HEADLIGHTS

A PUBLICATION
OF THE AutoCPAGroup

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IS YOUR DEAL JACKET A CRIME SCENE?

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Information is powerful and often considered a good thing; however, what happens when information is lacking or the wrong information makes its way into your deal jacket? Are your deal jackets splattered with sticky notes or missing evidence, or have they ultimately left you wondering, "Who did it?"

Deal jackets are often the key source of evidence used by regulatory agents to review your dealership's compliance with laws and regulations. The wrong information, or lack of information, can cost your dealership a lot of money in taxes, fines or penalties.

How can you protect yourself and reduce the risk of noncompliance? Below are a few suggestions to clean up your deal jackets and monitor compliance.

✔ **Deal jacket checklist:** A comprehensive checklist helps ensure that a deal jacket is complete. The checklist should include a place for preparer signoff, to identify who completed the task. Key content should include privacy notice, customer identification, presentation menu, waivers, final menu, final finance or lease deal, and signed risk-based pricing disclosure, as well as signed used car buyers guide, if applicable.

✔ **Internal inspection:** Establishing a periodic deal jacket review process by an appropriate person independent of the preparation process can highlight systemic issues with deal jacket completion. Develop an audit review checklist to verify that document information matches, includ-

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ing presentation menus matching the actual finance or lease deals. Make sure to remove sticky notes and other notes from the file, as they could put your dealership at risk.

✔ **Training:** Providing regular training for new and existing personnel is imperative in order to mitigate risk and maintain clean and complete documentation. Deal jackets contain legal documents, and your sales and F&I teams are often preparing multiple legal documents per day. In addition, regulations change periodically and can differ from state to state. Make sure the members of your team understand the documents and their responsibility when completing.

✔ **Tone at the top:** When owners and managers take compliance seriously and model ethical behavior, most employees will follow their lead. While it is sometimes tempting to circumvent a process to close the deal, it could cost your dealership bigtime in the end.

If your dealership receives more than $10,000 in cash from one buyer, your dealership is required to file Form 8300, Report of Cash Payments Over $10,000 Received in a Trade or Business. Multiple transactions occurring within a 24-hour period, or multiple transactions known to be a series of connected transactions, require a Form 8300 to be filed if total cash received from those multiple transactions exceeds $10,000.

Do not let your deal jackets be the perpetrators of a loss to your dealership. Contact an AutoCPAGroup member to discuss your dealership's procedures. ✍

ANALYZING AN UNDERPERFORMING DEALERSHIP FOR PURCHASE

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One of the many steps a prospective buyer of a dealership takes is to determine the amount he or she is willing to pay for it. A rational purchaser needs to project how he or she will perform as an operator of this specific dealership.

Ideally, if the target dealer is performing within a normal range of profits for a particular manufacturer in the geographic area, the purchaser will review the existing dealership's financial statements and normalize earnings by adjusting for items such as nonmarket-value rent and officers' compensation.

If, instead, the target is severely underperforming or losing money, using a multiple-of-earnings formula is not as useful. There are many reasons a dealership may underperform; disinterested ownership, inadequate staffing and oversaturated markets are just a few. To reconstruct earnings on a prospective basis, key expenses need to be analyzed:

✔ **Rent expense:** Obtain a copy of the lease and set your projection, taking into account term and renewal options. If purchasing the property in a separate entity, base rent expense on a realistic cap rate for your area.

✔ **Insurance expense:** Get a preliminary quote from a local insurance broker, preferably one with experience insuring franchised dealers based on projected annual payroll, estimated number of employees, amount floor-planned, and square footage of the dealership and location.

✔ **Repair and maintenance expenses on equipment:** Review the seller's list of fixed assets and dates in service, and project a range for annual repair and maintenance costs. Inspect the assets if needed.

✔ **Utilities expense:** Review current owners' monthly bills. If their utilities are not on a level payment plan, review a few months' bills, taking into account seasonal fluctuations for certain areas of the country.

✔ **Data processing expense:** The buyer often inherits an existing dealer management system (DMS) contract, which is transferred to the new dealer at closing. Contract terms, features and obligations should be analyzed. Best practice is to retain a third-party DMS consultant to review the current contract and suggest alternatives. If a less-expensive DMS provider is recommended and the current contract expires within 2 years, the reduction in monthly fees would be included in the buyer's year-3 projection.

✔ **Employment expense:** The underperforming dealer is often understaffed, and employees are underpaid. To estimate total employee cost for the new dealership, use available information such as NADA's Dealership Workforce Study with regional metrics by job description and on volume. Obtain a list of all manager compensation and pay plans to see if they are reasonable, and compare them to the NADA study.

Formulating an earnings projection using historical data from an underperforming dealer is not always realistic. No matter at what stage you are in the process, before closing on a deal, consult with your AutoCPAGroup member to discuss formulating a realistic projection of earnings for your dealership. ✍

THE NEW 2017 TAX CUTS AND JOBS ACT

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The recently enacted Tax Cuts and Jobs Act (TCJA) did not provide simplification for the taxation of dealerships and their owners. Most of its provisions are effective starting in 2018. There are still many unknowns. Additional guidance will come in the way of regulations and further interpretation. The following is a high-level look at some of the areas that will likely impact dealer taxation:

Business Interest Deduction—For most taxpayers, business interest will be limited to business interest income plus 30% of adjusted taxable income. For dealers, the limitation will apply to interest expense other than floor-plan interest. The TCJA provides that 100% of floor-plan interest can be deducted. However, a taxpayer deducting floor-plan interest cannot use the bonus depreciation provisions of the new law. Real estate entities separate from the dealership entity would be subject to the interest deduction limitation but can elect out of the limitation provision. When electing out, longer lives must be used for depreciation of real property, and no bonus depreciation can be taken.

Bonus Depreciation—The TCJA provides for 100% bonus depreciation of qualifying assets acquired after September 27, 2017. The TCJA also extends bonus depreciation to used property. A dealer cannot utilize the 100% bonus depreciation for assets acquired after December 31, 2017, if deducting floor-plan interest but can utilize it for assets acquired after September 27, 2017, and before January 1, 2018.

Section 179 Expense—The expense limit is increased to $1 million and the asset acquisition limit is increased to $2.5 million, beginning in 2018.

Pass-through Deduction—In an effort to equalize the tax treatment of C corporations and pass-through entities, a deduction is allowed for qualified pass-through income from a partnership, S corporation, sole proprietorship or rental property reported on the individual's return. The deduction is 20% of the qualifying income, with limitations depending on taxable income and type of business. There are other complexities to this, and further guidance will be needed from the IRS or Congress.

Net Operating Loss (NOL)—For both corporations and individuals, NOLs occurring in 2018 and after cannot be carried back but can be carried forward indefinitely. Also, the NOL can be

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THE NEW 2017 TAX CUTS AND JOBS ACT

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used to offset only 80% of taxable income of a subsequent year.

Estate and Gift Taxes—The exemption amount for transfers at death and during lifetime was doubled to approximately $11.2 million per taxpayer. In 2025, this will revert to the 2017 level of approximately $5.6 million or more.

Most of the items have exceptions and other intricacies. Planning opportunities will exist to minimize tax. Contact an AutoCPAGroup member to discuss how these changes can benefit you. ✍