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## Automotive News **INSIGHT**

# FINANCE & INSURANCE

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## GOING THE **extra** mile

F&I offices are breaking service norms to help customers build better lives

**Hannah Lutz**  
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**M**ost think of the F&I office as a profit center for dealerships, and it is. But many F&I departments have adopted a culture of service, too, going far beyond the norm to ensure that car buyers with economic or life challenges come away with the best solution for their needs.

Hennessy Mazda-Buick-GMC in Morrow, Ga., is a case in point. When some first-time car buyers come into the store, credit card and student loan debt already have hurt their credit scores. They "don't realize what missing a payment does," says Blake Bailey, director of finance at the dealership.

The finance department at the Hennessy store teaches consumers about

credit and matches them with cars they can afford. F&I managers even review credit card offerings with consumers after they've purchased vehicles to help them understand their options and advise them on a credit decision.

"We see these people come back with a small family, and they've gone from a first-time buyer to a 720" credit score, Bailey says. "I enjoy when we get that customer done that really needs it."

The F&I manager's job is to identify the customers' needs and figure out how financing or F&I products would help them, industry insiders say.

Some of that consumer knowledge can come from alternative data, such as income, job tenure, home ownership and

payment history, and some comes from conversations with customers.

Rick McCormick, national account development manager for Reahard & Associates, says consumers can smell what he calls commission breath "from a mile away." But "consumers will buy plenty from someone they trust," he says. Even if working for the customer means a smaller profit that day, "if you help more customers, you make more money in the long run."

Sometimes, the best solution for securing a long-term customer is to pull the customer away from a vehicle.

Becky Cherneq, president of Cherneq Consulting in Cumming, Ga., was a

dealership F&I manager before becoming a consultant. She says she can't even count the number of times she "talked a customer out of a vehicle because it wasn't right. It's a tough pill to swallow, but it's a pill we have to swallow."

Dealer Steve Cook of Cook Chevrolet-Buick in Vassar, Mich., agrees. In some cases, he's persuaded customers to keep their cars. "I don't need to sell a car so bad that I push them into a payment that accentuates their problems rather than helps," he says.

In this special section on finance and insurance, *Automotive News* will highlight how, through personal relationships, alternative data, financial education and more, some dealerships are going the extra mile for their customers to make F&I a true service. **AN**



**Bailey:** "People come back."

# F&I managers learn to look beyond numbers

‘Every customer has a story’ the lender should hear

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**F**&I is a numbers puzzle. Managers experiment to figure out which numbers give the dealership and the customer the strongest result. But getting the best result often requires looking well beyond credit scores.

The F&I manager’s job is to advocate for his or her customers, industry experts say. To do that, the manager needs to gather enough information to tell banks the tale behind the numbers.

“Every customer has a story, and it’s our job as their advocate to build their case to the lender,” said F&I trainer Ron Reahard, president of Reahard & Associates in Soddy-Daisy, Tenn. “Every business is in business to add value, to help people. If you’re not making enough money, you’re not helping enough people.”

F&I managers are doing that by taking a hard look at customers’ lives beyond credit scores, such as payment histories, employment and significant life changes, and promoting strengths to lenders.

Programs such as Equifax’s Work Number provide the name of a customer’s employer, employment status, job title, job tenure, income and pay frequency.

“It’s designed to help dealers understand the consumers sitting in front of them but at the same time



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help consumers get a faster, more efficient transaction,” said Angelica Jeffreys, vice president and automotive dealer leader at Equifax.

Within the dealership, Jeffreys says, there are two points in the transaction when staff members verify income and employment: at the beginning of shopping to match the customer with the right vehicle and later in the F&I office, when a manager pulls the same information to submit to lenders.



**Reahard: Stories matter.**

Customers often arrive at showrooms without accurate income information in hand. For dealers, having access to a pay stub file means the customer doesn’t have to leave the dealership to get it, keeping the deal moving, says Blake Bailey, director of finance at Hennessey Buick-GMC in Morrow, Ga.

**“The bank only has a paper score.”**

Santosh Viswanathan  
Willis Ford in Smyrna, Del.

Dealers and vendors also can prequalify consumers for loans and show them underwriting options.

CreditMiner’s Basis software provides dealership websites a built-in application to prequalify customers. That’s important, CreditMiner CEO Don O’Neill says, because some customers who regret that they had no choice of lenders refinance their auto loans shortly after buying the vehicle. Basis enables a customer to see which of the dealership’s lenders prequalified him or her and what the rate estimates are.

Credit scoring agencies are doing their part to help low-credit-score and no-credit-score customers, too.

