

Steering your dealership to higher profits

A publication of Woodward & Associates
Consultants to the Automotive Industry

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March 2011

January Monthly Profit Trends

January 2011 was a good profit month for most new vehicle dealers. As you can see below, the number of new vehicle dealers losing money was only 20%, and the profits, depending on the size of the dealership, were reasonable in many cases. Nationwide new vehicle sales in January 2011 increased over January 2009 and 2010, as reported by *Automotive News*. It appears that each month, for the last few months, has improved over the same month of the prior year. Nationwide new vehicle sales are rebounding and hopefully will be back to the level of a few years ago in the next year or two.

	Jan. Profit More Than \$40,000	Jan. Profit Less Than \$40,000	Jan. Loss Less Than \$20,000	Jan. Loss Less Than \$20,000
Chrysler	20%	60%	20%	0%
Ford	40%	40%	15%	5%
General Motors	40%	45%	10%	5%
Imports	45%	25%	5%	25%
Overall	35%	45%	10%	10%

Vendor Contracts

We regularly find dealerships that have signed either original or renewal contracts with suppliers for a long period of time (more than one year). In almost all cases, the signer was unaware that it is not common business practice to sign long-term non-cancelable agreements. Below are things to keep in mind when reviewing a contract:

1. Sign no agreement longer than 12 months unless included is a clause allowing to cancel a long-term agreement with a 12-month notice.
2. When signing any agreement with a vendor, be sure that there is no section buried in the agreement that extends it.
3. Since many employees do not realize all of the consequences of signing an agreement, we strongly suggest only the owner sign agreements and that it be made known in writing to any vendor requiring a signed agreement that the owner is the only authorized signer of such agreements.

4. Some vendors place in their agreements an automatic renewal provision, which in many cases is not highlighted by the vendor or is forgotten about by the signer, who may now have a long-term agreement renewal that seemed to come out of nowhere. We suggest deletion from all agreements any automatic renewal provisions. If the vendor will not allow this, send a letter immediately not agreeing to renew in order to protect yourself in case you forget.

Inside	
Public Dealership Companies	2
Vehicle Factory Service Contracts	2
Vehicle Service Contract Sales	2
Monthly Sales And Profit Survey	3
Dealership Charity Contributions	4
New Vehicle Inventory	4
Federal Government Tax and Spending	4

Public Dealership Companies

Below we have listed six of the public dealership companies along with their pre-tax net profit as a percentage of sales for 2010. As you know from reading our newsletters, dealers' profit margins have varied a lot over the last few years. Annual pre-tax net profit margins for the last four years approximate the following:

2010	2.3%
2009	1.5%
2008	1.0%
2007	1.5%

As you can see below, Autonation reported a 3% pre-tax profit margin while the other five reported 0.6% to 1.6%. Since most public dealership companies show larger gross profits on vehicle sales than privately-held dealerships, this would indicate to us that they have higher expenses than privately-held dealerships since they perform at a much lower pre-tax profit margin, as shown below.

Autonation	3.0%
Penske	1.6%
Group 1	1.5%
Asbury	1.5%
Sonic	1.1%
Lithia	0.6%
Average	1.6%

We have read that the public dealership companies might be a role model for some of the sales and business practices for privately-held new vehicle dealerships. Other than Autonation, none of the other above public dealership companies, based on their lower pre-tax profit margins, appears to be any such a role model.

Vehicle Factory Service Contracts

We have generally found that dealers do not sell a greater percentage of factory service contracts versus independent service contracts, though factories seem to think otherwise. We find that the name on the service contract does not seem to matter, rather it is the presentation to the customer that sells a service contract. We have heard of more than one factory auditing a dealer's service contract claims in which the dealer was selling factory service contracts. These dealers got charged back on technicalities, not fraudulent claims. What the factories seem to ignore or do not convey to their auditors is that dealers have a choice of whose service contracts are to be sold. We suggest you consider this when it is a close call, whether you sell a factory service contract versus an independent one.



**You never grow a wishbone...
where your backbone ought to be.**



Vehicle Service Contract Sales

The enclosed survey presents new vehicle service contract sales, showing on average that 32% of new vehicles retailed in January had a service contract sale coupled with them. This compares to the past where the percentage approximated 35%. The median percentage was 35% in January. The average of the top 80% of dealers reported selling 44%. Based on these numbers above, dealers should not accept less than 35% to 40%.

Dealership Charity Contributions

Many dealerships make “contributions” to charitable organizations. At times from an income tax perspective, these “contributions” are really advertising, promotion, or other expenses that do not classify as charitable. We would suggest you let your office staff know what is in fact appropriate to charge to advertising and promotion. If it is truly charitable (when you are not receiving any services or advertising in return) have these payments charged as contributions.

New Vehicle Inventory

We go through between 80 and over 200 sets of new vehicle dealership accounting records every year-end and ask to see the new vehicle factory invoices for LIFO purposes. We want to note any invoices for vehicles built before January 1st, but in which the new vehicles did not reach the dealership until later in January or February while being shown as a new vehicle purchase in January or February. Earlier this year at a smaller dealership, we noted 15 vehicles that did not reach the dealership until between 9 and over 30 days after the build date. Dealers need to watch this to see that they get the proper interest credits for delayed shipment of new vehicles and to let their factory representatives know about any and all vehicles that take an excessive amount of time to arrive at the dealership based on the date that the vehicles were manufactured.

Federal Government Tax and Spending

The federal government is budgeting to spend \$3.8 trillion. We might better understand just how large this number is with some comparisons. \$3.8 trillion of spending equals over \$12,000 for every resident of the U.S. \$1.6 trillion of deficit spending (spending exceeding income) equals over \$5,000 for every resident of the United States. The government will spend \$20,000 more than it takes in for a family of four. If the government reduces spending by \$1 billion, this is only \$3 per person or \$12 for a family of four. If income taxes were raised 100% on the wealthiest top 3% already paying 50% of their income in taxes, this would only decrease deficit spending by approximately 33%. This indicates that spending reductions are the only way to get the deficit to a lower, more manageable number.



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