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Dealer Insights

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Now is the time to conduct year-end tax planning

Is an item on your to-do list "Discuss financial strategies with my CPA for the coming year?" Maybe it should be.

The end of the year is an optimal time to sit down with your CPA, plan moves and discuss ways to trim your 2017 tax bill. Financial strategies you put in place by December 31 can save you big money come April.

Defer income, accelerate expenses

One common year-end strategy is to defer income into the following year and accelerate expenses into the current year. Doing so will delay the payment of some amount of taxes for one year by reducing your taxable income — and that boosts current cash flow. This strategy could be even more beneficial this year if tax legislation is signed into law reducing tax rates for 2018.

Additionally, you might be able to make a deduction for prepaid expenses, if they're recurring services and will be incurred within the next 12 months. Consult with your CPA about a specific election to expense these recurring costs.

Another avenue: Interest credits and other manufacturer payments can be treated as trade discounts deferred for tax purposes under certain circumstances. Reducing the cost of inventory in this way could significantly lower your dealership's taxable income in the current year. If you're not already taking advantage of this benefit, you'll need to file a change of accounting method.

Look at inventory management

Another way to possibly lower your 2017 taxes is to write down your used vehicle inventory to market value, assuming that this is less than cost value. Use an industry guide such as *Kelley Blue Book* or NADA guides as the basis for your market value adjustments. You'll then be able to take a deduction based on the lower resulting inventory value. If you use last-in, first-out (LIFO) inventory accounting for used vehicles, though, you can't take used vehicle write-downs.

Using LIFO to value used vehicle inventory hasn't been as beneficial in recent years as it once was, due to low inflation rates. By counting the last vehicles on the lot as the first vehicles sold, LIFO lowers taxable profits on these vehicles. In general, LIFO reduces taxable income by the rate of inflation, so if inflation picks up in the future, LIFO could become more attractive for valuing used inventory.

Meanwhile, if you use LIFO to value new vehicle inventory, lower inventory values could cause LIFO recapture

Make tax-deductible retirement plan contributions

One of the most commonly overlooked dealership tax-reduction strategies is making tax-deductible contributions to employees' retirement plans. Two examples are 401(k) plans and profit-sharing plans.

Your dealership can match contributions employees make to their 401(k) accounts at whatever percentage you desire. In addition or instead, you can allow employees to share in the dealership's financial success by making contributions to a profit-sharing plan.

For 2017, you can contribute up to $54,000 or 25% of compensation (whichever is less) to employees' profit-sharing and 401(k) accounts. This is on a combined basis, but reduced by any contributions the employee makes to the 401(k) other than "catch-up" contributions. The maximum amount of employee 401(k) contributions this year is $18,000, plus an additional $6,000 catch-up contribution if an employee is age 50 or over.

Even better, you have until your 2017 tax-filing deadline — including extensions — to make tax-deductible contributions to employees' 401(k) or profit-sharing accounts for tax-year 2017, as long as the plan exists on December 31, 2017.

income for 2017. But the change in the inflation index has a greater impact on your LIFO layer than does your inventory value.

Write off uncollectible receivables

It's not uncommon for dealerships to have uncollected accounts receivable at the end of the year. Review your past-due receivables and decide which ones are uncollectible — then write these off before the end of 2017 as bad debt expenses.

You can still pursue collection next year. If you're successful, you'll then need to include the collected revenue in your income for the year in which it's collected.

Still more ideas

Here are some more year-end tax strategies to consider:

Hire your children to perform work for your dealership. This could reduce your personal taxes, because you can deduct the wages (assuming they're reasonable) and your children's tax rate is probably lower than your individual tax rate. But make sure the kids are paid a market rate for their services and actually perform them.

Consider discounting or selling at auction slow-moving used vehicles. If you sell them at a loss before the end of this year, you can deduct this loss on your 2017 tax return.

Reconcile the parts inventory balances on your books with a physical listing of these parts. Then you can write off any discrepancies, along with any obsolete parts that are nonreturnable.

Impact of tax reform?