VantageScore and FICO have 13

scorecards, including ones dedicated to consumers with thin credit files.

About 10 million of VantageScore’s “new-score” customers are rated near prime or prime because the data are more predictive.

New-score customers are those who just entered the credit market, use credit infrequently, have no recent activity or have no open trades, VantageScore said.

**Conversation data**

Still, much of a customer’s story behind the credit score is often discerned through his or her conversations with dealership staff.

When an F&I manager at Hennessey Buick-GMC was working with a customer who had a mid-range credit score, the bank’s proposed interest rate on the loan was in the low teens, Bailey said. The customer men-

tioned that he had recently closed on a house but the closing was not yet reflected in his credit report, Bailey said. The F&I manager passed that information onto the bank because becoming a homeowner gives a loan

candidate more strength. The F&I manager figured out that if he added three months to the loan term and increased the down payment by \$250, the loan to value “hit a prime target within the lender’s scorecard,” Bailey said.

The interest rate dropped nearly 6 percentage points, and the monthly payment fell by \$60. “It’s a great feeling,” Bailey said. “It’s a good win for everybody.”

Bailey said after getting alternative information from programs such as Work Number, the structure of the loan and the dealership’s relationship with a lender play important roles. “I can call a lender and lay out the footprint of the deal and overshadow a low credit score or no score or any other issue,” he said.

Becky Chernetk, president of Chernetk Consulting in Cumming, Ga., agrees that the story matters. Banks want to know details about the customer if the customer has a credible relationship with the dealer, she said.

The story behind the numbers encourages the lender and the dealership to help the customer. “I can’t tell you how many times I’ve looked at a deal one way, but getting the story made it a completely different way of working the deal,” Chernetk said.

**Local connection**

Having a local connection to the customer boosts the likelihood that the shopper will receive the right loan offer, said Santosh Viswanathan, managing partner at Willis Ford in Smyrna, Del. Dealerships typically know what goes on in their communities, and many have long-lasting relationships with their customers. So if a well-known local company capsizes, and the customer did contract work with that company, the dealership will be able to explain to the lender that the customer’s low credit score is a reflection of that missed work.

“The bank only has a paper score,” Viswanathan said, but the dealership can share a tale with the lender.

Reahard agrees: “We have to take what’s happened in the customer’s life and tell a story. If it didn’t matter, everything would be computer-generated.” **AN**



**Bailey: Looking for a win for all**

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# How a salesman's kindness led teen to an auto career



Reahard restored this '71 Chevelle. It's close to the car he owned at 17, he says.

RON REAHARD

**A**s I searched for examples of extraordinary customer service by F&I staffers for today's Insight cover package, F&I trainer Ron Reahard of Reahard & Associates told me his own inspirational tale.

When Reahard was 17 years old in 1972, he bought a 1964 Oldsmobile 88 at a used-car lot for \$400. Fifty miles in, the engine started knocking. Staffers at the used-car lot had wrapped leather around the main bearing on the crankshaft.

When Reahard drove the 88 off the lot, it was quiet and smooth,

## COMMENT

but after those first 50 miles, the leather wore down and "the engine showed what it really was," he said.

Reahard went to Muscatell Chevrolet in Fargo, N.D., to trade in the car. The salesman there, Bob Kruse, said he could give Reahard only \$50 for it on trade because the engine wasn't worth anything.



**Hannah Lutz covers finance and insurance for Automotive News.**

"Never mind," Reahard said. "I'll sell it myself."

"Have you ever sold a car before?" Kruse asked.

Reahard said no but insisted that he would run an ad in the local paper. Kruse asked whether he'd ever placed or even written an ad before. Reahard said no.

So Kruse offered Reahard help. They wrote the ad together, after Kruse explained the paper's special: three lines for three days for \$3.

Reahard said he needed at least \$200 for the car, but Kruse suggested he ask for \$195. "It sounds cheaper, don't you think?" Kruse said. He also suggested Reahard add "or best offer" so that a potential buyer would know the price was negotiable. "After Bob helped me write the ad, we called it in right from Bob's office," Reahard recalled.

Reahard asked \$195 for the car and ended up selling it for \$125. It still wasn't enough for a down payment on another car, and the dealership could hold a car (with a \$100 deposit) for only three days.

Kruse said he didn't want Reahard to lose his \$100, so he said he'd put the 1971 Chevrolet Chevelle that Reahard wanted on a storage lot away from most customers' eyes if Reahard called him every day with an update on acquiring the down payment. Hopefully, the car would still be there when his down payment was ready.



