LGT DEALER SERVICES
Headlights
June 2015

MANAGING AND CONTROLLING YOUR PARTS DEPARTMENT

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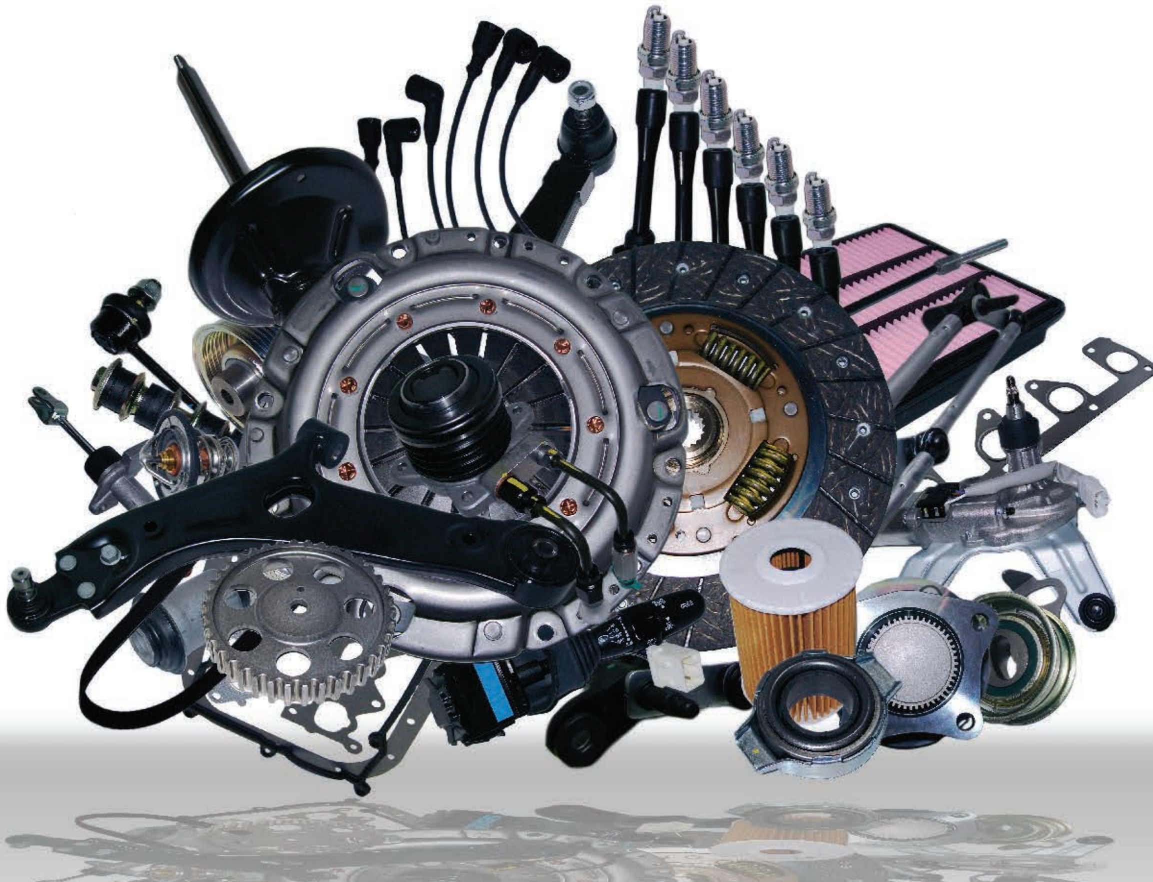

