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## Get ready: Flat-rate financing deals may be the norm in two years

Study affirms lender interest in moving to no-mark-up deals

A recent survey of dealers across the country predicts that lenders will move toward a flat-rate, no-mark-up approach to compensating your store for retail finance deals within the next two years. The upshot for you: Now's the time to set a goal of a 50/50 split between product and reserve income for your F&I department, and use the same ratio to guide compensation for your F&I managers.

"F&I departments are going to have to ratchet up their selling skills to improve product penetrations," says Mark Rikess, president of the Rikess Group, a Burbank, Calif.-based dealership consulting firm that conducted the study on behalf of captive lenders interested in understanding how dealers would regard a move toward flat-rate financing deals.

The study found that 65 percent of dealers believe lenders will move toward flat-rate deals in the next two years. Dealers pegged a \$400 flat fee as a figure that would be a reasonable amount to replace reserve income they'd lose under a flat fee structure. And a vast majority of dealers agreed that a flat fee system would reduce the risks of lawsuits and negative publicity over unfair markups.

F&I consultant **Gil Van Over** of gvo3 Consulting says the survey results are in line with current market trends. Lenders are concerned about liability risks from growing consumer interest in eliminating dealer mark-ups, an issue that cropped up in California and Louisiana legislatures in the past year.

Captive lenders, meanwhile, privately express interest in moving toward flat-rate deals, but they fear dealer backlash and a loss of business to regional banks, which typically offer buy rates a percentage point lower. To fund a flat rate payment, lenders would need to raise their buy rates between .5 percent and 1 percent, Rikess says.

Even so, "the industry will eventually have to go to a flat-rate system," Van Over says. His prediction: Lenders will initially migrate toward flat rates by offering dealers a choice of mark-up and flat-rate deals before making the latter structure the norm.

What might a flat rate system look like? Lenders may establish flat payment amounts based on customer credit tiers. Example: \$400 for A-paper, \$300 for B-paper, \$200 for C-paper and \$50 for D-paper. Rikess says dealers who finance their floorplan and majority of retail contracts with the same lender might also receive richer flat rate payments.

Van Over thinks a flat rate system may emerge that doesn't necessarily mean set payment amounts on given deals.

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Example: Lenders might add an additional "acquisition fee" for consumers on contracts to pay for the program (say, \$125), and then dealers may earn a flat payment based on a percentage of the amount financed (say, 2 percent). The figure's close to the caps that most captive lenders now set on dealer mark-ups, and average mark-up rates.

The transition to flat rate payments would cause the most income damage to dealers who still rely on reserve mark-ups for the majority of their F&I income and profits. Van Over says that dealers who move toward a 50/50 balance between product and reserve typically see a rise in F&I product profits and penetrations, as well as a drop in chargebacks. In the Rikess study, 75 percent of dealers who favor a flat rate system believe it would increase - not decrease - F&I income and reduce chargebacks. n

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