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Goodman & Company
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Goodman & Company, a Mid Atlantic regional certified public accounting firm working with dealerships representing virtually every manufacturer, delivering quality accounting, tax and specialized services.

Turning lemons into lemonade

Dealership acquisitions call for careful forethought

Ann Landers may no longer be with us, but one bit of her advice still rings true: "When life hands you a lemon, make lemonade." Nowadays, most dealers are being handed a lemon in the form of plummeting profit margins, stiff competition, rising interest rates and increasing demands from automakers.

Yet a few brave dealers are trying to take these sour times and turn them into lemonade by acquiring other dealerships and expanding their operations. Should you follow suit? Maybe, maybe not — deciding whether to acquire another dealership calls for careful forethought.

Ask the right questions

Before even considering an acquisition, you need to look at many factors. First, is your business in good shape in terms of cash flow, revenue and profitability? Uniting two struggling dealerships rarely creates one strong operation. Other pertinent questions to ask include:

- Do franchise requirements complicate the picture or, conversely, might there be factory assistance available when consolidating several brands under one roof?
- What do you see in the future for the brands involved? A weak brand today may be much stronger tomorrow — or vice versa.
- Is your dealership's area economically diversified or does it count on one company or one industry for its prosperity?
- How do your banking relationships and your access to capital look?

Remember, a successful dealership — selling at a premium — will require a substantial initial cash outlay and probably pose some challenges in generating a return on your investment.

Think geographically

Another important matter to consider before expanding is the degree to which the move will allow you to spread out your normal business risks.

For instance, your skill and good reputation may tempt you to expand in your community and to choose a brand that appeals to your current customer base. After all, these are the people you know, and who know you.

Unfortunately, a downturn in your community, or among that core of customers, could hit your businesses hard. For this reason, many dealers choose to venture into new territory. In some cases, that means buying in a different town with a different economic base. Or it may mean purchasing a dealership that is likely to appeal to a different clientele.

Thus, if there is an economic downturn in one area, the likelihood of it adversely affecting both operations is lessened. Diversifying in this manner can also help protect your dealership from being wiped out completely in the case of a natural disaster.

Consider your team

Although you'll need to thoroughly examine the books and the economy as a whole, you should also take a good look at the people working at the dealership you're considering buying. Easier said than done, of course — especially if the current owner doesn't want a potential sale to distract his or her staff.

But it's still important to determine the strengths and weaknesses of the workforce you'll be inheriting, because auto retailing is ultimately a people business. Also check the prospect's employment and work

Should you launch a satellite service facility?

You are busier than ever — and so are your customers. As a result, you may have noticed that more and more of your clientele are becoming increasingly lax about scheduling (and perhaps showing up for) service appointments.

Some dealerships are grappling with this problem by opening satellite service locations. Doing so not only helps your customers continue to use your dealership for service, but it provides an important sales tool — especially for dealers who sell to a wide geographic area.

In fact, satellite service facilities tend to do best for dealerships whose buyers live in a concentrated area far from the dealership as well as for dealerships adjacent to large, thinly populated areas.

Of course, there are risks: The startup costs will likely put a considerable drain on your cash flow. And if the facility doesn't carry its weight, you may have to pull the plug and face a considerable loss.

But if acquiring another dealership seems a bit too much, opening a satellite service facility can offer a potentially profitable alternative.

policies. Is there going to be a clash of cultures if you take over?

In addition, just as any acquisition is guaranteed to disrupt the business being acquired, it can also negatively affect your own staff. Questions, typically unspoken, will run the gamut from "Will I still have a job?" to "Will I be expected to do more work?" to "Could I get a promotion out of this?"

Generally, the best way to handle the disruption is through open communication. Let your workers know what is happening as soon as the ink is dry. Have a transition plan ready to go and implement it as quickly as possible. Acquisitions can be disruptive, but with a firm hand and a sound strategy, the dust should settle quickly.

Cover your bases

Even in today's tough auto retailing environment, expanding your business through an acquisition isn't out of the question. You just need to be cautious and take the time to do the necessary due diligence.

Be sure to bring your accounting and legal advisors into the picture as well. And, above all, don't rush into an agreement before you have done all your homework.

The Pension Protection Act of 2006

What do dealers need to know?

In a press release last August, the White House labeled the Pension Protection Act of 2006 (PPA) as the most sweeping reform of the nation's pension laws in more than 30 years. Six weeks later, The *National Law Journal* concluded that it could bring "a sharp rise" in legal work to attorneys who handle pension-related casework.

Both assessments may be a bit exaggerated, but the law will clearly have a substantial impact on your business and its employees. If you haven't already looked at its ramifications, now is a good time to review PPA's impact on your dealership's retirement plan arrangements — both those in place and any you might be considering.

