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Checking the backgrounds of new hires

An average of 178,000 employees per month were added to the payrolls of employers in the United States in 2016, according to an “Employment Situation Summary” released in December by the U.S. Bureau of Labor Statistics. And the pattern of a significant number of new hires per month is expected to continue into the New Year.

If your dealership plans to add employees in the foreseeable future, you’ll want to make sure you’re bringing in “good people” you can trust with sensitive customer information — and with your inventory. In this regard, one crucial step in the hiring process is the employee background check.

LAWS ON THE BOOKS

Background checks need to be performed without violating privacy rights and other laws, which vary from state to state and evolve frequently. So, you’ll want to consult an attorney before beginning your hiring quest.

The Fair Credit Reporting Act defines the standards for using credit checks in employment screenings.

The Fair Credit Reporting Act, for instance, defines the standards for using credit checks in employment screenings. Before requesting a credit (or “consumer”) report, an employer must: 1) disclose clearly and conspicuously to the employee or applicant (in a separate document that doesn’t refer to other subjects) that a report may be requested, and 2) obtain the applicant’s or employee’s written consent.

In many states, only law enforcement agencies, financial institutions, debt collectors, insurance companies and sureties can check credit reports. The Electronic Communications Privacy Act does,

however, permit credit history inquiries by other types of employers if they’re related to a “bona fide occupational requirement” of a particular position or group of employees. These limited exceptions exist for jobs that involve:

- ▶ Access to personal, financial or confidential information; trade secrets; or national or state security information,
- ▶ Unsupervised access to cash or certain assets valued at \$2,500 or more,
- ▶ Bonding or security required by state or federal law, and
- ▶ Signatory power over business assets of \$100 or more per transaction.

An exception also exists for managerial duties that involve setting the direction or control of the business.

OTHER RULES TO FOLLOW

The Driver’s Privacy Protection Act regulates how information from state motor vehicle department records can be released and shared. The departments generally will make the job candidate’s driving records available, usually for a small fee.

Most schools, colleges and universities, however, won't release records without the student's consent. Some schools will release records only to the student.

You also may need the candidate's consent before performing a criminal background check. In general, it's illegal to inquire about arrests — you can inquire only about convictions.

THE RIGHT PROVIDER

An employer may personally conduct a background check. Free general advice for doing so is available from the Small Business Administration and other organizations. But often the more convenient approach is to hire an outside agency such as a background check specialist, private investigator or credit agency.

Choose your background check provider carefully, however. There are many start-up companies in this field, and a less experienced or thorough firm might, for example, search for a criminal

history in only one or two states where an applicant has lived.

Most criminal records are available by county and then reported to the state. Thorough agencies typically check all of the counties in which someone has lived, worked or gone to school over the last 10 years.

Additionally, be wary of Web-based companies that offer "instant" checks. There isn't one national database that contains *all* federal and state convictions. Finding criminal records can be a fragmented task across multiple jurisdictions and courts. Moreover, many e-businesses offer low rates for public record searches, but the advertised rates may be deceiving. The more jurisdictions you want to search, the more you're likely to pay.

ONLY PART OF THE PICTURE

Conducting background checks is only part of the due diligence process in hiring new employees for your dealership. But it's a critical one that you've got to approach with the utmost care. ▀

Attention partnerships: Change ahead

New IRS regulations will affect tax strategies

Is your dealership structured as a partnership? If so, or if you're considering transferring property to a partnership, take note of new IRS regulations that took effect October 5, 2016.

SECTION 707 DISGUISED SALES

It's common for a partner to contribute appreciated property to a partnership and for a partnership to distribute cash or appreciated property to its partners. In general, no tax is owed on either the contribution or distribution. But, in certain instances, a contribution of appreciated property by a partner followed by (or sometimes preceded

by) a distribution of cash or property to that same partner will result in tax being owed.

These transactions are referred to as "disguised sales" and are addressed in Internal Revenue Code Section 707 and its regulations. They state that a taxable sale is presumed to have taken place if a partner makes a contribution, receives a cash distribution within two years, and one of several exceptions don't apply.

The prior regulations provided one exception for debt-financed distributions. If a partnership



borrowed money to finance a distribution to a partner after the partner contributed property, loan proceeds were considered part of a disguised sale only to the extent that the distribution exceeded the partner's allocable share of the partnership liability.

The IRS believes that some partnerships have used leveraged partnership transactions to take advantage of the debt-financed distribution exception. In these scenarios, contributing partners enter into guarantees or noncommercial payment obligations with the sole purpose of achieving an allocation of the partnership liability — thus avoiding a disguised sale.

