.

• What is your ability to meet this new or larger monthly obligation considering your other monthly obligations?

• Will you have a near-term increase in income or decrease in debt?

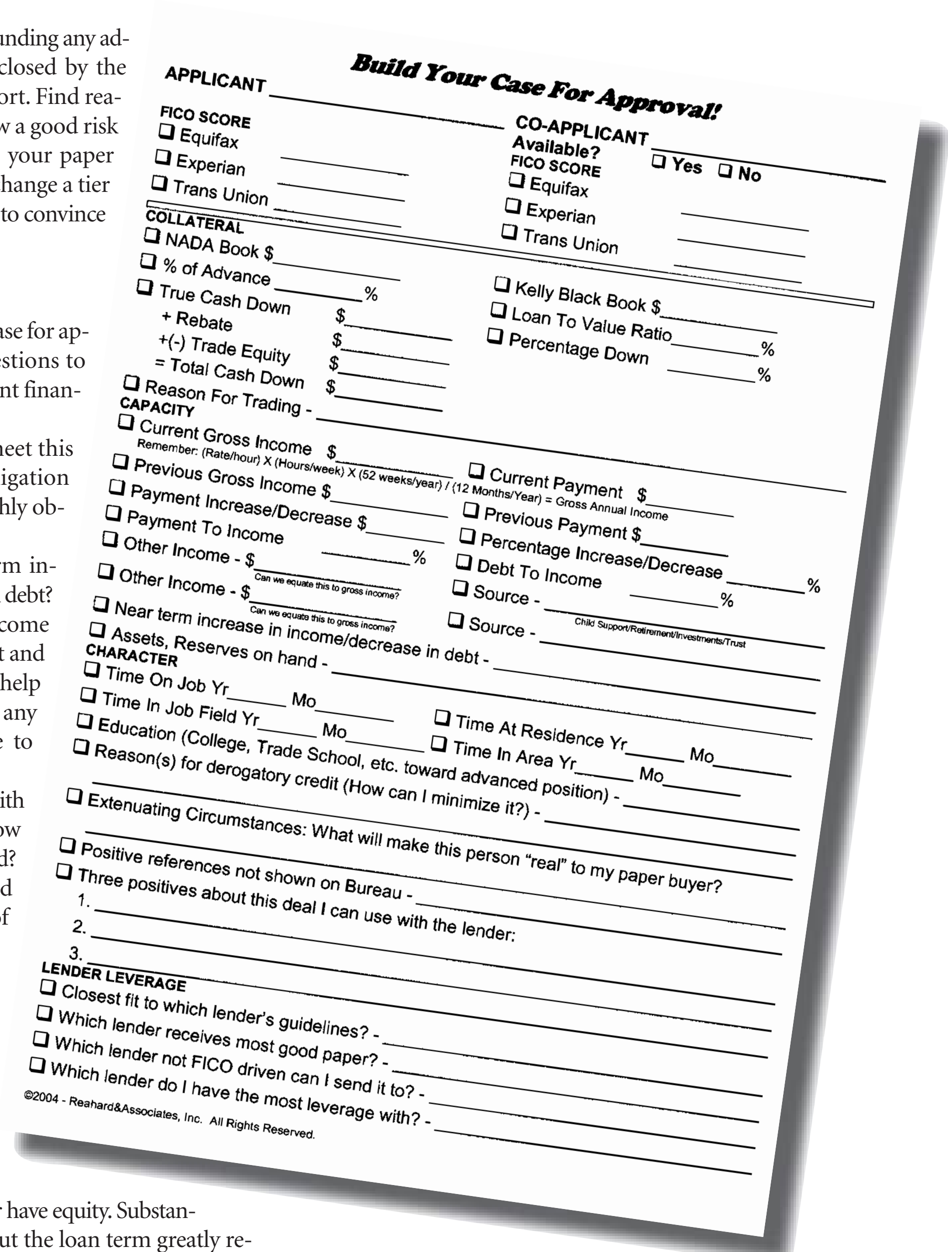
• What other sources of income (such as spouse, child support and investments) are available to help meet this obligation? Is there any way to include that income to strengthen the deal?

