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DEALER INSIGHTS



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Dealer Digest



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Batten down the hatches

Cross-training keeps you afloat when a key employee leaves

If key employees jump ship or fall overboard because of a new job, illness, retirement or death, their absence can leave your dealership critically understaffed as it navigates the stormy seas of auto retailing. Until you find and train a replacement for any of these star sailors, you risk being stopped dead in the water as competitors sail past.

To make sure your dealership can weather the storm if a key employee leaves for a week or forever, you need to start preparing your crew now. Cross-training employees — and reverse-training managers — can help you get ready for uncharted waters.

Who is a key employee?

An impressive title and a hefty paycheck are two clues; these people generally are invaluable to your organization for long-term planning and strategic vision. Yet, a top manager is not the only one whose unanticipated absence can have a significant effect on your immediate operations.

An employee with critical information or product knowledge, if absent, may adversely affect your routine — and profits — right away. For example, what if a top salesperson or the only staffer with access to the key lockbox fails to show up?

A top manager is not the only one whose unanticipated absence can have a significant effect on your immediate operations.

In recent years, as jobs and the technology supporting them have become more complex, a gradual movement from “generalist” to “specialist” (another key employee) has taken place. If a specialist leaves the organization, no one may be able to do his or her work. The remedy? While you don’t want to create specialist clones, you can train your flexible generalists to perform specific duties.



How can you create healthy overlap?

As you can see, the time to deal with a key employee’s loss isn’t the moment he or she turns up missing. Now, while you’re presumably fully staffed, is a good time to look at your operations, identify potential staffing vulnerabilities and develop plans that work. A rule of thumb: The more critical the skill or function, the better off you’ll be if more than one person understands it.

Pay particular attention to any new projects or procedures you may have established. Do all of the employees involved know how to cover for their co-workers? If not, start cross-training now.

Then again, backup personnel who never get a chance to practice what you teach them will soon forget what they’ve learned. The solution: Wherever possible, broaden staff members’ job responsibilities to create some healthy overlap.

For example, a dealership that self-administers its 401(k) plan can rotate the task among two employees every six months. That way more than one person will be capable of doing this critical job, which has a low tolerance for error.

In addition to ensuring a smooth workflow in the event of an unexpected absence, cross-training brings the scrutiny of a larger number of workers to each task. These extra eyes can improve efficiency — and discourage fraud.

Can your managers take the helm?

You hire (or promote) managers to provide leadership, so the sudden loss of an employee who performs key functions is a prime opportunity for managers to demonstrate their “stuff.”

Although managers need not know how to perform every function of every employee, they should know at least how to keep operations running without hitches in the short term. Encourage supervisors to

informally reverse-train within their departments. It will prepare them to fill in or train others in the event of an employee loss.

Beyond that, managers should know where to quickly find temporary help with the necessary tasks if needed.

Are you ready to run full-speed ahead?

Bear in mind, there is a positive side to the loss of a key employee. Turnover can infuse new ideas into a dealership and create opportunities for the remaining staff, which, in turn, can boost morale. To ensure any such transitions are as smooth as possible, however, make sure you have employees who know the ropes and can hit the deck running. ■

What's new about used?

Used vehicle sales are critical to the success of most dealerships. No different from new vehicle operations, your used vehicle business is subject to trends, and here are a couple to watch:

Trend 1: Price-comparison Web sites are playing a larger role. Just as realtors continue to chant, “location, location, location,” dealers seeking to move their used vehicle inventory should be chanting, “pricing, pricing, pricing.”

Why? In short, the Internet. Many Web sites now let shoppers enter the maximum price they want to pay for a used car. If your price for a shopper’s ideal make and model doesn’t squeeze in under the cutoff amount, your offer won’t even appear on the “shopping list.”

So if, based on the notion you can lower your price later, you’re still setting the price high when you advertise, think again. You must get the prospect in the door before you can negotiate.

Trend 2: Subprime lending is a growing option. A borrower is usually ineligible for a prime auto loan if he or she has a bad credit score (under 650), a lack of credit history, inability to come up with a down payment and so on.

For used vehicle sales, special financing — also called subprime lending — is a growing option. These arrangements typically lend money at higher interest rates (12% and up), with higher initiation fees and lower down payments as a percentage of price. Subprime loans also likely have longer terms, steeper loan-to-value ratios and higher retail turn rates than prime auto loans.

