



How to pick the right financing option to grow your business

Learn about the 3 different types of financing you can offer to your clients.



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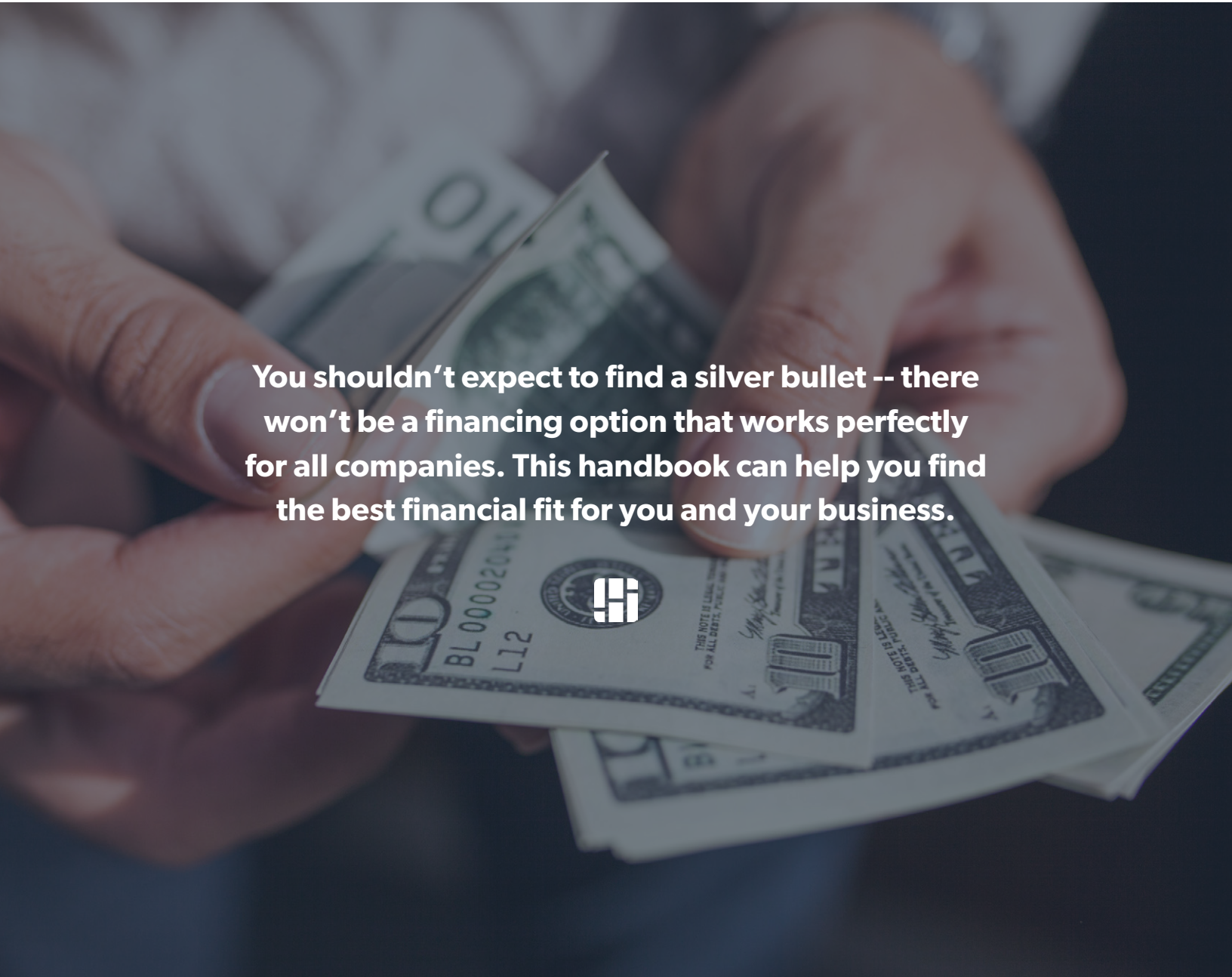


Introduction

You've probably heard how thousands of contractors are appealing to more clients, closing more deals, and growing their business -- just by offering financing.

But, while offering financing can have huge benefits, it can also impose hefty costs if you pick the wrong type for your business.

