Financing in the Sales Process

Understand Flexibility and Power

Creating Sales Opportunities Using Financing Programs

Financing and the use of credit in consumer retail selling can have many effects on contractors, mostly positive, some negative (if not managed properly).

Let’s examine some of those areas in this article, and help with the understanding of how you as a contractor may choose to use credit and financing as a strategy to increase your sales, gross profit dollars and ultimately your profitability!

Here are some basic questions all contractors should understand:

* What is financing?
* What is granting credit?
* What are consumer promotions and how do they affect you?
* Should you carry the paper on loans?
* What are extended warranties and how do they affect you?
* Are there negative consequences with using financing?

**What is Financing?**

Financing is simply the process of allowing a customer to extend the payment of any product or service beyond the immediate cash transaction or sale.

A financing process allows the current total selling price to be deferred in installment payments based on an agreement. There must be a financing company/entity that carries the risk. The contractor gets paid quickly by the financing entity usually within a three day period, after paperwork is approved by the financing company.

Benefits of this concept:

* Financing creates additional leverage, or what we call IMMEDIATE buying power by allowing a customer to use future earning power to pay for the purchase of goods/services today.
* The **financing company assumes the risk** of carrying the financing of the homeowner so you do NOT! The financing company can spread this risk over a wide range of customers some of which will be bad risks, or default, and the vast majority of which will pay their bills.
* Cash flow is quick, and there are no collection procedures, as payment is made within 3 business days or sooner.
* Consumer’s want and many NEED credit, so having a financing arrangement set creates comfort, professionalism, and promotes an ease of doing business.

What is Granting Credit?

And is it different than financing?

The idea of granting credit is extremely important when selling high cost, or large ticket items. Appliances, such as a “Total Comfort System” in HVAC and home related plumbing products fall into this category. These are appliances we know as brown goods.

Most consumers are used to the idea of having “White Goods”, items such as refrigerators, dishwashers, and washers & dryers sold to them from large box retailers through terms of credit. Behemoths like GE Financing or Citi-Financial are common in these areas and work with large retailers like Home Depot and others. Some big box retailers underwrite their own credit such as SEARS.

So when we speak of granting of credit, we are including the process of consumer financing, but we are also INCLUDING the idea that you as a contractor must have a means of creating credit for that customer.

There are two basic ways to accomplish this:

1. Have a 3rd party company (EGIA) create/grant/issue credit.
2. Do it yourself and carry the paper, and the risk.

The vast majority of HVAC and Plumbing contractors use a 3rd party as a source to grant credit. However, there are those contractors who have decided to take the additional risk and responsibility to increase the profit potential that can be made through the interest rate assessed on the carrying of credit.

There is “Additional” profit to be made from carrying the credit risk, although this needs to be balanced with the list of issues below that come with that potential profit.

**Issues With Credit**

1. Risk factor in providing credit – Bad debt potential.
2. Method of researching credit history to assess the risk.
3. Collection processes that accompany a consumer note payable.
4. Administration costs to manage notes payable.
5. Various state laws for those who grant credit.
6. Understanding the legal ramifications of granting credit.

Most financing companies charge an interest rate of some percentage of the credit being granted. Promotions often are integrated into the process of granting credit, to buy the costs down for the end consumer in an effort to sell more.

Third party credit providers, such as EGIA, may offer lower rates from time to time, or vendors may elect to pay EGIA a portion of the costs of credit.

This creates a lower cost for the retailer to use the program. Contractors will get a vendor coming to them with a $ 1,000 rebate, and 6 months no interest, no payments on selected equipment. This is a specialized promotion tied to a credit process.

These are referred to as Buy-downs/Rebates/Financing costs and are used regularly in periods of slower sales, in combination with other promotions to allow local retailers to sell more, advertise more, and generate leads.

1. Not all consumers will qualify for these programs.
2. Those that do not, are disqualified for varying reasons.
3. Lack of credit rating (cash buyers with little or no history).
4. Lack of Good Credit history – Meaning a bad history.
5. Previous bankruptcy filing in the history.

