HEADLIGHTS

A PUBLICATION
OF THE AutoCPAGroup

WWW.AUTOCPA.COM
1-800-4AUTOCPA

CONTROLLING EXPENSES AS SALES LEVEL OFF OR DECLINE

Wayne Zimmerman, CPA
Pomares & Co., LLP

It's been a great run. Dealership revenue and corresponding income have been, for many, at all-time highs. But great runs won't last forever. Many industry economic strategists have examined economic indicators and believe that the dealership boom has reached its peak and will soon begin a slide. How great a slide? Only time can answer that question.

Are you prepared for the slide if it does come? A short five years ago, dealership staff were attentive to essentially every expense. Expenses were detailed and compared with established standards. Variances were thoroughly analyzed to ascertain cause and correction. Correction was swift and definitive. Unfortunately, many dealers have gotten away from these essential expense control procedures. Dealership management has gotten too focused on revenue production and has spent too little effort on proper expense control.

Do you know your current employee count, and revenue and gross per employee? Do you know your service revenue and gross per technician and advisor? Do you know your variable net for each dealership department? Do you know your total employee cost? Do you know the monthly contents of significant expenses such as advertising, outside services and data processing? Do you know the monthly contents of other income and deductions?

If you can't answer these questions, perhaps it's time to get back to processes and procedures that allow for them to become a regular and routine part of the dealership

please turn the page ☞

SPECIAL NADA ISSUE: JANUARY 2017

WRITING OFF EQUIPMENT PURCHASES

USED VEHICLE DEPARTMENT PROFITABILITY

VISIT US AT **BOOTH #6001**

NADA100

NEW ORLEANS • JANUARY 26-29

management. Essential dealership management should develop an expense control process that includes, at a minimum, the following:

✔ A monthly, quarterly and annual forecast and budget. These should be developed in a manner that allows for quick and efficient change and should be a realistic representation of expectations. It is imperative that these be examined routinely to determine causes of discrepancies.

✔ A system that reviews departmental gross and variable net on a regular and continual basis.

✔ A system that details all expenses or, at a minimum, all significant expenses on a monthly basis by vendor.

✔ A system that evaluates all employee production, compensation and contribution to the dealership operation on a regular and continual basis.

✔ A system that details the content of other income and deduction on a monthly basis.

Getting back to the basics of expense management and control will help put a dealership in a position to make swift decisions regarding the actual economic conditions that exist. If expense controls are lacking, it can take significant time to adjust the dealership expenses to adapt adequately to the economic conditions, resulting in a potentially significant negative result.

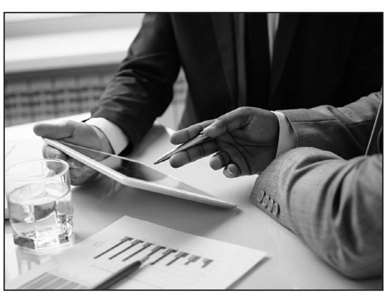
If you need assistance with the development of an expense control system, contact an AutoCPAGroup member. ✍

WRITING OFF EQUIPMENT PURCHASES

Scott Hasbrouck, CPA
Brady Martz & Associates, P.C.

Historically, there have been many times that late in the year, and even retroactively, the current rules for expensing or depreciation of the costs of equipment purchases have been changed. Sometimes there are lost opportunities due to the timing of tax law changes. However, for 2016 and the intermediate future, we have some stability with the enactment of the Protecting Americans from Tax Hikes (PATH) Act of 2015. Nothing is simple though.

With the passing of the PATH Act, Congress provided us with the tools needed to look forward and truly take advantage of certain expanded Bonus Depreciation and Section 179 expensing opportunities. Here is a quick summary of the current key expensing provisions for businesses.



SECTION 179 EXPENSING

Congress has made a number of changes to the Section 179 expensing election including but not limited to:

1. The $500,000 expensing limitation and $2 million phaseout amounts are made permanent and, starting in 2016, are indexed for inflation.