Keep in mind that the various tax reform proposals being discussed in Washington could affect some of these strategies. Talk to your tax advisor about the current status of tax reform and whether this could affect your plans.

Getting to "yes"

Financial keys to securing a commercial loan

Dealerships often use a floor plan to finance their vehicle inventory, but you might need another commercial loan or line of credit for an assortment of reasons. For example, you might decide to expand your facilities, hire more employees, or buy service department equipment. Or maybe you want a cushion to fund occasional working capital shortfalls.

Before contacting your lender, it's important to gather all relevant information to prove your business is creditworthy. By anticipating information requests, you can expedite the application process and improve your chances of approval.

GAAP

GAAP, or U.S. Generally Accepted Accounting Principles, is a collection of specific accounting rules and principles that's regularly updated by the Financial Accounting Standards Board. Lenders generally prefer GAAP financial statements over those prepared under special purpose frameworks, such as cash- or tax-basis financial statements, because GAAP financials tend to be more transparent and consistent from one business (or reporting period) to the next.

When you apply for a loan, underwriters may ask for both *GAAP financial statements and financial statements to your manufacturer.*

Dealerships that follow GAAP use accrual-basis reporting. That is, they record sales as they're earned and expenses when they're incurred. A

dealership's balance sheet also includes receivables, payables, prepaid assets and accrued expenses. These accounts generally are created only when a business uses accrual accounting.

Reports to manufacturers

Most dealership franchise agreements require submission of monthly financial statements to manufacturers based on a format the manufacturer provides. Sometimes these financial reports don't jibe with the format of GAAP financial statements. For example, a manufacturer's financial report might focus solely on income statement items or, conversely, contain extra information that's not relevant to lenders.

When you apply for a loan, underwriters may ask for *both* GAAP financial statements and financial statements to your manufacturer. If they receive both types of reports, underwriters are likely to inquire about any discrepancies. For example, if your vehicle sales differ between the reports, it might suggest that your dealership is holding open the sales ledger on the last day of the reporting period to boost sales. This might lead to questions about your cutoff policies.

Other hot spots

Other items lenders typically consider during the application process include:

Inventory turnover. Sales volume and how long vehicles sit on the lot can be key indicators of a dealership's overall health.

Customer satisfaction ratings. Satisfied customers are likely to return to your dealership to service vehicles and purchase vehicles in the future.

Accounts payable aging. Aged payables may indicate that you're having trouble paying bills in a timely manner.

Liquidity metrics. Short-term assets generally should exceed short-term liabilities. Lenders may be leery if you don't have surplus working capital to fund operating expenses.

Typically, a lender will visit your showroom before approving a loan application. He or she will evaluate operations from the perspective of a hypothetical customer. Are salespeople friendly and knowledgeable? Is the service area clean and organized? Is the showroom updated and easy to access from the street? A lender also may request a meeting with your manufacturer's representative to confirm financial results and discuss how you intend to use the loan proceeds for future operations.

Ready, set, apply

Need help securing a commercial loan for your dealership? Your CPA can be a valuable resource during the application process.

Is your website all that it can be?

The purpose of your dealership's website is to present your image, inventory and services in the best image, right? That may still be true but, in today's car-buying universe, the primary goals of your website should be to guide customers through the car-buying process and motivate them to eventually buy a vehicle from you.

Here's some information to consider the next time you redesign your website. And after you read this article, you may want to redesign it soon!

Making things easy

Car buyers now spend an average of 14 hours shopping online, up from just five hours a decade ago, according to a study by the National Automobile Dealers Association and global consultants McKinsey & Company. So, the more you can do to help customers zero in on the right vehicle using your website, the faster and smoother their shopping experience might be once they arrive at your store.

Focus, in particular, on your online product presentation. Make it easy for customers to browse your entire vehicle inventory online using whatever criteria they choose: used vs. new, price, make, model, mileage and so on. Include plenty of high-quality vehicle photos and even videos to enable customers to take a virtual test drive of the car or truck they're interested in.

Gearing up for trade-ins

To boost profitability, try to get your customers thinking trade-in before they set foot in your door.

