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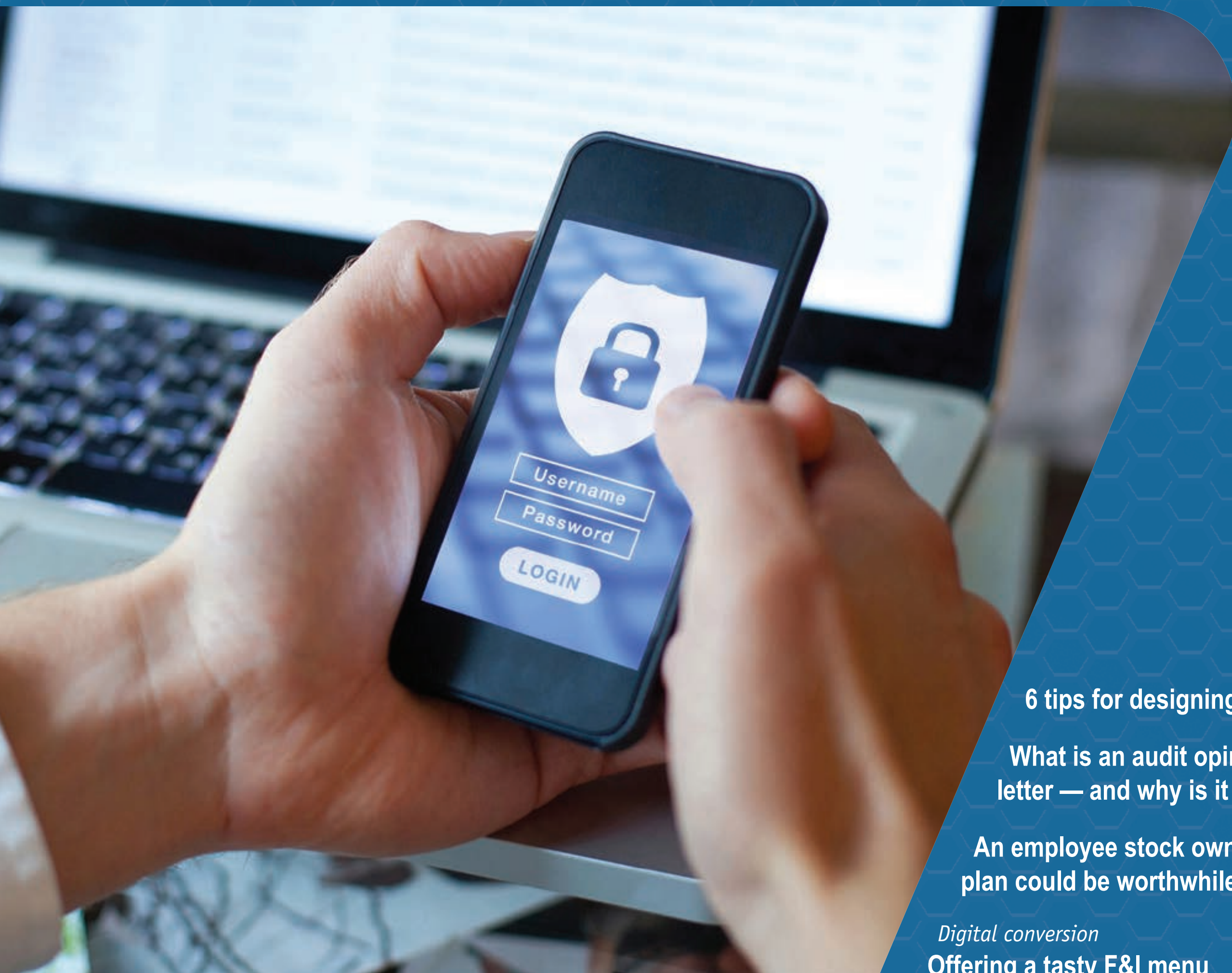

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6 tips for designing a data security plan

Over the past few years, there have been dozens of high-profile cyberattacks on major U.S. corporations. Cyber thieves have stolen sensitive customer and corporate information enabling them to hack into customers' financial accounts and businesses' computer systems to commit fraud and theft.

