NADC
NATIONAL ASSOCIATION OF DEALER COUNSEL

DEFENDER

The National Association of Dealer Counsel Newsletter SEPTEMBER 2013

In this Issue:

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A Good Regulation from Washington for Car Dealers?

By J. Timothy Sparks, *Sonic Automotive, Inc.*

Is it possible that one of Washington's famous unfunded mandates, requiring businesses, including car dealers, to check for potential identity fraud, might be a beneficial thing? Far be it for me to thank our federal government for additional intrusion into the free market, but when life gives you some lemons, even in the car business, it might be good to try and make some lemonade.

The Federal Trade Commission published the so called "Red Flag Rules" on November 9, 2007, which require car dealer and other business, to develop and implement an "Identity Theft Prevention Program." While the famous line goes something like, "We are from the government and we are here to help," generally does not ring true, the Identity Theft Prevention Program can become very beneficial to our dealer clients.

Imagine this scenario – your client reports it sold a car to a customer with little effort; even better, the customer bought two or three cars at once, paid pretty close to sticker, and maybe as the cherry on top, bought a few F&I products. High fives for everyone as our dealer client just made some quick and easy cash. This sounds so good, I must be dreaming. The fact of the matter is your client might be looking at a nightmare that is going to keep them up for many nights. Here is a very under-reported fact about the automotive retail business: sometimes, just sometimes, the customer is the one cheating the dealership.

The above situation can take place anywhere, and but for the purchase of multiple new vehicles at once, I suspect will be happening to almost every dealer before too long. There are few feelings in life better than buying a new car. You are excited, proud, and if you have pulled it off using someone else's credit, you never even have to worry about making your first payment. Identity ("ID") theft is a real problem, and when it hits your clients, it hurts a lot. In the above hypothetical ID theft situation, the assigned finance contract(s) would likely be reassigned to the dealer, and the dealership would be responsible for the loss, not the finance company.

The FTC's 2007 announcement of the Red Flag Rules saw several delays in the final enforcement. It was not until January 1, 2011 that the FTC actually began to enforce the rules. In case you are wondering, "What is a red flag?" A red flag is a pattern, practice or specific activity that indicates the possible existence of identity theft. The Federal Trade Commission's Red Flag Rules enumerated 26 specific red flags. A business is required to develop a policy which identifies the "red flags" in its operations, check for the 26 enumerated or other potential red flags that might arise in its particular operation, detail the actions the business will take when a "red flag" is triggered, and review its program at least once a year.

Like many dealers, some of Sonic's dealerships suffered losses from ID thieves. At Sonic, we instituted our Red Flags Program before the FTC's rules mandated it. The results since the policy's implementation have been promising. We are detecting potential ID thefts, and more importantly, we are preventing ID thefts as a result of this Red Flags Program.

As part of our sales process, we utilize RouteOne to obtain credit reports for all of our dealership customers who complete a credit application for financing or leasing a vehicle. Simultaneously with pulling the customer's credit report, by utilizing RouteOne's optional IDOne Theft Prevention Product, RouteOne's system also performs our OFAC and electronic Red Flag ID Theft Prevention reviews. If the IDOne system detects any anomalies in the customer's information, the IDOne system will generate questions based off of the customer's credit history that only the real customer should know. If the customer passes the credit quiz, then the deal proceeds. If the customer fails the credit quiz, then the dealership cannot proceed with the sale, absent some further investigation and approval from someone outside of the dealership and outside of the sales operation.

Once the customer has failed a RouteOne-generated credit quiz, the deal undergoes greater scrutiny from resources in the Corporate Office. There are many occasions where this process clears up the matter and the customer at our dealership is indeed legitimate and the deal proceeds. "False positives" occur somewhat frequently and the RouteOne system can be calibrated to increase or decrease the level of scrutiny. The higher the initial scrutiny level, the greater the number of initial false positives.

