POWER STEERING

Steering your dealership to higher profits

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As expected, March 2019 was a much better profit month than February 2019 for new vehicle dealers. As you read in an earlier issue, January 2019 was one of the worst months in many years. Many blame this on the weather. Profits improved in February or losses became less in February 2019 as compared to January 2019. As indicated below, 90% of new vehicle dealers had improved profits in March 2019 compared to February 2019. Though 90% is higher than normal, this is the expected trend for March compared to February. Approximately 10% of dealers' lost money in March, which is typical compared to prior years. Year-to-date losses remain higher than normal due to the poor January 2019 results. Hopefully the future profit trend will remain up to make up for the January loss so the year from a pre-tax profit margin on sales perspective will rebound to the average for the last 8 years of around 2.5%.

March Profit Trends

	MARCH BETTER THAN FEBRUARY	MARCH WORSE THAN FEBRUARY	MARCH BEST MONTH	MARCH NET PROFIT +3.0% SALES	MARCH LOSS MONTH	MARCH LOSS Y-T-D
CHRYSLER	85%	15%	55%	20%	15%	15%
FORD	90%	10%	65%	35%	20%	30%
G.M.	95%	5%	90%	20%	0%	20%
IMPORTS	90%	10%	80%	35%	15%	25%
OVERALL	90%	10%	75%	30%	10%	20%

Federal and State Income and Sales Taxes

Though it rarely occurs, some dealers become under financial distress and some fail and go out of business, due to losses incurred. Usually these dealers sell out before their financial distress causes them to fail and not be able to pay their obligations including, but not limited to, payroll taxes and sales taxes. The dealer, CFO, office manager, bookkeeper's (where they are involved with the responsibility to pay these taxes), and other responsible parties that fail to pay these taxes timely and in full, might have some personal liability for these unpaid taxes. Usually, they are not aware of this personal liability until it is too late. Dealers and their responsible employees should remit all of these taxes timely before any other bills and liabilities are paid as a general rule.

"There is a powerful driving force inside every human being that, once unleashed, can make any vision, dream, or desire a reality."
-- Anthony Robbins

Inside

Operating Profit

We have seen more than one article and heard some in the industry discuss "operating profit" and how it has declined. "Operating profit" would generally be shown on a dealer's profit and loss statement as a sub-total of profit/loss before other income categories and other deduction categories. Some authors have made a "big deal" about "operating profit" going down for dealers while more and more dealerships are reflecting an "operating loss." We do not see a big deal in this trend or why some authors write about it.

We do see "operating profit" going down, but what really matters is net profit as a percentage of sales or net profit as a percentage of total gross profit plus other income. These two metrics have changed very little since 2009. We also see that more and more factories are reflecting more categories of income, factory incentives, and programs moved from the new vehicle department, but put in prior and new named categories in the other income section of the monthly financial statement after the subtotal of "operating profit." Some of the categories in "other income" include:

DOC fees
Other Income (usually this is made up of factory incentives that probably belong elsewhere)
GM Reimbursements (often times this is called EBE)
Ford Motor Company Support
Factory Programs
Mercedes Programs (too numerous to list)
Kia (KRS program)
Toyota (Marketing Covenant Bonus)
Volvo (too numerous to list)

We went through the March dealer financial statements that are included on the next page, reflecting other income as a percentage of net profit. If the other income is more than the net profit, then the percentage of other income will be more than 100% as you can see. We did not include any losing dealer's y-t-d profits as it would make the numbers appear distorted. We found 26 of the 57 dealers in the survey reflected other income being more than final profit, or 45%. We also found the median dealer reflected other income was 89% of the final profit. What does all this mean? As long as net profit as a percentage of sales remains in the range of 2.5%, we do not know if it really matters if operating profit is going down along with more dealers reflecting an operating loss.

Medicare

We all read and hear about some politicians wanting to force us to give up our current health insurance programs for a government run program, sometimes called "Medicare for all." Most of these politicians say/feel the "middle man" (insurance companies and their representatives) should be taken out of the process, because the federal government can run the health care programs better than private industry. Their position infers that doctors and hospitals will "willingly" accept these lower Medicare payments for their services. We thought you might find the information below taken from our personal Medicare supplied information interesting.

Amount Charged Provider	Medicare Approved Amount	Amount Medicare Paid
$ 58.00	$ 11.88	$ 9.31
$ 29.00	$ 4.85	$ 4.75
$ 273.00	$ 54.93	$ 54.93

Look closely at these three examples between the amount charged (invoiced), first column, and how little is paid by Medicare, third column. If Medicare only covers a percentage of the total medical charges, then either the public has to make up the shortfall though higher deductibles, government has to raise taxes to pay for the shortfall, or the doctors and hospitals will have to absorb huge reductions in what they receive. What do you think this will do to coverages and access to the medical system?

Factory Relations

We receive several calls a month from dealers that have received “nasty” letters from their factory about the factory perspective on the dealer’s new vehicle sales effective performance. In other words, if the dealer is below “100%” (average or close to average for their market), the dealer needs to improve their new vehicle performance or the factory might try to terminate the dealer. Often times, dealers do not respond and/or do not adequately respond. If dealers do nothing and the factory initiates termination, we tell dealers they lose, even if they win the termination case. Why? We find the costs, legal and experts, will be in the six figure range to defend your position.

Recently in Iowa, there was an amendment to the Iowa Motor Vehicle Franchise law dealing with a dealer’s area of responsibility, which includes the following provisions for the factory:

Must provide 60 days’ notice before the effective date.
Cannot “unreasonably alter” dealer’s area of responsibility.
Cannot take adverse action against a dealer for 12 months following the change.

We have found in many of the factories area of responsibility determinations, that there are obvious, sloppy or intentional errors, in this area of responsibility calculation. If you get a “nasty” letter obtain some professional guidance before promptly responding. Do NOT ignore these letters.

Blue Sky Multiples

We see in at least two national quarterly publications, Erin Kerrigan and Alan Haig, where they list multiple of profits by various franchises to determine Blue Sky. Some third party new vehicle dealership valuators use these metrics to determine Blue Sky. Some of these third parties misuse, either ignorantly or intentionally, these publications in determining Blue Sky. Multiples of earnings are only rough guide posts and a starting point to a qualified appraiser. Earnings to apply these multiples to can be historical or pro-forma. It is the valuators’ responsibility to use an earnings number which is appropriate in determining the dealership value.