**Reahard: Got help with ad**

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**"The reason I am in the car business is because I was treated well."** Ron Reahard

Reahard called every day, and after two weeks, he got the Chevelle, a two-door hardtop in Mulsanne Blue with a white vinyl top, a 350 V-8 engine, power steering and brakes, white sidewall tires and an AM radio.

Reahard put together the \$250 down payment for the Chevelle by combining the money he made from selling his clunker 88 and some tires and wheels he had with his next paycheck from his after-school job at a Standard Oil gas station, where he pumped gas, fixed flats and changed oil.

Reahard bought his next two cars from Kruse at Muscatell Chevrolet. When he bought a third car from the dealership, Kruse was gone. He had opened his own dealerships.

When Reahard was 20, Muscatell Chevrolet gave him his first dealership job. He says Kruse's influence guided not only his career choice but his approach to it.

"The reason I am in the car business is because I was treated well," Reahard said. Kruse "set the standard, the model I tried to live up to."

You may email Hannah Lutz at [hlutz@crain.com](mailto:hlutz@crain.com).

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# Manager's mantra: Just talk to people

Credit counseling includes a path to home ownership

**Amy Wilson**  
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It's tax season, and G.P. Anderson is a busy man.

"I'm just slammed," said Anderson, finance manager at Thielen Motors in Park Rapids, Minn. He's just completed a 68-deal week to finish his February. The tally on Saturday, Feb. 27, alone: 14 car sales, half to subprime customers.

A snapshot of Anderson's week:

■ Candice, 29, bought a 2012 Buick LaCrosse with 20,000 miles. It was her first car loan after always paying cash for high-mileage clunkers. She came in with her tax refund after attending one of Anderson's Credit on the Rez seminars last year at a local American Indian reservation.

■ Tabitha, a repeat customer with a tough credit history, bought her second car through Anderson. She had traded in her previous Thielen Motors purchase at another dealership for a replacement that broke down soon after and got her deeper into credit trouble. So she came back to Anderson.

■ Josh, Tabitha's boyfriend whose credit is worse than hers, wasn't even thinking of buying a vehicle himself. But he has a good income working construction. Anderson is working with him to obtain a car loan once Josh sells his existing vehicle for a down payment.

■ John, a 60-year-old with a credit score of 800, was prepared to write a \$50,000 check for a new truck. Anderson put him into a single-pay



G.P. Anderson teaches a credit seminar at the Leech Lake Reservation in Cass Lake, Minn.



## G.P. Anderson

**Title:** Finance manager, Thielen Motors, Park Rapids, Minn.

**Age:** 59

**History:** 17 years in F&I; 25 years in auto retailing

**Specialty:** Giving credit seminars and working 1-on-1 with customers to improve credit rating

**Advice:** Talk to customers and learn their stories; practice, drill and rehearse to improve skills; establish deep ties with lots of lenders.

lease, and John kept more of his cash in hand.

For Anderson, juggling a variety of customers — from the most credit-challenged to a well-heeled doctor — is all in a day's work.

"Everybody's got a story," said

Anderson, 59. "So you've got to be all things to all people. Just treat them fair."

Subprime buyers typically represent about half of Thielen Motors' buyers, Anderson said. The dealership's territory, in lake country

about 200 miles north of Minneapolis, is home to luxury resorts and pockets of poverty.

## Tax checks

Anderson sees his highest ratio of subprime customers in late winter and spring when tax refund checks arrive. Many ask for Anderson personally when they get to the dealership. They know him from the credit seminars he teaches at nearby reservations and local schools. Others are friends and family members of customers Anderson has helped get financing.

The latter describes Sheila Cook of Bemidji, Minn. Cook's sister just brought her second car through Anderson and referred Cook to him. In early February, Cook, 34, bought her first car in five years at Thielen Motors, obtaining her first vehicle loan ever.

"He's a wonderful guy," Cook said of Anderson. Anderson is now working with Cook on a plan to eradicate her old debt, build her credit score and prepare herself for buying a better car at a lower interest rate in a year or so.

Cook had been spending \$300 a month on taxi rides to get to and from work and to get her son to and from school. Now her car payment is \$236 for a 2010 Impala with 93,000 miles, she said. She used \$2,800 from her tax refund to buy the \$9,000 Impala. Cook's sister met Anderson at one of the credit seminars he did for the Red Lake Band of Chippewa Indians.

## Mortgage goal

"Now that I have my foot in the door, my goals are to keep up with my bills," Cook said. "I want to gradually make my way up with good credit and hopefully get a house in the future."

It's a realistic goal. Anderson says

he has put other customers on a path to home ownership. He has many who have bought three or four cars in succession from him. He counsels them on paying off debt and cleaning up black marks on their credit report.

