PROTECT YOUR CASH

As a result of recent global financial stress, many financial institutions are struggling and several have been acquired or sought bankruptcy protection. In an attempt to protect your cash from losses, we have summarized some of the applicable rules and ideas for your consideration in managing and preserving your cash, as opposed to maximizing the yield.

US Treasuries

Arguably the safest investment in the world is one that is backed by the full faith and credit of the United States of America. The US government frequently borrows money and issues IOU's in the form of US Treasury bills, notes and bonds, with maturities ranging from less than one year (bills), to one to 10 years (notes), to over 10 years (bonds). These investments can be purchased through the US Treasury's "TreasuryDirect" program (treasurydirect.gov), or through a bank or brokerage firm. Fees and commissions, if any, will be the lowest through TreasuryDirect. Interest earned on US Treasuries is fully taxed on your federal income tax returns but is not taxable by state and local municipalities.

FDIC-Insured Accounts

The Federal Deposit Insurance Corporation (FDIC) is an independent agency of the federal government. Savings, checking and money-market accounts, certificates of deposit and other deposit accounts, when combined, are generally insured up to $100,000 per depositor per ownership category in each bank or thrift the FDIC insures. Please be aware there are state-chartered banks and thrifts that might not be FDIC-insured. The most common ownership categories are: (1) single accounts; (2) joint accounts; (3) certain retirement accounts; and (4) revocable trust accounts. For example, a married couple's accounts would be fully insured if they each had a single account of $100,000 and they had a 50/50 joint account with $200,000. Retirement accounts are generally insured up to $250,000. If you have any questions about your insurance coverage you can reach the FDIC, at 1-877-ASK-FDIC, or visit them online at www4.fdic.gov/EDIE/.

Many banks and thrift institutions now offer the Certificate of Deposit Registry Service, or CDARS. Funds in excess of $100,000 at your institution can be deposited at other banks in the network to obtain full FDIC insurance. You will be offered one rate for all CDs with the same maturity date and you will receive tax forms and statements from one institution only. FDIC insurance protection can reach $50 million through this program. A similar result can be achieved by purchasing certificates of deposit at various institutions through a brokerage account. In this case, you can pick and choose for the best yield, but it does require a little more work on your part. Finally, there is a similar program for money market accounts that a few banks offer through the Institutional Deposits Corp., which can provide protection up to $5 million. At present, no banks in the immediate Washington, DC area offer this program, although we expect they will in the near future.

SIPC-Insured Accounts

The Securities Investor Protection Corporation (SIPC) is a nonprofit membership corporation funded by its member securities broker-dealers. It is neither a government agency nor a regulatory authority, even though it was created by the Securities Investor Protection Act. Generally, cash, stocks and bonds held by your broker are protected by SIPC. Assets not registered with the SEC are not protected. Of course, the protection is to prevent loss of the asset - not loss of asset value. The amount of the protection is usually $100,000 for cash and up to $500,000 for all protected assets.

If you have questions regarding matters contained in this alert, please contact your local Auto Team America member.

CASH FLOW IS BECOMING AN URGENT MATTER

With the economy slowing down to a screeching halt as if we all tried to stop suddenly in traffic to avoid hitting the car in front of us, it is time to take a hard look at where you can not only conserve cash but generate it also.

If you are a normal dealer, you probably know or check on your cash balance daily. Some dealers run their business by their checkbook balance, while others use the actual bank account balance and release checks accordingly. Which is better?

The biggest difference we see between the two methods is the dealers that watch the actual bank balance don't seem to have as much cash to operate on as other dealers. They seem to struggle more and can only release checks to pay bills and other items if they happen to get a deposit that day. Most times the checks have already been printed or written and are being held by the accounting department until the funds are there to cover them.

Running your business this way means you are going to spend an awful lot of your time trying to manage your cash instead of actually running your business and selling cars. Your office manager is also going to spend considerable time assisting you by constantly checking the online balance of your cash account to see if any electronic deposits hit the account today. If a deposit did make it into your account, then you get to pay some bills today! If not, the bills will have to wait until another day.

A way to increase your cash flow is to review your receivables. Review your outstanding balances in your contracts in transit, vehicle receivables, accounts receivable, factory receivables such as warranty claims, incentives, pre-delivery, finance and insurance reserves and other receivables. If you have an outstanding balance in any of these accounts, review the aging of the balances. Each receivable has an average number of days in which it should be collected. This doesn't mean they can't be collected in a shorter time period. You can increase your cash flow just by concentrating on the collection of your receivables and trying to speed up the entire collection process.