Underfunding under the gun

While defined benefit plans may be losing favor among employers, plans that remain in effect will have to meet new requirements. Under PPA, most will have seven years, beginning in 2008, to become fully funded. Companies that fail to meet these terms could be subject to a 10% excise tax.

PPA also addresses issues surrounding cash-balance plans. In the past, controversy has arisen about whether these plans discriminate against older workers. PPA makes it easier and potentially safer for employers to convert to these plans, which are generally easier for employees to understand and often less costly to fund and administer.

401(k)s for everyone

PPA simplifies the rules for automatically enrolling employees in a 401(k) plan, using certain preset contributions. In the past, employees had to choose to participate by voluntarily filling out the paperwork. Now they'll have to opt out of the plan, if they so choose.

To make automatic enrollment an easier sell, and to increase the likelihood that a larger number of employees will stick with their 401(k)s, PPA eases provisions for hardship withdrawals. If an employee really needs the money in his or her plan for certain purposes, he or she may have less trouble getting to it.

Employees should also appreciate the provisions that ease the tax burdens on nonspouse beneficiaries. In the past, only a spouse could roll over the benefits inherited from a qualified retirement plan into an IRA. Now, nonspouse beneficiaries, such as children or domestic partners, enjoy the same tax benefits.

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In addition, PPA brings good news to people with — or employers considering — Roth 401(k) plans. Under previous legislation, these arrangements were set to expire in 2011. They are now permanent fixtures on the retirement planning scene.

A Roth 401(k) allows participants to contribute posttax dollars to the account. Funds build up tax free and aren't subject to the normal distribution requirements.

Charitable contributions scrutinized

If you are considering donating to charity, be aware that PPA imposes stricter rules on certain noncash donations, such as furniture, clothes and household items.

Under its provisions, donated items must be in "good" condition. Items in less than good condition don't qualify for a deduction. The law, however, doesn't define "good." As a result, enforcement of this provision may prove difficult.

If PPA makes some contributions more difficult, it at least eases the restrictions on charitable contributions from an IRA. Under its provisions, through 2007, taxpayers age 70½ and older may now make a cash donation directly from their IRA account to a recognized charity.

The ceiling is $100,000 per year and, because the donation involves a direct transfer, the IRA owner won't have to count the money as income. Of course, it won't qualify for a charitable contribution deduction either. Yet, because certain limitations can be avoided, it may prove advantageous.

The potential is in the details

The details of PPA are undeniably complex. But within those details lies the potential to reevaluate and, one hopes, improve the retirement benefits you choose for yourself along with those you offer your employees.

Subprime buyers bring both risk and opportunity

When interest rates and gasoline prices were low, subprime buyers became relatively easy to serve. The number of loans to these customers rose and many dealers profited. But times have changed.

Although vehicle repossessions and losses fell in 2005, according to the National Automotive Finance Association's 2006 *Non-Prime Automotive Financing Survey*, industry observers now report that the pendulum is swinging the other way. As this article went to press, many subprime lenders were expecting 2006 to go down as a significantly leaner year.

The market is growing

You may be wondering: Are subprime buyers still a viable customer base? As you might expect, there is no clear-cut answer. One thing, however, is for sure — the subprime market is growing.

Why? For one, the rise in interest rates over the last year has increased housing costs for many consumers, knocking debt-to-income ratios askew. Meanwhile, the nation's bout with high fuel costs earlier this year has created more credit card debt, which also has a negative effect on credit ratings.

And though the economy remains relatively strong, these factors will push many good customers into subprime territory when they visit your showroom.

It's whom you know (and employ)

You can take many steps to reduce the scope of this problem. For starters, if you haven't already, put all your lenders that specialize in difficult loans on speed dial. As bank rates increase, so does the importance of keeping these contacts up to date and regularly reviewing credit sources.

Also critical: Having salespeople that are skilled at guiding customers to *affordable* transportation options. This ability is, to some degree, innate. But it can also be learned: Look into sales training programs that address this issue.

Although the economy remains relatively strong, a variety of factors will push many good customers into subprime territory.

It pays to be cautious

Although you can't possibly serve every customer with questionable credit, even small improvements in this area can significantly improve your bottom line. Then again, become too aggressive and watchdog groups ranging from consumer advocates to government agencies may take an unhealthy interest in your business practices.

Dealers who have arranged loans that charge up to 25% interest have drawn scrutiny and prompted legal action — even when that level of interest was allowed by law. If you're uncertain about whether a prospective loan might raise eyebrows, contact your CPA for a second opinion.

