



THE STRATEGIC DEALER

Insight & Advice for the Successful Dealership

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Expense Control – Telephone and Utilities

By Wayne A. Fortier, CPA



This month we'll look at an age-old subject: expense control. Like unclaimed property (which we'll discuss in upcoming issues of *The Strategic Dealer*), expense control is an idea that resurfaces from time to time—and it's especially timely now, when interest rates are rising again

and folks are looking to make sure their houses are in order.

It's always a good idea for your dealership to get back to the basics and take a fresh look at your expense structure. Selling more vehicles and/or services can cover up many sins, but there comes a point where the growth, if it's there to begin with, cannot be sustained. Controlling expenses can mean the difference between showing income versus losses each and every month.

As you begin to review your situation, start with some critical questions. Have we sustained losses over successive months? Does this appear to be a trend for the near future? Does our company retain enough of the gross generated at the top of the statement? Exactly how much of the gross makes it to the bottom line? Do we have benchmarks to help us measure our performance in retaining grosses?

It's also helpful to look at this topic from a number of other perspectives, looking at some of the larger expense line items. Some of these heavy hitters are personnel (direct wages), the floor plan and advertising. Recurring expenses include data processing, supplies, policy/goodwill, delivery expense and outside services.

Paying the Bill

This month, however, I'd like to draw your attention to telephone and utilities expenses. So often, we just accept these costs because we think we can't do anything about them. Besides, they come from the utility company so they must be correct, right? Wrong!

When was the last time you performed an internal check on your bills? How do you know they were correct? Many dealerships have never tested their bills to see if they were correct. More often than not, when errors are discovered, overcharges have existed each and every month. It's a classic example of how we should all "inspect what we expect."

If your dealership finds overcharges, in many cases you not only reduce your expense for each month going forward but you may be able to recover some of the overcharges from your telephone and/or utility carrier. And these dollars can be significant. Here's a case in point: this is an extract from the NCUC (North Carolina Utilities Commission) Rules and Regulations on overcharges:

If the utility has inadvertently overcharged a consumer as a result of a misapplied schedule, an error in reading the meter, a skipped meter reading or any other human, machine or meter error, the utility shall, at the customer's option, refund the excess amount paid by that consumer or credit the amount billed as provided by the following:

- a. *If the interval during which the consumer was overcharged can be determined, then the utility shall credit or refund the excess amount charged during that entire interval provided*

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that the applicable statute of limitations shall not be exceeded.

- b. If the interval during which the consumer was overcharged cannot be determined, then the utility shall credit or refund the excess amount charged during the 12-month period preceding the date when the billing error was discovered.

You will need to check with your state's laws to determine your state's statute of limitations period. If it is three years, you can apply for a recovery of overcharges for that period.

Inspecting What We Expect

Now that we know there may be some cash on the table, what are some things we can do to "inspect what we expect?" Ask these questions when you review your bills:

- > What is the cost per minute (overall or blended rate) if maintenance fees are included? How does this compare to other vendor quotes? Actual or blended cost per minute factors in equipment costs, maintenance fees, taxes and other charges, and some carriers charge more than others. This results in a much higher cost per minute.
- > Was the negotiated long distance rate—say, three cents per minute—on all calls or just intrastate? Many times the interstate rates are much higher and in some cases are applied to all long distance calls.
- > Were all the agreed-upon rates and rate plans implemented and applied to my company correctly?
- > Have I been a victim of slamming (changing a customer's telephone service without permission) or cramming (placing unauthorized, misleading or deceptive charges on the customer's telephone bill) practices?
- > Have all applicable discounts been consistently and accurately applied?
- > Are there any unused phone, fax or modem lines that I have been paying for?



A periodic review of telephone and utilities expenses can net you some extra cash.

- > Is there a kilowatt demand error present in my bills? This error occurs when a customer is billed incorrectly for kilowatt usage through a meter reading error, when a bill is based on estimated usage rather than the actual meter reading or even a keypunch error that alters the amount of the bill because of a keypunch mistake.
- > When was the last time my meter was checked by the utility carrier for errors/accuracy on readings? What were the results of these tests?

Investigating some of these may seem a bit daunting at first, but the key is to dig in and get started! Take a stab at it. What have you got to lose? I have seen some dealers realize notable savings after going through this exercise. Some dealers review their bills every few years. When was the last time you reviewed your dealership's telephone and utilities records?