Your dealership could present an especially attractive target for hackers because of the treasure trove of customer financial data you possess. Thus, it's critical to take steps now to protect your sensitive data from this genuine threat.

WHY DEALERSHIPS ARE VULNERABLE

As dealerships have widely adopted customer relationship management (CRM) systems and dealership management systems (DMS) in recent years, they've become more vulnerable to the hacking of these systems. Hackers can access sensitive information stored in your CRM and DMS in a matter of seconds and use this data to wreak financial havoc on your store and its customers.

Many dealerships also remain susceptible to so-called "spear phishing" email schemes. In these scams, thieves send employees legitimate-looking emails that either contain viruses as attachments or links that download viruses if they're clicked.

At one dealership, a financial employee clicked on a link that she thought was taking her to their bank's website. Once there, she entered login information and bank account numbers which were used by the cyber thief to initiate a $400,000 fraudulent wire transfer.

At another dealership, an F&I manager opened an email attachment that downloaded a virus onto his computer. The virus enabled hackers to track his keystrokes and the websites that he visited. With this information, cyber thieves were then able to log into credit bureau sites and pull up credit reports on hundreds of the dealership's customers, which they used to commit fraud and theft.

HOW TO DESIGN A PROGRAM

Automotive retail is regulated under the Graham-Leach-Bliley Act, which deals with how financial institutions handle their customers' private information, including digital information. More specifically, the act's "Safeguards rule" requires dealerships to

CYBER-LIABILITY INSURANCE CAN MITIGATE COSTS

One way to mitigate some of the costs of a cyberattack is to buy a cyber-liability insurance policy. This type of coverage will pay some of the costs associated with a data breach in which your customers' personal information — including driver's license, credit card and Social Security numbers — is compromised.

Generally, a cyber-liability insurance policy covers legal fees associated with a cyberattack. It could also cover the cost of forensic analysis conducted to discover the cause of a data breach, public relations efforts undertaken to restore your reputation after a cyberattack, and credit monitoring and identity recovery services provided to affected customers.

implement security programs designed to protect this information.

Here are some guidelines for designing and implementing a data security program that can help you comply with the Safeguards rule:

1. Appoint a chief compliance officer. A dealership's chief operating officer or fixed operations director often assumes this role. It's critical that a high-level dealership employee take ownership of your business's data security program. That employee's leadership will encourage everyone else to buy into the program.

2. Perform a risk assessment. The goal here is to determine specific areas where your dealership is vulnerable to a cyberattack. Start by identifying everywhere data is stored, including on computer hard drives (both desktops and laptops), mobile devices and removable media (for example, thumb drives), as well as within your CRM system and DMS. Collect data from every department, including sales, service, F&I and human resources.

3. Establish basic security policies. These typically include things such as requiring verbal verification for all wire transfers and restricting employees' ability to transport electronic devices containing sensitive customer or corporate information. Also, store copies of customers' driver's licenses in a secure area and shred them once they're no longer needed.

4. Update security software patches. This is an easy but often overlooked data security step. More than 90% of dealerships don't have a system in place to keep their security patches regularly updated, according to a WardsAuto.com article. Your chief compliance officer should ensure that software updates are completed on all store systems and computers whenever they're due.

5. Train employees in basic data security measures. Doing so includes educating employees about spear phishing email schemes. Many of these fake emails are highly sophisticated and look legitimate, so don't assume employees will know how to spot them. Focus your training especially on employees who work in the accounting and F&I departments.

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6. Integrate third-party computer systems cautiously. Before allowing third parties to integrate with your dealership's systems and software, review their data security controls and procedures. Also obtain copies of their security certifications.

MAKE IT A TOP PRIORITY

The costs of a cyberattack can be crippling — financially, and in terms of lost customer confidence and damaged reputation. Make cybersecurity a top priority for your dealership if it isn't already.

What is an audit opinion letter — and why is it important?

You may want to have a financial audit performed at your dealership for a variety of reasons. With many owners today nearing retirement age, one of the most common reasons is to provide assurance to potential buyers that the dealership's finances are in good shape.