When you hear the term “special financing” your thoughts may turn to the disastrous subprime mortgage market of the last year or two. Yet subprime auto loan providers are generally exposed to less risk than their home mortgage counterparts. For starters, auto loans typically have fixed rates rather than the variable ones common in the mortgage market.

Also, subprime auto borrowers are usually renters and, thus, not part of the current mortgage crisis. Plus, most people buying a car need it to get to work and are, therefore, likely to honor a car-loan obligation longer than other debts. Last, repossession is a safeguard to auto loans that is much less easily executed in mortgage cases.

As with any market trend, you should make decisions about used car pricing and special financing based on your dealership’s particular profile and needs. Be sure to seek the counsel of your professional advisors.

Sound estate planning

An FLP can provide both tax and nontax benefits

After years of hard work to build your dealership, it's time to protect that legacy for your children or other loved ones with a sound estate plan. Otherwise, estate taxes could take a huge bite out of their inheritances.

A family limited partnership (FLP) is one of many tools that may help you achieve your estate-planning goals. It can allow you to reduce your taxable estate by giving away assets (perhaps even your dealership) to your loved ones during your lifetime — but without giving up total control of them. It also can provide a variety of other tax and nontax benefits.

How it works

You set up a limited partnership and transfer assets to it in exchange for general and limited partnership interests. Often assets other than your dealership itself (dealership real estate, other business assets and personal assets such as marketable securities) work best for funding an FLP.



If your dealership is a C corporation, for example, it can't be converted to a partnership without creating major tax issues — but *shares* can be contributed. However, if your dealership is an S corporation, its shares can't be owned by an FLP.

After funding the FLP, you retain a small general partnership interest (typically 1%). This allows you to continue to manage the FLP assets.

You then gift limited partnership interests to your children or other heirs. Provided the FLP is properly structured and you follow the FLP rules (see “8 ways to build a tough FLP” on page 5), the limited partnership interests and their underlying assets will be removed from your taxable estate.

How it can save gift taxes

Gifts made during your life are subject to gift tax, but you can minimize this by taking advantage of the annual gift tax exclusions. In 2008, you may give up to \$12,000 gift-tax-free per recipient. In addition to making annual exclusion gifts, you can pass up to \$1 million gift-tax-free to your heirs during your lifetime.

An FLP allows you to leverage your gift tax exclusions and \$1 million exemption. Because the limited partners lack control over the FLP and there isn't a ready market for their interests (the FLP may even restrict who can own them), these interests typically can be valued at a discount for gift tax purposes. Although the savings vary by FLP, minority interest and marketability discounts typically range from 25% to 40%.

This can result in substantial tax savings. For example, if the discount is 30%, you could give about \$1.4 million worth of FLP interests tax-free. That is, for gift tax purposes, you'd be making only a \$1 million gift, which is covered by your lifetime exemption.

Of course, such discounts also can apply to minority dealership interests given outright and through other transfer vehicles, such as trusts. But discounts aren't available for direct transfers of real estate or personal assets. An FLP, in effect, turns these assets into a discountable business.

How it can save income taxes

Partners must report FLP income on their individual income tax returns. To stand up to an IRS challenge

8 ways to build a tough FLP

The IRS often challenges FLPs, especially those that appear to be set up for the sole purpose of saving taxes, and you may need to negotiate (with professional help) the size of the discount you take. These eight guidelines, based on previous tax court cases, should prepare you to deflect an IRS challenge:

1. Establish a clear, valid business purpose for the FLP, such as the consolidation of assets for improved management.
2. Follow proper formalities in forming and operating the partnership, including filing a certificate of limited partnership, signing a partnership agreement, obtaining a taxpayer identification number, filing income tax returns, and conducting a formal, annual partner meeting.
3. Ensure that FLP assets are used exclusively for FLP purposes and not for private benefit.
4. Erect a wall between FLP assets and your personal assets — for example, a separate FLP bank account.
5. Retain sufficient funds outside the FLP so you can maintain your accustomed standard of living and pay anticipated estate taxes and costs *without* using the FLP's funds.
6. Make distributions based on size of ownership interest and consistently follow a clear distribution policy.
7. Plan for the FLP's continued operation after your death, investing assets according to the FLP's existing business objectives.
8. Involve younger family members in FLP matters and make sure they understand the plan, or receive advice from independent professionals.

