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What's Hot on Hotline? "Bullpenning" Trade-in Vehicles
by Robert Ebin

We've recently been receiving quite a few calls on Hotline regarding "bullpenning," or rather, the damage control options for not following the recommended practice. With October on the horizon, some of you baseball fans may be wondering why people are calling Hotline to discuss the practice of limiting the exposure of starting pitching by optimizing the use of relief pitching. Although a fascinating topic (and one which this Dodgers fan can discuss for days), relief pitching is not the topic of this article. Rather, this article will discuss how to properly "bullpen" a trade-in vehicle when one comes into your dealership.

Scenarios

Generally, the calls we receive about bullpenning start the same way. A new vehicle is sold to a customer, and the deal involves a trade-in vehicle. As is common practice, the new vehicle is spot-delivered. A few days later, the dealer pays off the trade-in. By the ninth day after the consummated deal, the dealer is unable to find financing and sends out a 10-day letter to the customer. "That's fine," says the customer. The customer brings the spot-delivered vehicle back and asks the dealer to return the trade-in. This moment is where the similarities in each situation end.

Lienholder on Trade-In is Paid

Although the dealer still has the customer's trade-in, the lien balance has already been paid off. The dealer has effectively "de-horsed" the customer by taking him out of his trade-in.

Trade-In Vehicle Has Been Sold

Other situations arise where the highly sought-after trade-in vehicle was already sold to a third-party and cannot be returned to the customer. Here, the dealer actually "de-horsed" the customer by selling the trade-in to another party altogether.

In both instances, the dealer is unable to return the customer to his or her pre-contract position. For these very reasons, we strongly recommend the dealer install a policy of bullpenning trade-in vehicles, and if such a policy already exists at your dealership, now would be a good time to review it with your employees.

How to Bullpen Trade-In Vehicles

Generally, all trade-in vehicles involved in a financed deal should be bullpenned and not added to your inventory until the deal funds. Bullpenning requires all the following:

- The trade-in vehicle's lien should not be paid off until the customer's new deal is funded. Recall that Vehicle Code § 11709.4 requires the dealer to pay off the prior credit or lease balance on the trade within 21 calendar days of acquisition. Some may ask, "well, what if the customer's deal doesn't get funded within 21 days?" I would respond by informing them that this situation should never get to that point. Section 11709.4(b) provides an exception where the dealer gives notice of rescission of the contract within those 21 days; the dealer is no longer required to pay off the lien on the trade-in vehicle. Now, this does not give you license to start sending out 10-day letters after the 10 days. Rather, it is a reminder for you to timely send out your 10-day letters, which will prevent you from having deals that are not funded within 21 days and having trade-ins that are not paid off.
- The dealer must not sell the trade-in vehicle before the customer's new deal is funded. This stems from Vehicle Code § 11709.4(a)(4), which prohibits the dealer from selling the trade-in vehicle until the dealer tenders the full payoff amount on the trade-in to the lienholder. Even if you have another buyer already lined up for the trade-in, you must not sell it until the customer's new deal is funded and the lien is paid off in full.
- The trade-in vehicle should be stored in a specially designated "not for sale" area at the dealership, and we recommend against commingling these vehicles with your general inventory. We also strongly advise dealers to place "not for sale" signs on these vehicles to help prevent any false/misleading advertising claims by consumers and serve as a reminder to dealer employees about these vehicles.
- The dealer must not advertise the trade-in vehicle for sale. Vehicle Code § 11713(b) prohibits a dealer from advertising or offering a vehicle "not actually for sale on the premises." Even though it is on the premises, the bullpenned trade-in cannot be "for sale" because the lien has not been paid off.

What Can You Do After the Fact?

In the scenarios discussed above, had the dealer bullpenned the trade-in, the ensuing problems could easily have been avoided. The deal would be rescinded, and the trade-in returned to the customer. However, hindsight is 20-20, and sometimes even the best of us are left trying to pick up the pieces. There is no easy solution when a trade-in vehicle is not properly bullpenned. However, what follows are a few suggested corrective measures a dealer can take:

Contact the lender with which you have the best relation and beg them to buy the deal.

The reason why the dealer is in this mess is that the contract could not be assigned in the first place. Therefore, it is worth another attempt (or two) to get the deal bought. Remember, however, that since the 10-day rescission letter was already sent out and the vehicle was brought back, the contract has already been rescinded. Although you cannot force the customer to accept financing, this may be a viable option if the customer is still interested in keeping the vehicle and is willing to enter into a new contract.

Carry the paper or unconditionally guaranteeing the deal

Admittedly, neither of these are attractive options to dealers, but they are options. As a reminder, these measures also require that the customer be willing to keep the deal together. The prior contract has been rescinded, and you cannot force the customer into a new contract.

