



100 Action Plans.

AUTOMOTIVE FINANCIAL STATEMENT FOR MANAGERS

For many managers, reading financial statements is like reading hieroglyphics. They know that there is insightful information in there that can help them do their job better, but can they interpret it?

Fortunately you don't need a Rosetta Stone or an accounting degree to break the code; you just need to know a few basics.

On July 27, 2017, Brooke Samples, President of Profit Blueprints LLC joined us for an online workshop to help us to better understand dealership financial statements.

Over the course of her long career, Brooke Samples has worked with with Lloyd Schiller's Dealer Service Corp, NCM and VW University, and as President of Profit Blueprints, has analyzed over 15,000 Dealership financial statements and coached and motivated hundreds of Dealership Managers in all departments across North America. Using her monthly financial analysis, Profit Blueprints, she compares Dealers' financial statements to key Benchmarks. She then uses her vast reservoir of experience plus feedback from her Clients to help Managers utilize over

This report is a summary of Brooke's comments and suggestions.

.....see Brooke's Contact Details on the last page.

"If you don't have regular and accurate financial statements, you're driving your business 100 miles an hour, down a one-way street, the wrong way, at night, in the fog, without lights."

Jim Blasingame Author

Reading, understanding and analyzing patterns in your financial statements is the key skill of top performing dealership management.

If you are just looking at a couple of ratios or target numbers, you are missing a lot... a lot of opportunity!

In this workshop Brooke showed us:

- ✓ What happens when you sell something... follow the transaction through the Financial Statement. What happens? Why?
- ✓ What happens when you buy something... how does that evidence itself in the Financial Statement & why it is important.
- ✓ Best practices for comparing the Financial Statement to your departmental reports and DOC... why they are different... when you should and should not worry.
- ✓ How to keep the Financial Statement accurate with daily self-audits... nothing worse than managing with corrupt data.
- ✓ How to read the Balance Sheet Accounts & how this knowledge can impact your performance.
- ✓ When and Why to compare your Statement to Benchmarks & Targets.

THE BASICS

As managers, we deal with a lot of reports with financial data, but what exactly is a financial statement?

While statements come in all sizes from a few pages to 12 page behemoths like Mercedes, they all are made up of two parts.

- 1. The Balance Sheet reflects ALL transactions and is typically page one.
- 2. The Income or Profit/Loss Statement which show sales and expenses.

The income statement is broken down into the following general categories.

- ✓ SALES
- ✓ GROSS PROFIT
- ✓ EXPENSES
- ✓ NET INCOME (also called "Selling Gross Profit" (Ford) or "Department Profit" CDJR)

And it follows a formula: Gross Profit – Expenses = Net Profit.

All of the combined income statement results flow onto the balance sheet and appear on a single line: Current Year's Profit.

NAME OF ACCOUNT		INCOM	E STATEMENT	DATE 06,049 06,551 0,170 11.6% 3,596 4.3% 3,091 -0.2% 3,825 0.1% 4,131 0.8%
	MONTH		YEAR TO DATE	
SALES	10,044,151		44,496,049	
GROSS	1,138,042		5,606,551	
EXPENSES				
Salespeople Compensation	143,123	12.6%	650,170	11.6%
Compensation F & I / Service Contracts	65,132	5.7%	238,596	4.3%
Delivery Expense	-2,890	-0.3%	-13,091	-0.2%
Policy Expense - New & Used	587	0.1%	3,825	0.1%
Demo Expense	2,131	0.2%	44,131	0.8%
Advertising - New & Used	82,438	7.2%	396,791	7.1%
TOTAL VARIABLE SELLING EXP	290,521	25.5%	1,320,422	23.6%
Compensation Supervisors	164,841	14.5%	784,066	14.0%
Compensation Clerical	41,311	3.6%	168,146	3.0%
Other Salaries & Wages	226,212	19.9%	982,121	17.5%
Payroll Taxes	61,987	5.4%	346,347	6.2%
Employee Benefits/Pension/401K/Workers' Comp	130,833	11.5%	611,514	10.9%
Absentee Wages - Productive	43,131	3.8%	167,501	3.0%
TOTAL PERSONNEL EXPENSE	668,315	58.7%	3,059,695	54.6%



The balance sheet shows the following:

✓ ASSETS

- Liquid assets can be converted into cash.
- Fixed assets that are not expected to be converted into cash in the next 12 months.

MINUS

✓ LIABILITIES

- Short term debt that will be paid back within a year, like bills, etc.
- Long term debt which takes more than 12 months to pay back, like a mortgage.