(again, see “8 ways to build a tough FLP” above), the amount of income allocated should generally be based on each partner's ownership percentage.

If the limited partners are in lower tax brackets than you, an FLP can reduce your family's overall income tax bite. However, it's important to note that the benefits of this strategy are limited for partners under age 19 or, if they're full-time students, under age 24. Their unearned income beyond \$1,800 will be taxed at their parents' marginal tax rates.

Other FLP benefits

FLPs offer several benefits in addition to tax savings. FLPs can:

- ❑ Keep assets in the family while protecting them from creditors,
- ❑ Ensure a smooth transition of ownership from one generation to the next,
- ❑ Consolidate the ownership and management of real estate and other business or personal assets, and

- ❑ Provide a mechanism for resolving disputes over the disposition of assets.

The IRS continues to challenge FLPs that appear to be created only to save taxes, so it's important to be able to demonstrate other business reasons such as these for your FLP.

Peace of mind

Auto dealers face many issues involving taxes and asset transfers to the next generation. An FLP can help you seamlessly transfer your assets as well as cut your income and estate taxes. But there may be other tools and strategies better suited to your needs. Your tax and estate planning advisors can help you determine what's best for your situation.

If you decide an FLP is right for you, be sure to have a qualified tax professional and attorney oversee each step of the process. Otherwise, it will be very difficult to ensure your FLP saves taxes and fulfills other goals while meeting tax code requirements. ■

Beating the shop-supplies-fee blues

Separate charge brings in cash but may rile customers

Have you ever walked past your cashier area and noticed a red-in-the-face customer asking a service advisor about a \$25 “shop supplies fee” on his or her bill? Worse yet, did the service advisor struggle to come up with an adequate response?

If so, you may need to reassess whether charging a supplies fee is worth the trouble it’s causing.

What it is

A shop supplies fee represents the costs of miscellaneous supplies used to service and repair your customers’ vehicles: solvents, cleaners, shop towels, grease, cotter pins and other materials not purchased on a job-by-job basis.

That may sound harmless enough, but including this fee on an invoice can make a customer feel nickel-and-dimed to death.



Even within your shop, there’s likely to be a split vote on a shop supplies fee. Service advisors typically don’t like it because the fee can be hard to justify, while service managers — who tend to focus more on profitability — do.

How to make it palatable

Shops that charge a separate shop supplies fee handle it in different ways, generally charging 3% to 10% of labor costs. Having no cap on the fee is risky. Consider a customer with a \$20 oil change. He or she may or may not object to \$2 (10%) added to that service. But a customer with a \$1,000 tab — and an extra \$100 fee — is likely to bristle. That fee

might seem excessive for a paper floor mat, three ounces of grease and several bolts.

To avoid that scenario, you can, of course, create a ceiling. A \$20 or \$30 cap is one way to go. Some dealers — as part of their quest for customer loyalty — also make an exception for certain kinds of repairs: a checkup for a vehicle coming off a lease, for example.

Dealerships experience the least customer “indigestion” when they voluntarily explain the shop supplies fee while going over the bill. Your service advisors should be trained to discuss the fee in the context of the customer’s total cost. “Your bill includes parts, labor, taxes and shop supplies” could be one way to put it. The advisor also should be ready to give a quick verbal listing of supplies the charge includes.

Alternatives to consider

If you decide a shop supplies fee isn’t worth the risk of customer ill will, you’ll need to figure out how to recoup those dollars in another way.

This probably means hiking your hourly rate. Dealer shops can get squeamish about doing this if it means advertising higher labor rates than the competition. But, simply put, you need to cover these costs somehow. The good news is that you won’t hear a customer say, “I suppose you’re going to charge me next for the electricity you use.”

To calculate the cost of shop supplies — and to control their use — the parts department should buy these items and inventory them as it would any other part. And the service manager should OK all charges to the shop supplies account just as he or she would any other expense.