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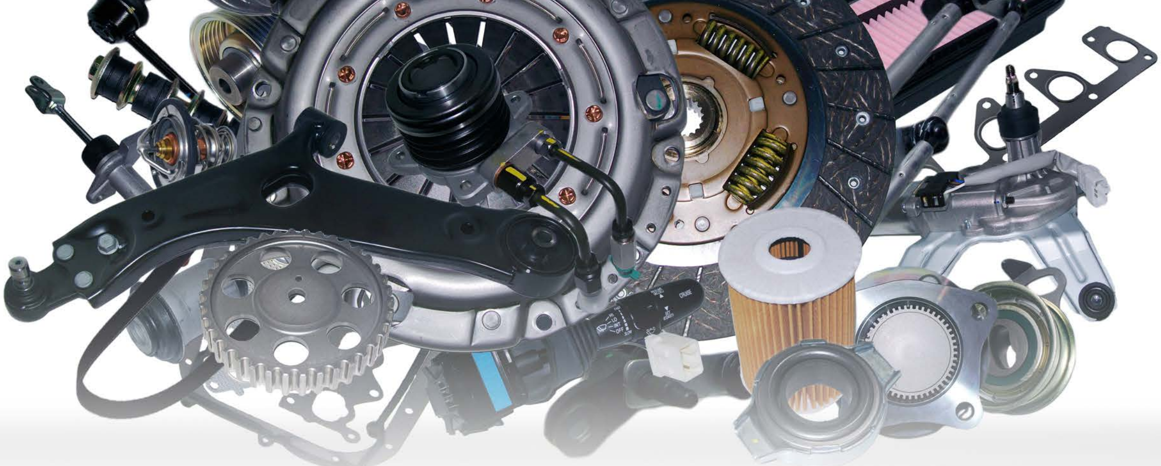
INSIDE FEATURES



MANAGING AND CONTROLLING YOUR PARTS DEPARTMENT

Article courtesy of Auto Team America members

When was the last time you walked through your parts department? Did you just cut through there or did you actually walk every aisle and maybe even look at the shelves and bins? I bet you have never actually walked into your parts department and gone up and down each aisle slowly, actually looking at each shelf, bin and drawer to see what you truly own and how much cash is tied up in inventory.

Why would you want to do this? One, to see if it is even halfway organized. Two, to see how clean or dirty the parts packages and shelves are. Three, to find out where the special order parts are stored and segregated. Four, to find out where all of your "used" parts are stored. Five, to see how busy they really are back there. And six, to see how much storage room your parts inventory dollars really need.

Organization in your parts department is central to having a well-run parts department so your employees working there can find the parts quickly, as every minute they make a technician wait costs you gross profit. If parts bins are not organized and labeled, how are any new hires or temporary employees ever going to find the parts to sell them?

Dirt and dust are necessary evils in the parts department due to the large, open area in which everything is stored, being next to the service department and the amount of traffic of everyone and all the parts going in and out of there daily. But that doesn't mean an effort should not be made to keep it clean and dusted on a regular basis.

Special order parts not picked up by a customer or installed on a customer car will cost you a lot of money over time. Special order parts use up your return allowance very quickly and erodes the amount of parts you can return which are becoming obsolete. If you have this problem, you should make sure they are stocked on the parts pad in a special separate source so they can easily be tracked and you can easily obtain the total dollars you have sitting on the shelves. You should also try to obtain prepayment on these parts as much as possible. At least then you can try to minimize the parts return allowance these parts use up.

Do you know where all of your used parts are you have taken off of vehicles over the years? Did you personally keep track of the $2,000 of tires and wheels you took off that ¾ ton pickup? I don't know of many dealers who can tell me what their used inventory value is or if they know it is still in stock, has been installed on another used vehicle or sold to a customer. What cost has been attached to these parts? These parts should also be tracked on the parts counter pad and have a cost attached to them. You should be able to run a report of these parts to physically check if they are still in stock. Without stocking these into your system, these parts can easily disappear out the back door and no one will remember you have them.

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How busy are your parts counter employees? One way you can tell before you walk through the department and spend some time back there, is to look at your financial statement parts sales and divide it by the number of employees you have in the department. I have seen average sales of $30,000 to $75,000 per employee. This is quite a range. Some stores find themselves with not enough sales to afford hiring an extra person but with sales too high for the number of people they have back there.

With daily parts orders and various factory programs these days for stocking guides, we have seen the average parts inventory reduce over time. With this in mind, do you really need all the room you used to need back there? Can it be put to better use? Could it become a special tool room, a work area for the technicians, etc., which may free up a bay in your service department which you can turn into a profit center? Or maybe you could use the room for a larger customer waiting area or service write up area?

You should also run your parts management report on a regular basis. This report will show you what the aging of your parts inventory is, how many dollars of adjustments have been made to the inventory value, how much you have on your parts pad versus your general ledger, what your projected obsolescence is, negative parts and dollars on hand, your parts turn, how many dollars are over 12 months old, etc. All of this information is normally trended by month side-by-side for comparison purposes. Find out if you are going in the right direction.

