HEADLIGHTS

A PUBLICATION
OF THE AutoCPAGroup

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MANAGING A PROFITABLE F&I DEPARTMENT

Finance and insurance (F&I) gross profit is one of the most significant profit-enhancing opportunities for dealerships today, especially as new and used vehicle grosses continue to erode.

The potential for missed opportunity is significant. Our top-performing domestic dealer clients generate approximately $1,500 of F&I gross per new and used vehicle retailed, and our import clients generate approximately $1,100. According to NADA, the average dealer in 2016 retailed 930 new and 700 used units. Assuming that a dealer sells an average number of units but only generates $850 of F&I gross per vehicle retailed, a domestic dealer is missing out on over $1,000,000 in F&I gross compared with our top-performing dealers, and an import dealer is missing out on over $400,000.

Bart Haag, CPA
Albin, Randall & Bennett, CPAs

Start with a professional team to maximize your F&I profits. Top performers work with third-party F&I professionals. These companies can help recruit and train your team. They also assist the F&I team in establishing procedures to ensure that products are systematically offered to your customers in the right product mix, and that your sales team is ethical and efficient. They meet with you quarterly to review your F&I team's performance and discuss new opportunities. Don't overlook the chance to establish a reinsurance company for these products to capture the underwriting profit.

It is critical to ensure that you sell products in which your customers are interested. Review your product offerings with your F&I team once per year. Ideally, we recommend doing this as part of your annual business plan. Most of our top clients offer around five products.

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These include vehicle service contracts (VSCs), gap insurance, tire and wheel protection, paint and fabric protection, and a key replacement product. We generally find the gross profit mix to be approximately 40% finance reserve and 60% other product gross. Maximizing this mix will help move more income to your reinsurance company, which has a compounding effect on your overall profitability.

If your dealership does a lot of leasing or customer financing through credit unions, with proper training and a suite of products for leasing customers, you will still make gross on these deals. Products offered might include lease wear and tear in place of a VSC, and gap insurance. It is important to have a plan for these customers, such as matching the flat fee for your salesperson that is offered by the credit union and having a slightly different product offering for these customers.

If you are not producing numbers to be a top performer, contact your AutoCPAGroup member to strategize opportunities for improvement. ✍

TAX REFORM

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In mid-November 2017, the U.S. House of Representatives passed a tax reform bill. The U.S. Senate's version of tax reform is being finalized as this is being written. If the Senate bill passes, then a reconciliation process to arrive at a final bill will occur. The comments below highlight in brief a few items of interest. Even if nothing is passed, this gives you a view into the thinking of Congress about tax reform.

There are proposed changes to pass-through entities (S corporations, LLCs, partnerships), tax computations and self-employment tax. The owners of such entities, whether active in the entity's business or not, would see numerous changes. Depending on which proposal you read, the tax amount would vary. Additional self-employment tax may be imposed on owners of pass-through entities, including those who are not active in that business. Whether there will be much tax relief for owners of pass-through entities is difficult to tell.

Interest expense paid by businesses would be limited to a computed amount. While this may not have a large impact in the current low-interest-rate environment, it would clearly have a negative effect as interest rates rise and days' supply of inventory increases.

While there have been discussions in Congress recently about limiting the deductibility of advertising expense and terminating the use of the LIFO (last in, first out) method for inventory accounting, neither of these issues are mentioned in the two tax bills. However, meals and entertainment expenses would become fully nondeductible, whereas today only 50% is deductible.

There is a provision in the House bill that would cause rental income to be subject to self-employment tax. Current tax law specifically exempts rental income from this.

Both proposals have changes to estate tax, but they are very much different.

Eliminating the dreaded alternative minimum tax (AMT) appears in both proposals, but the elimination of electric vehicle credits is in the House proposal only. All this barely breaks the surface.

By the time you read this, more will have occurred in Congress. Assuming that the Senate passes its version, the two bills will need to be reconciled and then voted on by both chambers. If the reconciled bill passes both chambers, it goes to the president to sign or veto. The AutoCPAGroup has been working with NADA on aspects of this tax reform proposal that would most affect dealers, one of which is the limitation on interest expense deductions. Contact an AutoCPAGroup member to discuss this further. ✍

SAFEGUARD YOUR DEALERSHIP'S ASSETS

Kevin Allison, CPA
Peterson Sullivan LLP

Clients often ask, "What can I do to safeguard the assets of my business and ensure that the monthly financial reports are accurate?"

Below are our top questions, which cover controls every dealership should have. Keep in mind, internal controls can only help prevent fraud, theft and error. They do not guarantee the elimination of these dangers because controls can be overridden in a variety of ways, such as collusion.

1. Bank statements: Is the monthly bank statement opened, and are the canceled checks reviewed by someone who is independent of accounts receivable, accounts payable, cash receipts and bank reconciliations?

Independent review of the bank statement and enclosures can catch fraudulent transactions, such as forged checks, modified checks, odd or improper vendors, multiple endorsements and improper cash transfers.

2. Journal vouchers: Are general journal entries reviewed and approved either during the month or at month end?

Journal vouchers are one of the most powerful accounting system tools. They enable corrections of errors and posting of nonstandard transactions. They can also be used to hide fraudulent transactions or manipulate the financial reports. Independent review and approval are critical to ensure that only necessary entries have been made.

3. Write-off approval: Are write-offs of accounts receivable, policy work and no-charge repair orders reviewed and approved by the sales manager or another manager?

4. Corporate credit cards: Do corporate credit cards have specified spending limits? Are employees required to turn in all receipts? Are statements and receipts reviewed regularly to ensure that all charges relate to dealership operations?

5. Reserve accounts: Are all liability reserve account postings (such as those to wholesale loss or service contract chargeback liability reserve accounts) reviewed and approved in detail?

Generally, reserve accounts do not have to reconcile with, or match, any specific item or amount. Independent approval and review can prevent fraudulent transactions or simple posting errors, which can be hidden by posting against the reserve accounts.

6. Flooring accounts: Is the flooring liability account reconciled in detail on a monthly basis? This helps ensure that outstanding amounts are related to inventory on hand or recently sold, and can detect errors or theft if an inventory item has been sold (or never existed) but the flooring balance has not been paid.

7. Schedules: Are the schedules produced by the accounting system reviewed and reconciled in detail on a monthly basis?

At least twice a month, schedules should be reviewed for old outstanding items and/or unusual balances. The reviewer should also be alert for entries posted through journals that are unusual for the account being reviewed.

8. Rotation of accounting duties: Are employees, especially those in the accounting department, required to take vacations? If not, are employees cross-trained on multiple functions, and do they change functions for continual two-week periods at least annually?

Rotation of duties or enforced vacation can create a gap in the perpetrators' ability for manipulation and may highlight improper transactions.

9. Used vehicle transactions: Are employees monitored to ensure that used vehicle transactions take place through normal dealership operations?

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SAFEGUARD YOUR DEALERSHIP'S ASSETS

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Relationships with all wholesalers should be evaluated at least quarterly, and all sales to wholesalers should be reviewed and authorized by the dealer or general manager.

Following the basic procedures outlined here will provide the foundation for a dealership's overall internal control. There are many other controls that may be necessary or useful to prevent fraud, theft or financial errors.

Contact your **AutoCPAGroup** member if you would like to discuss this matter in further detail. ✍