AUTOFOCUS

Fall 2017

You can save on taxes via some year-end moves

Consider NQDC plans to boost key employee retirement savings

Disaster preparedness
Are you ready for a catastrophe?

FTC ruling clarifies recall disclosure requirements

Automotive Dealership Group

Ernest Tyler, CPA
Kenneth Goodrow, CPA
James Godfrey, CPA
Virginia McGrody, CPA

TYLER, SIMMS & ST. SAUVEUR, P.C.
Certified Public Accountants & Business Consultants

You can save on taxes via some year-end moves

Don't look now, but the end of 2017 is fast approaching. And the window is closing for implementing strategies that could save your dealership money when you file your corporate tax return next year.

This could make now a good time to talk with your CPA about some tax-saving moves you might make. But December 31 is a hard-and-fast deadline for making most year-end tax steps, so don't delay.

WRITE OFF ASSETS THIS YEAR

Start by looking for assets on your balance sheet that you can write off and deduct before the end of the year to lower your 2017 taxable income. For dealerships, these often include:

Uncollectible accounts receivable. Eligible dealerships can write off past-due receivables that are deemed uncollectible per IRS guidance, whether they're vendor or customer receivables. Do so before December 31 to deduct these expenses on your 2017 tax return. If you end up collecting the receivables next year, the income will be reported as revenue in 2018.

Depreciated used vehicles. If used vehicles on your lot are now worth less than your cost, you can write them down to current market value before year end and deduct the difference, assuming you don't use last-in, first-out (LIFO) accounting.

Section 179 of the tax code presents one of the greatest year-end tax-saving opportunities for dealerships.

Say you obtain a car for $17,000 and spend $1,000 to recondition it, resulting in $18,000 in inventory carrying costs. But it's only worth $15,000 now, according to the *Kelley Blue Book*. You'd be able to write off the $3,000 difference on your 2017 federal return.

Auto parts. Have a physical parts inventory performed before year end and adjust the book inventory amount accordingly. Then write off any discrepancies between your book and inventory counts. Also dispose of — and write off — any obsolete or slow-moving parts as identified by your Dealer Management System.

TAKE ADVANTAGE OF SECTION 179 EXPENSING

Section 179 of the tax code presents one of the greatest year-end tax-saving opportunities for dealerships. This provision enables you to deduct up to $500,000 of the cost of tangible fixed assets during the year in which they are placed in service, up to certain limits. These assets include shop equipment, showroom furniture, and new computer systems and software.

PLAN A COST SEGREGATION STUDY

While you may be unable to fit it in between now and year end, having a cost segregation study performed is another effective tax-saving strategy for dealerships.

This study will separate the individual components that compose your facility into different categories for depreciation purposes. And that lets you take advantage of the shorter depreciable lives of some categories. Faster depreciation of property can result in lower taxes!

Dealership facilities are considered nonresidential income property that must be depreciated on a straight-line basis over 39 years. But components of the facility classified as tangible personal property or land improvements can be depreciated over a much shorter period of time: five or seven years for the former and 15 years for the latter.

A cost segregation study will reallocate some of the costs related to the construction, acquisition or remodeling of your facilities as tangible personal property or land improvements instead of nonresidential income property. Among the components that can likely be reallocated are plumbing and electrical systems, carpeting, and parking lot repaving.

The study also could identify repair and maintenance costs that can be expensed and deducted now, instead of capitalized and depreciated over a number of years. And you can perform a cost segregation study going back 15 years and file IRS Form 3115, "Application for Change in Accounting Method," to take advantage of catch-up depreciation.

In addition, you can deduct 50% of the cost of new (not used) equipment acquired and put in service before the end of this year. This bonus depreciation will be reduced to 40% and 30% the next two years before being phased out.

Be sure to plan your equipment acquisitions carefully to take maximum advantage of Section 179 depreciation and 50% bonus depreciation.

CONSIDER OTHER MOVES

Here are a few more year-end tax strategies that might be beneficial for your dealership:

Make tax-deductible retirement plan contributions. For 2017, you can contribute up to $54,000 or 25% of compensation (whichever is less) to your employees' profit sharing and 401(k) accounts combined. That's less any contributions employees make to their 401(k)s other than "catch-up" contributions.

Carefully time the payment of year-end bonuses and vacation pay. You can deduct bonuses and vacation pay accrued to nonowners before the end of the year. And you wouldn't have to pay the cash until 75 days after year end, thus preserving current cash flow. But bonuses accrued to owners must be paid by December 31 to be deductible.

Defer floor plan assistance and other manufacturer's credits. These credits are earned when you purchase vehicle inventory. But you can defer recognition of them as income until *after* vehicles are sold, presumably next year.