If you need help, you can get assistance from a number of organizations that specialize in this field. One that I have recommended in the past is the National Utility Review; their website is www.nationalutilityreview.com. You can also email chris@nationalutilityreview.com. If you know of others let me know and I will be happy to pass those along to our readers. It never hurts to compare.

The key, however is to get started. You will at least have the peace of mind that will come from checking that item off your list—and you may even pick up some cash that might be

sitting on the table.

Good luck and happy hunting! ■

Wayne Fortier is a recognized automotive industry authority. He has numerous years practicing as a CPA and as CFO of an automotive dealership group. For more information on this article, or any of your automotive needs, contact Wayne at wfortier@dixon-hughes.com or 888.683.4825.

COMPUTER BYTES

Running Parts Queries

Parts inventory aging can reveal the effectiveness of parts and DMS inventory management parameters. However, it is fairly easy to hide the true aging of a parts inventory by selling a part and then crediting it back into the inventory. This immediately moves the activity of the part into the 0- to 30-day column and can hide other inventory and internal controls problems. By running a query of part numbers to compare sales vs. credits, possible questionable activity within the parts department can be easily observed and managed.

ADP

There are a number of ways to monitor if your parts department is covering up aging problems. The Parts Data Archiving (PDA) function holds details on all transactions. Under the “PDA – Monthly Reports” menu, you can search for “Low Gross Profit Tickets.” This will display any tickets that are below the minimum gross profit you enter. Credits show as a negative gross profit. Another option is to use the Report Generator (RPG) and create a report to identify any transactions with a negative quantity sold (credit). With that information the suspected part number’s detailed transaction record could be viewed to determine if a fictitious credit was posted. Regular monitoring of the Report Transaction (RTR) and Daily Invoice Report (DIR) will also alert you to potential problems.

ARKONA

With the latest release of ARKONA, dealers can take the following steps to look for “mysteriously” returned parts:

1. Take option 20=Transaction Analysis from the Parts Inventory & Invoicing menu and take option 1=Select by Returns Analysis.
2. Select the manufacturer/stocking group and the stocking status of the parts you want to include (active/non-stock or all).
3. Key in the date range to select all the part numbers that were returned in that date range and press [ENTER] to display the analysis.

You can see part number/description, quantity returned in the date range, number of days since last sale, number of days since prior sale, current quantity on hand, piece cost and inventory value. You can also drill down to part sales history and view invoice numbers, sales and return dates, and counterperson for every transaction on the part.

REYNOLDS & REYNOLDS

The following is a report of parts that were on an RO and then removed and not sold to that RO. These are “potential” problems. I included the 12 month history in the column headings so you can see if the part has really been selling or not but the user will need to research the parts so see if there was a “real” sale or not.

User needs to go into 6910 from the parts application. Under REPORT NAME you can call the report any name that you would like. The FILE NAME is PROD.HIST for the current month and PRH.YYMM with YY being the two-digit year and MM being the month number – PRH.0403 would be March 2004. REPORT TYPE is SORT and set the report to sort by PART# in A (ascending order). The selection criteria is QTY LESS THAN OR EQUAL -1 AND SALE TYPE (CWI)~ EQUAL “” AND TRNSDATE GREATER THAN OR EQUAL <<ENTER START DATE>> AND TRNSDATE LESS THAN OR EQUAL <<ENTER END DATE>> AND INV#/PO# EQUAL RO#]. The column headings can be chosen by doing a “?” but the recommended ones are PART#;INV#/PO#;HIST-HORIZ-12~. ENTER FIELDS TO BREAK ON should be left blank and ENTER SPECIAL FORMAT should be “N.”

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Are You a Fox or a Hedgehog? Staying Focused

By Keith Ely



In his best selling book, “Good to Great,” Jim Collins discusses the hedgehog concept. He notes that while the hedgehog knows only one big thing—how to protect himself or herself from the fox—the fox knows about many different things.

Collins’ concept divides people into two groups. Foxes pursue many different ends at the same time because they experience the world as complex. Hedgehogs simplify the world into one single idea or organizing principle that guides and unifies everything they do; they ignore anything that does not relate to the main purpose (hedgehog idea).

We can apply this concept to the financial management of a dealership. Many dealerships are like the fox, using all sorts of measures and goals. Net profit, gross profit, CSI, expense management, employee satisfaction, DMS utilization, asset management and many other measures are used by these dealerships and their various departments. Bonuses and performance rewards are usually attached to attaining certain levels of performance. Although each measure is simple, the combination of the various measures, guides, standards and benchmarks can begin to confuse and cloud the real performance issue of the dealership, which is increasing dealer wealth. This all adds up to fuzzy financial management.

