

# Dealer



**F&I**

## **Stop Payment Packing - Now**

*How to detect it and procedures to prevent it*

By Gil Van Over

With all of the bad press constantly bombarding our industry regarding payment packing, I continue to be amazed by the number of sales managers that admit to leaving leg or room in the payments they quote so that the F&I manager can sell products.

Payment packing, the descriptive term the attorney general attached to this deceptive practice, continues to be the preferred payment-quoting method by some of today's sales and F&I managers. These managers continue to practice what they were taught years ago before the practice was deemed illegal; that is to sell the customer on a higher-than-required monthly payment during the sales negotiation so that the payment that includes F&I products does not seem to be as great.

Yet, when asking a dealer, "Are your managers packing payments?" the answer is usually a resounding No! Unfortunately, many dealers do not have the processes in place to detect and prevent payment packing. That has to change.

### **Today's landscape**

Without question, payment packing is a deceptive practice that attorneys general and plaintiff's attorneys are aggressively leveraging to pursue car dealerships. Their motivations differ, but the result for the dealership is usually the same: cash out of pocket in fines, settlements, time divert from selling vehicles, and damaged community reputation. Any dealer that knowingly perpetuates payment packing as its preferred selling technique is simply documenting an unfavorable attorney general inquiry or class-action lawsuit, or both. Fortunately, there are detection methods and preventive procedures available to assist in the defense of payment packing charges.

### **Detecting payment packing**

Contrary to common notion, payment packing is not the sole domain of the sales manager. Unscrupulous F&I managers also partake in this deceptive practice. Let's examine the common methods these two managers use to pack payments on unwary customers.

Sales payment packing is usually accomplished using a sales negotiation tool known as a four square. There are many variations of the four square in use today, but for the most part, a four square identifies the customer's likely hot buttons that must be addressed to successfully lead to the vehicle sale. These squares set out the transaction that generates the highest profit opportunity for the dealership and addresses:

- · Vehicle purchase price (normally MSRP or advertised used car price)
- · Trade in value (generally 10-20 percent lower than ACV) and payoff
- · Cash down (typically 20-30 percent of vehicle purchase price)
- · Monthly payments (no consistent methodology)

A generic four square looks like this:

Price: \$30,000 +++ Trade: NT

Cash Down: \$6,000 Payments: \$575-585 OAC

**Price** - This example lists a \$30,000 MSRP and includes the ever present "+++" which represents tax, title, doc and license fees. Let's assume the "+++" is equal to 15 percent of the cash selling price, making the total \$34,500.

**Trade** - For simplicity sake, this transaction does not have a trade.

**Cash Down** - This dealer looks for 20 percent of the cash selling price as a down payment on the first pencil.

**Payment** - This payment quote is based on 60-month financing at 8 percent APR. The actual payment is \$577 and fits within the range quoted. Many dealers use OAC or WAC to denote that the transaction still requires final credit approval from a third-party lender.

The first pencil is where sales managers can pack the customer's monthly payment, anywhere from \$20 to \$100 a month (\$675 - \$685). Other sales managers pack the payment by using an unacceptable range, in some cases as high as \$50 (\$575 - \$625, for example).

Yet when asked about the discrepancy, most of the offending managers have a ready explanation. Common ones include:

- "I used 48 months on that quote."
- "I allowed for a low Beacon score."
- "I was testing the waters to find out what the customer's budget was."
- "I don't pull a bureau before the first pencil."

The problem with these explanations is simple. The methodology used to quote payments on the first pencil is not consistent! One of the reasons that plaintiff's attorneys are continuing to file lawsuits against dealers is that patterns of deceptive practices lend themselves to class certification. Without a consistent methodology for accurately quoting payments on the first pencil, dealers are establishing a pattern of deceptive practices.

**Detection** - You need a few tests to help detect payment packing.

### **Test one**

Pull the four squares on deals that were closed last week and run the numbers. Taking the numbers on the first pencil, use this process:

1. Add the sales price and add tax, title, doc and license fees.
2. Subtract trade in value from step 1.
3. Add trade in payoff to step 2.
4. Subtract cash down to step 3.
5. Use the lower payment on the quoted range.
6. If a term is quoted on the four square, use it; otherwise use 60 months (or 48 months for an older used vehicle).
7. Plug these numbers from steps 4, 5 and 6 into the F&I system and rollback to an APR.