"Their eyes go open," he said. "Nobody's ever shown them."

After time in the first loan, when the customers' credit scores have improved, he helps them trade up to a better vehicle with lower interest rates. Becoming creditworthy enough to qualify for a mortgage is often the end goal, and Anderson recalls being invited to barbecues by clients when they are finally able to buy a home.

"We don't treat the subprime customer, the near-prime customer, the nasty-credit customer any differently than a million-dollar-a-month plastic surgeon," said Anderson, who's been at Thielen Motors for 17 of his 20-plus years in the car business. "It doesn't matter. They've never been in a new-car franchise store. They've always paid cash for their car. They're nervous to even come into the facility because they've never been in a place like this before."

Anderson works to put customers at ease with a sense of humor. He's dubbed his office the "house of happiness," and has coached sales reps to park the car being purchased just outside his window to keep the customers excited about the vehicle.

**"We don't treat the subprime customer, the near-prime customer, the nasty-credit customer any differently than a million-dollar-a-month plastic surgeon."**

G.P. Anderson

With subprime, a finance manager is chasing addresses, phone bills, electric bills, disconnection notes. Strong ties with lenders are a must — Anderson says he uses 48 banks.

To "roll lots of iron, you've got to know what to do in a very quick, timely fashion and keep very organized," Anderson said.

Anderson developed his organizational skills early. His family ran a longtime grocery business, operating a store and a distributorship, before selling out when Anderson was 28. He has a colorful background: His father was a Minnesota state senator, and Anderson is a musician who plays nine instruments and was in a songwriting class with Prince, a fellow Minnesotan, in the 1970s.

Quick with a joke or a word to put customers at ease, Anderson said, "Shyness does not run in our family." One of his mantras is: "You've just got to talk to people."

His outgoing nature has paid off. Anderson has won numerous finance-and-insurance industry awards. And potential customers keep walking into his credit seminars and then to the dealership, this time of year often with tax refund in hand.

"Money follows service," Anderson said "Everybody wants to give you their money if you give them service." **AN**

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# What traits make a good F&I manager?

Insiders go for ethical, personable, accountable

**B**lake Bailey, finance director at Hennessy Mazda-Buick-GMC in Morrow, Ga., wants F&I managers who are warm, inviting, knowledgeable and adept at helping customers identify their needs. They also must be confident enough to overcome objections but not so confident that they come off as arrogant, he says. We asked some other industry insiders what traits F&I managers should have. Here's what they said.



**Becky Cherek**  
President, Cherek Consulting

"You have to have the desire to be ethical, credible. It's a white-glove position. You're dealing with the customer, with the bank, with the service department, the sales associate. Accountability, intuitiveness, assertiveness and professionalism are key." F&I managers should be "personable and caring. People pick up on that. They feel it."



**Santosh Viswanathan**  
Managing partner, Willis Ford, Smyrna, Del.

"I look for someone who has the same values ... as the company. You cannot train value, but you can train processes and procedure. I ask interview questions that relate to past experiences, something they saw around them that wasn't right. We all have adversities. [It's about] how you handle them."

**Andrew Calderon**  
Finance manager, Toyota of Butte (Mont.):

"The majority of people I hire are people who work at the front desk at a hotel, for example. You get to see them in action. I've

hired a couple people from Starbucks, and they're great salespeople and service writers. If I'm unhappy that they only gave me one shot of caramel in my coffee and I complain and they give me an extra shot for free, I know they'll go the extra mile. Also, if they tell a joke during the interview, that is likability to me, and that will cover everything. You hire character and you train skill, so that's how I go about that."



**Lycia Jedlicki**  
Performance partner for 20 group operations, NCM Associates

As an F&I manager "you're kind of a counselor. You become a confidant with that person. You really want an ethical person there. Dealers need somebody who's going to cover them and make sure that they are compliant."



**Renay Winston**  
President, People Management Solutions, Marietta, Ga.

Dealers "are looking for a more energetic person" for F&I. "People tend to be more guarded and on edge when they go into the finance office. When it comes down to financing, it becomes an adversarial conversation. It's very important to have someone with the personality to bond with the customer."

**G.P. Anderson**  
Finance manager, Thielen Motors, Park Rapids, Minn.

"You have to have unbelievable personality skills, character skills, be able to understand character types, personality types, look past the human foibles. And you have to be able to do that in two seconds."



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"Credit Acceptance gives me the opportunity to help my customers get back on their feet, improve their credit, and purchase a new vehicle from me down the road. I use the program both as a profit center, and as a stepping stone to transition credit-challenged customers from one of our pre-owned vehicles into the car of their dreams. Credit Acceptance helps me sell more cars...on both sides of my business."



