HEADLIGHTS

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THE USED-VEHICLE MARKET AND IMPLICATIONS FOR THE NEW-VEHICLE DEALER

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Much attention is given in both the trade and the national press to new-vehicle unit sales each month. What about used-vehicle retail sales? All dealers know the importance of selling used vehicles and the profits they generate. On an annual basis, the number of used-vehicle retail unit sales from all types of sellers (independents, franchised, private party) is greater than the number of new-unit sales at franchised dealerships, although the number of used-vehicle retail unit sales is smaller at the average franchised dealership.

NADA recently reported that the 2014 average selling price of a used light vehicle sold at franchised dealerships was $18,846, which reflects a steady increase since 2011. This amount represented 58% of the average new-vehicle selling price, which is near the top range of this statistic. This could indicate a slowdown or leveling off of used-vehicle retail sales prices in 2015. If the percentage increases to 60%, the auction company ADESA believes that consumers considering either a new- or used-vehicle purchase will choose a new-vehicle purchase.

As supply of off-rental vehicles increases, the timing of their entry into the market can also have an impact on the pricing of used vehicles.

If retail sales prices are rising, these findings imply that what a dealer pays for used vehicles is also increasing. This translates to a larger investment in your used-vehicle inventory, which means either using the dealership's money to

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own these units or floor planning some portion of your used inventory. If you choose to internally finance used inventory, you will need to retain some amount of cash profits.

Due to the potential profits from these sales, used vehicles are a great investment for a dealership. From the standpoint of inventory management, your ability to anticipate the used-vehicle market month to month, acquire the type of used vehicles that are the most saleable, size your inventory to maximize turns, and have a used-vehicle sales department that knows what is in stock and how to sell it can result in more profits for the dealership.

NADA statistics for 2013 showed that 67% of used vehicles acquired by franchised dealerships came from trade-ins and 26% from auction purchases.

The process your dealership uses to value trade-ins and purchase used vehicles from auctions must be closely monitored by the appropriate managers. Profits in the used-vehicle department start with the purchase side. If your dealership can't properly purchase the units, it won't matter how many used vehicles you sell.

In many ways, managing used-vehicle inventories from purchase to sale is more complicated than managing new vehicles, where consumers know what you paid for the vehicle. Constant communication between owners, managers and salespeople is important to move the used-vehicle department to its highest profit potential.

Contact an **AutoCPAGroup** member to discuss used-vehicle inventory planning and profitability. ✍

TAX OPPORTUNITIES FOR FACILITY IMAGE UPGRADES

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In recent years, a significant number of dealers have completed or are addressing renovations to their facilities. Many of these are factory-mandated image programs; others may involve new facilities. The process outlined below has been used by dealers to maximize deductions related to these type of projects.

Perform a quantitative and qualitative analysis of the project. Evaluate the condition of the property at the conclusion of the renovation compared with the condition of the property when you last renovated it. Then consider these questions:

✔ Did you improve it, or have you merely brought it back to the same condition as it was when you placed it in service or the last time you renovated it?

✔ Did you adapt any of the interior space for a different use?

✔ Did you increase the exterior footprint of the facility?

✔ Did you replace or improve the building's structural components or systems?

Depending on your situation, some or all of the costs incurred may not need to be capitalized and depreciated; some or all of the costs incurred may have gone merely to refresh your facilities, allowing them to be expensed as repairs. The results can vary dramatically depending on the situation.

The IRS's new Tangible Property Regulations (TPR) provide significant guidance in this area. They will help you determine which and how much of the costs are deemed a capitalized cost vs. a repair.

If the TPR analysis determines that a significant portion of the renovation must be capitalized, a more in-depth review of the effort and its impact on existing facilities needs to be performed. That will allow you to determine the appropriate depreciable tax lives and methods associated with the new investment, and what impact, if any, this may have on the preexisting dealership–facility investment.

✔ **Cost segregation:** Unless a cost-segregation study is performed, building renovations are typically expensed over 39 years. The objective of such a study is to determine what and how much of the investment can be appropriately classified as 15-, 7- or 5-year depreciable property in an effort to recover these costs more quickly.

✔ **Preexisting facilities:** It is not uncommon for certain assets to be demolished or discarded prior to a renovation. Under the new TPR, dealers have a significant opportunity to review the investment in facilities that existed prior to the renovation and obtain a noncash tax write-off associated with the property removed. The regulations could also allow a dealer to currently deduct demolition and removal costs associated with the project; these costs previously had to be capitalized as part of the renovation.

✔ **Look-back provisions:** Even if you completed your renovations before 2014, it is not too late to take advantage of the new TPR. The IRS will allow dealers to review their depreciation schedules and identify the costs of assets and facilities that have been totally or partially removed from service as a part of the renovation or that may have been inappropriately capitalized in prior years. Cost-segregation studies for prior years can also be performed. To take advantage of the TPR and cost segregation in prior years, the dealer needs to file a Form 3115, Change in Accounting Method, with a timely filed return and deduct all prior-year benefits in the current year.

Talk to an AutoCPAGroup member about these new regulations and the deductions for facility upgrades that you can take sooner than you could before. ✍

SATURDAY SERVICE WORK SURVEY

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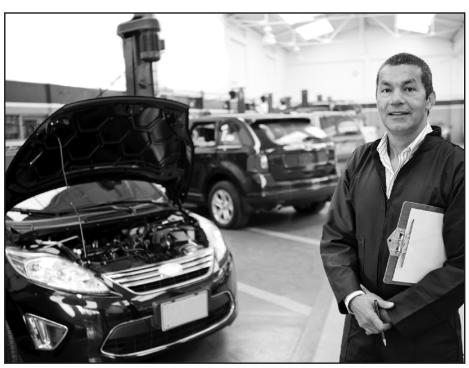
We recently conducted a survey of new-vehicle dealers in several states that asked if their service departments were open on Saturday and, if so, how many technicians were kept busy that day compared with the number of technicians they had during the week. Approximately 150 dealerships responded to our survey.

We found that 77% of the dealerships' service departments were open on Saturdays. About half the service departments open on Saturday were open 4 to 5 hours; the other half were open 7 to 9 hours. Most of the departments open on Saturday were able to keep only half as many technicians busy as they would during the regular Monday-to-Friday workweek; in other words, they ran at a staffing level of 50% or less.



We have observed that if customers are asked if they want their new-vehicle dealer's service department to be open more during the week and on Saturdays, many customers will say yes. The better question is, what percentage of customers would use the service department on Saturdays? Although most customers do not work on Saturdays, our survey determined that most customers do not use new-vehicle dealers for Saturday service, either. It appears that customers use their weekends for personal matters, which doesn't include bringing their car to the dealership's service department.

Using a reservation system should assist service and parts managers to determine a staffing level for Saturday service work. From a financial standpoint, you should review Saturday service work for

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SATURDAY SERVICE WORK SURVEY

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patterns in the type of service work being done, the average repair order totals and the average gross profit per service repair order.

Generating a level of Saturday service work that makes your dealership more profitable requires careful thought on the marketing side and an ability to get customers in the door. Are Saturday specials needed? The side of the equation that includes staffing as well as monitoring results is just as important as you adjust to what the market is bringing to your service department.

Talk with an AutoCPAGroup member about whether Saturday service hours make sense for your dealership. ✍