You shouldn't expect to find a silver bullet -- there won't be a financing option that works perfectly for all companies. The three main financing options -- Institutional, Buy-Down, and Profit Protection -- each have their own characteristics, benefits, and drawbacks. This handbook can help you understand the differences between the three so that you can find the best financial fit for your business.



You shouldn't expect to find a silver bullet -- there won't be a financing option that works perfectly for all companies. This handbook can help you find the best financial fit for you and your business.




Why should I offer financing to my clients?

Think of your typical experience with potential clients. You spend hours spec'ing out the project, preparing your proposal, and visiting the site. You walk through the project and show your clients the high quality proposal, crew, and experience that you have to offer.

But then the price comes up. The [average savings account](#) for Americans is only \$5,000 -- an amount that can make home improvement projects out of reach for many. If your client can't cover the project with the cash they have on-hand and you don't have an alternate payment option to offer, you're faced with three choices: Do you lower your bid? Do you downgrade the project? Do you walk away?

When you offer financing, you don't have to worry about making those choices. You're giving your clients the ability to spread out their project's costs over time -- allowing more clients to afford their projects and to sign on the dotted line!

Even if your current clients haven't asked for alternate payment options, financing is still a nifty tool for your business to have. Beyond building your client base and closing more sales, it can help you improve your customer service, manage your cash flow, and give you the competitive edge you need to distinguish yourself in the industry.

A photograph of three people in a workshop or office setting. A man in a dark suit is pointing at a laptop screen. A woman with blonde hair is looking at the screen. A man in a plaid shirt is standing behind her, also looking at the screen. They appear to be in a collaborative discussion. The background shows a brick wall and a ladder.

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The 3 types of financing options

There are 3 different types of financing that you can use:

- **Buy-Down Financing:** You pay a financing company to show lower rates to your client than the client would've seen otherwise.
- **Profit Protection Financing:** You maintain your margins by not paying a percentage of your profits to buy down rates.
- **Institutional Financing:** Traditional financial institutions (e.g. a bank or credit union) provide the funds to the homeowner over a longer time frame.

You'll learn the ins-and-outs of each of these financing options in the sections below:

Buy-Down Financing

What is Buy-Down Financing?

Buy-Down Financing is a point-of-sale financing option where you pay for your clients to see lower rates than they would otherwise receive.

You'll typically be charged 7-15% of the financed job -- a cost known as a dealer fee or merchant fee. Depending on your clients' credit profile, though, your dealer fee could be as high as 25% of the project. That amount comes directly out of your profit margin and goes to a third-party financing provider.

How does it work?

- **Application:** You can offer options to your clients right in their home. They can apply online or through a mobile app. (Note that this process will usually result in a hard credit pull that lowers their credit score.)
- **Approval:** Clients can receive an approval decision and get the funds quickly.

How are rates determined?

If approved, your clients will likely see the same rate every time they apply, but the amount that you're spending to buy down the rate will depend on your client's financial profile.

For example, Client A, who has a 600 FICO score may see higher rates than Client B, who has a 750 FICO score. You'll have to pay more to buy down Client A's rates than Client B's.

In short, the higher the rate that your client would have seen otherwise, the more you'll have to spend to bring that rate down.

What are the upsides?

- Instant approvals
- Lower rates for clients than they would have otherwise seen
- Usually no income verification requirement for homeowners

What are the downsides?

- **Lower profit margins:** In order to buy down rates, you'll pay a percentage of your profits in dealer fees.
- **More work to make the same amount of cash:** You might have to take more jobs just to make the same amount of cash that you're losing in dealer fees.
- **Stringent requirements for your business:** Most financing programs won't work with your business if it's younger than two years old, isn't part of a specific industry, or doesn't reach a certain amount of annual revenue.
- **Limited access for your clients:** Many Buy-Down Financing providers can't work with homeowners with low credit scores.
- **Checking eligibility affects your clients' credit score:** Companies that offer Buy-Down Financing often perform a hard credit pull on your clients' credit report, negatively affecting their credit score.

What are some common types of Buy-Down Financing options?

- 0% APR loans
- Buy-Down installment loans

Example companies that offer Buy-Down Financing:

- GreenSky
- Service Finance

When should I use Buy-Down Financing?