Since 2010, Sonic dealerships have sold more than 600,000 vehicles and have stopped approximately 81 known identity thefts. The percentage of known frauds is incredibly minimal, but the dollar value is pretty high. Sonic's dealers would have faced buy back demands totaling approximately $3,000,000 for those 81 fraudulent deals we caught before the vehicle was delivered. The system, the training, and our process have paid for itself many times over.

All car dealers need to work to prevent purchases procured through identity theft. Sometimes criminal syndicates will target dealers in a particular location. Many times, the cars purchased via ID theft are quickly loaded onto docks and sent overseas. This

NADC Welcomes New Members

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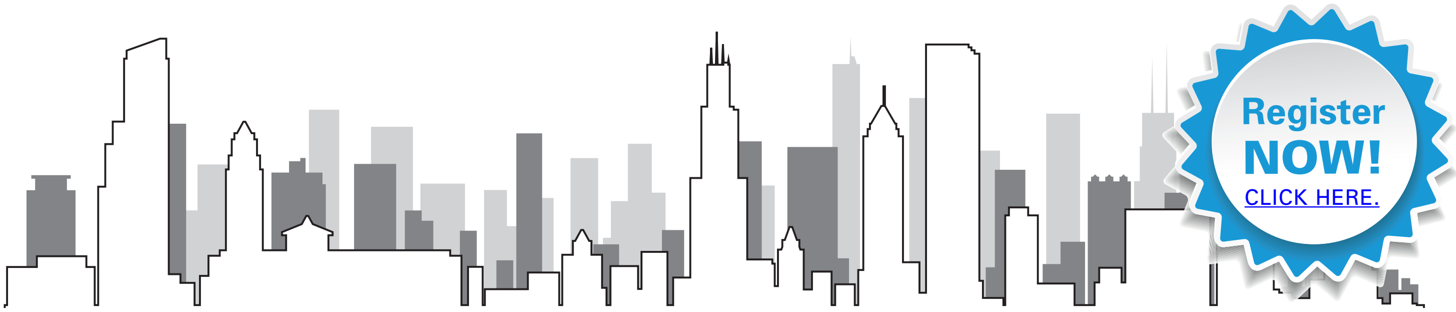
type of criminal activity is different than the possibly more common tactic of exporters using various means of buying luxury cars in the US to ship to China or Europe.

The best part of our Red Flags Program is when the fraudster is caught and prosecuted. Unfortunately, the bad guys sometimes get away, even if the deal is prevented. I suspect that rarely does the foiled thief "See the Light" as Jake Blues did so memorably in that scene from the Blues Brothers, and turn away from a life of crime. What is more likely is that the thief picks the next dealer down the road, hoping that their identity theft system is not working as well. And when an experienced ID thief finds a dealership which is an easy mark, they come back for more.

Accordingly, it is important for our clients to work with their local law enforcement agencies as well as their local and state dealers associations, to share the information about attempted identity theft purchases.

Further, stay on your clients to actively monitor and enforce their existing Red Flags and other ID-theft policies. The greatest policy does no good if it is not followed. A really good thief can sometimes beat the system, but if someone ignores the red flags, or someone does not do sufficient follow-up investigations when red flags are triggered, an avoidable loss is incurred.

Maybe I will thank the FTC for their role in helping push Sonic and other dealers into implementing ID theft prevention programs. And maybe the currently 0-2 Panthers will win the Super Bowl in February 2014. ■



2013 NADC Fall Conference • October 6 - 8, 2013 • The Trump International Hotel & Tower • Chicago, IL

Session Topic Descriptions

Monday, October 7, 2013

8:45 – 9:45 am
Session 1: Getting Ready for 2015–Offering Health Care Coverage to Employees: Who, What, How, and When?
James Harbert, *Hinshaw & Culbertson LLP*
The employer mandate to provide employees with health coverage is the most daunting aspect of health care reform facing employers. While the mandate has been delayed until 2015, the time is now to prepare your clients for the employer mandate. The session will cover the following: What employers are "applicable large employers" that are subject to the mandate? Who in the work force must be offered health coverage? What must the health coverage include? Is the offered coverage "affordable"? What are the penalties for failure to satisfy the mandate? What are some alternatives?