But financial management does not occur only in the accounting office of the dealership. Financial management includes all of the policies, processes, procedures and systems that the management of the dealership uses to lead, control and drive dealership performance. Typically, most controllers and CFOs have not taken the time to blueprint their overall financial management system and to ask how good it is as a whole. In order to do this, the following items should be considered:

- > What are the performance goals of the dealership?
- > How are these goals and the progress toward the goals communicated by management?
- > What set of measures are used to keep track of successes and failures in moving toward the performance goals?
- > What processes are used to develop performance action plans?
- > How do managers make decisions involving tradeoffs (such as holding GP% vs. increasing market share)?
- > How are rewards aligned with the long-term goals of the dealership?

Most dealerships employ a complex set of measures, methods and messages for the above purposes that is typically like a bowl of spaghetti of disconnected messages and decision loops. Dealerships that follow the hedgehog concept, however, organize themselves around the principle that anything not relating to the main purpose of the dealership should be eliminated. Collins points out that those companies that have gone from good to great have identified one overriding economic measure that is the focus of all personnel in the organization. For example, Walgreens measures economic profit per customer visit. What is the main economic measure of your dealership?

Focus Like a Hedgehog

Once you’ve identified this economic measure, the financial management system can be set up to focus on it. All eyes, hands, processes and systems should be structured to focus on this economic measure. The measure that I believe encapsulates total dealership performance is Stern Stewart & Company’s Economic Value Added (EVA®) measure. This measure takes into account both the balance sheet and the income statement and can be easily calculated as follows:

$$\text{Dealership Net Operating Profit (after taxes) –} \\ \text{(net assets x cost of capital)}$$

EVA® is an estimate of true economic profit, or the amount by which earnings exceed or fall short of the required

minimum rate of return that dealership owners and their financing sources could get by investing in other investments of comparable risk. In its simplest form, EVA® is excess income. For an investor to earn an adequate rate of return, the return must exceed the risk. Accounting measures profit while only taking into account the interest cost of debt. The accounting measure of net income does not take into account a required return on the net worth (owner's equity) of a dealership. Is net worth really a "free ride" to the dealership and its management team, or does the dealer demand a return on the investment, just as the debt holder does? The answer is a common sense "yes."

The use of EVA® as the overarching measure allows the dealer to understand the relationship between profit and cash. The dealer does not have to ask "Where is the cash?"—The use of the EVA® measure easily allows the dealer to ascertain whether or not cash and dealership resources have been wisely used.

The EVA® measure shows the true effect that a large parts inventory and receivable balance have on the performance of a parts department or the impact that outstanding WIP and receivables have on the performance of a service department. The managers of the departments do not become simply income statement managers, they become dealer investment managers, since what they are managing (both P&L and Balance Sheet) are reflected in the EVA® calculation. The dealership's balance sheet and income statement collapse into a single economic profit measure that reflects the operating efficiency and asset management of the dealership's management team.

The use of EVA® as the focus for dealership financial performance allows the CFO/controller to build the financial management system to focus on the measurement and improvement of dealership EVA®. In order for EVA® to improve, one or a combination of five things must occur:

- › Reduce cost of capital – this is the interest cost to the dealership. The lower the interest cost for the dealership, the greater the EVA® for the dealership.
- › Operate more efficiently – gross margins and expense management are the key issues here. This includes personnel management, processes within the dealership and DMS utilization.

- › Improve asset management – by lowering the asset base wisely, the cost of the assets will decrease. This includes dealership processes and DMS utilization.
- › Grow profitably – volume and growth need to occur while maintaining a positive EVA® growth. It is important to remember that EVA® must be positive for growth, not the accounting earnings.
- › Assess tax implications – because EVA® is calculated by subtracting the cost of assets from dealership income after taxes, the income tax issues of the dealership should be examined.

Great companies focus on a single economic measure of performance. Companies using the EVA® or Economic Profit measure as their focus have shown significantly better results than those companies that focus on other measures. For example, Walgreens (both a Good to Great company and user of the EVA® concept), has recorded performance returns far in excess of the stock market for over ten years (since 1993). Focusing on a single key measure and developing the financial management system around this measure should lead to improved performance results for a dealership.

Are you up to the challenge to go from "Good to Great?" Can you be a Hedgehog? Can you build your dealership's financial management system to be Focused rather than Fuzzy? ■

Sources:

"Focused Finance" by G. Bennett Stewart, Stern Stewart and Company May 12, 2003. www.sternstewart.com.

