

Death of an Automobile Dealership

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Closing a store requires considerable effort and attention and the items listed below, in no particular order, are minimal considerations when terminating a franchise and closing a dealership operation.

THIS CHECKLIST IS NOT "ALL INCLUSIVE". YOU SHOULD CONSULT WITH YOUR ATTORNEY AND ACCOUNTANT AND THIS LIST SHOULD BE CONSIDERED AS AN ADDITIONAL AID FOR YOU TO USE TO BUILD UPON WHEN YOU CONFER WITH THEM.

Basic Preparation

1. Officers, Directors and Shareholders

Be certain to hold both directors and shareholders meetings and to obtain resolutions from each entity, authorizing the dealer to liquidate the dealership, or a substantial portion of the dealership's assets.

Determine whether or not the board and shareholders may authorize you a termination bonus and prepay your for your services in "winding down the business". Consult with your accountant and attorney to determine what would be a reasonable amount of compensation in the event a company creditor challenges the transaction.

Determine if it is reasonable for officers to buy themselves and their spouse vehicles. Pay "Net" "Net", as that would be the sales price if the vehicle were returned to the factory or sold to a purchaser of the business.

The officers should open a new bank account, at a different bank, and: (a) use a PO Box, or Private Mail Service as a mailing address; and (b) use a different check color in order to easily determine pre and post closing checks written.

Authorize payment to and pre-pay the company's attorney and accountant with a retainer. Their services will be needed to properly close the business and the company might not be able to pay them later.

Authorize pre-payment of whatever services or supplies the company will need to be serviced during the wind-down period. For example, property and personal insurance, real property taxes (if the property is not owned by a third party), rent, utilities and such.

2. The Facility and Insurance

A one-sheet summary of the lease should be attached to the original, in order to facilitate matters. The summary should include such items as: the dates of the base term; the base rent; the current rent; the dates of any option periods, together with notations regarding rent increases; the facility ownership; the lessee and lessor; a notation as to whether or not the factory has point, or site protection; the rent as an equivalent to the dollar value per new unit sold; and, a notation as to WHETHER OR NOT THE LEASE IS ASSIGNABLE and under what conditions.

Other considerations regarding the facility lease include violations of the ADA, hazardous materials (underground gas tanks, or underground oil disposal tanks) being located on the property.

Owned Facilities

With respect to receiving "factory termination assistance", some Sales and Service Agreements, General Motors for example, make a distinction between "owner occupied" and "leased" dealership facilities. Be sure to read your Sales and Service Agreement in order to understand and be able to capitalize on the distinctions.

Leased Facilities

If the selling dealer's rent factor prior to the sale of the dealership is within factory guidelines the factory should make the dealer's lease payments for the period specified in the Service and Sales Agreement. (See, however, the EPA section.)

Check with your insurance agent to determine the requirements for insuring an empty building.

Other Insurance

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In addition to facility insurance the dealer will need a "tail" or rider on his or her garage keepers insurance. Most insurance today is "claims made" versus "occurrence".

In actual practice, most cases that are settled are settled within the insurance policy limits and the insurance company will have paid for both the defense and the settlement.

With respect to Medical Insurance, arrange for COBRA all employees of the company. Again, officers and directors may be able to include medical insurance payments as part of their wind-down compensation.

3. UCC, Mechanic's Lien and Title Searches

Most dealers are not cognizant of all existing liens on dealership's assets.

In order to accurately estimate the selling dealer's anticipated net proceeds, all of these liens will have to be discovered, preferably, prior to negotiations.

Possession of title reports and UCC-1 reports will give the dealer adequate time to address the issues and to have readily available answers, if and when a prospective purchaser raises the issue.

4. Taxes Due and Anticipated

The dealership's comptroller or accountant, should prepare a sheet of all taxes currently owed by the dealership and all anticipated taxes. The list should identify the amount, to who owed and the reason. In certain states unpaid taxes have a "superlien" status and if unpaid the selling dealer's assets can and will be attached to recover unpaid taxes due by the selling dealership. This attachment can occur months after the dealership has closed.

