



HEADLIGHTS

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VALUATION OF DEALERSHIP FIXED ASSETS

Many times, dealerships need to determine the value of their fixed assets. Some of the reasons to value the fixed assets include buy-sells of dealerships, insurance coverage, estate-tax returns and stockholder issues. In this article, guidelines for reasonably determining the value of the dealership's fixed assets will be provided. Fixed assets include computer equipment and software, service department and body-shop equipment and tools, parts department equipment, office equipment, furniture and fixtures, etc. Fixed assets do not include land and buildings, leasehold improvements, company vehicles, or lease and rental vehicles.

The starting point for determining the fixed-asset value is the fixed-asset schedule prepared annually by the dealership's CPA firm. This fixed-asset schedule should be adjusted to include purchased fixed assets expensed at acquisition, such as franchise special tools and other existing fixed assets that are not included on this schedule.

Items that are missing should be added to this schedule, and items that are not usable should be removed from this schedule. A physical inventory is suggested to be taken of all fixed assets of the dealership and reconciled with the schedule. After all appropriate adjustments have been made, the items included on the schedule of fixed assets should agree with the physical inventory. The items on this revised schedule should include only those items that exist, are in usable condition and are still used regularly.

Those in the industry know that a fixed asset purchased today is worth 100% of its cost, something less than 100% at the end of 12

months, and as long as it is usable and it is being used, it is worth a minimal amount, say 10% of original cost, at the end of seven years. You can cal-

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culate an estimate of this residual value based on your specific circumstances by estimating what it will cost to replace the items and comparing that value to their original cost. In forming your estimate, be sure to include the cost of locating the items in a reasonable length of time, making them usable and delivering them to the dealership. Generally, there is an amount someone will pay for a functioning used item rather than buying a new item for a substantially larger investment. Typically, equipment depreciates faster in its earlier years and at a slower rate in later years.

As an example, assume you purchase an item of shop equipment today for \$10,000. What will it be worth at the end of 11 months? You might be lucky enough to find it at a distress auction for a small percentage of its original cost, but this is not likely. It is more reasonable to view this as a choice of buying a new car or one that has been used for 11 months with average mileage. What is the value differential between the new item and one that is 11 months old? Those in the industry with whom I have discussed this concept agree that the “value” of this used equipment versus the new item approximates 80% of the original value (plus or minus 5%). The computer and software that comprise your dealership’s system, if purchased today, might be worth as much as 50% of the original cost at the end of the year at an auction. However, if it is still usable in one year and after considering costs to replace it, including the time needed to find a replacement (the

“going concern” issue), this computer has a value greater than it would have at a distressed auction sale, but still something less than the original cost. For computer equipment, it is assumed a maintenance agreement exists to keep it operational.

In my experience, no two equipment appraisers would appraise used equipment within 5% of the true “going concern” value due to the lack of comparables, the large amount of judgment needed to determine the value of certain higher value items and the difficulty of assigning a value to acquisition costs, such as search time and delivery cost (including price paid at auction, assuming the items are even able to be found).

The following guidelines should produce a reasonable overall total value of fixed assets for most dealerships. Apply the following percentages to your updated and adjusted fixed-asset schedule to obtain a reasonable estimate of the “going concern” value of your dealership’s fixed assets.

Assets purchased	% of original cost
Less than 12 months old	80%
12 mos. to less than 24 mos.	65%
24 mos. to less than 36 mos.	50%
36 mos. to less than 48 mos.	40%
48 mos. to less than 60 mos.	30%
60 mos. to less than 72 mos.	20%
72 mos. and older	10%

WHO PAYS FOR DEMONSTRATOR LIABILITY?

For years, dealerships have routinely awarded demonstrators to sales department employees and other department managers. However, that’s been slowly changing due to concerns about demonstrator liability.

Frequently, users of demonstrators believe they have a right to the vehicle and don’t exercise proper care or judgment. What happens when an employee wrecks the demonstrator? We suggest that dealers should hold their employees responsible for

any and all deductibles, whether or not the accident is the employee’s fault.

If the accident is not the employee’s fault, the deductible from the dealership’s insurance policy is the responsibility of the employee, no matter how high, and the other person’s insurance company should reimburse the employee for the deductible.

If the accident is the employee’s fault, the employee can’t complain about paying 100% of the deductible. The employee would have been required to pay the

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deductible if he or she owned the vehicle personally.

What should you do if an employee does not want to honor this demonstrator policy? Quite simply, the employee forfeits the right to drive a dealer-

ship-owned vehicle. For full-time drivers for the dealership, such as parts drivers, you might want to modify this policy slightly by limiting the portion of the deductible they would have to pay. ↵

WALKING OFF WITH THE STORE ... AND WHAT YOU CAN DO TO PREVENT IT

Every profession has its own jargon and the world of accounting is certainly no exception. For example, dealers have “flooring,” “bushing,” “spiffs,” among others, and we have words like “internal controls,” “separation of duties” and “employee defalcation.” Accountants’ terms are often less colorful and descriptive, so to keep the glaze from forming on your eyes, let’s use “loss prevention” in this discussion about theft.

Think theft is not happening at your dealership? A recent study estimated that dealerships lose approximately 2%–3% of their total annual revenue per year to cash theft and mishandling of assets by employees. Dealerships are especially vulnerable because they often lack the controls found in larger organizations with internal auditors (although as we’ve seen, this is no panacea either). And the “out-of-sight, out-of-mind” nature of employee theft usually means that any efforts to prevent it are taken only after the discovery of it. Sometimes, theft comes to light by sheer dumb luck, but it’s more likely that theft is discovered by functioning loss-prevention procedures.

An understanding of factors that lead employees to become dishonest is necessary. Research in the area of fraud has identified three things that usually exist when fraud occurs:

1. opportunity;
2. motivation; and
3. rationalization.

Disrupt any of these factors and your risk goes down. Of the three, the dealer has the best chance to lower the “theft threat” by taking away the opportunity. This means putting effective theft-

prevention routines in place and your employees knowing what they are. These steps are rarely given the same priority as customer satisfaction, but the potential impact of theft to the bottom line can be as significant.

Motivation and rationalization factors are more difficult to evaluate when hiring employees. Unfortunately, oftentimes the particular employee caught stealing from you is the biggest surprise. A sobering fact is that employees caught stealing can be trusted, senior employees. Worse, it’s a sad truth that the more senior the employee, the greater the loss. Does this mean you should adopt airport security measures and distrust everyone? Clearly, the answer is no, as trust is invaluable to healthy employer–employee relations. However, blind trust is a mistake.

Feeling confident about the strength of your dealership’s controls? Call your AutoCPAGroup member for a complimentary 10-point test to check if you are justified in feeling that way. We recommend that loss-prevention procedures be reviewed annually or more frequently if there are specific concerns about certain employees or questionable activities. In the case of theft and loss, an ounce of prevention is worth a pound of cure.

Finally, it’s no secret that the most successful deal-

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erships have the best employees. Your chances to land the honest ones are enhanced when you:

- ✓ Obtain references from past employers;
- ✓ Require applications from all prospective employees;
- ✓ Obtain a credit report (employees with bad credit are a bigger threat);
- ✓ Perform drug testing;
- ✓ Request a criminal report, when appropriate; and
- ✓ Bond employees when it makes sense to do so.

See your attorney first to learn how to legally implement the above hiring procedures. In matters of hiring the best employees, your “gut instincts” may be better suited to ordering lunch. ☞

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