									ט	arari	CC	<u> </u>
					LINE							
ASS	ETS				-	LIABILITIE						AMOUNT
Cash on Hand				850		Accounts			Creditors	3		893,13°
Cash in the Bank				1,231,451	2	Vehicle L	ien Payo	ffs				296,133
Cash Clearing				0	3	License	and Regi	stration F	ees			
Contracts in Trans	sit			2,259,796	3	Custome	r Deposi	ts				
TOTAL CASH AND O	ONTRACT	rs		3,492,097	4							
Vehicle Accounts	Receivab	le		540,176	5	N P		- New V	ehicles &	Demos		10,365,41
Service, Body Sho	p & Part	s Accts.	Receivable	129,702	6	O A L T Y E E A E		- Used \	/ehicles			541,31
Factory Receivabl	es			51,421	7	S B		- Lease/	Rental V	ehicles		1
Warranty Receiva	bles			45,919	8	TOTAL A	COUNTS	& NOTES	PAYABLE			12,095,992
Finance Reserve				23,144	9	Interest	Payable					
TOTAL RECEIVABLE	S			790,362	10	Payroll F	ayable					125,15
New Vehicles	UNITS	254		9,734,713	11	Taxes Pa	ayable	- Sales				118,878
Used Vehicles	UNITS	123		1,277,245	12			- Real E	state			38,50
Parts				395,303	13	TOTAL SI	HORT TER	M DEBT				12,378,52
Accessories				77,956	14							
Body Shop Materi	als			1,245	15	TOTAL LO	ONG TERM	1 DEBT				1,534,013
Sublet Repairs				4,512	16							
Work in Process	- Labor			3,451	17	TOTAL LI	ABILITIES	(Line 12 +	Line 14)			13,912,53
Tires						RETAINED				rofits)		3,313,31
TOTAL INVENTORIE	S			11,525,794	19	CURRENT	YEAR NE	T EARNING	SS - PROF	IT OR (LOS	S)	405,81
TOTAL FIXED ASSE	TS			1,823,411	20	TOTAL NI	T WORTH	I (LINES 1	7 & 18)			3,719,120
TOTAL ASSETS (LIN	IES 4. 10.	19 & 20)		17,631,664	21	TOTAL LI	ABILITIES	& NET W	ORTH (LIN	ES 16 & 19)	17,631,664

Balance Sheet

EQUALS

✓ NET WORTH

WHY IS THE FINANCIAL STATEMENT IMPORTANT?

- ✓ It's YOUR report card! It reflects everything that in a dealership from a financial standpoint.
- ✓ Pay Plans often use the data to establish compensation.
- ✓ Gauges the health of the business and identifies areas of opportunity.
- ✓ Important when applying for loans and can determine what interest rates you pay.
- ✓ Can affect how much tax you pay (or keep if you are audited).

SO HOW DO SALES SHOW UP ON THE FINANCIAL STATEMENT?

Good question. Brooke walked us through a typical car sale with a trade.

A car that cost \$18,000 is sold for \$20,000 for a gross profit of \$2,000 and the income statement would look something like this.

So how does it show up on the balance sheet? If this was the sole business transacted it would look something like this.

The \$20,000 car was paid for by a combination of:

\$2,000 CASH, a \$12,000 loan which is called CONTRACTS IN

Units Sales Gross Profit Per Unit
1 20,000 2,000 2,000

TRANSIT and a \$6,000 trade called USED VEHICLE INVENTORY.

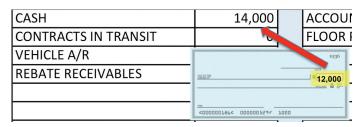
The cost of the car was \$18,000 called NEW VEHICLE INVENTORY

BALANCE SHEET (1st Page of the financial statement)

ASSETS			LIABILITIES (We Ow	e \$1 & NW
ASSETS		·		
CASH	2,000		ACCOUNTS PAYABLE	
CONTRACTS IN TRANSIT	12,000		FLOOR PLAN	
VEHICLE A/R				
REBATE RECEIVABLES				
			SALES TAX	
NEW VEHICLE INVENTORY	-18,000			
USED VEHICLE INVENTORY	6,000		PAYROLL	
PARTS INVENTORY				
			TOTAL LIABILITIES	
			NET WORTH / PROFIT	2,000
TOTAL ASSETS	2,000	=	LIABILITIES & NET WORT	2,000

The TOTAL ASSETS shows the \$2,000 profit from the sale, which equals the LIABILITIES AND NET WORTH of \$2,000.

To illustrate how cash moves around the financial statement, consider what happens when the bank pays the dealer the \$12,000 that the customer borrowed.



CONTRACTS IN TRANSIT goes to \$0.00 and CASH goes to \$14,000.