If you do not consistently end up with the same APR, your sales managers may be packing payments.

### **Test two**

Again, using last week's deals, compare the payment quoted on the four square to the base payment quoted on the F&I menu. If the sale price, trade information and cash down remain the same, the menu base payment must fall

within the range quoted on the four square, or payment packing charges would be hard to defend.

### **Test three**

From last week's deals, select the financed deals where the customers did not purchase any ancillary F&I products. If the sale price, trade information and cash down are consistent from four square to Retail Installment Sales Contract, the monthly payments must also be consistent.

Now, let's TO this transaction to the F&I manager. The top of an F&I menu usually looks like this:

Customer: Mr. & Mrs. Jones Purchase Price: \$30,000

Vehicle: New Car Trade Value: NA Trade Payoff: NA

Base Monthly APR: 8.00% Cash Down: \$6,000 Payment Term: 60 months Taxes & Fees: \$4,500

\$577.88 Amount Financed: \$28,500

The information at the top of the F&I menu must accurately reflect the terms that the customer can take delivery of the vehicle for without the purchase of F&I products. It lists the purchase price, trade information, cash down, taxes and fees, amount financed, term in months, APR and base monthly payment.

There are two opportunities for an F&I manager to pack the base monthly payment on a menu.

1. The first opportunity is to simply inflate the base monthly payment by \$20 to \$100. The manager's motivation is simple; to reduce the payment walk in the customer's mind, thereby facilitating the purchase of F&I products. This is the most common approach used by F&I managers that use handwritten menus. Managers that are not completing the terms on the handwritten menu may be doing so to mask payment-packing practices.
2. A second, more subtle approach used by some nefarious F&I managers is to inflate the amount of the taxes and fees, thereby inflating the amount financed. An increased amount financed leads to a packed base monthly payment. This is becoming the deceptive practice of choice by some F&I managers that are using F&I menu software that computes the base monthly payment.

### **Use these tests to detect these practices:**

**Test one** - As in the four square test, run the numbers. Look at the menus in last week's deals. There are three variables needed to calculate a monthly payment (amount financed, term, APR) and all three should be listed on the top of the menu. If you do not arrive at the base monthly payment quoted, payment packing is likely taking place.

**Test two** - Compare the base monthly payment to the payment range quoted on the four square. If the payment variables are consistent from document to document, the base monthly payment must land within the payment range quoted on the four square.

**Test three** - Determine what products the customer agreed to purchase on the F&I menu. Add up the premiums for those products and divide that sum by the number of months the customer financed the car for. If the payment walk that the customer agreed to on the menu is less than the answer you come up with, the base payment is likely packed.

**Test four** - Compare the purchase price and the taxes and fees listed on the menu with the Retail Installment Sales Contract to ensure that they are consistent between the two documents. If not, the amount financed on the menu is likely inflated in an attempt to pack the base monthly payment.

**Test five** - Compare the base monthly payment on the F&I menu to the monthly payment on the Retail Installment Sales Contract on a deal that the customer did not purchase any products. If they are not consistent, the F&I manager probably packed the base monthly payment.

Now that you can detect possible payment packing in your dealership, what should you do about it (besides terminating all of the offending managers)? Fortunately, there are processes and procedures you can put into place that prevent payment packing from being the preferred methodology in place in your dealership. These processes and procedures include:

- Establish a payment quoting methodology
- Install and require the use of F&I menu software
- Publish procedures that outline your expectations, train your employees on your procedures and require acknowledgement
- Implement a three-level audit process
- Require industry certification
- Punish future offenders

### **Establish a payment quoting methodology**

You must understand one thing before establishing a payment quoting methodology in your dealership; does your sales manager pull a credit bureau report before providing the first pencil or not. The answer determines your methodology.