• How long have you been with your current employer? How long have you been in this field? Are you likely to stay employed in this field for the duration of the contract?

• What assets do you have to fall back on——savings accounts, IRAs, stocks, mutual funds, real estate equity, any recognizable investments or other family assets?

Consider the value of the vehicle being purchased and whether the customer will ever have equity. Substantial negative equity throughout the loan term greatly reduces a customer's willingness to pay. Also, look at the customer's intended use of this vehicle and past use of and mileage on their current vehicle. Does it seem like the actual cash value of the new vehicle will continue exceeding—or ever exceed—the amount owed? Is a shorter term possible? If the payment exceeds their capacity, is a longer term possible?

To convince a lender to buy a marginal deal, emphasize its strengths. Highlight the customer's years with the current employer, true cash down payment or good auto credit history. Other positives include the customer's reason for purchasing a vehicle, reason for any adverse credit or demonstrated ability to make similar payments in past. Look for customers' additional assets, reserves on hand and other extenuating circumstances to emphasize to the lender.



Build Your Case For Approval!

APPLICANT ______ CO-APPLICANT ______

Available? ❑ Yes ❑ No

FICO SCORE
❑ Equifax ______
❑ Experian ______
❑ Trans Union ______

FICO SCORE
❑ Equifax ______
❑ Experian ______
❑ Trans Union ______

COLLATERAL
❑ NADA Book $______
❑ % of Advance ______%
❑ True Cash Down $______
+ Rebate $______
+(-) Trade Equity $______
= Total Cash Down $______
❑ Reason For Trading - ______

❑ Kelly Black Book $______
❑ Loan To Value Ratio ______%
❑ Percentage Down ______%

CAPACITY
❑ Current Gross Income $______
Remember: (Rate/hour) X (Hours/week) X (52 weeks/year) / (12 Months/Year) = Gross Annual Income
❑ Previous Gross Income $______
❑ Payment Increase/Decrease $______
❑ Payment To Income ______%
❑ Other Income - $______
Can we equate this to gross income?
❑ Other Income - $______
Can we equate this to gross income?
❑ Current Payment $______
❑ Previous Payment $______
❑ Percentage Increase/Decrease ______%
❑ Debt To Income ______%
❑ Source - ______
Child Support/Retirement/Investments/Trust
❑ Source - ______
❑ Near term increase in income/decrease in debt - ______
❑ Assets, Reserves on hand - ______

CHARACTER
❑ Time On Job Yr______ Mo______
❑ Time In Job Field Yr______ Mo______
❑ Time At Residence Yr______ Mo______
❑ Time In Area Yr______ Mo______
❑ Education (College, Trade School, etc. toward advanced position) - ______
❑ Reason(s) for derogatory credit (How can I minimize it?) - ______
❑ Extenuating Circumstances: What will make this person "real" to my paper buyer? ______
❑ Positive references not shown on Bureau - ______
❑ Three positives about this deal I can use with the lender:
1. ______
2. ______
3. ______

LENDER LEVERAGE
❑ Closest fit to which lender's guidelines? - ______
❑ Which lender receives most good paper? - ______
❑ Which lender not FICO driven can I send it to? - ______
❑ Which lender do I have the most leverage with? - ______

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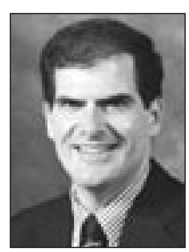
F&I personnel must develop and maintain a professional relationship with each lender that is based on honesty, integrity and mutual respect. Never attempt to convince a paper buyer to make a poor business decision. Instead, give them a logical basis on which to make a favorable decision. ■

Ron Reahard is president of Reahard & Associates Inc., an F&I training company providing in-dealership F&I training programs, consulting services and solutions. Contact him at 866/732-4273 or ron@go-reahard.com.



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