In this case the new vehicle was purchased from another a dealer for \$18,000 and now needs to be paid and unless I sell the used vehicle, I'm overdrawn.

BALANCE SHEET (1st Page of th Uh Oh!

Page of t
-4,000
(
6,00
2,00

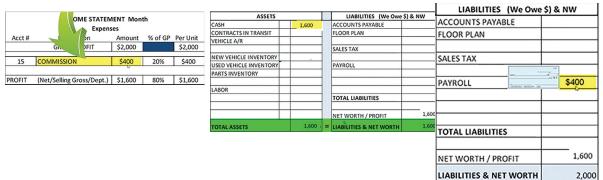
Being overdrawn too many times can create problems, so it pays to have enough cash in the bank to cover fluctuations in cash flow.

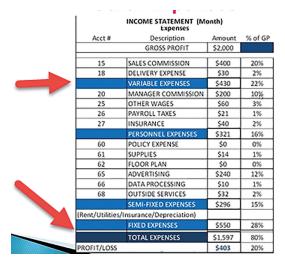
Once the used vehicle is sold, it replenishes the cash.

BALANCE SHEET (1st Page of th

ASSETS		
CASH	2,000	
CONTRACTS IN TRANSIT	0	
VEHICLE A/R		
REBATE RECEIVABLES		
NEW VEHICLE INVENTORY		
USED VEHICLE INVENTORY	,	
PARTS INVENTORY	- Q	
LABOR		
TOTAL ASSETS	2,000	

When the \$400 commission is paid on the income statement, it shows up as a payroll liability on the balance sheet. When the check is cashed the total assets on the balance sheet are reduced to \$1,600.





As a general rule, Expenses are arranged on the Income Statement from the most controllable like Variable Expenses to the least controllable Fixed Expenses.

When put into the perspective of % of GP, it makes it easy to track and evaluate to ensure that they are consistent with your guidelines, since every dollar trimmed from expenses is one less dollar that you have to earn through selling something.

D	LABOR AMOUNT		\$45.00
E	PARTS AMOUNT		\$850.00
S	GAS, OIL	Т	\$0.00
С	SUBLET	0	\$0.00
R	MISC. CHARGES	T A	\$12.00
P	TOTAL CHARGES	L	\$907.00
Т	ADJUSTMENTS	S	-\$24.00
1	SALES TAX		\$57.40
O N	PLEASE PAY		
14	THIS AMOUNT		\$940.40

So how does a Service repair flow through the financial statement? Consider this tire sale.

In this example we had a Labor sale of \$45.00, a Parts sale of \$850.00, a Misc. sale of \$12.00 and an adjustment or discount of (-) 24.00 split evenly (\$12.00 each) between parts and service for a grand total including tax of \$940.40.

Invoice	SALE ACCOUNT	COST OF SALES	GROSS PROFIT		
LABOR AMOUNT	\$45.00	\$15.00	\$30.0	00	
PARTS AMOUNT	\$850.00	\$750.00	\$100.0	00	
MISC. CHARGES	\$12.00	\$10.00	\$2.0	00	
TOTAL CHARGES	-\$1	2			
ADJUSTMENTS	-\$24.00		-\$24.	00	
SERVICE DEI	INCOME PARTMEN	1.1	ENT Mo	GROSS	GP %
ACCOUNT		RO	SALES	PROFIT	SALES
LABOR ACC	COUNT	1	\$33	\$18	55%

The income statements for this transaction look something like this with \$12.00 each coming off of the Labor and Parts sale.

So instead of collecting \$45.00, the service department collected on \$33 for installing the tires.

Brooke noted that the proper place to apply discounts is against the sale rather than to advertising and promotion.

While this seems wrong, the advertising account is for the <u>cost of conducting the promotion</u>, such as printing and mailing expenses rather than the discount given to the customer.

And this makes sense for a couple of reasons.

- 1. It keeps the sales and gross amounts accurate.
- 2. It ensures that compensation calculated from sales or gross is accurate.

Analysis of the income statement shows that when the \$10 commission is paid to the service advisor, it absorbs 56% of the \$18 gross profit made from the sale.