Consider developing a trade-in page on your website that includes an explanation of the benefits of trading in at the dealership vs. selling a vehicle to a private party. Also explain how your trade-in process works. And work with your website designer

to create an online trade evaluation tool that customers can use to get an idea of their trade-in's approximate value.

Providing useful content

Content is king in the online marketing world, so include plenty of resources on your site designed to help educate and inform customers, rather than just sell to them. Adding fresh content to your site regularly also can help improve your search engine optimization results.

Articles, e-books and videos on buying and maintaining vehicles are helpful types of content found on dealership websites today. Some dealers prefer to outsource content creation to an agency that specializes in this instead of trying to create and manage it themselves.

Putting it all out there

Many dealerships use a wide range of digital marketing tools such as e-newsletters, social media marketing and online videos. Your website should centralize and organize all of these marketing initiatives.

Are there prominent links on your home page to your social media platforms, such as your dealership's Facebook, Twitter and Google+ pages and your YouTube channel? Is there a sign-up option for your e-newsletter? Also, consider adding a live chat option (if you don't have one already) so customers can communicate virtually with a customer service rep.

Spotting trends

The desire among customers to adopt a *fully* digital car-buying experience is relatively small but growing, according to Foresight Research's recent Dealer Action Report, *Making Digital Work for You*.

A full online showroom where they can complete the car-buying process without visiting a dealership was preferred by 14% of respondents, up from 10% a year earlier. Conversely, 60% said they prefer physically visiting the dealership, down from 68% a year before.

Content is king in the online marketing world.

Not surprisingly, a higher percentage of car buyers ages 18–34 (20%) and a lower percentage of buyers age 55 and over (11%) prefer a full online showroom.

Given these trends — and because young buyers are especially interested in purchasing cars online — it might be smart to begin taking steps toward creating a fully digital car-buying experience for the customers who want it.

The best website, ever

Common dealership wisdom used to be that your showroom should be the most attractive, comfortable and inviting place it can be for prospective buyers. And that might still be the case. But your *website* also should meet those criteria if you want the best shot at making the sale.

How to prepare for a sales slowdown

Vehicle sales are expected to decelerate from the breakneck speed of the past two years, according to some industry analysts. This makes now a good time to strategize about how your dealership can maintain (or exceed) revenue and profit levels in 2018 and beyond even if vehicle sales slow.

One of the keys is to focus more sharply on fixed operations (parts, service, paint and body repair) and F&I to drive revenue and profits. In fact, the vehicle sale should be viewed as just the first step in tapping your customers' lifetime value.

Service: Get them in the door

Fixed operations account for a large share of profits at many dealerships, even when vehicle sales are booming. Your initial goal should be to encourage car buyers to visit your dealership for their very first service appointment.

To do this, walk buyers over to your service department and introduce them to your service manager. Ask them if they'd like to schedule their first appointment now, and consider giving them a complimentary first oil change.

Next, make sure you provide outstanding service and value to customers when they come in for that appointment. This will help position your dealership as their go-to option for vehicle service — and not give them any reason to try out an independent repair shop.

Also make sure your customer relationship management system is capable of initiating regular communication with buyers after the sale via email, text and postal mail. This way, you can let customers know when their vehicles are due for regularly scheduled maintenance and perhaps offer an incentive for visiting your dealership for service. Also, enable customers to make service appointments via your website.

F&I: Sell profitable products

F&I is a source of tremendous untapped revenue and profit for many dealerships. To maximize the financial contributions of this department, start by identifying the highest margin F&I products your customers are most likely to buy. Vehicle financing? Extended warranties? Rust protection?

Also focus on educating your customers about the benefits of F&I products, instead of using hard sales tactics to try to pressure them into buying. Devise and implement a standard F&I selling process and use it with each vehicle sold. And make sure your employees thoroughly understand the nuances of all your F&I products so they can clearly explain them to customers and answer common questions.

It's time

Get ready now for a possible slowdown in vehicle sales: Strategize about how you can boost sales from fixed operations and F&I to help make up potential lost revenue and profits. You'll be ahead of the game.

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