A dual-purpose decision

When you reach a decision on whether to charge a shop supplies fee, make sure it recovers the costs of the supplies in question while preserving your customer relationships. Both are critical to your dealership’s bottom line. ■

Initiative aims to slash third-party health care costs

Better management of the outsourcing of health care claims administration can chop administrative health care costs by almost one-third.

So says the Automotive Industry Action Group (AIAG), which recently developed guidelines to help dealerships and other businesses better manage these third-party-administrator (TPA) costs.

Many self-insured businesses farm out the complex administrative handling of employee health care claims to TPAs and pay high premiums — AIAG calls them “excessive” — for the convenience.

The new guidelines suggest TPA program structures and zero in on terms and arrangements that hinder a company’s ability to properly analyze data, thereby contributing to reporting errors and claim data misrepresentation.

Guideline topics include bill review, nurse case management, avoiding claim status escalation, litigation management, old claims management, value-based incentives and predictive modeling. The *Third Party Administration Guideline* is available in print and electronic formats through www.aiag.org. ■

Nimble sales teams hurdle leasing stumbling blocks

Lower monthly loan payments to compensate for higher monthly fuel costs seem to be one of the reasons for the current bump in leasing popularity. New high-tech options, such as self-parking systems, iPod docks and onboard GPS guided maps also lure customers to the lease-and-trade-in route.

To profit from the present leasing upsurge, make sure your salespeople:

- ❑ Contrast the advantages and risks of both leasing and ownership, and know when a potential lessee is better off as a buyer,

- ❑ Keep it simple when selling to customers — the size of the monthly payment and the money required up front are the two most important numbers for most lessees,
- ❑ Can communicate the simple steps required for a lessee to transfer one type of lease for another, an option made relatively easy now through numerous Web sites, and a selling point for customers turned off by a lease’s fixed period, and
- ❑ Have backup suggestions available for would-be lessees who don’t qualify for the heavily advertised leasing deal that brought them in (for example, turning to another credit source or buying a lower-cost used vehicle instead). ■

E-scheduling appointments sets your service staff free

More and more dealerships are turning to “e-scheduling” as an improvement for both customers and service advisors.

How does it work? Via a link on your Web site, customers schedule appointments, receive speedy confirmation and get an e-mail reminder just before their appointment date.

The system sends any customer who misses an appointment a rescheduling request. And some systems offer the option of requiring a credit card number to reserve a service time, which decreases the likelihood of a missed appointment.

Many service advisors like this latest big thing in customer service because it frees them up from nonstop phone calls, allowing them to focus their attention on customers bringing in, or waiting for, their vehicles.

But before you consider switching from your phone-based system, evaluate the risks. If you’re not prepared to put the needed time into finding the right system and teaching your staff how to use it, the investment could be a waste of money — and mishandled scheduling can lead to unhappy customers. ■

SUCCESSION PLANNING

By: Sean A. Fraser, Esq.

Succession planning is much more than naming the appropriate person in the Successor Paragraph of the dealer sales and service agreements. Proper planning must consider not only how the dealership will be transferred, but when and to whom will it be transferred. Further the following factors will impact your decision:

- Should I plan to sell to an outsider or "groom" a successor?
- When will the next generation be ready to operate the dealership?
- What is the current value of the dealership versus the expected future value of the dealership?
- What if anything do I need to do to make sure all my beneficiaries share in my estate equally or in accordance with my intentions?
- How will assets passing outside of my estate impact my planning, e.g., life insurance, retirement plans?
- How can I insure that my estate can take advantage of the IRS provided tax payment deferral (which can be as long as 15 years)?
- I have a buy-sell in place, but is there sufficient money available to pay for the transfer of my ownership to the next generation? Should I consider life insurance?
- Can I transfer my dealership while living and still maintain a significant income stream?
- I have children from a prior marriage. How can I insure that there will be no infighting causing the estate to pay large legal and accounting bills to sort out ownership after I die?
- I have no heirs interested in operating the dealership. Is an ESOP viable?
- My General Manager is interested in acquiring the dealership, but he does not have the wherewithal to finance the acquisition. Can I sell the dealership to him gradually and still maintain control throughout the process?

The value of a dealership generally is a significant part of an estate. Proper planning to minimize taxes, costs and to insure an orderly transfer of the dealership, as well as your other estate assets is essential. Contact Sean Fraser or George Malis at 313-566-2500 to discuss your best course of action.

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