Steering your dealership
to higher profits

A publication of Woodward & Associates
Consultants to the Automotive Industry

Written by Carl Woodward **November 2017**

September 2017 was a down profit month for most new vehicle dealers. As you can see below, 70% of our new vehicle dealers' profits were down in September 2017 compared to August 2017. This is not unexpected since September results are usually not as good as August. The trend for the number of dealers losing money is getting worse. Nationwide new vehicle unit sales in September were improved over August and similar to October 2017. Overall dealer's pre-tax net profit as a percentage of sales year-to-date remains good and comparable to all years back to 2010.

September Profit Trends

	SEPTEMBER BETTER THAN AUGUST	SEPTEMBER WORSE THAN AUGUST	SEPTEMBER BEST MONTH	SEPTEMBER 3% NET SALES PROFIT MARGIN	SEPTEMBER LOSS MONTH	SEPTEMBER Y-T-D LOSS
CHRYSLER	35%	65%	5%	20%	10%	10%
FORD	25%	75%	5%	25%	20%	10%
G.M.	25%	75%	0%	10%	25%	15%
IMPORTS	35%	65%	10%	20%	10%	15%
OVERALL	30%	70%	5%	20%	20%	15%

Dealers Selling Automobile and Truck Insurance

Some dealers are now selling insurance policies to their customers that cover the vehicle including physical damage and liability insurance. Some dealers, we understand, are using Allstate. Though no reflection on Allstate, we do not believe this is in the best interest of most dealers no matter which insurance company they represent. Why? We understand it is a service some of your customers might want and would like to obtain their insurance from your dealership. We understand you might increase your dealership profits slightly. However, even allowing for these two reasons for selling this type of insurance, we would suggest you do not represent any insurance company. You very likely will upset the local insurance agents in your area of responsibility. If they now know you are in competition with them, they will be more likely to direct their customers to any dealership but your dealership when they have the opportunity to refer a customer. We really doubt the perceived benefits are worth the loss of customers.

"Success seems to be connected with action. Successful people keep moving. They make mistakes, but they don't quit."

-- Conrad Hilton

Inside

Dealer Fraud

We read and see at times about "fraud" paperwork and actions that dealers have been involved in. It is usually paperwork issues where someone in the sales department illegally "enhances" a "weak" retail deal to a financial institution that buys retail installment contracts. Sometimes this "illegal "enhancement is done by dealership employees not really understanding what they are doing is "criminal" and an offense that could result in jail. Not realizing this is not an excuse. Some of these "frauds" include:

1. Overstating the down payment the customer is making on the deal.
2. Overstating the income of the borrower on the credit application for the retail installment contract.
3. Borrowing the down payment funds on the retail installment contract without the advance knowledge or approval of the lender.
4. Reflecting equipment and options on the vehicle being financed to increase the loan value of the vehicle. This is sometimes called "power booking."
5. "Doctoring" documents with computer printers and using liquid "white-out" to improve the appearance of the customer's information or creating totally phony documents.

We do not believe this occurs at most dealers, or often, but would suggest at least once a year, or more often, to have a meeting with all the sales department employees letting them know the above types of action will cost them their job, and they could go to jail for the above fraudulent activity.

Monthly Dealership Financial Statements

Often times dealers send in their monthly financial statement with dollar amounts and statistics that appear to be "wrong." Why do you care? One reason is almost none of us want to send out financial statements that have what appears to have obvious "errors" in them whether to your financial institution or your factory. A second reason is we don't want the factory to use these "erroneous" financial statements, sent to them monthly, against us in a future legal proceeding.

Some of the most obvious "errors" or apparent "errors" include:

1. On the asset side of the balance you reflect negative balances including negative cash.
2. On the liability and equity side of the balance sheet you reflect "negative balances.
3. Prepaid assets appear very large and unreasonable.
4. Notes payable not including new floor plan, used floor plan, and notes lease and rental, need to be shown properly under short-term or long-term. It is better to have long-term notes versus short-term notes.
5. Make sure the factory "working capital guideline" is confirmed twice a year and updated on the financial statement when needed. Often times no one confirms this metric and it is not accurate.
6. Confirm your actual working capital equals or exceeds the factory guideline and if not, take the time to find out why. If you are below the guideline do something about it.