**Troy Duhon**  
Premier Automotive (LA)



# First, take auto finance course, then get the loan

Store, credit union aim to help 1st-time buyers succeed

**Nora Naughton**  
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Picking out and financing a vehicle for the first time can be a tricky task, but one used-car dealership in Michigan is rolling out a program to make the process a little less daunting.

Viers Auto Sales in Lapeer, Mich., has teamed up with a local credit union to run a crash course in auto financing for young, first-time buyers.

The First Time Auto Buyers Program, which is headed by Viers' sales and finance manager, Chris Babcock, aims to help young people leave the lot with more manageable payments and to create a pool of long-term customers.

"We used to always have young adults come in without a co-signer or without a sizable down payment, and in those cases, all we could offer were these unfavorable interest rates," he said. "We were just setting them up to fail."

Babcock teaches a "buyer's training" course, which can be taken in a classroom or online, with Amy Ford, Team One Credit Union's community relations representative in Saginaw, Mich.

Students learn about building credit and financial responsibility and are even required to prepare a written budget. At the end of the course, the potential buyers are tested on their ability to manage the loan they might qualify for.

Those who complete the course must meet five underwriting requirements to qualify for a low-interest rate auto loan, including job and income minimums, according to the course brochure on the [viersautosales.com](http://viersautosales.com) website. (See box, right.)

"It's not easy, but it's not supposed to be," Ford said of the final exam and qualification process. The students are required to "show a real sense of responsibility as well as an understanding of just how serious it is to finance a vehicle."

Babcock and his team encourage course participants to take things slowly. Sales representatives cannot allow their customers to start and finish the course in one day, and younger buyers are asked to bring their parents to the class.

"We've gotten the most overwhelming positive feedback from the parents so far," Babcock said. "Getting them involved really keeps the ball rolling."

Viers Auto and Team One Credit Union launched the buyer's training course on a pilot basis in September.

"It's a little too early to tell how successful this will

## Path to success



To be eligible for a low-interest loan under the Viers Auto First Time Auto Buyers Program, participants must complete a buyer's training course and meet 5 qualifications

1. Must have a valid Michigan driver's license and be 18 years or older with no derogatory credit, excluding medical bills
2. Must have 3 months' minimum job time — 6 months for temp jobs — with no more than 2 jobs in the last year
3. Income must be verifiable. Cash and seasonal jobs do not qualify.
4. Must have a gross monthly income of \$1,235 or higher
5. Must meet Team One Credit Union membership requirements

end up being, but I can say that we have had absolutely zero delinquencies since the program went live on Sept. 1," Babcock said.

As far as building a new pool of long-term customers goes, he said the effects of the program already are apparent.

"Starting in about the middle of January, the referrals really started picking up," he said. "We're earning the trust of these young buyers, of their parents, of their siblings and of their friends. That's a huge deal for us."

If the 18- to 24-month pilot proves successful, Team One will consider rolling it out at other dealerships in the area, but only at select stores. The partnership with the credit union works only if a dealer has an honest staff to run the show, Babcock said.

"The credit union has given us a lot of authority here," he said. "You need a team you can trust." **AN**

"Our goal is to help them get back on their feet."

Rich Hyde, COO, Prestige Financial Services

# Auto lenders work to lift borrowers out of subprime

Employees and programs act as guides

**Hannah Lutz**  
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Many dealership F&I managers advise customers on credit decisions that would suit them best over the duration of their vehicle ownership. But auto lenders, especially those whose portfolios include subprime borrowers, are providing guidance, too.

Subprime borrowers, typically those with credit scores of 600 and below, often have bruised credit as a result of a low-income job or a significant life event such as divorce. Some auto lenders have the goal of helping those borrowers re-establish their credit. Among them are Prestige Financial Services in Salt Lake City; Exeter Finance Corp. in Irving, Texas; and Ally Financial Inc. in Detroit.

## No-repeat goal

Prestige's goal for borrowers is for them to move beyond the subprime tier, Rich Hyde, the subprime lender's COO, says. Prestige walks customers through their loans and emphasizes the importance of making timely payments. The account manager with whom the customer works when the loan is originated stays with the customer through the life of the loan. "That person understands their situation and helps them through" any problems, Hyde said.

Although it's more expensive to have the same manager assigned to the customer for the duration of the loan, "it's for the benefit of the customer and to Prestige," Hyde said. Many subprime borrowers have recently divorced or filed for bankruptcy, he said, "Our goal is to help them get back on their feet."

