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3 ways to boost fixed operations' profits

Some dealership owners assume that most of their store's profits come from the sale of new and used vehicles. But data shows that this isn't the case for the average dealership.

According to the National Automobile Dealers Association (NADA), new vehicle sales generate 26% of a dealership's gross profit and used vehicle sales generate 25% of gross profit. Parts and service generate 49% of gross profit! In other words, parts and service (commonly referred to as "fixed operations") generally account for about the same percentage of a dealership's gross profit as new and used vehicle sales combined.

Boosting the bottom line

Given the importance of parts and service to your dealership's financial performance, it's smart to look for ways to boost their profitability. Dealerships sometimes try to achieve this by increasing repair order volume, labor hours, or lines-per-repair-order. These steps are a good start, but there are other ways to boost your fixed operations' bottom line.

Here are three tips for increasing profits in your fixed operations:

1. Eliminate shop supply abuses. For example, technicians sometimes order unnecessary parts because they aren't sure which exact parts are needed for repairs — this is sometimes referred to as "firing the parts cannon." Or technicians take supplies home to do their own repairs and fail to return them.

Shop supply abuses such as these can result in thousands of wasted dollars, which drag down fixed operations profits. Here's a remedy: Create reports that include:

- The dollar amount of all supplies charged,
- The technician who ordered the supplies,
- The document number of each order, and
- The vehicle repairs the supplies were eventually used on.

These reports are critical to keeping track of parts and supply orders. They call for some administrative work, but they're well worth it in the long run.

2. Be sure customers sign all repair authorization forms. Most dealerships say they require customer signatures before repair work begins, but not all service departments are diligent in obtaining written authorization. The excuses run the gamut, from "too busy" service counters to customers simply leaving the store without signing.

A repair authorization is a legal contract between a dealership and a customer — if a customer doesn't sign this form, he or she isn't legally required to pay for the repair. This could leave your dealership holding the bag for thousands of dollars in repairs. These authorizations should itemize and price all necessary parts and detail

Focus on KPIs

As you think about boosting fixed operations profits, service department key performance indicators (KPIs) are a good place to start. Here are a few KPIs related to the service department, along with industry benchmarks that some dealerships have found useful:

	Domestic	Import
Gross profit as a percentage of sales	70%	72%
Net profit as a percentage of sales	20%	17%
Total expenses as a percentage of gross profit	90%	76%
Technician efficiency	107%	111%
Flat hours per repair order	1.4	1.2
Technicians per service advisor	3.5	3.4
Daily repair orders per service advisor	13.5	15.0

the repair methods to be used. Also make sure customers approve in writing any changes to the repair authorization that will increase the price of the work.

Legally valid customer signatures generally include ink signatures on paper repair forms, electronic signatures on a mobile tablet, and ink signatures on preauthorization forms dropped in an after-hours drop slot.

3. Reduce turnover of service technicians. According to NADA's 2017 *Dealership Workforce Study*, the annual turnover rate for experienced service technicians was 27.2%. Put another way, one out of every four service techs quits his or her job each year. Even worse, a majority of service techs said they wouldn't recommend their job to a friend.

When you lose experienced service techs, your dealership may suffer lower productivity as you look for replacements and eventually hire less-experienced technicians to take their place. For example, it could take a new technician twice as long to perform a repair as the experienced tech who left, which hurts profitability.

One way to reduce service technician turnover is to view your techs as an investment, rather than a cost. Investing in their job satisfaction — for example, by paying higher-than-average wages and offering a performance-based bonus plan — can pay big dividends by boosting productivity, efficiency and, ultimately, your fixed operations' bottom line.

Honing in on customer service

Don't discount the importance of providing outstanding customer service when it comes to increasing fixed operations' profits. For example, do employees give customers a warm and friendly greeting when they enter the parts and service area? Are problems diagnosed accurately and repairs done correctly the first time? Such things can boost customer satisfaction, which may lead to more repeat and referral business and, therefore, higher profits.

Talk to your parts and service department manager about implementing these and other strategies to improve fixed operations profitability. They may come up with more ideas that are particular to your shop.

Prepare your dealership for a disaster

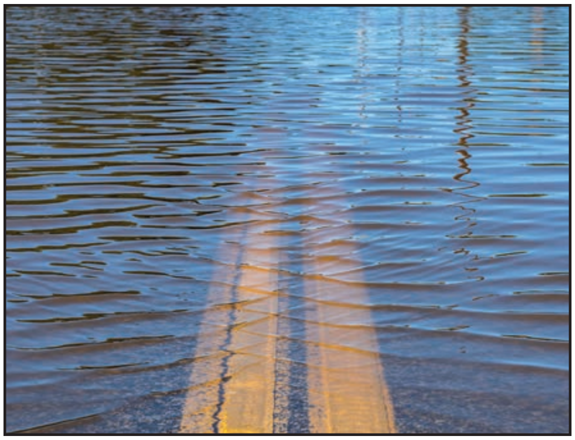
Disaster planning is important for all businesses, including dealerships. While natural disasters such as hurricanes, earthquakes and wildfires generate significant media attention, these aren't the only kinds of calamities that can affect your business.

