THE CPA TUNEUP®

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ABOUT US

Henry & Horne, LLP is one of the leading accounting firms in Arizona with offices in Tempe, Scottsdale and Casa Grande. We combine the knowledge and expertise of a premier consulting firm with the personal attention of a local CPA, meaning unmatched service to you. Our services include: daily, monthly and annual bookkeeping and accounting; audit, review and compilation of company financial statements; audits of 401(k) plans; tax planning and compliance; CPA Tuneup®; cost segregation studies; internal control reviews; estate, gift & trust services; real estate appraisal and consulting; and valuation and litigation support services.

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Revenue Recognition for Dealerships

By Brian Campbell, CPA

Dealerships that prepare financial statements in accordance with accounting principles generally accepted in the United States of America ("GAAP") are going to feel the major impact of a new Accounting Standards Update that will affect how you recognize revenue in your dealership. In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers. The ASU introduces a five step approach to recognize and measure revenue from contracts with customers: 1. Identify customer contracts, 2. Identify performance obligations, 3. Calculate the transaction price, 4. Allocate the transaction price, 5. Recognize revenue.

The areas of a dealership that may be affected are free maintenance agreement contracts, extended warranty contracts, manufacturer incentives/holdbacks, financing agreements and vehicle trade-ins. Here are some examples:

Free maintenance agreement contracts are sometimes provided to customers as an incentive to sell a vehicle. The revenue guidance will delay the timing in which a dealership recognizes revenue from the contract, as this may be considered a separate performance obligation. Generally, the revenue will be recorded as deferred revenue and recognized over the life of the agreement.

Extended warranty contracts that are owned and sold by a dealership may need to be considered as a separate performance obligation similar to the free maintenance agreement contracts discussed above. When a vehicle is sold with an extended warranty, the two performance obligations are the vehicle and the extended warranty. The sale of the vehicle will result in revenue being recognized at a point in time, and the sale of the extended warranty will result in revenue being recognized over the coverage period of the extended warranty.

Rebates and incentives received from manufacturers are deemed variable consideration under the new revenue recognition guidance. Variable consideration requires an entity to estimate and include an amount of variable consideration in the transaction price only in an amount that the entity will likely not have to reverse once the uncertainty is resolved. An entity does not wait for the uncertainty to be resolved before including the variable consideration in the transaction price.

With the new revenue recognition guidance, noncash consideration (trade-in) must be included in the transaction price at its fair value. The appraised value of the trade-in is usually not equal to its fair value. The dealership is trying to make a profit on the sale of cars and as such, will typically reduce the trade-in value of a car to increase profits on the sale of a new or used vehicle. Appraised value does not always equal fair value and fair value is the value of the trade-in that must be used to determine the transaction price.

An automotive entity may guarantee a minimum resale value on a vehicle. Historically, an entity accounted for such an agreement as a lease. Under the revenue guidance, an entity may have to account for such an agreement as a right of return, a lease, or a financing, depending on the facts and circumstances.

For a public entity, the guidance is effective for annual reporting periods beginning after December 15, 2016, and any interim periods that fall within that reporting period. Early application is not permitted. For a nonpublic entity, the guidance is effective for annual reporting periods beginning after December 15, 2017, and any interim and annual periods after that date. A nonpublic entity is allowed to adopt the guidance early, but not before the implementation date for public entities.

These are just a few areas where a dealership will be impacted by the new revenue recognition guidance. There are a few years before it will become effective but you need to start now in determining how processes and controls within your dealership need to change to comply. Do not hesitate to contact one of our dealership professionals if you have questions or need assistance regarding the new revenue recognition guidance.

If you have any questions, Brian can be reached at (480) 839-4900 or BrianC@hhcpa.com.



Reviewing the Trial Balance

By Kane Lavin, CPA

Over the past several years during my audits, reviews and CPA Tuneups® I have noticed a lot of controllers and office mangers ignore a very important report at month-end and year-end. I was surprised to learn very few do not run a trial balance and review it before closing out the month or year.

I discovered they are more concerned with reviewing the operating report, detail schedules, and detail of certain income and expense accounts. While these are important, the trial balance should be reviewed as well. The trial balance basically lists each account in the chart of accounts with a beginning balance, net activity for the month and an ending balance.

While the operating report is the focus at month-end, it can be misleading depending how accounts are grouped into certain line items on the operating report. Each line of the operating report is made up of one or more general ledger accounts. Because several accounts may be posted to one specific line item, certain accounts with miscellaneous and incorrect balances may not be discovered by reviewing the operating report alone. The operating report can be misleading if you have a liability account that should be grouped with an inventory account sitting in the liability section of the operating report. This happens a lot with new and used inventory accounts and corresponding pack accounts that are sitting in liabilities. It is important to group these accounts to the same line item on the operating report.

I had a client who had gone through a computer conversion in the middle of the year and their Dealer Management System provider created a few accounts they were unaware of. They had parked certain balances in a miscellaneous account. Another client neglected to clear out a remaining note payable balance when its last two payments of a capital lease were rolled into a new lease. On another occasion, the client forgot to post their EFT payment of sales tax. This left their cash and liabilities grossly overstated. This caused a few adjustments at year-end they were not expecting.

While most Dealer Management Systems have one report called "trial balance", some systems break up the trial balance into two reports. For instance, ADP's trial balance is made up of two reports, one is named "balance sheet" and the other is named "income statement".

While reviewing the trial balance, it is important to understand the different accounts and what should be in those accounts. Balance sheet accounts generally stay fairly consistent from month to month; however, they can increase or decrease significantly once in a while. When they do change, it is important that you are comfortable as to why they changed. If you are not sure why the account changed, it should be investigated. The sales tax account mentioned earlier is a good example of an account changing significantly from one month to the next. Income and expense accounts are easier to review with a trend analysis report, but a trial balance can be used if the trend analysis report is not available.

By adding this procedure to your month-end close, you should avoid any surprises.

If you have any questions regarding the trial balance or how to review it, please do not hesitate to reach out to one of Henry & Horne, LLP's dealership professionals.

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extra parts

According to the New York Daily News, 2015 technology trends for new cars and trucks will include laser headlights, lane change assist technology, apps to find empty parking spaces and help you remember where you parked, and Wi-Fi hotspots.

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Crowdfunding carmaker Local Motors is currently building a 3-D printed electric car. It's full-size, completely drivable and made up of just 40 parts. The 3-D printer makes the majority of the parts, though the electric powertrain, suspension, wiring and battery are from outside sources.

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Sales of small crossover SUVs are booming in the U.S. According to AutoData Corp., sales were up almost 14 percent so far this year, compared to 9 percent for the overall market.

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