POWER STEERING

Steering your dealership to higher profits

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Written by Carl Woodward **March 2016**

January 2016 was a mediocre profit month for many dealers. We had only 10% of new vehicle dealers make 3.0% net profit as a percentage of sales or better. This is down from past months in 2015. The percentage of dealers that lost in January was 5%.

We also see a trend of new vehicle day's supply increasing, which is not good. It will be better measured to see the new vehicle dealer's day's supply at the end of March since March is historically a good month. We do not like to use the *Automotive News* day's supply since fleet sales and other factory issues can distort the day's supply to appear to be less than a typical new vehicle dealer that does not sell fleet vehicles.

Retail Installment Contracts

We go through over 200 sets of new vehicle dealership accounting records in the first four months of each year. One area we question is vehicle receivables/contracts-in-transit. If we see an open balance of $3,000 or less, we might inquire at times: why? In many cases, the dealer has "cashed" the retail contract but the customer still owes some balance on the deal. This would be considered a violation of your terms with the financial institution that purchased the retail installment contract. In other words, dealers are not allowed to cash the contract until all funds owed by the customer are received. We have also seen where a dealer will pay a third party check-guaranteeing service a fee for guaranteeing this customer "hold check," believing this protects the dealer with the lending institution. If you are going to have any hold checks, including "check guarantee service" checks, we suggest you obtain written approval from your lenders for this process. If you violate the lender rules and the lender finds out, they can require you to repurchase the retail installment contract.

Dealership Lifetime Products

Every few years, we write about dealers that sell/include certain products with their vehicle sale. These products can include: free tires for life; free lifetime oil changes; free lifetime service contracts, etc. Dealers that supply this product to the customer and include it in the deal for no charge believe they will sell more vehicles or sell more parts and service products. Theoretically, this might make sense, but based on experience with some dealers that have had these types of products, no one yet has been able to validate that these free products pay for themselves in extra vehicle sales or parts and service sales.

"To be successful, you must accept all challenges that come your way. You can't just accept the ones you like."

- Mike Gafka

Inside

Federal Government Pay Changes

The government is looking into and planning to change the pay rules for overtime pay. This has not been finalized yet, but it appears these new pay plan rules will be implemented and could cost dealers many tens of thousands of annual increased compensation. Dealers do not know yet if any of these rules will affect their employees. Basically, in the past, dealers did not have to compensate certain employees for overtime, the hourly 50% premium for hours worked over 40 in a week. For example, a dealer might pay a qualifying employee $600 per week based on working a 50-hour work week.

This works out to $12 per hour. If the government now requires the 50% premium for hours over 40, the new compensation would be 40 x $12 = $480 + 10 x $18 = $180 for a total of $660, or an annual pay increase of $3,120 with no increase in employee productivity. Dealers have a few options: accept the change and have their annual cost go up $3,120 per qualifying employee; reduce the hours of this person but upset this employee; reduce the hours of this person and hire a part-time employee to make up the hours, but again upset the current employee; reduce the hourly rate of this employee so after allowing for the overtime component, the employee continues to make the same compensation based on 50 hours and 10 hours of overtime. We suggest you implement this last option and explain to the employee why this is being done and their compensation will stay approximately the same. You need to prepare for the implementation of this expected government rule change.

TruCar, Inc.

Below are some of the reported information from the SEC Form 10-K for TruCar.com as of December 31, 2015. This company acts like a “broker” to take a portion of a new vehicle dealer’s gross profit, without having the infrastructure needed, supplied by new vehicle dealers. In economic terms, they could be considered a “free rider.”

	2015	2014	2013
Accumulated Deficit (balance sheet)	$275,900,000	$210,989,000	
Annual Revenues	$259,838,000	$206,649,000	$133,958,000
Sales and Marketing Expenses	$151,002,000	$128,569,000	$75,180,000
Loss Before Provision for Income Taxes	$64,305,000	$47,789,000	$24,477,000

As you can see above, revenues went up $53,000,000 with sales and marketing expenses going up $22,000,000 and losses increasing over $16,000,000. In other words, the annual revenues are increasing, but the losses continue to materially increase. How long will new vehicle dealers continue to support this company and how long can TruCar, Inc. stay in business?

Tesla Motors, Inc.

Below is some of the reported information from the SEC Form 10-K for Tesla Motors, Inc. as of December 31, 2015. As you know, this company manufactures and sells electric cars.

	2015	2014	2013
Accumulated Deficit (balance)	$2,322,323,000	$1,433,660,000	
Annual Revenues	$3,740,973,000	$3,007,012,000	$1,921,877,000
Loss Before Income Taxes	$875,624,000	$294,040,000	$74,014,000

Their sales went up over $700,000,000, but their loss increased $581,000,000, which is not a good ratio or trend. A large reason they are able to sell their very expensive electric car is due to federal tax credits that are $7,500 per new vehicle. Once this company has sold 200,000 vehicles, this federal tax credit is scheduled to phase out. How many of these expensive electric cars will they then sell, especially with gasoline prices so much less than Telsa had planned?

Unclaimed Property Reporting

Some states require businesses to report “unclaimed property” so the state can have these funds. This usually applies to financial institutions that might have checking accounts, savings accounts, and stock and bonds that have been “abandoned” by the customer. Dealers do not have these types of customer property, but your state might feel that “liquidated damages” on abandoned vehicle deposits and vendors and employee checks you owe but they did not cash might qualify. Illinois has this law, but they now do not mail this form to businesses. This process seems unfair since few will remember this remote law and form to file. If you are audited by your state, they will be looking at your general journal and your CPA’s year-end adjustments for items written off to income. In some cases, these funds should have been remitted with the tax form.

Government Mailings

All businesses receive mailings from the government. Some of these mailings are time sensitive. Governmental agencies date the notices and give you a time period to respond. Be careful; the time period is usually from the date of the notice, not when it’s postmarked or received by you. We know of a dealer that lost a dispute with the government regarding a notice that was never received.

We suggest that on all mailings to the government someone write on the face of the sent letter the date mailed. We suggest that you keep all government notices you receive and note the date received. Keeping a copy of the envelope the notice was received in, along with their notice and your response, is the best way to handle this.

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