Options regarding the trade-in

What if your customer in the scenario above insists, "I want out of the deal and want my car back!"? You still may have some options. First, you can carry the note for the trade payoff in-house. Essentially, the dealer is stepping into the shoes of the lender that was paid off. However, if you choose to carry the note, it is important to have an attorney assist you in drawing up a note reflecting the payments owed to you. The note should include language providing a retained security interest in the vehicle to allow for repossession rights. Also, ensure that the dealer is recorded as the legal owner on the title.

Another option may be to give the trade-in back to the customer free and clear. Although this option likely would be a last (and most expensive) resort, it may be viable where the entire payoff was relatively low.

But what if the trade-in was already sold to another customer, as in the more complex scenario above? This is a sticky situation because returning the trade-in vehicle is required under the "Seller's Right to Cancel" language on the LAWCA-553, and arguably, you as the seller may have breached the contract. California law provides that in the event a trade is not returned (for any reason) and the contract is breached by the dealer, the customer may recover either the amount allowed on the contract for the trade-in or the fair market value, *whichever is greater*. [Civil Code § 2982.7(b)]. The fair market value is calculated using a generally accepted vehicle guidebook, and you should credit this amount to the customer. If the fair market value or contract allowance exceeds the payoff for the trade-in, then you would owe the customer the difference. Conversely, if the payoff for the trade-in is greater than the fair market value or contract allowance (i.e., negative equity), technically, the customer owes you money, which would likely make this option a tough sell. In situations where there was no payoff for the trade-in, the full fair market value of the trade-in (or contract allowance) should be tendered to the customer. Although the customer still may have a bone to pick because s/he is out of a car, tendering this amount is a good starting point. Remember, you only have five business days from the date of the breach to tender this offer to the customer, and this offer does not preclude the customer from pursuing other legal remedies against the dealer as well. [Civil Code § 2982.7(b) and (c)].

Other Trade-In Best Practices

Although it is the main subject of this article, bullpenning is not the only potential pitfall dealers face when acquiring a trade-in. For a more detailed discussion of the best practices for dealers when acquiring trades, please refer to the September 2018

Transmission article, *Vehicle Trade-In Best Practices*.

Questions?
If you have any questions regarding this issue or any other situation that may arise in your sales or service departments, hotline clients are invited to contact us at (800) 785-2880 (then press "4" for hotline) or hotline@autoadvisory.com.

Fraud by Dealership Ownership and Personnel Continues to Result in Criminal and Civil Liability at Every Level of Dealerships - A 2019 Example

by Shane McCallan

This time last year, we published an article called "FTC Chargers Dealer Group for Falsifying Credit Applications." The article discussed an FTC action against four affiliated dealerships who were alleged to have overstated customers' monthly income on their credit applications, overstated downpayment amounts shown on retail installment sale contracts and published deceptive advertisements. The FTC also alleged that, in some cases, dealership employees altered documents after the customers signed them. Not only were the four dealerships named in the complaint, but the owner and his wife were listed *personally* as defendants.

That article references an article that we wrote in 2017 called "Check Your Credit Checkers," which stated:

"*We are not aware of any issue that results in more dealership personnel, at every level of seniority, facing a prison sentence than falsifying information in a consumer's credit application. And the issue has been heating up over the past couple of years. Why?*"

Unfortunately, it's time for a 2019 example. Recently, the federal government accused the former president of the National Independent Automobile Dealers Association of defrauding four banks and credit unions, as well as General Motors, by using fake vehicle sales and *fraudulent* loan applications to pocket millions of dollars in a four-year scheme.

He was named personally in the lawsuit along with his former finance manager. The two were accused of falsely indicating that customers made a downpayment and inflating their incomes to banks, as well as taking money from customers and lenders for service contracts and GAP, and not sending the paperwork and payment to the vendor.

"Selling Out of Trust" Fraud

Just as prominently, the dealership allegedly defrauded its floorplan lender and other financial institutions. It did so by failing to notify its floorplan lender when it sold a vehicle financed with funds from the bank. Selling vehicles but not repaying the lender for the floorplan loan is known as selling out of trust.

On this end, the dealer and his finance manager were accused of submitting fake buyers order to the floorplan lender. These buyers orders were dated later than the actual sales dates in an effort to justify late repayment or non-repayment of the vehicles. In other instances, the two submitted fake vehicle sales to General Motors to capitalize on expiring incentive rebates.

Consequences

The dealer principal faces up to 510 years in prison and a fine of $17 million, while the finance manager faces 330 years in prison and an $11 million fine. These consequences don't take into account the lawsuits filed by the banks and consumers.

We will end by reiterating the quote from "Check Your Credit Checkers" article:

"*We are not aware of any issue that results in more dealership personnel, at every level of seniority, facing a prison sentence than falsifying information in a consumer's credit application. And the issue has been heating up over the past couple of years.*"

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