A big step to consider

Some dealerships are taking a big step when dealing with subprime customers (and everyone else). They're opting to not only sell them vehicles, but also collect payments from them. These so-called "buy here, pay here" stores are a potential solution, but a fairly extreme one.

Properly run, "buy here, pay here" operations can be very profitable. But they're also very risky. Default rates on subprime customers in recent years have run between 6% and 8%, according to a recent *Automotive News* article. And defaults can go as high as 25%, says the same source.

The future seems certain

Although not much is certain about subprime customers, one thing is — the future will likely hold many more of them. Start developing your plans for dealing with them today.

Always be closing! 5 ways to motivate your sales staff

In the 1992 film *Glengarry Glen Ross*, a venomous sales consultant played by Alec Baldwin tells a beleaguered sales staff that first prize in the new sales contest is a new Cadillac Eldorado and second prize is a set of steak knives. What's third prize? "Third prize is you're fired," he spits. Now *that's* motivation.

Of course, here in the real world, such an approach probably won't get you very far. Nonetheless, keeping your sales staff in the game is important to the financial success of your dealership. Here are five ways to do so:

1. Provide sound leadership. Cinematic dramatics aside, salespeople work best in a *positive* environment. And for that to exist, you need a top-notch sales manager who can set appropriate goals; clearly explain your dealership's sales policies, procedures and requirements; and be on hand to ensure everything runs smoothly.

2. Reward success. Make sure your most productive, successful salespeople are properly and equitably compensated. Figure commissions in a timely manner. There is nothing more destructive to morale than to reduce your rock stars to begging for their paychecks.

3. Use contests wisely. Sales contests work, but setting up goals that only experienced salespeople with many repeat customers can reach may actually disenfranchise eager, but less experienced, staff members. Develop contests in which anyone who puts in the extra effort to achieve reasonable goals can succeed.

4. Discover your salespeople's personal goals. Learning what your sellers want in life helps you and your sales manager better develop each team member's career path. For example, some salespeople have management aspirations from the get-go, while others don't. You need to know what direction a salesperson wants to head in before offering guidance.

5. Fix your mistakes quickly. Who hasn't hired a promising salesperson only to discover that he or she is a huckster or a source of negativity? Although you should always make an honest and well-documented effort to help poor performers improve, sometimes the best solution is to show them the door. (Before you fire anyone, however, consult your attorney.)

From cars to cotter pins

Inventory management tips for dealers

It's a fact: Dealers have massive sums of money tied up in inventory. From the new vehicles on the showroom floor to the used vehicles on the back lot to the seemingly infinite number of items in the parts department, each and every item has to be ordered, shipped, received, inventoried, stocked, safeguarded and sold.

From cars to cotter pins, the financial success of your dealership lies in inventory management. For this reason, it's imperative that you stay on top of this critical task.

New vehicles: The biggest challenge

What to order for the showroom floor is typically a dealer's biggest inventory challenge — especially when a new model is unveiled. In these cases, manufacturers often make your life easy by building only fully loaded, premium vehicles.

But, once "new car fever" has cooled, your choices become more difficult — and more important. With floorplanning costs now taking a bigger bite out of most dealerships' profits, many dealers are ordering only what they know will sell quickly — even if that means passing on some sales.

Others, however, are banding together and pooling inventory. These dealers typically handle the same brand and are close enough geographically to make this sharing practical but far enough apart to not directly compete for customers.

Parts: A tricky balance

Dealers are increasingly looking at the turnover rates for inventoried parts. If yours are too long, you may be wasting money tying up funds in slow-moving parts or vehicles. Then again, too short a turnover may mean you're losing sales by not having the parts or products customers want because these items aren't in stock.

One way to find the right balance is to closely track pattern failures in any or all of the vehicles you stock (or typically service). When a clear pattern emerges, it's a safer bet to order larger than normal quantities of the appropriate parts, as there will likely be a greater-than-normal demand.

If you still find yourself holding excessive quantities of some items, look at your return allowances. Can you renegotiate these with your suppliers? Are your parts managers using them optimally? These are important questions to ask.

Technology: More important than ever

Whether it's vehicles, parts or some other product you sell, having an adequate — but not excessive — supply on hand is the name of the game. And, to this end, technology is more important than ever.

Meet with your financial and technology advisors regularly to discuss whether you're getting the inventory data you need (and when you need it) and to look at what new hardware and software has hit the market.

Of course, the best technology available is only as good as the people using it. So also be sure you're providing your staff members with the necessary ongoing training.

New year: New opportunity

As we usher in a new year, you have a prime opportunity to make 2007 your best inventory management year ever. You'll no doubt find the fruits of this endeavor quite sweet.

Meet the Goodman & Company Auto Dealership Specialists

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