As a general rule, anyone authorized to sign on the checking account can be held personally liable for at least ½ of the payroll withholding tax, as well as 100% of all of the sales taxes due. In addition, in some instances dealers have been held personally liable for monies collected from customers that should have been treated as "trust" monies, such as:

customer trade payoffs, customer credit and life insurance premiums, and customer warranty and service contract premiums.

5. Notes and Accounts Receivable From Others

The "Notes and Accounts Receivable - Other" account is usually a "catch-all" account on the dealership statement. For purposes of a dealership sale, this account should be purified (1) in order to apprise the dealer of any extra funds, which may be available for final sales and property taxes and (2) to make both the dealer and accountant aware of any "in-house" loans to officers, directors and employees, which may have to be repaid.

6. Prepaid Expenses

The prepaid expense account is another "catch-all" account that must be purified. When scheduling the prepaid expense account the comptroller should make a thorough search for all lease and contract deposits. In many instances, service equipment on lease, vehicles on lease, computers on lease, and other leases made to the dealership carry security deposits, or the last month's payment, or both.

7. Dealership Employees

Along with the normal employer-employee relations, there are two very important legal areas that may affect automobile dealers: (a) pension fund liability; and (b) state and federal laws regarding closings.

In some states the selling dealer could be personally liable for funding employee pension funds; while in others the dealer must give employees advance notice of any closing. Also, the United States Congress passed legislation regarding "closings". In the instances of "closings", both state and federal laws put a minimum on the number of persons employed, usually 50 or 100, before the law applies to the dealer's company. Check the Hart Scott Rodino Act (HSR) and the WARN Act.

With respect to wages, some jurisdictions have enacted statutes making certain shareholders personally liable for corporate debts owing to laborers and other employees. Welfare and pension funds also qualify as wages under New York's statute.

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The comptroller, or accountant should prepare a list of these liabilities, to include any amounts due the employees, with respect to accrued vacations, withholding taxes, pension and profit sharing plans and wages, as of the date of close.

Insofar as the actual terminations are concerned, if the dealership is "union", the dealer should talk to the union's representative in order to be sure that all of the conditions of the union contract are met.

8. Long Term Debt

All long-term debt should be itemized and a method of repayment determined. Interest should be computed. When past due interest and past due payments are added to the loan balance, the loan pay-offs are generally higher than anticipated.

The comptroller should prepare a list of these debts, to include the amount owed including interest, to who owed, purpose of debt, maturity, terms and security given. In addition, after the list is completed, the comptroller should keep a running total, daily, through close of escrow.

9. Other Notes Payable

As with long-term debt, other notes payable should be listed by amount including interest to date of close, to whom owed, purpose of note, maturity, terms and security given; and arrangements should be made to retire the debt.

10. The Financial Statements

The retail automobile business is one of the few businesses requiring a complete closing of all books and records, promptly, at the end of each and every month. Factories and finance companies require reporting on factory originated, or approved forms.

In preparing the store for closing, a reconciliation statement may be used, explaining categories such as "other income & expense", warranty, finance and insurance income not shown on the statement, along with extraordinary items.

You will need a final financial statement for tax purposes.

11. Storage of Records

Dealerships amass a great deal of paperwork, the safe, accessible, storage of which will present a necessary problem to the selling dealer. No dealership record will be as important as it is on the day it cannot be found. Former dealers have related stories of attempting to retrieve documents from mini-storage facilities, in both rain and snow.

The appropriate time period should be determined, only after the dealer's accountant and attorney have considered and advised the dealer with respect to statute of limitations problems and other document retention regulations, peculiar to the political area in which dealership is located.

12. In-House Service Contracts

If the dealer has sold any "in-house service contracts", the selling dealer will not want former customers calling at his or her home for repairs, or complaints; therefore, a system of service, along the following lines, should be negotiated with a dealer located in close proximity to the closing store.

13. The Hard Assets

Parts and Accessories

Each factory has its own definition of "returnable" parts and returnable accessories. Most also include a discount for packing and shipping.

Just prior to closing, a computer printout ought to be obtained listing all parts and accessories, their purchase date and cost in invoice.