For example, a major power outage, server crash or well-coordinated cyberattack could bring activity and sales to a standstill for days or even weeks. Your disaster recovery plan should account for how your dealership will respond to a wide range of both natural and manmade disasters.

First priority: Reopen ASAP

The top priority after a disaster should be to reopen your doors for business as soon as it's safe to do so. Your goal is to restore customer traffic and minimize lost revenue. This usually means repairing any damage on your physical premises and infrastructure — not only damage to the building itself, but also to your computers, servers, telecommunication systems, furnishings and repair bays.

You may need to restock your inventory, including both vehicles and parts. Talk to your floor plan lender and manufacturer now about how vehicles that have been damaged or destroyed will be replaced and how long this will take. Also think about how you'll guard inventory from thieves and looters in a disaster's aftermath.



Consider setting up a bank line of credit to provide fast access to funds you might need to keep operations going while you await insurance settlements.

Data recovery should be another postdisaster priority. Most of your critical data — sales and service records, repair orders, vendor contracts, vehicle titles and customer information — is likely contained in your dealership management system (DMS). Back up the DMS daily and take the most recent copy offsite and store it securely. Better yet, take advantage of the digital archiving and cloud storage features offered by most DMS providers today.

In addition, plan for how you'll communicate with employees after a disaster to keep them informed about your timetable for reopening. Compile employee contact information (landline and cell phone numbers, email addresses and street addresses) and store it somewhere offsite so you can retrieve it easily. You also may use social media to update employees on the status of your reopening and allow them to let you know how they're doing.

Stay financially viable

It's crucial to plan for the financial viability of your dealership in the days, weeks or months after a disaster. For example, consider setting up a bank line of credit to provide fast access to funds you might need to keep operations going while you await insurance settlements.

To minimize the potential negative impact of a disaster on your employees' personal finances, talk to your bank about procedures for making payroll on schedule postdisaster. And compile a list of all passwords and login credentials needed to access bank accounts. Be sure to keep this list in a secure location offsite, such as in a fireproof safe in your home.

Review insurance policies

Now is the time to review your insurance policies to identify what kinds of disaster-related expenses are covered. The main policies to examine are your property and casualty (P&C) and business interruption insurance.

Your P&C insurance will generally cover the cost of repairing or replacing tangible property that's damaged or destroyed, such as your physical buildings, furnishing and fixtures, computers and telecommunications equipment, and inventory. Make sure that coverage amounts have kept pace with your current exposure, which may have increased if you've recently expanded your dealership. Having a video of all your dealership's property will be helpful when filing P&C insurance claims.

Business interruption insurance will provide money to cover ongoing business losses, such as the property's ongoing mortgage and utilities expenses, employee payroll and lost revenue for a predetermined period after a disaster strikes. Study both your P&C and business interruption policies carefully to see if there are any exceptions that preclude coverage. For example, some policies don't cover flood damage or pay claims that arise due to offsite disaster-related events, such as downed power lines that result in lost power or electrical damage to a business.

"Readiness" is the word

No one knows when or where disaster will strike next, so disaster recovery planning is pivotal. Meet with your department managers to discuss these and other aspects of disaster recovery planning for your dealership.

How large should your sales staff be?

As every auto dealer knows, vehicle sales fluctuate from year to year. For example, industry forecasters J.D. Power and Associates recently predicted that U.S. industry sales would fall to 16.8 million in 2020, a decrease of 1.8% from projected industry results in 2019.

"If the industry ends at this level [in 2020], it will be the first time the industry has sold fewer than 17 million units since 2014, when the U.S. auto industry was still growing out of the recession," said a J.D. Power and Associates vice president of data and analytics consulting. "Peak industry sales [took place] in 2016 when the industry hit 17.5 million, which would put 2020 down nearly 750,000 units, or -4.2%, since then."