So this brings us to the kinds of credit there are relating to contractors and business owners, and how we deal with these issues, knowing full well if we DO NOT find a financing alternative for the prospective customer, someone will!

1. **Tier 1** (68-75%) – Consumer Financing – Non-collateralized – Standard Rate (8-15%).
2. **Tier 2** (10%) – High Risk Financing – Non-Collateralized – High Rate (18-30%).
3. **Tier 3** (12-14%) – Collateralized Note Payable – Such as Home Equity, or establishing a form of an asset, car, and house, something of value to a bank to back the risk of the note in case of default.
4. **Tier 4** (1-3%) – Deadbeat – No form of credit makes sense to anyone – Record indicates a poor risk no matter what the payment terms are, so no one is willing to underwrite the excessively high risk of fraud, theft, or bankruptcy potential.

Credit Granting Services:

Those 3rd party credit providers that underwrite credit and take risk use credit tracking agencies to support their “Business Processes” to make specific conclusions about granting credit.

1. They use a rating service to conduct credit scoring.
2. They have detailed statistical models of those consumers that are not immediate yes candidates, to plug credit details into the model, to predict the statistical risk of granting credit. They use this to create approvals and turndowns. Which is why only 68-75% of the Tier 1 group gets approval through a promotional offer, because that is the percentage of the US population that meets the criteria, and how the credit provider makes money and minimizes risk.
3. Those that score outside of the range are turned down, which then forces the retailer to seek alternate means of providing credit. Meaning Tier 2-4 type financing options must find a credit provider willing to create an interest rate that meets the increased risk.

These processes are honed, but are far from perfect.

For example, a person who is a cash buyer and has been for many years will show no history of credit paying ability. The credit provider will search for this history, and lack of history creates a risk factor that ends in a red flag. Are you a thief, a drug dealer, and why do you not behave like most other Americans? So the immediate red flag goes out to the retailer as a turndown, causing frustration in many cases.

Example: My father, a depression era child, has never owned a credit card in his life, has always paid cash, and has for the better part of 30 years not had a mortgage, or needed credit.

Should you offer him a promotion he accepted, and credit provider used a search agency such as TRW, to locate a credit history, there would be none. This could result in a turndown due to insufficient credit history. This does happen and is why you need multiple sources of credit.

My father would accept the 6 months no interest no payments, then pay off the credit note after the term of six months was up, effectively using other people’s money, which the EXACT reason you offered it in the 1st place, so he would buy from you!

Consumer Promotions – How Do They Affect You as A Contractor?

**Simple – Credit is a sales tool**.

**Consumer financing promotions effect your company, positively if you aggressively**

**use them, negatively if you do not because you are LOSING sales to those who do.**

We sell 4 things:

1. Ourselves.
2. Our company reputation and credibility to create trust.
3. Our products/services including warranties and guarantees to support our company brand.
4. The Money – Which is the price to value relationship, and the ease of how money is handled in the sales transaction (Credit/Cash/Financing/Special Promotions & Incentives).

Retailers understand these four principles and neglect none of them.

Many contractors understand 1-4 yet neglect number 4 in the worst way!

Offering credit is mandatory, early and often in the selling process.

About 85% of US population WANTS to use credit, and a large majority of that 85% NEEDS to use credit due to financial constraints in their personal lives.

I recently read one contractor who wrote that in his region in the West, the mix of demographics dictates that financing is not important. Translation, because it is not important to him it is not important in this region or demographic. So his community is represented by a cluster of ONLY those people in the 15% who do NOT want credit ease when buying?

Why are you making your customers decisions?

That same contractor also wrote that financing was only presented at the end as a closing tool because it cost him a few percentage points in use of credit, and it was administrative intensive.