Parts and Accessories need to be segregated into "returnable" and "non-returnable" categories. Returnable parts and accessories need to be inventoried and packaged according to the factory's specifications

Non-returnable items need to be marketed to other dealers or parts houses such as "Napa". Note: Some "non-returnable" parts may in fact be returnable to the supplier from who it was purchased, such as Delco, MotorCraft, Mopar, Napa, etc.

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Do not mark on or damage original packages when inventorying or packing as some factories will not classify items in marked packages as "returnable".

Be sure to account for aftermarket items such as Gas, Oil & Grease, Nuts, Bolts, Supplies, Work in Process and Repair Order (Need to collect A/Rs), Signs, Tools, Miscellaneous Equipment & Supplies.

Furniture, Fixtures and Equipment

The hard assets fall into two categories: (a) Those repurchased by the factory, such as special tools, parts equipment, signs, some computer systems, etc.; and those not repurchased by the factory, such as desks, chairs, etc.

Repurchased and non-repurchased items should be segregated and an inventory / auction service contacted to bid the auction on the non-repurchased items. When considering the auction, terms such as advertising time, location, minimum bids, guaranteed minimums from the auctioneer, and so forth, must be considered.

Leasehold Improvements

The value of Leasehold Improvements is generally lost in the termination process.

Vehicles

While accomplishing a new vehicle inventory valuation is a relatively, routine matter, it is also time consuming; consequently, in order for a dealer to realize full value, or each vehicle, at time of transfer, a checklist must be compiled and maintained. There are certain additions to, and subtractions from, the invoice price that must be made.

The difference in cash to be paid by purchaser's flooring entity to the dealer's flooring institution can be considerable, especially with respect to domestic lines, where holdback monies routinely average between \$400 and \$600 per unit, or more.

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A dealer needs to be aware of this figure, early on in order to provide for the contingency during negotiations.

Various states have laws more liberal than the factory's Sales and Service Agreements and the specific laws of the terminating dealer's jurisdiction should be review. For example, Maine requires that the factory repurchase terminating dealers' entire new vehicle inventory, regardless of model year. Some states require the factory repurchase only current model year vehicles and others current plus one year carry-over.

In MSO states, the dealer should control all vehicle keys and MSOs - if the lender does not already have them.

Prepare to liquidate used vehicles and any dealership vehicles such as parts trucks, courtesy vans, demonstrators and snow plows. It is generally easier to obtain a good price for them by not letting anyone "cherry pick". Several wholesales should bid them as a "group".

Make list of carryovers and if the factory will not repurchase them have the wholesalers bid them separately and also shop them with other dealers.

Dealer plates must be surrendered and accounted for when the dealer license is terminated.

13. Appraisals and Auctions

There are a number of competent, recognized appraisers, our firm could recommend. In order to maximize the dollar value of an appraisal or auction, the dealer should contact several firms, determine how they operate, what records will be required, the method for valuing. After obtaining such information, the dealer should know the precise form and schedules necessary in order to maximize the appraisal or sale of the fixed assets. In addition, by assigning an employee to thoroughly prepare the assets and schedules, the dealer will better understand the value of the assets at the premises.

Perhaps the greatest problems, with respect to appraisals and auctions, are:

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- (1) neither party takes the time to understand the methods and reasoning used by the appraisal/auction company; and
- (2) the dealer almost never adequately prepares the assets and schedules. We invariably find that all of the dealership's assets do not appear on schedules, either because they have been fully depreciated, or because of an error.

14. Contracts for Services

Service maintenance contracts and personal service contracts should be reviewed for personal guarantees, term and assignability. An oversight could mean that personal liability, for performance, would remain with the selling dealer. Service maintenance contracts should be scheduled, with the detail indicating the amount of each payment, duration of agreement, service to be rendered, and any personal liability. Any contracts that can be cancelled should be calendared for cancellation.

15. Contingent Liability and Reserves

The dealer should know the amount of all outstanding retail paper, which has been unconditionally guaranteed by the dealership, or the dealer. The dealer should know which the dealership's reserve account will be subject to charge backs, for early payoffs and the amount, if any, of recourse against the dealer and the dealership.