If you don't mind giving up a sizable chunk of your margin to show your clients lower rates, then Buy-Down Financing may be a fit for you.

A quick note on passing dealer fees on to your clients...

You know that your clients are looking for the best service at the lowest price. When you increase your bid to account for dealer fees, you'll increase your risk of losing the job to a lower bid.



Profit Protection Financing

What is Profit Protection Financing?

Profit Protection Financing is a type of financing focused on protecting your profits. Instead of buying down your client's rates, you're allowing the client to cover the loan's cost themselves, saving you an average of 7-10% of every financed job.

How does it work?

Many Profit Protection Financing providers -- including Hearth -- work with a network of lending partners to find financing options for as many homeowners as possible. Unlike Buy-Down Financing, your clients typically would get pre-qualified before submitting a loan application with a lending partner.

- **See available options:** Clients can request financing from the comfort of their own home through a website or mobile app. They'll fill out a basic form (which includes questions about their name, address, income, FICO score, and employment status) to get prequalified for financing options. Getting prequalified requires only a soft credit pull so their credit score won't be affected!
- **Apply for a loan:** If your client sees options, they'll complete a quick loan application and receive an approval decision from the lending partner shortly after. Your client will have to verify their income and, if approved, will receive the funds about 1-3 business days later.

How are rates determined?

Two characteristics determine the rates your clients will see with Profit Protection Financing.

The first is the type of loan -- unsecured loans usually have higher rates than secured loans. When a client takes out a secured loan, they're putting up home equity that the lending partner can take if the loan isn't paid back. With an unsecured loan, a client isn't pledging any home equity. Instead, they'll see higher rates, which covers the risk to the lending partner if the loan isn't paid back.

The second is a client's financial profile, which includes income, FICO score, debt to income ratio, credit history, and other factors.

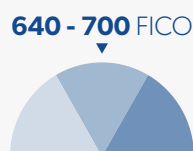
Typical Rate Plans for Profit Protection Financing

Excellent Credit Plan



PRE-QUALIFICATION RATE*	EST. APR RANGE**	LOAN AMOUNT	LOAN TERM***	LENDING PARTNERS
90%	5.34% - 16.30%	\$1,000 - \$100,000	1 - 10 years	13

Good Credit Plan



PRE-QUALIFICATION RATE*	EST. APR RANGE**	LOAN AMOUNT	LOAN TERM***	LENDING PARTNERS
70%	13.00% - 26.87%	\$1,000 - \$100,000	1 - 7 years	11

Building Credit Plan



PRE-QUALIFICATION RATE*	EST. APR RANGE**	LOAN AMOUNT	LOAN TERM***	LENDING PARTNERS
39%	19.95% - 30.61%	\$1,000 - \$50,000	1 - 5 years	5

*For each self-reported credit score range, pre-qualification rate is calculated by dividing the number of pre-qualified Hearth users by the total number of users who submitted a loan request.

**For pre-qualified Hearth users with this credit score range, our lending partners returned loan options with this range of minimum APRs for the 65% of pre-qualified users with minimum APRs between the 10th and 75th percentiles.

***For example, a loan in the amount of \$10,000 for a term of 5 years with an APR of 6.00% would be repaid over 60 monthly payments in the amount of \$193.33.

What are some common types of financing options?

- Unsecured installment loans
- 0% APR promotional period credit cards

Example companies that offer Profit Protection Financing:

- Hearth

What are the upsides?

- **Higher profit margins:** Because you're not paying any dealer fees, you don't have to give away 7-15% of every sale to buy down your clients' rates.
- **Fast, easy, and predictable:** You can help your clients overcome sticker shock by automatically breaking down the project into predictable monthly payments. Clients receive the funds upfront so you can get the project started right away.
- **Open to all contractors:** Profit Protection Financing is open to all contractors, regardless of how long you've been in business, your industry, or your annual revenue.
- **Your client becomes a cash buyer:** The money goes directly into your client's bank account, and they can pay you just as any client with cash on hand would.

"It was great finding a company that focuses on helping small business owners like myself compete against the big guys."

Richard Stidham

Enchanted Hills Cooling & Heating LLC



What are the downsides?

- **Your clients may see higher rates than they would with Buy-Down Financing:** You're no longer buying down rates and allowing your clients to see subsidized options.
- **Your client could hypothetically use the funds with other contractors.** The funds are deposited into your clients' bank account and are not directly tied to you or your bid.