10:00 – 11:00 am
Session 2: Understanding Your Dealership Insurance Program
Steven Gibson, *Dealer Risk Services, Inc.*
Richard Minor, *AmWins Brokerage*
Understanding Your Dealership Insurance Program will provide creative techniques to effectively protect the Dealership against losses. We outline an aggressive approach designed to show Dealers how they can take control of their Insurance programs and the costs. The overall objectives are to provide the tools necessary to understand and navigate the Garage Insurance Marketplace. We will explore proven techniques that will protect the Dealerships against catastrophic events (both weather and man-made) and litigation trends.

11:15 – 12:15 pm
Session 3: Service Department Legal Issues: Loaner Contracts and Repair Orders
Michael Dommermuth, *Fairfield and Woods, P.C.*
Jami Farris, *Parker Poe Adams & Bernstein*
Join Jami and Michael as they look under the hood at the mechanical legal issues involved in Service Departments. They will repair a riveting diagnostic of loaner agreements, shop charges, repair orders and invoices. You will be at the edge of your seat for this long awaited presentation on this topic.

1:30 – 2:30 pm
Session 4: Arbitration Update: What You Can do to Protect Your Dealer Clients
Thomas Hudson, *Hudson Cook, LLP*
Christian J. Scali, *The Scali Law Firm*
Automobile dealers and finance companies were slow to embrace mandatory arbitration as a means of reducing class action and other risks. This session will describe the early development of arbitration agreements and their acceptance by the industry, and will describe how drafting techniques have evolved over the years to meet changing theories of unenforceability advanced by the plaintiffs' bar. The session will also explore several recent court decisions that have impacted arguments for and against the enforcement of consumer pre-dispute arbitration agreements. Decisions expected in the next year will further clarify the enforceability of these agreements. This session is a deep dive into arguments for and against enforcement of pre-dispute arbitration agreements to guide drafting of effective arbitration agreements and to provide effective arguments for the enforcement of these agreements when they are challenged in court.

2:30 – 3:30 pm
Session 5: Current Buy/Sell Market
Alan Haig, *Presidio Automotive*
Erin Kerrigan, *Presidio Automotive*
The dealership buy/sell market is very active today. This presentation will examine some of the key drivers of this activity including the credit markets, dealership profitability, blue sky values and the expected growth in new car sales. It will also discuss buyer's return on investment expectations and how those expectations determine what they are willing to pay for a dealership. The presentation will also review the current blue sky multiples for franchises in the U.S.

3:45 – 5:00 pm
Session 6: Open Mic – The List-serve "In Person": Hot Topics and Questions You've Always Wanted to Ask
Moderator: Oren Tasini, *Haile, Shaw & Pfaffenberger, P.A.*
The NADC member list-serve will jump from the computer screen to an in-person discussion during this session. Attendees can delve deeper into the hot topics and issues discussed on the list-serve such as, adverse action letters, internet advertising, new car raffles, bankruptcy and much more. In addition, conference attendees will have the opportunity ask questions and get advice from their colleagues.

Tuesday, October 8, 2013

8:30 – 9:30 am
Session 7: NADA Update
Paul Metrey, *Chief Regulatory Counsel, NADA*
During this session, NADA Chief Regulatory Counsel Paul Metrey will provide an overview of the latest developments surrounding the CFPB's Disparate Impact Initiative and NADA's efforts to respond to it.

9:45 – 11:15 am
Session 8: Sales and Finance Litigation Update
Geoffrey Chackel, *Higgs Fletcher & Mack, LLP*
Rob Cohen, *Auto Advisory Services, Inc.*
Patty Covington, *Hudson Cook, LLP*
Some plaintiff attorneys in California are finding new and, at times, unethical ways to sue dealers. Join Geoff Chackel, Rob Cohen, and Patty Covington for a lively discussion related to recent theories of recovery related to sales and finance practices. This session will address the types of lawsuits dealers are currently facing and provide attendees with some practical advice to pass along to clients. Patty Covington will also lead the panel in a discussion related to fair lending practices and how dealers can protect themselves from credit discrimination claims.

