POWER STEERING

Steering your dealership to higher profits

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April 2020 was a "terrible" profit month as expected based on the Virus. It appears that April 2020 was the worst month from a profit perspective for the last 50 years or longer. The month of May 2020 reflects improving new and used vehicle sales compared to or slightly improving from April along with smaller losses or improved profits. The metrics below reflect the results of over 200 new vehicle dealerships. These metrics could be somewhat misleading. Differences are due to the franchise involved and state "law" differences. In many states how much a new vehicle dealership could be open for vehicle and parts and service sales and which departments could be completely open varied materially.

April Results

	APRIL BETTER THAN MARCH	APRIL WORSE THAN MARCH	APRIL NET PROFIT % SALES	APRIL PROFIT % SALES + 3%	APRIL LOSS MONTH
CHRYSLER	35%	65%	-1.7%	0%	65%
FORD	30%	70%	-2.3%	10%	65%
G.M.	35%	65%	-2.5%	5%	55%
IMPORTS	20%	80%	-9.8%	10%	70%
OVERALL	25%	75%	-4.0%	10%	65%

The enclosed survey reflects April results including April dollar sales, profits (losses) and net profit as a percentage of sales. The net profits as a percentage of sales are extremely volatile.

Operating Profit

We have again seen articles on dealership financial statements that discuss the category PROFIT ON OPERATIONS or OPERATING PROFIT. Dealers have a sub-total account amount shown before Other Income on the dealer financial statement which is often called Operating Profit. Many readers see articles discussing that reported OPERATING PROFIT is a loss or a very small profit, misleading the reader about the overall profits of a dealership. The reader is led to believe that dealerships have been making little or no profit or losing money. Over time, manufacturers have been putting more and more income into the Other Income category which causes OPERATING PROFIT to be a low, or loss, confusing the reader. In summary, the "profit" term that really matters is Net Profit as a Percentage of Sales. This metric has been in the 2.4% range for many years.

"The function of leadership is to produce more leaders, not more followers."
– Ralph Nader

Inside

Dealer's Information Technology (I.T.) Data

We have written in the past about dealer's knowingly and unknowingly sharing their I.T. data. Our first concern was dealer's sharing a valuable asset, I.T. data, for free or where it is used by third party vendors taking dealer's information and "stealing" a dealer's customers. Many, if not most dealers still continue to allow this to occur.

The second related issue is two articles written by Pete Bigelow and Diana Lee, *Automotive News* Shift February 2020, about dealers allowing third party access to their data without the dealer's customer approving of their data being shared. Some comments about the California Consumer Privacy Act include letting consumers know what data is collected, why, and the third parties that have access. We suspect most dealers do not know all the third parties that have access. This includes manufacturers that share dealer's data with third parties. Customers should be informed about their data being monetized. Consumers must be given a means to delete personal data and should be able to opt out. How many dealers do you think are violating these California laws as if they were located in California?

There was also an opinion article in *Automotive News* by Lynn Rohland about data privacy. It talked about one massive data leak from a third-party vendor exposing 198 million records. Really.

We will give some thoughts and possible solutions for dealers to minimize their risk from consumers next month. Initial thoughts are dealers need to recognize data sharing and they need to recognize something needs to be done now, not later when it "blows up."

Finance-Insurance-Service Contract Chargebacks

We recently went through almost all manufacturer financial statements as it relates to "chargebacks." Chargebacks mean cancellation and repayment of prior income to suppliers for prior sales of finance reserves, insurance products, and service contract income. Best accounting would be setting up a payable reserve for refunds for expected chargebacks on a monthly basis (very few dealers make this monthly entry). This would reduce current income while setting up a payable for estimated future chargebacks. This would reduce net worth and working capital. This amount can only be estimated for there is a very wide range of what this payable/reserve will ultimately be. We recently went through most major manufacturers' financial statements to analyze these chargebacks. We found that several manufacturers did not have an account that reflected how much service contract income chargebacks were. They include: Audi; BMW; GM; Jaguar-Land Rover; Kia; Mazda; Mercedes; Mitsubishi; Subaru; VW; and Volvo. Hopefully, these manufacturers will "freshen" up their financial statements to allow for this missing metric.

We have a "rule of thumb" for estimating what a chargeback reserve should be for a dealership. This has worked out to be an approximation of 24 times the most recent average month's chargeback.

We analyzed the chargeback amounts for three dealerships that sold out several years ago. Their last year in operation, total finance-insurance-service contract income before chargebacks were as follows: $2,050,000; $1,130,000; and $685,000. The chargebacks over the next five to six years after these dealerships closed were: $1,650,000; $330,000; and $110,000. The chargebacks as a percentage of the last full year in operation for finance-insurance-service contract income were: 80%; 29%; and 16%, respectively. This is a significant difference with a large amount of volatility. Based on the chargebacks for the last year in operation, the number of months of chargebacks, compared to our 24 months guideline were: 50 months; 24 months; and 26 months. In hindsight, this would indicate what the chargeback reserve should have been at the sale of the dealership.

Compensation Plans - Overtime

In the past, some employees that are paid an hourly or fixed salary also received a commission. If a dealer really wanted to follow the payroll laws, it was a very complicated formula to accurately pay these certain employees properly allowing for overtime and their commission. Usually, dealers did not know this and only found out when they had a wage and hour audit and they ended up owing many thousands of dollars of extra compensation. Very few dealers knew about this or allowed for this special payroll computation requirement or were able to accurately pay these select employees. The Federal Department of Labor recognized this complication and have recently produced a final rule guiding how to now pay these selected employees. This applied to "overtime compensation of salaried non-exempt employees who work hours that vary each week." This is called "fluctuating workweek method of computing overtime." It is a bit complicated to cover the calculation in an article like this. You might perform a web search to obtain knowledge and guidance to implement this procedure. You may need to change your specific pay plan to better fit this new guidance. If you do nothing, you could have a substantial legal liability for the "covered" employees you are not paying correctly. (Fluctuating Workweek Method Under the Fair Labors Standards Act (FLSA)).

SBA PPP Loan Forgiveness Programs

The law, rules, guidelines and regulations for the SBA loan forgiveness programs continue to evolve and change as we write this. Below are a few observations and comments:

All dealers we know applied for and received this PPP loan.

All dealers we know plan to claim some portion of the loan, even though subsequent guidance questions whether or not the dealership really should have claimed this loan forgiveness. This concern deals mainly with the financial strength of the dealership. At the time of loan, almost all dealers kept some of their employees on payroll which they would have otherwise terminated if this loan forgiveness program had not existed. This is the main reason the loan forgiveness is valid for almost all dealers.

Some dealers had such financial strength that the government might claim they did not need the loan. Read prior comment though.

With the new law at this time, almost all dealers, 24 week loan forgiveness period versus 8 weeks, will meet the first criteria of keeping all the loan funds. However, the second and third reduction criteria will probably cause many dealers to forfeit or have a reduction of some portion of the loan forgiveness piece of this overall program.

We strongly suggest dealers do NOT make an accounting entry to put any of these PPP loan forgiveness amounts into income until the amount has been determined and confirmed. If you feel it makes sense, we would have you put the loan forgiveness amount into other income, not against various expense accounts. You may want to leave the forgiveness amount as a year-end auditor entry.

Most dealers do not plan on paying their employees on this loan forgiveness income, but possibly pay some special "bonus" at the end of the year based on the final income results.

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