But Prestige, a unit of auto dealership group Larry H. Miller Group of Cos., isn't looking to have repeat customers. That would mean it didn't do its job right. Borrowers "say thank you and move on," Hyde said. Prestige doesn't want them to be subprime customers again.

Prestige also has an interest rate-reduction program. When customers make payments on time, their rates are reduced and their credit scores improve.

## Free monitoring, tips

Exeter, another subprime lending specialist, also has a program to help customers learn about and improve their credit. It offers borrowers a free online financial literacy program to help them understand and manage their finances. It includes credit score and interest components, financial goal planning and monthly budget guidelines. Borrowers who complete the program are eligible for six months of free credit monitoring, an Exeter spokeswoman said.

Ally, though mainly a prime lender, offers Wallet Wise, a website with free financial literacy information about budgets, credit, banking, investing and auto financing. The lender offers occasional in-person Wallet Wise community forums and shares tips each week on its Twitter channel @ally.

Ally also teamed with the National Association of Minority Automobile Dealers, giving dealers a brochure for their customers with 10 tips for financing or leasing a vehicle. The brochure and other planning tips are available at [allywalletwise.com](http://allywalletwise.com). **AN**



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# Leasing is pressuring F&I? Depends on dealer

Stores can make money by changing product mix and mindset, experts say

**Jamie LaReau**  
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**M**ore consumers are leasing vehicles, and that could mean a drain on profits in F&I offices. But it doesn't have to be that way.

"Leasing can have either a negative or a positive impact on F&I profitability depending on the approach a dealer takes," said Marie Knight, vice president of strategic relationships at F&I product provider Zurich North America. "The important thing is to offer products that are tailored to lease customers."



**Calderon: "A huge benefit"**

Take Toyota of Butte in Montana. More than a third of the dealership's finance deals are leases, yet its F&I profit is rising. "Leasing is a huge benefit to F&I," said Andrew Calderon, finance manager. "It just depends on how you look at it."

If the customer buys the vehicle at lease end via a new loan, "that's my biggest payer of any customer who walks through the door," he said.

For dealers, taking a positive, long-term approach to lease customers may become vital. Edmunds.com analysts estimate leasing will climb 1 percentage point to account for 30 percent of U.S. new-car sales this year, compared with 22 percent five years ago.

To make money on lease deals, "the F&I manager has to take the time to explain what the manufacturer's warranty does and doesn't cover," Knight said. "There are



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products that address every one of those areas that could be offered to lease customers." (See box, above.)

Lease deals could dent F&I profits

because for most F&I managers, the two best-selling add-ons, extended service contracts and guaranteed asset protection (GAP), are typically off the table, says Dave Duncan, president of Safe-Guard Products International in Atlanta.

A leased vehicle is often protected by the manufacturer's warranty for the life of lease, so the customer rarely sees value in buying an extended service contract, which has a wide profit margin. And nearly all manufacturers include GAP as part of the lease, Duncan said.

J.D. Power data released in November show that just 18 percent of premium customers buy an extended warranty when it's offered compared with 30 percent of nonpremium customers. That broad disparity most likely is because "leasing is more common among premium customers than nonpremium," J.D. Power's report said.

Still, leasing is rising across all makes. As a percentage of new-vehicle financing, leasing reached an all-time high of 34 percent in the fourth quarter last year; in the fourth quarter of 2011, it was 23 percent, according to ExperianAutomotive's "State of the Automotive Finance Market Fourth Quarter 2015" report.

## Steady needle

So far, as leasing has grown, F&I managers have kept profits intact, likely helped by robust growth in new-car sales industrywide.

Last year through November, F&I product sales accounted for about 16 percent of a new-vehicle sales department's gross profit, up 2 percent vs. the first 11 months of 2010, says Steven Szakaly, chief economist for the National Automobile Dealers Association. Financing profits represented 23 percent of new-vehicle gross profit through November last year vs. 18 percent in the 2010 period.

U.S. light-vehicle sales rose 51 percent from 2010 to 2015, according to the Automotive News Data Center.

"Leasing has been climbing in this [five-year] time period, and

## Lease menus

To keep F&I profits intact as leasing rises, some F&I managers sell protection products on vehicle parts the manufacturer's warranty doesn't cover. Those products include

- Maintenance plans for oil changes and tire rotations
- Paint protection against environmental damage, dents and dings
- Interior protection against rips and stains
- Tire-and-wheel protection

while it has moved the needle a little bit, it hasn't moved it much in terms of [F&I product sales] and financing profits," Szakaly said.

But if car sales slow and leasing continues to grow, F&I managers ill-prepared to make the most of lease deals could see F&I profitability decline, said Safe-Guard's Duncan.