Consider sales and transaction totals

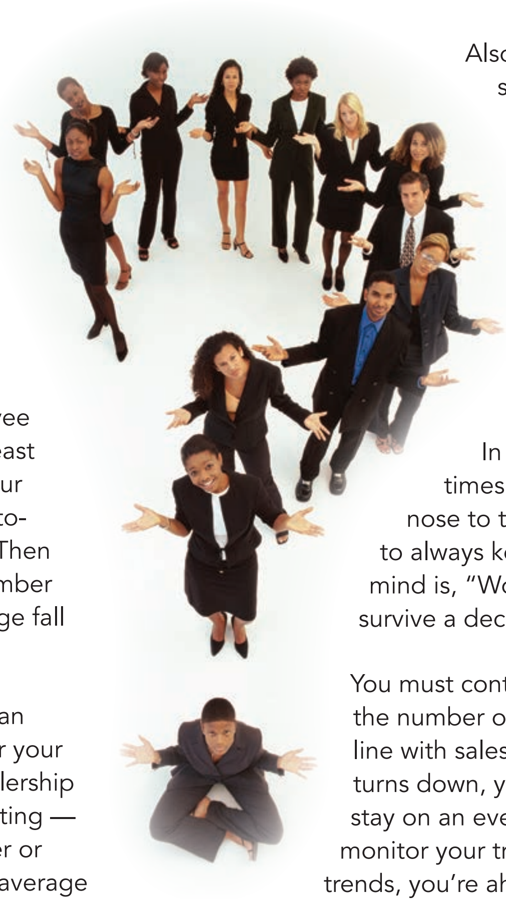
It's not all bad news for dealers. Combining sales and transaction prices, consumers are spending more than ever on cars, trucks and SUVs. In fact, 2019 is up 1.5% in total dollars spent compared with dollars spent in 2018, according to the J.D. Power representative.

So, based on current and projected sales in your part of the country, how do you know the ideal size for your store's sales staff?

To reach your optimal sales staffing level, there are several steps you can take. A good place to start is your monthly gross profit per employee.

A rule of thumb is that each employee should generate gross profit of at least $7,200 per month. To determine your average, take your December year-to-date gross profit and divide by 12. Then divide the result by your current number of employee count. Does the average fall above $8,800?

Depending on your circumstances, an $8,800 average may not be right for your business. Always compare your dealership to the market in which you're operating — consider checking with manufacturer or group composites to see how your average stacks up.



Also think about the staffing levels you need for key weekday and weekend hours and for special promotions. Answering these questions will help ensure you have the staffing necessary to handle all your peaks.

In good times or bad times, you should have your nose to the future. A question to always keep in the back of your mind is, "Would our dealership survive a decrease in traffic?"

You must continue to work at keeping the number of sales employees in line with sales so that, if the market turns down, you'll be better able to stay on an even keel. If you already monitor your traffic and keep tabs on trends, you're ahead of the game.

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Keep up with the ebb and flow

Reaching your optimal sales staffing level isn't a clear-cut matter. To customize your approach, you'll need to think about the needs of your dealership. Consider, for example, how you handle staffing when sales employees take vacations or call in sick.

Financial problems that arise from carrying too many sales employees can creep up on you. Be careful not to hire at a rate faster than your sales and gross are increasing. Continually adjust your headcount to match your sales, and you'll have a better chance of maintaining your dealership's profits during challenging periods.

Time for review

With a slight decline in overall U.S. vehicle sales predicted, it might be a good time to re-evaluate the size of your sales staff. But make sure that you consider sales and profit trends in your region and your community. Then make sure your store is ready to handle any downturn while poised to take advantage of opportunities that might come its way.

Floor plan lending

The importance of remaining in trust

Remaining in good standing with floor plan lenders is critical to financial success for most dealerships. These lenders provide revolving lines of credit that allow dealerships to finance inventory instead of having to pay manufacturers out of pocket for vehicles on the lot.

Monitor trust compliance

Dealerships are expected to remain in trust compliance with their floor plan lenders, which gauge this in several different ways. One of the most common methods is to use the dealer statements they receive each month to monitor the store's net cash position. Another method is to perform periodic audits of vehicle inventory.

Lenders may also track a dealership's payment history after vehicles have been sold. If a dealership has been slow to pay for vehicles, this could indicate underlying problems with the business's net cash position.

The phrase "out of trust" is often used to describe a dealership not paying for vehicles within the time frame allotted in the floor plan financing agreement. For example, a lender might require that vehicles be paid for within two or three days of delivery.

While late payments could be a sign that a dealership is out of trust, late payments don't create an out of trust position in and of themselves. In some situations, floor plan lenders allow large dealership customers or fleet customers to have longer than normal payment plans or delayed payment plans. Under these situations, the dealership is sometimes allowed to pay the floor plan when the customer pays for the vehicle.

Stay in your lender's good graces

Falling out of trust with your floor plan lender can lead to financial problems, notably the loss of floor plan financing. Lenders also may increase the frequency of floor plan audits, which can drain cash and pull employees away from more productive tasks that add to your bottom line.

This issue should be a top financial priority for your dealership. Work closely with your accounting professional to monitor your net cash position so you remain in trust with your floor plan lender.

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