It does cost a few percentage points, but how many jobs are lost because the consumer who needed credit, was NOT listening to you because while you told them how great your company is, they couldn’t rationalize how to afford you, so they were NOT listening to your benefits while they were considering how they were going to afford your great benefits? Think about it!

In addition, a company that does not promote financing as a primary source for buying from you, will NOT get a call from those who need it or want it (85%). So while this contractor may be saving a few percentage points, he is losing hundreds of thousands, if not millions of potential sales to those who simply take a simple approach to credit.

*Learn to promote it and grant it!*

In that same city out west where demographics dictate relative unimportance, I personally know two wildly profitable contractors that each sell over 10 million a year, and financing plays a major role in their selling strategy – up front – early and often.

They both finance over 70% of their jobs.

**Financing is a lead generator and a selling tool!**

**Consumer promotions are lead generators and selling tools!**

**Specialized Financing and promotions create leads and open up doors!**

Can you imagine SEARS without credit card?

That DOES NOT mean people with assets will carry the note, they may elect to pay it off early, or upon term like my father, but smart money people use other people’s money when they can.

How do You Use a Consumer Financing program in Your Company?

There are a variety of ways to use promotions.

Most contracting companies are not retail focused. This means they are focused on the technical work, and are not effective at marketing and generating leads.

To be a retailer, you have to embrace the power of consumer credit, in this case, special financing programs and promotions that draw consumer interest.

**$1000 INSTANT Cash Rebate**

**0% Interest for 12 Months**

**No payments No Interest for 6 Months**

**3, 5, 7 10 YEAR Financing**

**& FULL 10-12-16 Year Parts/Labor WARRANTY**

It doesn’t matter what you’re selling. There are always consumers in the market for products and services. HVAC, Plumbing, Solar, Renovation, Home Remodeling, you name it. Savvy marketers understand these consumer promotions create a reason, a call to action to call the company making the offer.

Does it cost money to use these financing or promotional offers?

**YES!!!**

Do they create more leads and sales?

**YES!!!!!!**

Would you rather have the extra leads and sales and pay the 4-5% of the sale, or simply not have the sale?

**The Promotional Budget**

Each year, at the beginning of your calendar or fiscal planning year, you sit down and create a budget. Within that budget you establish a chart of accounts.

Buy-down / Rebates / Financing Account

It is a cost of sale, or Cost of Goods Sold.

Just like Direct Labor, it belongs as part of the sales related costs. You budget a small percentage on each job, exactly the same as gasoline companies do when we buy gasoline for our cars. You used to be able to pay cash and get a discount. No more! Now, everyone pays the same price, and the cost of credit is baked into the sale price whether you pay cash or not.

This is the same concept.

We want you to consider a small percentage as a budget amount, ours is about 2% of 1,000,000 or $ 20,000 to offer promotions on our OWN calendar when we need leads, and to offer financing programs as a matter of sales closing tools ALL the time.

The 2% budget across all jobs does raise our price by the costs plus our desired markup, but we find during the peak selling season no one notices or cares, allowing us to be extremely aggressive when it is a slower season, or demand has slowed for our products and services.

So when we offer a financing promotion like 12 Months 0% Interest, that may cost us 8% of the sale price, but we DO NOT have to raise the sale price during the very time we needed to be aggressive in the market, because we budgeted a small 2% reserve during the year, and recovered the expense across many previous jobs.

**The Planned Promotional Calendar – Tied to Consumer Promotions**

Just as we said moments ago, we plan to be slow. We KNOW we are going to slow down. So we have a planned marketing calendar that coincides with our marketing budget.

Lead tracking tells us we are going to get so many service leads from our technicians.

So many maintenance leads.

So many water heater leads.

We never have enough leads to cover our sales plan, so we have to market some, and so do you. During slower periods, you have to be creative and aggressive.

The budget we spoke of above is there to allow you to think creatively BEFORE you are in PANIC mode!!!! Panic leads to poor decision-making.

You may NOT follow your plan exactly, we rarely do, but we find having thought about how we may use financing and rebates, and consumer trips to HAWAII, and incentives that draw consumer interest makes us smarter during panic mode.