WATCH TAX REFORM CAREFULLY

Several different tax reform proposals are being discussed in Washington that could impact these strategies. So be sure to talk with your tax advisor for more details about your situation.

Consider NQDC plans to boost key employee retirement savings

Are you looking for a retention tool for key employees or a way to build your own tax-deferred retirement savings? You might look into adopting a nonqualified deferred compensation (NQDC) plan.

WHAT ARE NQDC PLANS?

NQDC plans are agreements between owners and executives and their dealerships to pay out tax-deferred compensation at some future time, such as at retirement. Two key advantages: 1) They *aren't* subject to the contribution limits and the distribution and funding rules that apply to qualified retirement plans, and 2) the qualified plan nondiscrimination rules do not apply.

Dealerships can tailor the amount, form and timing of the payment of the benefit to a participant's specific needs. One of the most common types of NQDC plans is the salary reduction plan, which is usually in the form of a "mirror" 401(k) plan.

THE MIRROR 401(K) PLAN

The key employee participating in a mirror 401(k) plan is able to elect to defer income taxation on compensation for services provided until there is "actual or constructive" receipt. However, the compensation generally will be subject to Federal Insurance Contributions Act (FICA) and Federal Unemployment Tax Act (FUTA) taxation when entitlement to the compensation vests. This will usually be at the time of the deferral.

The rules governing income taxation, along with the application of the special timing rule for FICA taxation, typically result in reducing employment taxes and allow the compensation to grow income-tax-deferred. Executives participating in a mirror 401(k) plan usually must make their initial deferral election prior to the year in which they perform the services giving rise to the compensation.

So, for instance, executives who wish to defer their 2018 compensation to 2019 or beyond must have made the deferral election by the end of 2017. There are exceptions for new employees and certain elections to defer performance-based compensation.

WHAT ABOUT RESTRICTIONS?

NQDC plans are subject to IRC Sections 409A and 451, which apply to nonqualified plans. Sec. 409A imposes strict requirements on the timing, form and amount of the deferred compensation payments. This severely limits any subsequent changes. Moreover, these rules require that the deferred compensation be paid on a permissible payment date specified in the plan document.

Examples of permissible payment dates are death, disability, separation from service, change in

ownership or control of the employer, and unforeseeable emergency. Penalties for noncompliance with these IRC rules are harsh: They include taxation of any benefits at the time of the deferral (which is usually the time of vesting), a 20% excise tax and a 1% increase in the applicable tax underpayment interest rate.

Dealerships can tailor the amount, form and timing of the payment of the benefit to a participant's specific needs.

OTHER DRAWBACKS AND RISKS?

Unlike a qualified plan, an NQDC plan is an unfunded, unsecured promise to pay deferred compensation in the future for services performed today. All plan assets of a mirror 401(k) plan are generally held in the general assets of the employer and are subject to its creditors.

The dealership can choose to fund this arrangement by establishing a "rabbi trust" to hold and administer plan assets or invest in corporate-owned life insurance. Or the deferred compensation can be accounted for and paid directly from the dealership's general assets. Because these aren't qualified retirement plans, the participants will be unable to elect rollover contributions into an IRA or other retirement account at the time of distribution (separation from dealership service or retirement).

Finally, U.S. Department of Labor rules prohibit nonqualified plan participation by employees who aren't members of a "select group of management or highly compensated employees," also known as the "top hat" group. Care should be taken not to include rank-and-file employees as participants in mirror 401(k) plans to comply with this rule.

Disaster preparedness

Are you ready for a catastrophe?

Disaster planning is critical for all companies to help ensure that normal business activities can resume as soon as possible after a disaster strikes. However, dealerships face unique risks when it comes to preparing for catastrophes.

Unlike most businesses, the bulk of your inventory is sitting outside, where it's exposed to the elements. Natural disasters such as hurricanes, tornadoes and floods can damage or destroy all or part of your inventory.

DRAFTING YOUR PLAN

The first step is to draft a disaster recovery plan. Assign a team of employees who'll be responsible for drafting the plan and keeping it current. Include representatives from across the dealership — such as the sales, parts and service, and IT departments — to draw on a broad perspective.

Your plan will lay the foundation for resuming normal operations as soon as possible after the disaster to minimize downtime and lost sales. This would typically include reopening the physical store, restocking inventory (both vehicles and parts) that's been damaged or destroyed, and repairing or replacing damaged or destroyed computers and other equipment.

