



Truck Financing Facts

PREPAYMENT BASICS

Manufacturers offer discounts to entice fire departments to prepay their truck. This complex financial transaction is often painted in simple terms. Most fire departments fail to accurately analyze the risks and true benefits of these offers. This sheet can help you understand the basics of these transactions.

Why do manufacturers offer discounts? The discounts are offered so that the manufacturer can use your funds, instead of borrowing them from a bank, to pay for the parts and labor of your new truck while it is being built. Essentially, you are lending the manufacturer money.

How do manufacturers calculate the discount? The manufacturer will know how much it will pay to borrow from its bank to pay for the parts and labor when building your truck. They calculate the prepayment discount amount at or below that amount.

Are prepayments and prepayment discounts a good deal? They can be. It is important to fully understand what benefits and risks you are assuming when you prepay a truck.

How do I calculate the benefit of prepaying my truck? Most people incorrectly focus solely on the size of the discount and miss the cost of prepaying the truck.

If you are using savings to prepay your truck, you will lose the interest earnings while the manufacturer is using your money.

If you are borrowing money to prepay your truck, you will be paying interest to earn the discount.

Regardless of how you prepay your truck, you should measure the cost of lost interest (when using your savings) or paid interest (when borrowing) against the discount.

If the discount is greater than the interest (either lost or paid), the discount provides the greater financial return.

If the discount is not great than the interest, the discount does not provide the greater financial return.

What are the risks of prepaying? You assume many financial and non-financial risks when prepaying your truck. In essence, you are becoming a lender to the manufacturer and you should assess the risks. The risks of prepaying are include:

1. The possibility of losing some or all of your money and time if a manufacturer should fail to deliver or go bankrupt while building your truck.
2. The loss of control over the manufacturer if the truck is delayed—they have your money.
3. You may earn more than the discount by investing differently than prepaying.

What can be done to protect myself? The manufacturer should provide a performance bond to ensure your truck will be built. However, the bond will not cover any financial losses for truck costs over the bond amount and loss of time while your truck is being built by another manufacturer.

For more information about Performance Bonds, please request our Truck Financing Fact sheet called **Performance Bond Basics**.

To Learn More:

www.FirstBankers.net

Call Toll-free: (877) 323-1776

Key Fact:

Prepayments and prepayment discounts are complex financial transactions with many risks.