We call it rearranging the deck chairs while the boat is on fire!

It’s not good.

So you have to create the “Consumer financing budget”, then the plan to use it.

Manufacturers

Manufacturers have good intentions.

They create promotions. They offer buy downs on costs of financing, usually around ½ the overall cost.

This is good!

If a program costs 10% to run through the financing company, they pay 5% leaving you the burden as a retail contractor for the remaining 5%.

What’s not so good is they usually tie this to the high end products only. They limit the timeframe to when they are slow, and they limit the type of product that can qualify.

This is not good!

Have you ever had a real retailer selling you an appliance tell you ONLY the expensive refrigerator qualifies for financing…NOT! Why? They don’t care because they can sell benefits. So they DO NOT limit!

Manufacturers are scared to death we cannot sell the higher end benefits, so they do not want to offer financing and promotional offers on all equipment afraid their budget would bust!

We have battles all the time with the manufacturer about their rules and how they want to limit how our promotions are run. We respond by saying, guarantee us the leads and sales and then tell us when and how to promote! Otherwise, let us be retailers, you can be manufacturers and distributors.

* You as a contractor make less money on the low end.
* It is to your benefit to sell the higher end product and install it in the same labor hours, maximizing gross profit $ per man-day/man-hr.

So we promote them all – Despite our manufacturer friends protests!

If you are a retailer, you have a budget and have planned for the panic of fire on the boat.

You can NOT raise the price of the job and expect to be aggressive!

If you are a contractor technician and raise your price by the 5% to cover your increased cost, you failed to plan for the promotion, and two things will happen:

1. You raise the price 5% and become less competitive and frustrated
2. You simply do NOT participate because you DO NOT want to raise your price to become uncompetitive, and now you are in effect NOT competitive during a slow time with a retailer who planned for the fire!

Remember that manufacturers are notorious for promoting high end, higher efficiency boxes, water heaters, and all manner of products and try to limit their dealer’s use of promotions. Do not let that happen to you. Plan and use promotions in your marketing and sales strategies.

Are there negative consequences with using financing?

The answer is Yes!

**Be aware of the negative potential and avoid the pitfalls.**

1. **Financing requires you to be able to track accounting flow** – You have to be able to know what paperwork and CASH you have out there at the financing company. Countless times we have seen contractors who are marketing oriented and do a great job of selling using financing as a tool, but are weak at paperwork, or the administrative side and simply have not submitted the proper documents to get paid by the financing entity.

This above itself is not a negative, regarding financing or credit, but is a real issue that needs to be dealt with if your company is to use retail financing and consumer promotions so you get paid and do not negatively impact your cash flow.

We have had contractors argue that there is an administrative burden that adds costs to conducting business. Once again we agree and this is true, however, because we will sell more gross profit dollars per man hour by securing additional leads and sales, the advantages to offering financing, rebates, consumer promotions and credit in general far outweigh the cost burden, and in the vast majority of cases adds very little to the administration of a company. In fact we even find that it lowers overhead as a percentage due to increased average sale prices, increased closure rates and simply spreading overhead over more jobs (leverage).

1. **Financing does cost your company a percentage to use it.** This MUST be COSTED and accounted for in your pricing practices.

There is absolutely NO question you will sell more jobs by offering financing early in the in-home sales process, even in a pre-sales call letter that notes financing options, or at dispatch function, but it does cost the company a small percentage to offer the convenience.

It must be accounted for as a cost properly, through the budget process and having a chart of account as discussed earlier.

1. **Consumers will wait on the promotion and be used to a deal.** This is also real! If consumers are used to retail programs in the market, they get smart and wait for the promotions. I do it for tires, tools, and all manner of consumer goods. So it becomes the double edge sword.

The simple fact is, even if this is the case, then you are losing out on potential leads and sales because if you DO NOT aggressively market financing, then how do you capture those customers who ARE waiting for the deal?