When should I use Profit Protection Financing?

Profit Protection Financing best suits contractors who want to protect their profit margins.

This type of financing also allows you to start projects quickly because your clients typically receive the funds within a couple days.

Institutional Financing

What is Institutional Financing?

Institutional Financing is a loan or line of credit from a traditional financial institution, such as a local bank, branch of a national bank, credit union, or government office.

How does it work?

- **Application:** Depending on the institution, your client can apply either online or in person. The institution will likely need to verify their identity (through a Social Security card or an equivalent document) and income (through a W-2 or paystub). Your client will also probably need to get an appraisal if they're getting a secured loan and need to pledge their home equity.
- **Approval:** The processing period depends on the type of financing option, but your client may have to wait several weeks before the lender lets them know whether their application was approved or rejected.

What are the upsides?

- **Competitive rates.** While clients probably won't see rates as low as the ones they see through Buy-Down Financing, they'll still have competitive options.

What are the downsides?

- **Slow time to fund:** Your client may have to spend time on the phone or in person validating their identity, completing paperwork, and agreeing to the terms. As a contractor, you may be waiting to get the project started until the bank has processed and approved the loan and deposited the funds into your client's bank account.
- **Usually not point-of-sale:** It's rare that you'll be able to offer Institutional Financing in your client's home.
- **Often limited to high credit clients:** If your client doesn't have a premium FICO score (think 700 or higher), the institution may think that they're too risky of an investment and won't extend them a loan.

What are some common types of financing options?

- Home Equity Lines of Credit (HELOCs)
- Home Equity Loans
- Federal Housing Administration Loans (FHA Loans)

When should I use Institutional Financing?

Businesses specializing in luxurious renovations (such as kitchen remodels) will probably benefit the most from an Institutional Financing.

How do I pick the right option?

Although we listed all three options, you'll probably work mainly with Buy-Down Financing or Profit Protection Financing. (If your client wants to use Institutional Financing, they'll probably go directly to their financial institution.)

While choosing between Buy-Down Financing and Profit Protection Financing is not always easy, here's the key question to keep in mind: are you focused on low rates or maximum profits?

If you're focused on offering low rates, look towards Buy-Down Financing. If you want to maximize your profits, Profit Protection Financing is your best bet. There are other details that could cause you to pick one financing option over the other, but the question above illustrates the main tradeoff between the two.

Pro-tip: You aren't limited to one option. You can offer Profit Protection Financing first and keep Buy-Down Financing in your back pocket in case you have a client who will close only with very low rates.

Comparing the 3 Types of Financing

Remember, there is a tradeoff between the rates your client will see and your own profit margin.

You can show your clients lower rates than they would see with Buy-Down Financing, but you'll sacrifice your profit margin.

TYPE	WHAT IS IT?	MAIN BENEFIT	MAIN DRAWBACK
Buy-Down Financing	Point of sale financing where the contractor buys down the homeowner's rates	Often lowest available rates for homeowners	Lower profit margins due to 7-10% dealer fees
Profit Protection Financing	Quick financing where contractors maintain their margins by not buying down rates	Protected profit margins	Potentially higher rates than Buy-Down Financing
Institutional Financing	Traditional financing from banks, credit unions, etc.	Competitive options	Can be a slow/lengthy process to acquire funds

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Conclusion

Financing options are not one-size-fits-all. Institutional Financing, Buy-Down Financing, and Profit Protection Financing are all different, and this handbook aims to give you an overview of their unique features, trade-offs, and benefits.

If you think that Profit Protection Financing is the right fit for your business, we would love to talk to you. Call us at **512-686-4141** to start offering financing, closing more deals, and building your bottom line!



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All loan information is presented without warranty, and estimated APR and other terms are not binding. Hearth's lending partners generally present a range of APRs (for instance, from 5% to 35.99%) with a range of terms and monthly payments. As an example, a \$10,000 loan with an APR of 14.50% and a term of 36 months would have a monthly payment of \$344.21. Actual APRs will depend on factors like credit score, requested loan amount, loan term, and credit history. Only borrowers with excellent credit will qualify for the lowest APRs. All loans are subject to credit review and approval.