Start the planning process by talking to your manufacturer and lender about how vehicle inventory

would be replaced. For example, how long will it take for new vehicles to arrive on the lot? How will damaged or destroyed vehicles be removed to make room for new ones? And how will you protect inventory from thieves and looters postdisaster?

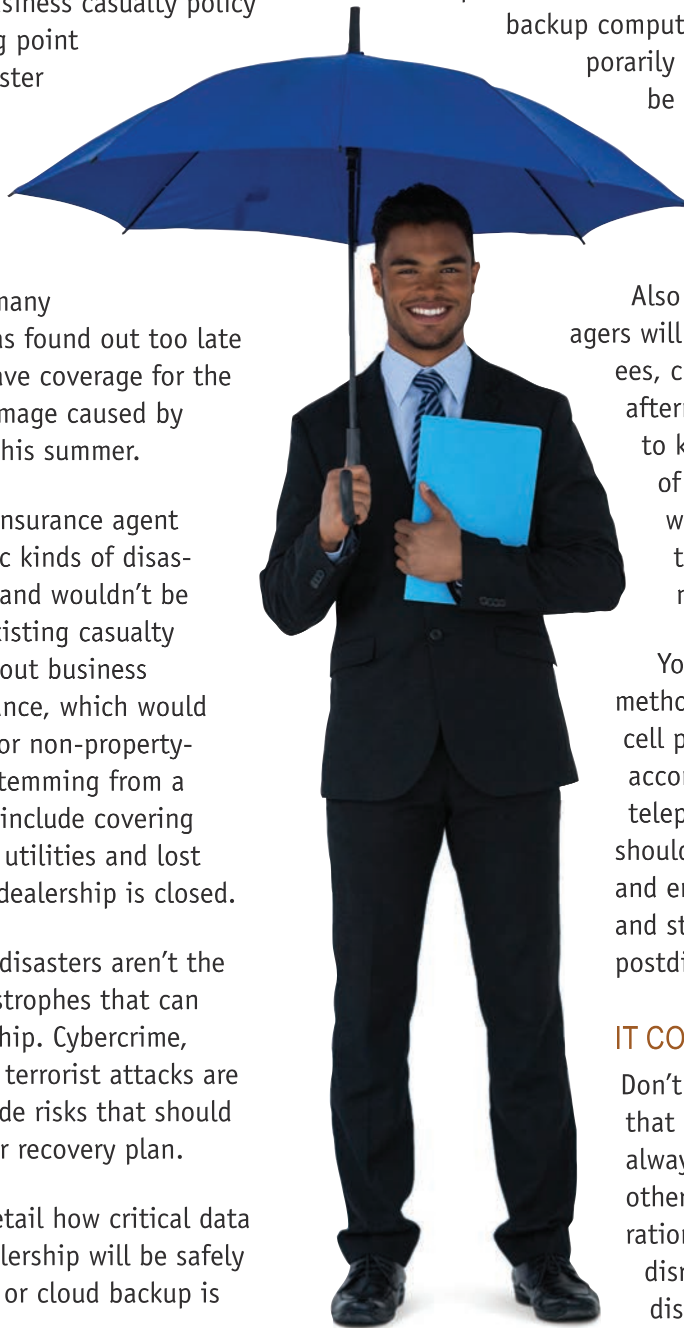
REVIEWING INSURANCE COVERAGE

Also carefully examine your insurance coverage. A standard business casualty policy is only the starting point for dealership disaster insurance — it might not cover the damage caused by a natural disaster. For instance, many dealerships in Texas found out too late that they didn't have coverage for the extensive flood damage caused by Hurricane Harvey this summer.

So talk with your insurance agent about what specific kinds of disaster damage would and wouldn't be covered by your existing casualty policy. Also ask about business interruption insurance, which would provide coverage for non-property-related expenses stemming from a disaster. This may include covering payroll, mortgage, utilities and lost profits while your dealership is closed.

Of course, natural disasters aren't the only kinds of catastrophes that can strike your dealership. Cybercrime, server crashes and terrorist attacks are among the manmade risks that should be included in your recovery plan.

The plan should detail how critical data stored by your dealership will be safely backed up. Offsite or cloud backup is usually preferred for such data as customer billing and contact information and vehicle sales and service records. This will help ensure the preservation of this information if onsite servers and computers are damaged or destroyed.



Arrange ahead of time for a generator that can provide power to your dealership until normal power is restored. And look into securing an offsite backup computer system that can be used temporarily until your onsite computers can be repaired or replaced.

PREPARING FOR POSTDISASTER COMMUNICATIONS

Also decide how you and your managers will communicate with your employees, customers and vendors in the aftermath of a disaster. You'll need to keep them updated on the status of reopening so employees know when to return to work and customers and vendors know when normal operations have resumed.