This is a cost, and a negative, but it is once again worth the price of having to offer financing options.

In the end, the positive aspects of offering strong consumer financing programs, and consumer related promotions far outweigh the negatives.

* You DO have to plan for the cost.
* You DO have to create a chart of account for tracking and budgeting.
* You DO have to plan ahead.
* You DO have to think about what your customers want.
* You DO have to create a calendar and support the marketing.
* You DO have to offer it to the customer in the early stages of retail selling.
* You DO have to THINK like a RETAILER, not like a contractor.

How do you use Consumer Financing and Promotions?

1. Commit to the idea that credit is crucial in the sales process.
2. Commit to the idea that offering financing and promotions EARLY and OFTEN is a step in the selling process and build it into your standard operating procedure.
3. Establish a chart of account in your accounting general ledger that is called, rebates/financing/buy-downs which is pre-planned, soon to be budgeted expense for your use of creative financing and credit costs.
4. Budget for the cost associated with financing programs, credit, extended warranty, and consumer promotions.
5. If you installed 200 jobs in a year, at an average of $3,000 a job that would be $600,000 a year in sales. In step # 4, we are going to estimate that the average cost of credit in a year’s time, across all our promotions, is 2% of the price of the job. So we are going to budget in the year, for 2% of $600,000 or $12,000 in our cost of sales, across all 200 jobs.
6. This forces us to raise our price $ 60.00, so our new price is $3,060. This covers the cost of the predetermined budget for credit/rebates/financing/and buy-downs that we may elect to use during slower periods. We no longer have to raise our price by the cost from the vendor.

Old example – If I were to use a vendor program that cost me 5%, and they paid 5%, to offer 12 months no payments no interest, I would have had to raise my price from $ 3,000, to $ 3150, during the very time that I was slow to begin with. That is a bit counter-productive if not outright questionable from an ethics standpoint!

1. Establish your new prices, so the credit, financing, rebates, extended warranties are part of the overall package. It is much easier to discount then to raise your price. Make the package a part of your strategy before you get to the slow periods, or when leads are slowing down.
2. Begin offering financing in your presentations early on. The idea of promoting credit and financing options is important marketing to many consumers who are already worried about affordability. Without proper financing, the amount of the average ticket is certainly going down.
3. Track the results of your financing programs. Include any form of consumer credit, financing or promotion in your tracking, so you know where the lead came from, and also how productive the promotion is relative to other forms of leads. This will allow you to track average sale prices & closure rates.

Why is this critical to your success?

1. Financing creates leverage for consumers to spend more of their future earning potential, on products and services you are offering right now. This affects your ability to increase sales.

If you sell more jobs, you lower your overall costs.

If you sell more jobs, you also recover your fixed costs of overhead sooner in the year, getting you closer to breakeven, allowing more flexibility as slower periods of lead generation approach.

1. Properly presented financing, early and often in the sales process, alleviates concerns from many homeowners who may want to afford you, may want to buy from you, but realize as you are presenting you could be expensive. They may not have the cash available to afford you even though they like you and the benefits you are offering them. A properly structured sales process allows for communicating subtly to the homeowners that many varieties of financing options are available allowing them to concentrate on your sales presentation and benefits, and not worry about the money!
2. Financing has been proven to statistically raise the average sale price of a ticket or sale, and increase the closure rate of a company. This reduces your overall costs by requiring fewer leads to meet a sales forecast.
3. Financing options allow for the use of specialized consumer promotions that can attract buyers via advertising and marketing. Examples include 12 months no payments no interest, 6 months same as cash, and 0% financing for 12 months. There are many such examples, and the opportunity is to create additional leads and sales via creative credit options.
4. The use of financing programs expands the universe of those that will upgrade.
5. Financing is a function of demographic trends where consumers are using extended payment plans to afford more material luxuries, they otherwise would not afford, if immediate cash was a requirement.
6. **Financing increases your profitability by adding convenience and leverage.**