RECOURSE AND NONRECOURSE LIABILITIES

For the purposes of disguised sales, the previous regulations had separate rules for a partnership's recourse and nonrecourse liabilities when determining a partner's share of a partnership liability. Keep in mind that a partner bears the "economic risk of loss" (EROL) if the partnership can't pay a recourse liability (one he or she guarantees) and that partners aren't individually liable for nonrecourse debt.

Previous guidance stated that a partner's share of a recourse liability consisted of the portion of the liability for which the partner bears the EROL. The new IRS regulations change the method of allocating partnership liability as it relates specifically to the disguised sale rules. All liabilities are now treated as nonrecourse liabilities (for purposes of

potential disregarded sale transactions), and are allocated according to the partner's share of profits.

Because liabilities are allocated based on a partner's share of profits for disguised sale purposes, a partner can't be allocated all of a loan's liability. As a result, contributing partners can't offset gains from the distribution of loan proceeds with 100% of a loan liability. This severely limits leveraged partnership transactions as a tax planning strategy for partners.

AN EXAMPLE

Consider a hypothetical dealership involving ABC Motors Inc., an S corporation that owns an unencumbered parcel of real estate (on which the dealership operates) that is worth \$2 million. The property is in need of a \$1 million renovation to satisfy its manufacturer's branding requirements.

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ABC Motors will contribute the \$2 million property to XYZ LLC, a multimember limited liability company (LLC) taxed as a partnership that will be jointly owned by ABC Motors and an unrelated third party investor who'll contribute the \$1 million in cash needed for the renovation. The profits, losses and membership units will be owned 50-50.

After the renovations are complete — and within 24 months of the contribution of dealership property — XYZ LLC places a \$1 million mortgage on the property. All of the borrowed funds are then distributed to ABC Motors to equalize the partner equity at \$1 million each.

Because the distribution of cash happens within the 24-month presumption period, and the funds are allocated in a percentage greater than ABC

Motors' share of profits, the distribution is considered sales proceeds for the portion in excess of ABC Motors' 50% profit interest. (\$500,000 is the excess.) In essence, ABC Motors converted its direct ownership of real estate into cash (to an extent greater than its ownership interest in the LLC-partnership). This will result in a taxable sale transaction with \$500,000 of deemed proceeds.

THE TAKEAWAY

Although the regulations are complex, the take-away for dealerships structured as partnerships is relatively simple: More property transactions between partners and the partnership will likely be classified as disguised sales under the new requirements. Consult your CPA about how these new regulations could affect your dealership. ▀

Words matter when selling vehicles

When talking to customers about vehicles they're considering buying, salespeople can boost the chances of making a sale by using certain words to describe vehicles — as well as *not* using other words.

This is one of the findings of research conducted by CDK Global, which provides IT and digital marketing solutions to the automotive industry. The study sought to identify the words and phrases that are most effective in converting automobile shoppers into buyers.

“PASSING” INSTEAD OF “TORQUE”

In short, the less technical lingo salespeople use with customers, the better. One good example cited by the study is the preference of the word “passing” with customers instead of the words “torque” or “horsepower.”

Sure, an automobile engineer or gearhead will know what torque and horsepower mean, and the average person might have a vague idea. But what customers really want to know is whether or not the vehicle has enough power to easily pass another car on a two-lane road. Mazda has it right with “Zoom-Zoom.”

Other high-converting words identified by the research are “climate,” “comfort,” “blindspot” and “quiet.” Conversely, words salespeople should try to avoid include “tire,” “test drive,” “features” and “amazing.”



According to the study, these low-converting words simply aren't very helpful when it comes to enabling most car buyers to understand the benefits a particular vehicle might offer. It's better for salespeople to use clear, descriptive words that are easy for the average customer to comprehend.

INCORPORATE IN YOUR TRAINING

You should keep these research findings in mind as you design training programs and materials for your salespeople — because the words they use (and don't use) could be the difference between making a sale and watching a befuddled customer walk out the door. ▀

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- Gift and estate planning
- Representation before tax authorities



Paul A. Cerrone, CPA, MST, CVA, managing partner, is an ADP Certified CPA with more than 30 years of experience in serving automotive dealers. He specializes in helping clients minimize taxes, maximize profits and achieve their business and personal financial goals. Paul can be reached at 508-845-7600 or pcerrone@cgscpas.com.

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