Speeding up the process starts when the receivable is generated. Make sure the documentation you have for the receivables is adequate to ensure you even have the possibility to collect it timely and maybe even before the average days it normally takes to collect it. When we are reviewing aged receivable balances, we ask why they are still on the books. The most common answer is almost always accompanied by a story. Sometimes these stories are interesting and sometimes they are not. Either way, it means they are not being collected because something was not completed correctly or there are problems with the way it was generated.

These types of receivables seem to come in groups and don't tend to be collected as they are not a priority anymore. It is going to take more than normal work and effort by someone to correct the problem. Normally the person responsible for correcting the problem is now too busy to spend the time on it and is more concerned with the current day's business. Unless their pay plan includes compensation based on maintaining current receivable balances, their priorities will never be on the aged balances. This means the balances will become older and older until it may become impossible to collect them.

Normally we see the accounting office trying to collect these old balances. They are normally hampered in these efforts because they were not involved in the original transaction. As a result, they are not very successful. We, as accountants, end up writing these off to bad debts at year end. So, they do eventually go away, but not the way it was intended. It doesn't put money in your bank account.

Other accounts that tie up cash are prepaid expenses. Try to minimize the amounts you invest in prepaid assets. Make sure it makes economic sense to invest in the prepaid expense if you have the choice. If a discount is offered make sure you can afford to take advantage of it. Without adequate cash flow, you may have to pass it up.

We know you know this. We don't have to tell you again. Inventory management. There, we said it. The biggest offender of cash flow is lack of inventory management. Now, with the economy slowed to a go cart pace, inventories have ballooned up due to lack of sales. It is not that you were overstocked when sales were good. It may be you were not really paying attention to maintaining the proper mix of costs and models. Now what do you do? You can't afford to take all these overage vehicles to the auction and dump them. The losses would be horrific. You may owe more on them than they will wholesale for. That means you are as upside down as some of your customers are when they come to you and want to trade. Not a good feeling or position to be in.

Most dealers we have talked to are going to have to work their way out of the inventory they no longer need or are buried in since the price drop in trucks and SUV's. We don't have the magical wand to wave over your inventory to cure these problems. There will be a time when the prices will stabilize on these vehicles and maybe increase somewhat once consumers "get used to" higher gas prices and adjust their overall mileage. Right now they can't afford to keep driving them and you can't afford to trade for them.

If the economy doesn't stabilize soon, dealers may be forced to liquidate some of their overpriced inventory to strengthen their cash flow. If this happens, wholesale losses will increase and or retail gross profits will decrease dramatically nationwide at the same time dealers are experiencing low volume sales and increased competition from each other.

Only time will give us the answers. Take a look at your cash position and see how much ready cash you actually have. Do you have some cash reserves in a cash management account? If so, hang on to them. Try not to manage your business by watching your actual bank balance.

For further information on managing your cash situation, please contact your local Auto Team America member today!!

TAX TIP

HOBBY LOSS RULES

Dealers may be engaged in an activity that may promote their business by advertising and promoting the dealership on the side of a race car or a race boat. An activity that is not engaged in for profit is considered to be a hobby.

In determining whether an activity is engaged in for profit or merely a hobby the following factors should be considered:

- Does the time and effort put into the activity indicate an intention to make a profit?
- Do you depend on income from the activity?
- If there are losses, are they due to circumstances beyond your control or did they occur in the start-up phase of the business?
- Have you changed methods of operation to improve profitability?
- Do you have the knowledge needed to carry on the activity as a successful business?
- Have you made a profit in similar activities in the past?
- Does the activity make a profit in some years?
- Do you expect to make a profit in the future from the appreciation of assets used in the activity?

If an activity is not for profit, losses from that activity may not be used to offset other income and deductions cannot exceed the gross receipts from the not for profit activity. Further, hobby deductions are claimed as itemized deductions in the following order and only to the extent stated in each of three categories:

- Deductions that a taxpayer may claim for certain personal expenses, such as home mortgage interest and taxes, may be taken in full.
- Deductions that do not result in an adjustment to the basis of property, (e.g. advertising, insurance premiums and wages) may be taken next, to the extent gross income for the activity is more than the deductions from the first category.
- Deductions that reduce the basis of property, (e.g. depreciation and amortization) are taken last, but only to the extent gross income for the activity is more than the deductions taken in the first two categories.

When engaged in an activity that may be deemed "not engaged in for profit" or a hobby, you should consult with your Auto Team America advisor to establish and document your business motive thus potentially avoiding the disallowance of the above referenced expenses.