Always feel free to send us, no charge, your monthly financial statement and we will briefly analyze it looking for obvious likely reporting "errors."

New Vehicle Inventory (Day's Supply)

We compare at times the day's supply of new vehicle inventory for over 200 new vehicle dealers with the *Automotive News* day's supply of new vehicle inventory. *Automotive News* always seems to be substantially less than our day's supply (we are not blaming them, but something is distorting these numbers). It is possible "fleet sales" distort the *Automotive News* metrics. *Automotive News* defines **Day's Supply**: Number of days needed to sell all vehicles in inventory. **Inventory**: Unit count of vehicles on hand at dealerships, factory lots, port of entry, and in transit on a specific date. Using the *Automotive News* definition, which includes in transit vehicles, assume 15 days, our day's supply should be increased by approximately 15 days. Our day's supply in the enclosed survey of 101 + 15 (in transit vehicles) yields 116 days. *Automotive News* reports a total of 65 days. This is a huge difference of 51 days. Based on this we would not necessarily rely on what is reported in the *Automotive News*. As an aside, with our group of dealers overall reporting a 101 day's supply, this is an indicator many dealers need to reduce and cut back on the ordering of new vehicles depending on what your day's supply guideline is.

New Tax Legislation Proposals

Congress is moving forward with their overhaul of the tax code. After the House passed their version of the Tax Cuts and Job Act, the Senate continues to work through their version. The Senate and the House must agree on a compromised bill to be able to present to President Trump to sign into law. Republicans are still hopeful this can be accomplished by year end. If this act gets passed it would be the biggest transformation of the code in more than 30 years affecting nearly all US companies and individuals. While both versions of the Bill have a lot in common, there are also some key differences to note as well:

Individuals:

- Bracket changes – House proposal has 4 brackets with the highest being 39.6% .Senate has 7 brackets with 38.5% as the highest rate.
- Alternative minimum tax (AMT) would be repealed
- Mortgage interest deduction would be limited to loans of $500,000 for House bill and $1MIL for the Senate. The house eliminates second home interest, the Senate keeps it intact.
- The state and local income and sales tax deduction would be eliminated
- The Senate would eliminate the deduction for property taxes, the House proposal would limit it to $10,000.
- The standard deduction would roughly double
- The personal exemption would be eliminated
- Charitable contribution deduction remains, with some modifications
- Exclusion of gain from sale of principal residence. Home must be principal residence 5 of past 8 years; exclusion allowed once every 5 years

Businesses:

- A flat 20% rate would replace the current four tier schedule of corporate rates for C corporations. This would be effective 2018 in the House bill and effect in 2019 in the Senate bill.
- Interest expense deduction would be limited to 30% of adjusted taxable income for businesses with average gross receipts in excess of $25 million in the House bill. The Senate bill would apply the limit to business with average gross receipts in excess of $15MIL.
- Section 179 expense would be increased to $5,000,000 with phase out beginning at $20,000,000 for the House bill. The Senate limits would be 1,000,000 of expensing with the phase out beginning at $2,500,000.
- The House bill would tax a portion of business income from Pass-Through entities at a 25% maximum rate. For nonpassive activity income (including wages), 30% of the income would be subject to the 25% rate, and the remaining 70% to be taxed at the ordinary income rate. Current rules for self-employment stay intact. The Senate bill would provide a new 17.4% of income deduction for Pass-Through entities.
- Replace 50% bonus depreciation with 100% expensing of the cost of depreciable assets acquired after September 27, 2017 and before January 1, 2023

Estates:

- The House bill rises the Estate tax exclusion amount to $11.2 million in 2018 and would be fully repealed the tax in after 2023. The Senate bill raises the exclusion to same amount with an annual inflationary increase but does not eliminate the tax.
- Top gift tax rate would be lowered to 35%

With the potential for these big changes, tax planning has never been so relevant. It is important to talk to your tax advisors to determine your best strategies to mitigate your tax liabilities for this year and the next.

To Subscribe:
Send $96.00 (Annual Subscription) to:
Woodward & Associates
P.O. Box 1584
Bloomington, IL 61702
carlswoodward@cpauto.com

For More Information:
Call (309) 662-8797
or Fax (309) 662-9438