Duncan said his company began getting more requests for training to sell F&I products to lease customers about three years ago, as the lease penetration rate was rising about 10 percent year over year at the average mass-market dealership.

"That 10 percent rise in lease penetration per year over three years" could have cost dealers "a \$100 to \$250 per-car loss in F&I profits" over that time frame, Duncan said.

## A new mindset

The ones who win are those who change their mindset about lease customers and change the mix of products presented to them, he said.

At Toyota of Butte, leasing accounts for about 35 percent of financed deals, up from 20 percent two years ago. In the past two years, the store's average F&I revenue per vehicle retailed has increased from \$800 to \$1,200.

F&I Manager Calderon faithfully follows "the 300 percent rule" to ensure success: "Offer 100 percent of products, 100 percent of the time to 100 percent of customers."

For example, if a customer on a three-year lease plans to drive 15,000 miles a year, he or she may be receptive to an extended service contract because Toyota's warranty covers just 3 years/36,000 miles. A service contract wrapped around the manufacturer's warranty in this case would cost about \$1,000. "They see the value of it, and I'll take a discount to sell it," he said.

Calderon's best-selling product to lease customers is excess wear and use protection, which costs about \$800. Around 95 percent of lease customers buy it.

Many F&I products allow dealerships a substantial retail margin, Duncan said. One high-profit product designed for lease customers is Safe-Guard's Precision Care. It covers belts, hoses, lightbulbs, wiper blades and one set of brake pads. Precision Care costs dealers \$300 to \$450 but retails for \$699. About a quarter of U.S. dealers offer it. Said Duncan: "As leasing grows, more [dealers] are wanting it." **AN**

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# Used-car values, residuals, leasing linked

When prices fall, you had better be ready to recalculate the others

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The substantial uptick in off-lease vehicles returning to the market this year will put downward pressure on late-model used-vehicle prices and residual values, analysts agree.

It's anyone's guess when used-vehicle prices will drop appreciably. Many analysts had thought it would happen last year, but strong new- and used-vehicle demand and low interest rates buoyed prices.

But when used prices fall — and they will — lease residuals and trade-in values will follow them down, robbing some consumers of the equity in their trade-ins. And some automakers will have to recalculate the costs vs. benefits of the leases they have been subsidizing through their captive finance companies.

To compensate, automakers likely will either boost the amount they spend on new-car incentives and subvented leases or pull back on leasing through their captives.

Joe Spina, director of remarketing at Edmunds.com, predicts that leasing will either plateau or dip a bit this year. He says competitive one-upmanship among automakers to gain and keep market share will keep leasing from falling dramatically, but it won't continue to grow.

Spina believes that finance companies are expecting higher residual losses based on the higher number of vehicles expected to return to the market. Though they have set aside funds to cover those losses, he said, the companies will want to mitigate future losses. Also putting pressure on finance companies is that they are financing more vehicles in general.

## Scale back leasing?

"I think they will start decreasing residuals in their forecast to intentionally scale back a little bit on the leasing penetration; that's a lot of leasing," Spina said. "At the same time they are financing more cars, and some of



Dealer Rick Case predicts leasing will remain strong as a result of manufacturers' incentives.

those deals aren't great, so they've got credit risk, too. So they've got these two big buckets of risk.

"If you look at those two things as a stand-alone item, that sort of forces their hand to ratchet back [on leasing]. We definitely expect them to do that this year."

Eric Lyman, vice president of industry insights at TrueCar and its ALG division, sees it a bit differently.

Lyman said ALG's residual value forecast for 2015 model-year vehicles returning to the market in 2018 is in the 48 to 49 percent range, which is higher than the typical 45 percent range the company has seen over the years.

He also said he expects the supply of 1- to 5-year-old used-vehicles to increase 10 percent year-over-year in 2016, 2017 and 2018, reflecting the industry's strong sales in recent years.

Lyman agrees that used-vehicles prices will soften this year, but he expects residual values to remain "well above long-term historical averages" and leasing to remain strong.

He said leasing benefits the auto industry because manufacturers know exactly when

lease consumers will be back in the market and the dealership for a new vehicle. That promotes customer loyalty, he said.

So automakers are purposely engaged in aggressive leasing strategies, part of which involves shifting funds to cover possible residual shortfalls from their traditional marketing budgets to their variable marketing budgets, Lyman said.

## Funding leasing

"That means throwing money that you otherwise would have used on another TV advertising campaign or some sort of dealer campaign and using it to support a higher residual to get a lower payment for a lease customer," he said.

"Not only am I getting that person into the showroom today to lease that vehicle, I'm going to get that person into the showroom in three years. I might have a new product for them in the same segment or another segment to dangle in front of them to get them into another vehicle from my brand."