2. Qualified real property—which includes qualified leasehold improvement property, qualified retail improvement property and qualified restaurant property—continues to be eligible for expensing, without a carryover limitation. Note that each of the three types of qualified real property above has its own specific rules to meet before it becomes eligible for Section 179 expensing.

3. Also made permanent is the ability to expense off-the-shelf software.

4. Expensing of portable air-conditioning and heating units placed in service is allowed.

It should be noted that for Section 179 expensing purposes, “qualified retail improvement property” is limited to a retail business. Section 179 expensing arguably would not be available for a service business.

BONUS DEPRECIATION

Congress also has expanded Bonus Depreciation and extended these rules through 2019. The Bonus

Depreciation percentage is 50% for 2016 and 2017, and phases down to 40% in 2018 and 30% in 2019. There are special timing rules for long production period property and aircraft.

For property placed in service, the new law largely leaves in place the prior rules as to what kinds of property qualify for additional first-year Bonus Depreciation, which is tangible depreciable property with a recovery period of 20 years or less; computer software; or qualified leasehold improvement property with the original use of the property commencing with the taxpayer.

The new law includes a new type of real property, which is called "qualified improvement property," an expansion of the old "qualified leasehold improvement property." The new terminology is broader and provides for the inclusion of any improvement to an interior portion of a nonresidential real property building if the improvement is placed in service after the date the building was first placed in service. The expanded qualification does not include enlargement of the building, elevators and escalators, or any internal structural building framework.

It is also notable that under the new PATH Act provisions, Congress has made it permanent that any costs of "qualified leasehold building improvement property" and "qualified retail improvement property" not deducted using Section 179 or Bonus Depreciation are to be expensed over 15 years using straight-line depreciation.

Contact an **AutoCPAGroup** member to learn more about your expanded Section 179 and Bonus Depreciation year-end, intermediate and long-term opportunities. ✍

USED VEHICLE DEPARTMENT PROFITABILITY

Carl Woodward, CPA
Woodward & Associates, Inc.

Two functions in managing the used vehicle department are inventory management and retail pricing management. Most dealers would like to have no "water" in their used vehicle inventory and believe they will make more money if they have no "water." This sounds good but may not be realistic. I have seen dealers write their used inventory down to current wholesale value, a one-time write-down the dealership absorbs. For the next few months, the front-end gross might go up for a short period of time, but then the dealer is back to prior front-end gross profit margins. Why? Some dealers work from cost or "perceived cost" when selling vehicles and products. Their goals were admirable, but they were not able to keep their inventory "clean." In effect, they gave away gross profit to the customer by writing down used vehicles this one time.

Web service companies can assist dealers in valuing used vehicles for appraisals and guide dealers on the retail pricing when selling used vehicles. However, dealers using these Web service pricing mechanisms (perhaps incorrectly) may find their front-end gross profit margins are below industry average. I hear that some Web vendors tell dealers they will make less front-end gross per unit but will sell more units. I tested this premise on some of my dealers and did not find increased used retail sales.

I recently did a study of dealers with low used vehicle front-end gross profit margins to see how effective they were, by measuring their total dealership net profit as a percentage of sales. This year, the average dealer profit is around 2.4% of sales. Many dealers with low front-end used retail gross profits rely too much on Web service inventory values and selling prices. I found their net profit was less than 1.2% of sales. This indicates

please turn the page ☞

USED VEHICLE DEPARTMENT PROFITABILITY

(continued from page 3)

that allowing used retail front-end gross profit margins that are much lower than average causes dealerships to be far below average in overall dealership profitability. Some dealers are not properly using the Web service companies used vehicle inventory and pricing features. Talk with the Web service representative to find out how to obtain a better front-end gross. If you can't raise your used retail gross, I would suggest going back to the old way and discontinue using the used vehicle Web services. ✍