



*Steering your dealership
to higher profits*

A publication of Woodward & Associates
Consultants to the Automotive Industry

Written by Carl Woodward & Scott Woodward

December 2020

October 2020 profits continued to be excellent. As you can see below 55% of dealers performed better from a pre-tax profit perspective in October compared to September. Also, approximately 55% of dealers made 3.0% + pre-tax profit on sales in October. Pre-tax profits have never been so good.

Monthly Profit Trends

	OCTOBER BETTER THAN SEPTEMBER	OCTOBER WORSE THAN SEPTEMBER	OCTOBER BEST MONTH	OCTOBER 3% + PROFIT % SALES	OCTOBER LOSS MONTH	OCTOBER LOSS Y-T-D
CHRYSLER	65%	35%	25%	60%	0%	5%
FORD	40%	60%	15%	65%	10%	15%
G.M.	55%	45%	20%	60%	5%	10%
IMPORTS	55%	45%	25%	45%	5%	10%
OVERALL	55%	45%	25%	55%	5%	10%

Profit Trends

The enclosed survey reflects various financial metrics. New vehicle dealer pre-tax profits and pre-tax profits as a percentage of sales have been the best ever for many dealers from May 2020 through October 2020. The ten month y-t-d pre-tax net profit is 2.6% while the October 2020 pre-tax profit is 4.2% for this group of dealers, though the average for all of our dealers is 3.4%. Remember the industry average over the last 10 years as reported by the NADA approximates 2.5%. The typical dealer, after not having a very good March 2020 and had a poor profit month or lost money in April, has had super profit months from May 2020 through October 2020. The NADA reported y-t-d through September 2020 pre-tax net profit as a percentage of sales of 3.1%. This is the best y-t-d performance we have seen in forty years. The annualized NADA sales for new vehicle dealers is \$56 million which will be less than 2019. Also y-t-d sales for the average NADA dealer is down approximately 10% from 2019. NADA reports advertising expense through September 2020 is down from 2019 approximately 20%. This is part of the reason pre-tax profits are increased in 2020 from 2019. NADA also reported floorplan interest is down from 1.4% of total gross to a negative 0.9% of total gross. This is due to less new vehicle inventory and also part of the reason pre-tax profits are improved in 2020. The enclosed profit survey reflects front end used retail gross profit approximates \$2,300 per unit. This is approximately \$500-\$600 increase from 2019. This is also a main reason pre-tax net profits and pre-tax net profit as a percentage of sales has increased in 2020.

**“Someone is sitting in the shade today because
someone planted a tree a long time ago.”**

- Warren Buffett

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Used Vehicle Writedown

Most new vehicle dealers write their used vehicle inventory down at the end of the year for income tax purposes or should. We agree with this procedure and our office sees that this is done for almost all of our new and used vehicle dealers that are not using used vehicle LIFO. The purpose of the writedown is to minimize and accurately reflect your taxable income. The IRS allows dealers to value their used vehicle inventory at the lower of cost or market. This means that if the wholesale value of the vehicle is “worth” less than what you have in it, you are allowed to adjust its value to current wholesale market value.

We believe strongly in the above concept however, we believe the accounting of the writedown should be dealt with in a certain way. After these vehicles have been written down, they are usually sold in the first three months of the following year: January, February, and March. Usually a larger than average gross profit will be shown when these vehicles are sold and the dealership shows large “false” net profits on the monthly dealership financial statement due to the recapture of these “writedowns.” We do not like to see this for several reasons:

1. It distorts the real net profit picture of the dealership.
2. It distorts the gross profit margins on used vehicles.
3. How do you pay the salespeople and sales managers on this.
4. When you look at your financial statement later in the year, you “feel” better about your net profits than you should because the writedown (false) profits are in the year-to-date profits.

The process to make this used vehicle writedown is not complicated. You need to have your staff or CPA firm “Black Book” each used vehicle at the end of the year. We suggest you compare your value of the vehicle with the “average Black Book” value for that vehicle. If the “Black Book” amount is less than your value, then the difference between these two values is the amount of writedown for that vehicle. You need to do this for all of your used vehicles and then add up the total amount of the writedown. If you want to individually determine whether the vehicle is “rough”, “average”, “clean”, or “extra clean” that is up to you. We suggest you use “average” value for all vehicles. After you have the total of the writedowns, you will make one entry to charge cost of sales- used vehicles and to either credit your used LIFO reserve (even though you are not on used LIFO) account or credit a used vehicle with a dummy stock number. You do not apply the writedown credit to each individual used vehicle and this credit remains on your books all year.