It's not just lease customers who are impacted by falling used-vehicle values. More finance customers are likely to be "upside

down" — a term for owing more on the loan than the vehicle is worth — on their trade-ins.

Melinda Zabritski, Experian Automotive's senior director of financial solutions, said there are "many possibilities" for those consumers.

Some consumers may have to switch from a new vehicle to a used one, or manufacturers may have to up the new-car incentive ante to keep buyers in the fold. Consumers may have to dig a little deeper for heavier down payments, too, she added.

Though loan-to-value ratios have loosened a bit, don't expect many lenders to finance negative equity that pushes those ratios over 100 percent, she cautioned.

"You'll readily see LTVs over 100 percent to allow for taxes, titling and licensing, after-market services and warranties, but many lenders have policies that the amount that pushes it over 100 percent cannot be negative equity," Zabritski said.

"Some lenders will finance it, but many lenders will not."

## More for less

Dealers are keeping a watchful eye on leasing, too.

Rick Case, CEO of Rick Case Automotive Group in Miami, predicts that new-vehicle sales will grow, though at a slower pace than we have seen in recent years, and that leasing will remain strong, as a result of manufacturers' incentives. That's a good thing for lease consumers "who can drive more car and pay less per month," he said.

It's not bad for dealers such as Case, either.

He operates a robust used-vehicle operation and buys "virtually every" off-lease vehicle that rolls back onto his dealership lots, he said.

The used vehicles he sells are warrantied either under an automaker's certified used-vehicle program or his own in-house program, which covers most noncertified used vehicles — all domestic and Asian brands plus Volkswagen — that are up to 8 years old and have fewer than 80,000 miles with a 10-year/100,000-mile powertrain warranty.

Case said: "One great thing about a lease return is you [have the opportunity to] sell another new car." **AN**



Zabritski: "Many possibilities"



# by the numbers

## Quarterly scorecard

Rising new-vehicle sales are only part of the story behind climbing F&I profits. Per-vehicle revenues also are rising generally. Here are the public dealership groups' F&I gross profits per new vehicle retailed. Figures are on a same-store basis unless noted otherwise.

DEALERSHIP GROUP	2014				2015				ALL 2016 EST.*
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
Asbury	\$1,330	\$1,331	\$1,334	\$1,371	\$1,365	\$1,373	\$1,362	\$1,426	
AutoNation	\$1,401	\$1,395	\$1,403	\$1,447	\$1,515	\$1,528	\$1,549	\$1,556	
Group 1**	\$1,476	\$1,461	\$1,463	\$1,525	\$1,529	\$1,525	\$1,518	\$1,518	
Lithia***	\$1,181	\$1,202	\$1,203	\$1,260	\$1,233	\$1,280	\$1,274	\$1,330	\$1,210
Penske	\$1,100	\$1,112	\$1,096	\$1,069	\$1,100	\$1,127	\$1,123	\$1,205	
Sonic***	\$1,206	\$1,211	\$1,207	\$1,255	\$1,254	\$1,268	\$1,274	\$1,321	\$1,400

\*Guidance provided by company \*\*U.S. dealerships only \*\*\*Figures are for all stores. Source: Companies

## F&I penetration rates

How does your store stack up against these penetration-rate percentages from 2 publicly traded dealership groups? Figures reflect all new and used units sold at retail.

Group 1 PRODUCT	2011	2012	2013	2014	2015*
	Financing	70%	71%	69%	67%
Service contracts	36	37	34	34	40
GAP	22	22	22	24	28
Maintenance plans	8	8	8	9	12
Sealant	12	14	15	18	19

Note: Penetration rates are for all stores.

\*2015 penetration rates are for U.S. dealerships only.

## Lithia

PRODUCT	2013	2014	2015
Service contracts	42%	42%	43%
Lifetime oil contracts	36	37	25*

Note: Penetration rates are on a same-store basis.

\*Lifetime oil contracts figure for 2015 diluted by DCH stores acquired in late 2014 that introduced the product in 2015.

Source: Companies



## Used-only F&I

F&I results at Sonic Automotive's used-only EchoPark stores trail those at the company overall but are improving.

EchoPark	ALL 2014	Q4 2014	ALL 2015	Q4 2015
F&I gross profit/unit	\$905	\$905	\$943	\$1,047
Sonic stores*	ALL 2014	Q4 2014	ALL 2015	Q4 2015
F&I gross profit/unit	\$1,227	\$1,260	\$1,288	\$1,330

\*Figures are on a same-store basis. Source: Sonic Automotive