Your plan should describe what methods of communication, such as cell phone or email, will be used to accomplish these goals if landline telephone service is disrupted. It also should detail how cell phone numbers and email addresses will be gathered and stored so they're easily accessible postdisaster.

IT COULD HAPPEN

Don't fall into the trap of thinking that disasters are something that always happen somewhere else to other businesses. Begin your preparation now to minimize potential disruptions and lost revenue if a disaster hits. ◣

FTC ruling clarifies recall disclosure requirements

To help appease some customers' concerns about buying a lemon, many dealerships perform multipoint inspections of their used cars before listing them for sale. Some dealerships then tout this in their advertising, telling shoppers that the store's used vehicles have passed these rigorous inspections covering everything from the engine and steering systems to the axles and brakes.

But heads up: There's another important detail that dealerships must disclose when highlighting these inspections in their advertising: whether or not the vehicle may be subject to unrepaired safety recalls.

FINAL CONSENT ORDERS APPROVED

On March 31, 2017, the Federal Trade Commission (FTC) settled charges with three automobile dealership groups that they violated provisions of the FTC Act against unfair or deceptive business practices. The groups touted such inspection programs without adequately disclosing that some cars were subject to unrepaired safety recalls.

U.S. auto dealerships can't claim that their used vehicles have been repaired for safety issues unless they are free of open recalls.

According to the settlement, the dealership groups — and by extension, all U.S. auto dealerships — can't claim that their used vehicles have been repaired for safety issues unless they are free of open recalls. Conversely, dealerships can "clearly and conspicuously" disclose that used vehicles may be subject to

unrepaired safety recalls and explain how buyers can find out about them.

The settlement doesn't require dealerships to note any specific recall problems or make any repairs due to safety recalls. This resulted in criticism from some lawmakers and consumer advocacy groups who believe the settlement doesn't go far enough.

A COMPETITIVE ADVANTAGE?

When it announced the settlement last December, the FTC noted that dealerships that do make recall repairs on used vehicles may state this in their advertising, even though they're not required to. This could give such dealerships a competitive advantage over those that don't make recall repairs and must note in their ads that vehicles may be subject to unrepaired safety recalls.

Discuss with your managers the best possible strategy about whether or not to make recall repairs to your used vehicles.

This publication is distributed with the understanding that the author, publisher and distributor are not rendering legal, accounting or other professional advice or opinions on specific facts or matters, and, accordingly, assume no liability whatsoever in connection with its use. ©2017 AFCfa17

Your success is our business

At Tyler, Simms & St. Sauveur we recognize that the challenges of owning and operating an automobile dealership are unique and ever changing. That's not only because your enterprise is essentially several different businesses rolled into one, each with its own special features. It's also because your business has evolved to where you need a CPA as well versed in estate and succession planning, tax strategies, and benefits administration as in dealership accounting, valuation, systems reviews and related areas.

Consequently, you need more than simply a CPA to prepare your taxes. You need an adviser who has invested time and effort into learning your industry and is trained in the dealership environment. At Tyler, Simms & St. Sauveur, we understand the challenges you face. Our professional staff includes former dealership CFOs and Controllers, so we know the demands placed on your people and how to lessen their burden. Most important, we realize that you now need more services than ever before, and we excel at delivering them.

To help you achieve your dealership's full potential — and make your job easier — we will meet with you quarterly to analyze your numbers and point out how you compare to your peers and where you may have opportunities to improve. We will not tell you how to run your dealership. But, drawing on our extensive experience, we will show what others have done to enhance their success and suggest ways you can do the same.

In addition to traditional audit, review, compilation and tax services, we can help you with:

- Operational audits
- Employee benefits consulting
- Estate and succession planning
- Management evaluations
- Business valuation
- Due diligence purchase systems reviews
- LIFO calculations and compliance
- Internal controls review
- Budgeting and forecasting
- Business consulting, and much more

Our expertise has enabled us to be instrumental in designing and presenting a series of accounting courses for the New Hampshire Automobile Dealers Association, and we have been featured speakers at NADA 20 groups. Also, we are members of Auto Team America, a national group of accounting firms specializing in dealership accounting that we meet with several times a year to discuss current and emerging industry issues.

Call us today at 603-653-0044 or visit www.tss-cpa.com to learn how Tyler, Simms & St. Sauveur is uniquely positioned to help you increase your success.

TYLER, SIMMS & ST. SAUVEUR, P.C.

Certified Public Accountants & Business Consultants

19 Morgan Drive
Lebanon, NH 03766
(603)653-0044
(603)653-0209