In summary, we suggest that you write your used vehicles down for income tax purposes. We also suggest you do not apply this writedown to individual vehicles, but put the total amount of the writedown in used vehicle inventory as a negative vehicle, or put it in the LIFO reserve. In each of the future years, you then will adjust this writedown reserve amount to what it should be for that year-end.

Unemployment Compensation

We have read where states have been paying fraudulent payments for unemployment claims this year. Our state, Illinois, has reported that they are overwhelmed with fraudulent claims. Many states send a letter to businesses when someone has claimed unemployment benefits. We suggest you tell your office staff to carefully review each letter and confirm with the person that they claimed unemployment. Why? If the person you received the letter for did not receive the unemployment payment, then you need to respond in writing to the state that this person did not receive unemployment payments. Why? You do not want this fraudulent claim to be charged to your unemployment account. Your unemployment tax rate will cost you more as the unemployment claims increase. Also, at the end of the year you might confirm with your state unemployment department a listing of all the unemployment benefits paid in 2020 and closely review looking for possible fraudulent payments. Where you see excessive payments, and you do not believe the person received the unemployment benefits as reported, you need to report this to your state so they can reduce the unemployment benefits charged to your account to help reduce your unemployment tax rate and reduce future unemployment taxes.

Marketing Firm

One of our dealers had a marketing firm approach them to supply certain services to the dealership. They wanted the dealer to supply them the dealership's I.T. username and password. This marketing firm wanted ten years of data of every sales and service customer. Fortunately, the dealer read their agreement. It is too risky to allow any third party firm almost unlimited access to the dealer's data. Does any dealer have authorization from all of their customers in their I.T. data file to share the customer's information with any third party? We know dealers allow this, but many do not realize the legal risk they have. There was nothing in this marketing firm's agreement that limited their use of your confidential data. Be careful.

Another dealer sent us an email from another marketing firm. They wrote "If General Motors relies on us, why aren't you?" Just because they say this does not make it so. Also, if any manufacturer shares your data with unauthorized vendors, who will be responsible if the data the manufacturer shares with third party vendors is misused? Probably your dealership. Are you willing to take this risk?

New Vehicle Inventory

We measured the day's supply of a random sample, 50 dealers, to see how much new inventory in dollars compares from November 2020 to December 2019 based on the number of new vehicles that were sold in December 2019. The franchises that had more dollar inventory at the end of November 2020 compared to December of 2019 included one Lexus dealer and one Chevrolet dealer. Out of 50 dealers, only 12, had less than a 60 day's supply based on the number of new sold in December 2019. What does this mean? Most dealer's have more than a 60 day's supply at the end of November 2020 based on the number of new sold in the month of December 2019. This indicates that if a 60 day supply of new vehicles is reasonable, most dealers now have a reasonable inventory, especially if they sold less new units in November 2020 than December 2019. Interesting.

We also measured the day's supply of new units at the end of November 2020 compared to the number of new units sold in November 2020 for a different 50 dealers than above. The average Chrysler dealer had a 107 day's supply; average Ford dealer has a 78 day's supply; average G.M. dealer had a 80 days' supply; average Import dealer had a 60 day's supply; and overall average dealer had a 75 day's supply. These two measurement groups reflect overall that dealer's new vehicle inventory is close to guidelines, though we recognize there are certain model shortages.

Compensation Pay Plans

We continue to see many dealers' have wording in their commission, salary, and hourly pay plans that have some ambiguity. This wording can often be used against the dealer in expensive lawsuits. In "close calls" the dealer can expect to lose and the amount of legal and professional fees to defend the dealer's legal position can be expensive, even if the dealer wins. We have written in the past that all dealers should have their attorney develop language for all pay plans that there is a limited time period the employee can complain about the calculation. We suggest all dealers have such language.

To Subscribe:
Send \$96.00 (Annual Subscription) to:
Woodward & Associates
P.O. Box 1584
Bloomington, IL 61702
carlswoodward@cpaauto.com
For More Information:
Call (309) 662-8797
or Fax (309) 662-9438