Tires	INCOME STATEMENT (Mon Expenses	th)	
1 I'm			
^,,,, [SERVICE GROSS PROFIT	\$18	
15	SALES COMMISSION	\$10	56%
20	MANAGER COMMISSION	₹\$2	10%
25	OTHER WAGES	\$1	6%
26	PAYROLL TAXES	\$0	2%
27	INSURANCE	\$1	3%
	PERSONNEL EXPENSES	\$14	76%
60	POLICY EXPENSE	\$0	2%
61	SUPPLIES	-\$2	-11%
65	ADVERTISING	\$0	0%
66	DATA PROCESSING	\$1	3%
68	OUTSIDE SERVICES	50	0%
	SEMI-FIXED EXPENSES	-\$1	-6%
(Rent/Util	ities/Insurance/Depreciation)		
	FIXED EXPENSES	\$3	17%
	TOTAL EXPENSES	\$16	87%
PROFIT/LO	OSS	\$2	13%

The \$2.00 charged for supplies such as wheel weights, etc. shows as (-) \$2.00 because it reduces that expense charge.

In this case, the net profit from the transaction is \$2.00 or 13% of the Gross Profit.

While not bad, it's also not the 20% benchmark which is why having a plan to maximize the yield on low margin opportunities with complementary services such as alignments, road hazard protection, etc. or found work such as brakes, etc.is important.

DEALERSHIP DEPARTMENT REPORTS

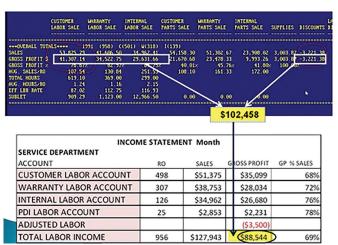
Managers rely on DMS generated system reports to manage their departments. But often they don't match the financial statement. Why?

In this example, the service manager experienced a large variance between the gross profit on the DMS report and financial statement.

Some reasons could be:

- ✓ That the technicians are costed wrong. For example, it is not unusual to find that hourly technicians show ZERO cost.
- ✓ Production/CSI/Sales bonuses are not accounted on for on the production report.
- Accounting entries such as:
 - Backed out warranty repair orders.
 - Adjustments of work/labor in process.
- ✓ Adjustments made to repair orders after closed.
- ✓ Discounts posted to the wrong account.

So how does the Service manager fix this?



Well, not all can be, however some tips for reducing the variance are:

- ✓ Make sure that tech hourly cost is correct. Maybe the rate from \$22 to \$24 was never changed in the DMS report.
- ✓ Flag clock hour techs at their average rate based on cost.
 - For example a \$10 hour tech is paid for 40 hours but only produces 20 hours. His average cost is \$20 per hour.
- ✓ If techs are assigned tasks, such as training, equipment maintenance, janitor, etc. move their cost for that project to the appropriate expense account.
- ✓ Adjust cost to reflect consistent bonuses.
 - Tech T.J always hits a production bonus of \$2 per flagged hour.
- ✓ Any adjustments to sales or gross must be signed off by the department manager.
 - For example if a service advisor decides to offer a discount or not charge for a repair, the manager must first approve it.
- ✓ Verify the DMS settings send entries to the correct accounts. ASSUME NOTHING!
 - Dig deeper if something doesn't look right.
- ✓ Reconcile the Work in Process on the General Ledger to labor paid on open repair orders every month.
- ✓ Run exception reports daily to catch errors in real time.
 - Set them to run in the nightly job stack.
 - Service: CDK=REX, R&R= 3619
 - Parts: CDK=ROV, R&R= 2542

So how does the Sales Manager ensure that his sales summary report matches the financial statement?

Start by ensuring that the closed sales are posted to accounting.

Some reasons for variance could be:

- ✓ Internals posted after the deal was sent to accounting.
- ✓ "We Owes" not allowed for in the deal.
- ✓ Receivables not collected/rebate adjustments.
- ✓ The deal was backed out from the previous month.
- ✓ Finance income adjusted by finance source.
- ✓ Reserves (Free Oil Changes, etc.)

So what can the manager do?

- Employ a recap sheet with every deal.
 - Accounting verifies the accuracy of the deal.
- ✓ Any write-offs must be signed off by the department manager.
- ✓ Accounting notifies Finance when a finance source pays reserve or notified reserve amount varies from the amount set up.
- ✓ Understand where document fees and packs are accounted for in the statement.
- ✓ Spot check by comparing the Vehicle Sales Journal to the actual sales report.

DAILY OPERATING CONTROL (DOC)

The DOC is an important tool for managing the department, so it is vital that it match the financial statement.

- ✓ Brooke recommends that a secondary DOC with more accounting detail be set up to provide better clarity to key accounts. For example, maybe there is value in knowing what is going into various sub-accounts for Advertising such as paper expense, internet, or payments to various vendors.
- ✓ Compare the DOC to department reports to highlight variance in close to real time.
- ✓ Compare recap sheets to the DOC.