PAGE ONE

Financial audits are performed by CPAs and public accounting firms that conduct an exhaustive confirmation and inquiry of a business's financial statements. Based on this documentation, the CPA will prepare an extensive audit report that details the findings and whether the financial statements are prepared in accordance with Generally Accepted Accounting Principles (GAAP).

Before you get to the "meat and potatoes" of the audit report, however, you'll want to pay close attention to the audit opinion letter. This usually constitutes the first page of the report. In the letter, auditors state their opinion on the quality of the financial statements and whether you're complying with accounting principles.

An audit opinion letter is usually three paragraphs long. The first paragraph lists the name of the business in question, the responsibilities of the auditor and the accounting period being analyzed. The second paragraph details the scope of work performed by the auditor. And the third paragraph gives the official audit opinion, based on the auditor's review.

POSSIBLE OPINIONS

The auditor may issue one of four different opinions about your dealership's financial statements:

An unqualified opinion. Also known as a clean opinion, this is the most desirable result of a financial audit. This opinion essentially gives your dealership a clean bill of financial health.

By issuing an unqualified opinion, the auditor is stating that he or she found no material misstatements or violations in your financial statements. Also, an unqualified opinion usually states that the financial statements have been prepared in accordance with GAAP.

A qualified opinion. This opinion is issued if the auditor concludes that your financial statements contain minor deviations from GAAP. As a result, the auditor can't give your dealership a totally clean bill of health.

An auditor may also issue a qualified opinion if there's a limitation in the audit's scope — or, in other words, if he or she can't audit one or more areas related to your financial statements. The qualification will relate only to the financial areas the auditor couldn't audit.

An adverse opinion. This is the most unfavorable opinion your dealership can receive. An adverse opinion means that the auditor discovered significant material misstatements that affect your financial statements overall.

The auditor is essentially declaring that your financial statements aren't prepared in accordance with GAAP, and your dealership's financial information should be considered inaccurate and unreliable. An adverse opinion could be a red flag that there's fraud at your dealership. The opinion letter may contain an additional paragraph that details the problems discovered.

A disclaimer. An auditor will issue a disclaimer if he or she is unable to complete the audit report or unwilling to form an opinion about your dealership's financial statements. This could happen due to missing financial records, a lack of management cooperation, significant audit scope limitations or material doubts about your ability to continue operating as a going concern.

A disclaimer also may be issued if the auditors determine that they lack enough independence to provide an unbiased third-party opinion of your finances. For example, this could take place if the auditor is providing management advisory services along with the audit. The audit opinion letter may contain an additional paragraph explaining why the auditor is unable or unwilling to opine on your dealership's finances.

Note: The audit opinion letter shouldn't be considered an endorsement or evaluation of your dealership's financial *results*. It's simply a statement of the auditor's professional opinion regarding the quality of your financial statements and whether they were prepared in accordance with GAAP.

UNDERSTANDING YOUR AUDIT

It's important to understand these audit opinions and what they reveal about your dealership's financial statements. Be sure to contact your accounting professional if you have further questions about financial statement audits and the audit opinion letter that accompanies them.

An employee stock ownership plan could be worthwhile

Are you looking for a smart way to exit your business while benefiting the managers and employees you leave behind? If so, you might consider an employee stock ownership plan (ESOP). This type of plan can be a tax-efficient technique for sharing equity with employees as well as a powerful retirement and estate planning tool.

START WITH THE BASICS

An ESOP is a qualified retirement plan, similar to a 401(k) plan. But instead of investing in a selection of stocks, bonds and mutual funds, an ESOP invests primarily in the company's own stock.

ESOPs are subject to the same rules and restrictions as qualified plans, including contribution limits, minimum coverage requirements and nondiscrimination testing.

BUILD IN FLEXIBILITY

An ESOP can be an appealing alternative to selling on the open market. It offers flexibility in structuring the payout to meet your income needs after you sell. For example, you can receive a steady stream of funds to support your living expenses if you plan to retire after selling. Or you can structure income payouts to invest in another business if you're not yet ready to hang up your hat.