Check your parts grosses on your financial statements. Are your internal parts grossing at least what your customer pay parts sales are grossing? If not, why not? You are giving up gross profit which can help increase your parts and service absorption of fixed expenses. Have you parts manager increase the parts matrix to a higher markup until you achieve at least the customer pay gross profit percentage. This should not affect your average used vehicle gross profit. If anything, I have seen it increase the average vehicle gross instead.

Take a chance and spend some time with your parts department. Maybe you will find out why they never to seem to have the right parts in stock.

TAX TIP

INTEREST EXPENSE ON LOAN SECURED BY RESIDENCE

May 13, 2015

The IRS ruled in TC Memo 2015-56 that interest expense on loan proceeds secured by the taxpayers' residence was not deductible as investment interest expense when the proceeds of the loan were loaned to the taxpayers' C Corporation.

Married taxpayers were denied deductions for investment interest expenses. The individual taxpayers refinanced an existing personal loan through home equity indebtedness. They allocated some payments to mortgage interest and the remaining payments to investment interest expenses. The investment interest expense claimed by the individual taxpayers was disallowed because they could not substantiate that the money was used for investments. The money was deposited into the husband's corporation's bank account, with notations that the funds were a loan from the individual taxpayer to the company. Further, adjustments made by the IRS to the amount of allowable mortgage interest deduction were sustained.

Section 163 allows taxpayers a deduction for "qualified residence interest" paid on the mortgage on their first or secondary home. Qualified residence interest is either "acquisition indebtedness" or "home equity indebtedness." Acquisition indebtedness is a loan of up to $1 million that is used to acquire, construct, or substantially improve a residence when that residence also secures the loan. New debt to refinance old acquisition indebtedness is also acquisition indebtedness as long as it is not more than the refinanced debt. Home equity indebtedness is any other type of loan secured by a qualified residence but is capped at the lesser of $100,000 or the fair market value of the residence minus any acquisition indebtedness on the residence.

The taxpayers contended that the interest paid is deductible as investment interest because the loan proceeds were deposited in the corporation's bank account. The taxpayers' noted that the interest in the corporation is property held

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for investment because it is a type of property that generally produces dividend income. It is not necessary for the Court to decide whether the corporation is property held for investment because the taxpayers did not purchase or contribute the loan proceeds to the corporation. Instead, the corporation's general ledger notes that the company treated the mortgage proceeds as a personal loan from the husband to the corporation. In other words, the husband borrowed the money so that he could lend it to the corporation and the corporation would repay him. The husband has not shown that the funds disbursed for his mortgage to finance his ancillary loan to the corporation was for investment.

The taxpayers did not demonstrated that the deduction is allowable pursuant to any statutory provision because they have not shown the funds were used for investment. Accordingly, the court determined that the taxpayers' home mortgage and investment interest expense deduction for the interest paid on the home equity loan was not allowed.

If you have any questions regarding the above, get in touch with your LGT representative.

2015 CONTROLLERS' ROUNDTABLE EVENTS

Semi-annually, the LGT Dealer Services Group organizes nearly two days of seminars for dealership controllers across the Southwest. Each time, guest speakers present the very latest on financial issues facing dealerships. Continuing Professional Education ("CPE") credit is awarded to attendees. We know that as a controller or CFO, it is hard to get away and visit somewhere relaxing; that's why we choose to host our events in exciting areas that you can enjoy while attending.

CLICK HERE TO REGISTER

LGT

WE LOOK FORWARD TO SEEING YOU!

DISCUSSION TOPICS

Spring Event on June 18 & 19:

- Power Generators for Dealerships: Operational Insurance and Additional Revenue Stream—Brandon Lobb, Locke Lord
- The "New Culture" and HR Updates—Stephen Roppolo, Fisher and Phillips
- Alternative Lending for Dealers—Dan Garces & Gabe Robleto, Cars
- ERISA and DOL Compliance—Tonia McBride, LGT
- CFPB Impact On Dealers and Texas Legislative Update—Michael Dunagan, Jameson and Dunagan
- Kevin Smith—Better Resource
- Excel Training Session—Erica Tang, LGT
- Roundtable Discussions—LGT to facilitate

Fall Event on October 22 & 23:

- Legislative Update
- Tax Update
- HR Update
- Alternative Energ Savings for Dealerships
- Roundtable Discussions

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