MANAGER RESPONSIBILITIES

- ✓ To be relevant the financial statement must be accurate, complete and timely so it is critical that managers turn their paper work in as soon as possible.
- Review the schedules regularly.
 - Sales:
 - Receivables, rebates and inventory aging.
 - Deals in Process keep it clean.
 - Service/Parts/Body Shop:
 - Receivables aging.
 - Open repair order aging.
 - Parts inventory reports.
 - Special Order aging.
- ✓ Review your direct staff's Pay Checks/Detail Report.
- ✓ Insist on authorizing expenses.
- Review key expenses weekly.
 - Use schedules or detail reports.
- Review details on advertising expenses.
- ✓ Review policy expense.

ACCOUNTING RESPONSIBILITIES

- ✓ Notify managers when entries are made that impact their departments.
- ✓ Use a checklist to confirm all normal expense bills and invoices are posted before closing the month.
- ✓ Reconcile assets and liabilities like bank statements, receivables, payables, inventories, etc. at least before the end of the month.
- ✓ Accrue for payroll and bonuses.
- ✓ If payables receives a statement and has no matching invoice, get the invoice and make sure that the manager authorizes it.
- ✓ Make sure the payables clerk is familiar with expense accounts as a backstop to catch errors.
- ✓ Allocate fixed and overhead expenses fairly.

PUTTING PERFORMANCE INTO PERSPECTIVE

To understand performance and to ID areas of opportunity, it is useful to compare yourself to something. Some common methods are:

- ✓ Your historical data and trends.
- ✓ Industry metrics.
- ✓ Other dealerships in your group.
- ✓ Your targets and goals.
- ✓ 20 Groups / CPAs.
- ✓ Outside sources like Profit Blueprints.

Actionable information must be compared to something.

Sales:

- ✓ Gross Profit per Unit.
- ✓ Units sold as % of last month and last year's average.
- ✓ Days supply.

Finance:

- ✓ % Penetration: Contracts sold as % of unit sales.
- ✓ Gross per unit retailed.

Service/Parts/Body Shop:

- ✓ Gross Profit Retained.
 - Is it too good? Could be a red flag.
 - Is it too bad? Needs investigation.

Expense control: Are they in line with expectations/targets?

IN	COME STATEMENT (YTD) Expenses		
Acct #	Description	% of GP	Target
	GROSS PROFIT		
15	SALES COMMISSION	20%	
18	DELIVERY EXPENSE	2%	
	VARIABLE EXPENSES	22%	
20	MANAGER COMMISSION	10%	
25	OTHER WAGES	3%	
26	PAYROLL TAXES	1%	
27	INSURANCE	2%	
	PERSONNEL EXPENSES	16%	
60	POLICY EXPENSE	0%	
61	SUPPLIES	1%	
62	FLOOR PLAN	0%	
65	ADVERTISING	12%	
66	DATA PROCESSING	1%	Y.
68	OUTSIDE SERVICES	2%	
	SEMI-FIXED EXPENSES	15%	
Rent/Utilities/	Insurance/Depreciation)	0	
	FIXED EXPENSES	28%	
According to the second	TOTAL EXPENSES	80%	
PROFIT/LOSS	(Net/Selling Gross/Dept.)	20%	

The best targets come from comparing yourself to yourself.

How do they compare to year to date totals?

How do they compare to previous years?

Frozen Capital: Are they in line with expectations/targets?

Are they too much relative to sales?

Are they too old to sell or collect?

Brooke offered a free spreadsheet to evaluate your assets:

https://offers.dealersedge.com/samples.php

CONCLUSION

To better understand how financial statements are organized, Brooke recommends:

- ✓ Looking at a blank statement and then study your statement.
- ✓ Take advantage of other DealersEdge webinars that deal with other aspects of the financial statement analysis.
 - How to get more smart data from your DMS
 - How to turn balance sheet profits into hard cash
 - Expense control... when sales are soaring...many lose focus on controlling the controllable
 - Benchmarks and Key Performance Indicators...a deeper look at the 'every manager' tool
 - What Fixed Ops managers need to know about the financial statement and analytical reporting
 - How to fine-tune the new vehicle departments to spot weakness and supercharge results
- ✓ Be active in getting the answers that you need to be a better manager.
- ✓ When you make a change, think about how it will affect your department and where it will show up on the financial statement. For example:
 - Add a tech:
 - I expect to increase sales & gross profit.
 - I expect to increase personnel expenses.
 - Increased Net Profit.
 - Increase advertising:
 - I expect increased unit sales and gross profit.
 - I expect more factory income.
 - I expect increased advertising and variable personnel expenses.
 - Increased Net Profit.

Everything shows up on the Financial Statement "selfie", so doesn't it make sense to make it as accurate a possible?



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