A spreadsheet of the outstanding contracts should be compiled, detailing, in addition to collateral description, remaining term and delinquency status, and credit grade, such as A, B, or C, or whatever system the finance company uses. The type of recourse, average monthly reserve charge-backs and the current reserve balance should also be included.

Shortly after informing the financing institutions of the dealer's intent to close the dealership, the lenders should again be approached, regarding the availability of any "walk-away" programs. Furthermore, in the event the dealership has been operating with reduced reserve retention, the amount required to bring the reserve(s) to standard, upon cessation of retail operations, should be determined. On occasion, this amount has proved to be significant.

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Eventually, when confidentiality is no longer an issue, the dealer should discuss with the lender, the handling of future repossessions, extensions, renewals and other maintenance functions. If the prior dealer-lender relationship was good, the dealer will discover that an incredible amount of help available from a cooperative finance company.

Lastly, if the dealer discovers a large contingency, a certain degree of assistance may be negotiated with the buyer.

16. Accounts Receivable and Cash

Cash

While apparently obvious, dealership cash must be considered. Generally a new checking account should be opened at a financial institution that is not affiliated with the dealer's current business. Also, if possible, a locally owned bank should be used, versus a national bank. The dealer should consider reducing the number of signatories on the checking account(s) to two, one of which is the dealer and, effective the day of the close, the number of signatories should be reduced to the dealer principal only.

Factory Receivables

From the moment a decision to close the store is reached, factory receivables should receive concentrated attention. The very instant an awareness of the pending closing reaches the factory, the payments cease.

Try to resolve all problem receivables, such as warranty disputes, well before the closing. In any event, assistance from the factory, following the close of escrow will be essential to process warranty re-submissions and other problems. **Employee Receivables**

Employee receivables should also be thoroughly analyzed during this preliminary stage. An immediate policy, of no advances, should be established.

Without causing alarm, employee receivables should be scheduled and a course of repayment established. One of the better methods is to prepare a schedule of what each employee owes and, as the final pay periods approach, make certain the receivables are deducted from the employee's

final checks. Unfortunately, some states do not allow the dealer to set-off debts against wages. Your state's policy/law should be reviewed with your attorney before proceeding to set-off any employee debt.

Customer and Vehicle Receivables

The selling dealer should make certain that vehicle receivables and customer accounts, other than service and parts, are pure. Necessary adjustments and write-offs should be made, with the purpose of arriving at a receivable figure which realistically depicts the amount of cash which can be expected.

If the dealership's service and parts policy has been well monitored, these accounts should pay in an orderly manner. In addition, the dealer should decide whether collections should be performed by dealer, and one or more employees, or whether the dealer can sell the accounts to a factoring house.

17. Leased Equipment

Not all leases can be cancelled. The dealer should determine which, if any, of the leases have personal guarantees, and with respect to such leases, make a concerted effort to negotiate a settlement with the lessor. That assumes that the corporation is insolvent. If the corporation is solvent, than settlements need to be negotiated with respect to corporate leases.

18. EPA Inspection

If the real property is owned by the closing dealer, it is important for the dealer to determine where and what the problems are likely to be. If underground gas or oil storage tanks have ever been located on the dealership real property, the dealer should, if not already available, contact a private inspection agency and obtain a certificate of clearance, or compliance, with respect to it.

Be aware, no agreements between the parties can modify, or redistribute their respective liabilities, with respect to state and federal laws.

19. Expenses of Transaction

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There are certain extraordinary expenses, such as real estate appraisal fees, consultant fees, attorney and accounting fees, which are incidental to the preparing a dealership for closing. These expenses will be paid both from the dealership general account and directly from the closing dealer's personal account. The dealer should alert the bookkeeper to maintain a separate journal, in which to record these expenses, in order that the accountants may readily determine the costs of sale and categories of expenditures, for income tax purposes, both personal and business.

Closing Date

Absent exigent circumstances, the dealer should estimate the amount of time necessary to prepare the store for closing, usually approximately thirty days. If possible, the closing should be on a payday.