**No - Credit Bureau Report** - This is the simplest methodology to implement. If a credit bureau report is not pulled, you do not know what the cost of credit will be. Therefore, use an average APR on the first pencil for all customers. An average APR of 8 percent for new vehicles and 10 percent for used vehicles tends to work well. This average APR should change as interest rates change.

**Yes - Credit Bureau Report** - If you do pull a credit bureau report before the first pencil, you have an idea as to the likely cost of credit. Using this information, establish a matrix of what the APR will be, based on the customer's credit score and vehicle selected. You can establish the APRs by averaging the buy rates from your three or four predominant lenders and adding 100 to 200 basis points of reserve. For example, a customer with a bureau score over 700 purchasing a new vehicle will be quoted using a 7 percent APR, whereas a customer with a 585 Beacon score purchasing a four-year-old car will be quoted using a 18 percent APR.

Finally, always use the standard term for the model year vehicle. Sixty months is appropriate for new and current year through two year old vehicles. Use 48 months on vehicles three-years and older.

**Install and require the use of F&I menu software** - A number of excellent software packages are available today and the use of these automated menus greatly reduce the opportunities for payment packing abuse. Look for software that will import the sales data from your sales system. This helps to reduce duplicate data entry and mistakes by the F&I manager and lead to quicker acceptance by the manager. One word of caution automated F&I menus are not the cure all. The data can still be manipulated by F&I managers that intend to deceive. The only sure cure for this type of manager is a set of walking papers.

**Publish procedures that outline your expectations** - Once you settle on a payment quoting methodology and install automated menu software, reduce your expectations to writing and include them in your dealership's Policy and Procedure manual. Be certain to review the procedures with all employees that are tangentially associated with the two processes and obtain their signature on a piece of paper acknowledging their understanding of the expected behavior. This piece of paper should include the statement that "Willful violation of this procedure is unacceptable and is cause for disciplinary action, up to and including termination."

**Implement a three-level audit review** - Too often I see dealers that take the great pains to implement a procedure, train employees on the procedure, tell the employees that they are expected to follow the procedure, and then let the employees return to the old way of doing business. This is because the dealer has not set up a process to audit the new procedure, or using a well-worn, but still rings true phrase "Inspect what you expect".

A three-level audit review is your best tool to catch offenders.

The first level requires a deal jacket checklist that your billing clerk uses to make sure all the required documents are in the file before the F&I manager is paid. Some experienced billing clerks try to tell me they don't need a checklist;

however, without a completed checklist in every file, how can you be absolutely sure the billing clerk looked for everything you require? Make sure this checklist requires a completed, signed F&I menu (and four square, if you use one) in every deal jacket.

Your office manager is the likely candidate to perform the second level review. She or he simply takes the F&I logs at the end of the month, selects five deals per F&I manager in which products were sold and performs the tests outlined earlier.

Finally, your CPA or outside consultant should perform a random review of deal jackets on a quarterly basis. The value of this third-level review is that it provides an independent look. You'll be surprised at how the deceptive practices seem to disappear when the managers know there are compliance cops coming in on a regular basis to look at deals.

Require industry certification - Two excellent industry certifications are the Association of Finance and Insurance Professionals ([www.afip.com](http://www.afip.com)) and The Institute for Ethical Behavior ([www.theinstituteforethicalbehavior.com](http://www.theinstituteforethicalbehavior.com)). They complement each other, require testing to achieve certification, and deliver the message you want your managers to hear.

Punish future offenders - You certainly could not terminate your entire management team after you completed an initial deal jacket audit. However, after you've taken the steps to audit deals, publish and train on procedures and certify your managers, if you still have a manager that is packing payment, that manager must go. What a powerful message to the rest of your crew!

Attacks on the way you do business are not going away. You can continue to travel down the non-compliance road and hope you don't hit that oncoming attorneys general four-wheeler, or you can take the steps to ensure your dealership can defend itself against payment packing charges. The choice is yours.

If you wish to discuss this article with other dealers, or with the author, please go to the "Discussion Forums" at [www.DEALER-magazine.com](http://www.DEALER-magazine.com) and enter the "F&I" forum.

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