ESOPs also can have a positive effect on employee morale, productivity and loyalty. Many employee-owners work harder, smarter and more efficiently than nonowner employees because they've a stake in the business's success. This can lead to faster growth, higher profitability and lower employee turnover rates — all of which may result in a higher selling price for your dealership.

You could also realize significant tax benefits by making an ESOP the centerpiece of your dealership succession plan. You'll make tax-deductible contributions of cash or ownership shares to a trust that's established when you set up the ESOP. Cash is used to buy ownership shares on behalf of employees, who don't have to pay income tax until they later take distributions from the ESOP.

Also, dealership profits contributed to an ESOP are taxed at the preferable long-term capital gains rate of 20%. If these profits are distributed to the business owner, taxes are assessed at ordinary-income tax rates that are as high as 37%.

An ESOP can be a good succession plan for the dealer who has no children or relatives interested in taking over the dealership's operations. It also can be attractive to a large dealership group that might be difficult to sell without splitting up the stores. An ESOP can help transition dealer ownership to a large group of owners and employees.

CHOOSE YOUR ESOP TYPE

There are two different types of ESOPs: unleveraged and leveraged. With an unleveraged plan, the dealership will contribute cash or shares to a tax-exempt trust, as described above. With a leveraged ESOP, the dealership will borrow money to buy the stock and then contribute cash to the plan. The cash is used to repay the loan.

An ESOP can be a good succession plan for the dealer who has no children or relatives interested in taking over the dealership's operations.

Ownership shares in the ESOP trust are allocated to accounts set up for all participating employees, usually in proportion to their compensation. When the owner is ready to exit, the dealership can make tax-deductible contributions to the ESOP to buy out his or her shares. Or the ESOP can borrow money to buy the shares.

CONSIDER FUTURE COSTS

The dealership must formally adopt the ESOP and perform other administrative duties, including submitting plan documents to the IRS. Annual business valuations also may be required to determine the current stock price.

Thus, you should carefully consider the potential costs — in both time and money — of setting up and maintaining an ESOP. For instance, private companies must repurchase the shares of any departing employees, which can be a major expense. Also, if the ESOP is ever terminated for any reason, there can be significant costs and tax penalties.

NOT FOR EVERYONE

An ESOP isn't the right business strategy for every dealership. Discuss the pros and cons in depth with your CPA.

Digital conversion

Offering a tasty F&I menu

The F&I department remains a source of untapped profit potential for many dealerships, which is especially important when margins on new vehicle sales are tight. One way to boost F&I sales and profits is to switch from a paper to a digital F&I menu.

This new type of electronic F&I menu can be presented to customers via a tablet, such as an iPad, or via a display built into the F&I manager's desktop. Using a digital menu could make sense, given the greater comfort level many customers have with accessing information on their smartphones and laptops.

STREAMLINING SALES AND BOOSTING TRUST

Some digital F&I menus use prescriptive selling by having customers answer questions on the device and then tailoring product offerings to their answers. This can help streamline the F&I sales process while also building trust in your dealership.

Digital F&I menus use multimedia to reinforce your sales message.

There are other potential benefits to switching from a paper to a digital F&I menu. For example, many customers will view your dealership as more technologically advanced than competitor dealerships still using an old-fashioned paper menu. Other pluses may include:

- A more consistent presentation of F&I products to all customers,
- The ability to customize the menu for different customers,
- Automatic "on the fly" adjustment of payment amounts based on changes in menu options,

- The use of multimedia to reinforce your sales message, and
- Greater transparency, which may lead to higher customer satisfaction levels and CSI ratings.

In addition, using a digital F&I menu allows for electronic capture of customer signatures and retention of all forms in an electronic deal jacket.

Of course, implementing this technology will come with purchase, implementation, training and maintenance costs. The software for implementation on tablets costs about $500 while digital menu displays built into desktops can cost from $10,000 to $12,000 per desktop. Most vendors offer basic training on how to use the menu at no extra charge. Consultants offer more advanced training for a fee.

MORE INTUITIVE AND ENGAGING

A digital F&I menu can offer a more intuitive, interactive and engaging experience for your customers. Talk to your F&I manager about whether switching from a paper to a digital menu would make sense for your store.

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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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