The Comptroller's Responsibilities

The Dealer's comptroller should prepare, or be responsible for the preparation of, the following items and documents, for transfer:

- The Books & Records;
- All Purchase Orders and Deposits;
- The Franchise Termination Letter and the Factory's, or Distributor's Acceptance of the Buyer's Resignation;
- The Accounts Receivable List;
- Prepaid Expenses;
- Preparing a Leased Equipment Inventory;
- Securing Old Credit card plates and Machines;
- The Parts and Accessories Return, Vehicle Return, and Rent Assistance Demand Letters;
- The Transfer and/or cancellation of various: Telephone Numbers; Post Office Boxes;
- The insurance arrangements: life, garage keeper's tail, real and personal property, health, etc.

The Dealer's Responsibilities

The Dealer should prepare, or be responsible for reviewing and supervising all of the items in the checklist and for the preparation of the following items:

- Decide on the employees that are required to stay in order to complete the closing of the store.
- Check for sold orders decide whether to deliver, cancel, or refer to another dealer.
- Cancel company credit cards, including any phone credit cards and any mobile phones - except your own.
- Secure telephone service. Set a Voice Mail message regarding a dealership referral.

DETERMINE THE FACTORY'S OBLIGATIONS WITH RESPECT TO ITS RIGHTS TO LEASE AND PURCHASE. BE SURE TO MAKE CLAIMS AND REQUESTS FOR ASSISTANCE WITHIN THE TIME PERIOD SPECIFIED IN THE SALES AND SERVICE AGREEMENT.

If necessary, talk to a Realtor and list the facility on the market (lease or sale).

- Find out where credit card monies are deposited and move the account if it is in the same bank where the company's general account resides.
- Close out, or transfer to another dealer all active service ROs. If possible, negotiate a referral fee.
- Create a press release for store closing.
- Cancel all new vehicle orders that are not scheduled, do not order any new cars.

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- Close out all service ROs so that work is completed by date of close. Do not accept any work that can't be completed by store shutdown date.
- As always, when closing a dealership, you should always consult with a qualified attorney and accountant.

Starting in 1972, Pico entered the automobile business by representing dealership groups such as Tasha Corporation (once the 17th largest dealer group in the country before it sold to AutoNation), and handling sales such as Lucy DiGulio's sale of her deceased husband's share of Prospect Motors (currently the largest General Motors dealership in the nation) to Skip Halverson.

Before retiring from the active practice of law in 1980 Mr. Pico and his law firm represented numerous automotive dealers in the reorganizations, purchases, and sales of dealerships. He both tried cases as the attorney for the dealerships and arbitrated and mediated dealer related cases.

Mr. Pico built upon his experiences and became a student of the industry by receiving training and attending seminars with respect to the various departments in new car dealerships, participating in National Automobile Dealer Association (NADA) Management Education Program, having "hands-on" experience operating a store by filling in as General Manager on an "interim" bases. In 1986, after five years of research and two years of writing, Mr. Pico authored and National Legal Publishing Company published the nation's first book on Buying and Selling Automobile Dealerships.

Mr. Pico is recognized as an expert in the field of buying, selling and investing in automobile dealerships. In addition, both State and Federal Courts have also recognized Mr. Pico's expertise and in various legal proceedings he has been:

- Approved by the U.S. Bankruptcy Court, 10th Circuit, District of Colorado, pursuant to Rule 202 of the Bankruptcy Code, as "Consultant to Debtor" in sale of a new car automobile dealership;

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- Approved by the U.S. Bankruptcy Court, 9th Circuit, Northern District of California, pursuant to Rule 202 of the Bankruptcy Code, as "Consultant to Debtor" in sale of a new car automobile dealership;
- Approved by the U.S. District Court, 8th Circuit, Wisconsin, as Arbitrator/ Appraiser in new car Dealership litigation;
- Approved by the District Court of Colorado as expert in dealership valuation litigation;
- Approved by the Superior Court of California as:(a) "Consultant to Court Appointed Receiver" in check-kiting case,(b) "Expert Witness", with respect to dealership valuations, and(c) Superior Court Mediator in dealership/lender litigation.

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