"Good to Great" by Jim Collins, HarperCollins Publishers 2001, pp. 90-97, pp. 104-106.

Keith Ely is Manager of Heavy Truck Services for Dixon Hughes Dealer Consulting Group. He has worked with over 250 heavy truck dealers in either a consulting or educational forum. He is an advocate of dominant fixed operations as well as optimal and aggressive asset management; he has spoken at numerous ATD conventions and has authored several articles for various industry publications. Contact Keith at kely@dixon-hughes.com or 888.683.4825.

The Next Wave of Class Action Lawsuits

By Gil Van Over



I frequently refer to the various, sometimes nefarious, creatures pursuing car dealers as Sharks. You know who I mean...Aspiring Governors, Plaintiff's Attorneys, Federal and State Regulators, Special Interest Groups and the Media.

The members of the Plaintiff's Attorneys Shark Club are getting their surfboards out to start riding the next wave of class action litigation: Negative equity.

All of the ingredients for successful Sharks' class action litigation are in place.

The Law Has Been Around For Seven Years

The changes to Regulation Z that provides for the proper disclosure of negative equity has been in effect for seven years now. Yet many dealers do not comply with the regulation.

Consumers Know It

The majority of consumers are buried in their trades—and worse yet, know what the terms upside down and negative equity mean.

Sharks Know It

Plaintiff's attorneys have been attending 20 Sharks meetings (similar to dealers 20 group meetings) and are now prepared with templates of briefs to start filing class action litigation.

Judges Know It

The appellate court in California recently ruled against the dealer in a case involving the rolling of negative equity into line one, stating in its opinion that such a practice is a violation of both state and federal disclosure laws.

Some Creditors Don't Care

Some creditors are not permitting dealers to properly disclose negative equity on the Retail Installment Sales Contract. These shortsighted companies just don't seem to understand that dealers look to them for guidance on all things credit-related. GMAC, however, recently announced that it would accept negative equity on contracts in all states except Vermont. Hopefully, the rest of the lending community will follow GMAC's lead.

Disclosure and Advertising

Not only is it a potential violation of disclosure laws, but rolling negative equity could lead to false advertising claims by disclosing a sale price on the Retail Installment Sales Contract that is substantially higher than the advertised price.

Disclosure and Taxation

Additionally, rolling negative equity into the purchase price could lead to charging a higher sales tax in those states that tax on the purchase price and not the trade difference.

How Can You Protect Yourself?

Immediately require that the appropriate trade allowance is properly reflected on your Buyer's Orders. Lenders can't dictate how your Buyer's Orders are prepared, and this will give you at least one document that accurately reflects the transaction.

Call every lender you do business with and ask, "How do you want me to disclose negative equity?" Get it in writing so that

you do not unnecessarily increase your CIT's.

If necessary, stop doing business with those creditors that refuse to allow you to properly disclose negative equity. After all, the dealers are the ones being bit by the Sharks on the negative equity issue, not the lenders. Eventually the lenders who haven't seen the 21st Century light will get past worrying about Y2K issues. ■



Call every lender you do business with and ask them how they want you to disclose negative equity.

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UCS

Open POWER Workstation, press Alt+End to open the Direct Dispatch window, select Parts Inventory Control [Options] from the drop-down menu, and press F12. Then, click on Functions > Define Parts MIA Report > MIA Report Setup. Close the Report Number Lookup window, press CTRL+A to add a new report, enter a Report Number, and press F12.

Enter a Description for your report, select "Part Number" for the Sort Sequence, and press F12 to add the report.

From the Subscreens menu, click on MIA Select Criteria – Screen 1 and make the following entry:

Sales (Pieces): High 0 in 12 Months (Use your obsolescence criteria.)

Weeks Since Last Sale: High: 5

These selections will display all parts that have a net sale quantity of zero (or a negative number) for the previous year. Searching for parts that show a net sale of zero (or less) while also showing sales activity within the previous five weeks would indicate credits being applied. Controllers should review this report each month, since it may indicate questionable activity in the parts department. The report also lists the previous five months of sales data so you can easily spot trends.

Request your report from the Print menu by selecting MIA Report, entering your Report Number, and pressing F12. ■

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Fixed Operations Seminar	October 17-19	Atlanta, GA
Office Management Training 101+	October 20-21	Miami, FL
Internal Audit Seminar	November 10-11	Ft. Lauderdale, FL
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