HEADLIGHTS

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BLUE SKY FROM A BUYER'S PERSPECTIVE

We are often asked the question, "What is my blue sky?" As you might guess, the answer is, "It depends." Many factors affect this intangible value of your dealership. Obvious factors include which franchises you own, their location, market size, profitability, workforce and competition. These and other factors are important because a prospective buyer will use them to determine an expected return on investment. This analysis is the same for every investment decision, whether you are buying a dealership or a doughnut shop. Buyers typically pay a price that provides them with an acceptable rate of return based on the perceived risks they are taking.

Thomas P. Goekeler, CPA, CVA
Sartain Fischbein & Co.

The formula illustrated on page 2 can assist you in determining the intangible value of your dealership from a buyer's perspective.

Purchasers will want to see the prior year's operating statements. They will use these statements to determine what future sales they can expect and what your net profit as a percentage of sales has been. It is important that you disclose to the buyer any unusual or nonrecurring items that have affected your profitability. These normalization adjustments can make a significant difference in the calculation of blue sky. Also, if a facility upgrade is needed or will be required of the buyer to get factory approval, the buyer will need to factor that into the equation. Generally, the buyer would amortize the expected cost, net of factory reimbursements, over a 10-year period at the buyer's borrowing rate. The expected annual pretax income would be reduced by the annual amortization.

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WINTER 2015

NATIONWIDE MONTHLY NEW-VEHICLE UNIT SALES

THE POWER OF GIFTING

The expected return on investment is a very subjective element of the formula; 25% is the historical average for dealerships. This equates to a multiple of four to get to the total enterprise value.

However, each franchise and dealership is different. Currently, Mercedes, BMW and Lexus franchises are yielding much-higher-than-average multiples. Stores located outside a metropolitan area generally have lower multiples than do stores located in a metropolitan area. Public dealership groups tend to pay higher multiples. The variables specific to your dealership and the prospective buyer will affect your multiple.

The final step in the calculation is to reduce the computed gross dealership value by the working capital and fixed assets needed to adequately operate the dealership at the expected volume.

The formula below is a good tool to help you determine a range of blue sky you might expect from a buyer. However, every transaction and buyer is different, and the result of the formula may not match what you are offered.

When looking to buy or sell a dealership, contact an **AutoCPAGroup** member to discuss a valuation of your blue sky, as well as other factors that may influence the price of the transaction. ✍

Expected annual sales based on historical results		**$40,000,000**
Multiply by expected annual return on sales based on historical results after normalizations	×	3%
Expected annual pretax net income	**=**	**$ 1,200,000**
Divide by expected return on investment (25% is the long-term historical average for dealerships)	÷	25%
Gross dealership value	**=**	**$ 4,800,000**
Subtract working capital requirement	–	1,000,000
Subtract fixed asset requirement (excluding leaseholds)	–	400,000
Blue sky/franchise/goodwill/intangible value	**=**	**$ 3,400,000**

NATIONWIDE MONTHLY NEW-VEHICLE UNIT SALES

Carl Woodward, CPA
Woodward & Associates, Inc.

We keep track of and graph new-vehicle unit sales both on a month-to-month and year-to-date basis. These graphs are very consistent in predicting trends. Most knowledgeable people in the industry expect national new-vehicle unit sales to increase from the lows of late 2008 and 2009. These continuing upward trends would be expected until they rebound to the levels in the year immediately preceding the beginning of the latest recession. We would also expect nationwide new-vehicle unit sales to continue to grow as the population continues to increase.

Those who follow the monthly new-vehicle unit sales have given us some very interesting explanations as to why sales are going up. Some of their reasons include longer loan terms, lower monthly payments, lower credit standards, change in consumer sentiment and the scrappage rate of vehicles (which is going down because people are holding on to vehicles longer for many reasons).

In other words, while some writers give reasons as to why the numbers of new-vehicle unit sales have gone up, they seldom see the main reasons for the gradual growth: population increase and the economy's expansion.

Based on graphs of nationwide monthly new-vehicle unit sales trends from one year to another for the past eight years, we find that whether comparing one month to the next month or to the month before, the trend is the same. January is the lowest new-unit sales month of the year. December always has more new-unit sales than does November. April new-unit sales are always lower than in March, and in May sales are usually higher than in April. New-unit sales drop off from August to September. This information can help forecast the level of new inventory needed and determine the forecasting process for your monthly bottom line.

Please contact an **AutoCPAGroup** member by e-mail or telephone for your own copy of our graph showing monthly unit sales over the past eight years. You will find it interesting. ✍

THE POWER OF GIFTING

Richard Heider, CPA
Heider, Tanner & Dirks, Inc.

Over the years, a successful dealer can build a sizable estate, including the dealership business, real estate related to the business, reinsurance company assets, retirement accounts and personal residences, as well as other investments purchased over time. For 2015, each person can pass $5,430,000 estate-tax free to the next generations of family members (the number is adjusted annually for inflation). Or you can use some or all of that exemption during your lifetime to gift assets to your heirs. Generally, a married couple will not pay estate or gift tax on the first $10,860,000 of their net assets.

When discussing gifting of assets, there are practical and important issues to consider. The starting point is the amount of assets the person making the gifts needs over the course of his or her remaining lifetime. If you need those assets to maintain a comfortable lifestyle, then you should consider keeping them and not gifting them.

When you gift an asset to another person, the income tax basis for determining a gain when he or she disposes of the gifted asset is the same as your income tax basis—in many cases, your original purchase price. Thus, when the recipient sells the gifted asset, there is no income tax savings for him or her. One advantage of keeping an asset until your death is that your estate's beneficiaries get the advantage of establishing a new basis for the asset, avoiding income tax on any increase in the value from the time you purchased it through your date of death.

If you do have an estate that will grow over time and eclipse the $5,430,000/$10,860,000 exemption amount (depending on your marital status), then you should consider gifting assets. Absent the need to keep all your assets to fund your lifestyle until you die, you should look at your basket of assets to see what would make sense to give away. In many cases, we see gifts of interests in the dealership entity and the real estate entity as prime candidates. One reason is that the dealership and real estate can be expected to increase in value, while providing an annual income that will go to the person receiving the gift. Gifting assets that you expect will appreciate is a big consideration when choosing which assets to give away.

Over the years, my experience has shown that, if you expect to have a taxable estate upon your death, the sooner you start gifting, the better. There are costs in gifting that include valuations of the entities or the assets being gifted and the cost of having a gift-tax return prepared by your attorney or CPA. But the estate-tax savings down the road from a strategy of gifting are much greater than the costs incurred to make the gifts.

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THE POWER OF GIFTING

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There are other techniques besides gifting for transferring assets to the next generations. These may include having your children become owners in the real estate entity or dealership entity when it is first set up, in addition to more complex strategies that may also work for your particular situation.

Although gifting can be very straightforward and understandable, this strategy requires expert input to make sure it works for you. Make an appointment with your **AutoCPAGroup** member to discuss how a gifting strategy might fit your own situation when planning your estate. ✍