11:30 – 12:30 pm
Session 9: Estate Planning Vehicles – Model Year 2013
Mitchell A. Drossman, *U.S. Trust*
This session will provide an overview of transfer tax (estate, gift and generation-skipping tax) planning, with particular focus on estate planning techniques ("vehicles") for transferring business interests to successive generations. With a lifetime gift tax exemption of $5.25 million (twice that for married couples), lifetime estate planning opportunities are numerous. But along with opportunity come several pitfalls. This session will explore the advantages and disadvantages of lifetime planning versus testamentary planning. Unique tax and non-tax issues for the closely-held business owner will also be addressed, as well as the overall need to preserve flexibility.

Treasurer's Report

Andrew J. Weill
Benjamin, Weill & Mazer
NADC Treasurer

The purpose of this column is to provide some information about the activities of the officers of NADC. This time, it's my turn. I'm the Treasurer, a position for which I assume I was deemed suitable due to my extensive background in accounting (two whole semesters in college) and the sophisticated financial transactions I am involved with on a daily basis (evaluating my son's most recent requests for supplementary funds for his college education).

Fortunately for NADC, the real work on financial matters falls into the capable hands of Erin Murphy and her equally competent colleagues at AMS. Our financial statements are reviewed by an outside accountant.

I review the financial statements on a monthly basis. I determine if we are on track for our annual budget based on deep, highly sophisticated principles of financial management, such as: more revenue than budget is good, more expense than budget is bad. Most of the time, everything is exactly on track. On the few occasions where something seems at variance with what I expected, I ask for further details, and usually there is a very easy explanation. For example, conference expenses increased because we added a half day to the conference, requiring an additional meal and longer room rental.

We have had a sufficient surplus in funds that Steve Linzer made the excellent recommendation that we deposit a prudent portion into an interest-bearing account, which has been adopted.

At the quarterly meetings of the Board, the most up-to-date financial information is circulated. Most of the statements are self-explanatory, but I give a report to address any items that I believe deserve further discussion or clarification.

I think it's very safe to say that financially, we are doing just fine. Revenues are sufficient to pay for the quality conferences, maintain the website and List-Serve, get The Defender and the directory published and distributed, and allow the Treasurer to go on expensive junkets at your expense. Well, maybe the last item isn't accurate, but I wanted to check if anyone is actually reading this.

It has been a pleasure to serve as Treasurer, and I would be happy to answer any further questions you may have about our finances. ■

NADC Job Board

Please remember to check the NADC Job Board in the members only section of the website if you are seeking employment.

Please send any job postings to:
emurphy@dealercounsel.com

Taxation of Demonstrator Vehicles

By Paul L. Charles, CPA
Richards, Witt & Charles, LLP CPA's

Feature Article

The use of company provided vehicles by employees is an issue affecting sales tax and income taxes. The sale tax rules vary by state but the income tax rules are established by Federal tax laws and regulations. Company provided vehicles are considered by the IRS to be a "Taxable Fringe Benefit" and its use is taxed to the individual driving the vehicle. The rules differ for "Full-time salespeople" and non-sales employees and owners. Prior to 2001, a full-time salesperson's use of a demonstrator vehicle may not have been taxable to salesperson only if very detailed records were kept on the use of the car. These records had to show the miles used on a daily basis, and personal use was extremely limited. Since most sales employees did not comply with the record keeping rules, the IRS took the position in tax audits that the use of a demonstrator was fully taxable to the sales employee.

In 2001, the IRS issued guidelines (Revenue Procedure 2001-56) on the taxation of the personal use of a demonstrator vehicle provided by automotive dealers to their employees. This revenue procedure allows the dealer, instead of the salesperson, to determine the taxability of a demonstrator vehicle. Since ten years have passed since the issuance of Rev. Proc. 2001-56, it's time to revisit the rules.

Rev. Proc. 2001-56 allows four methods of determining the taxable amount of the use of a demonstrator vehicle. These are "Full Exclusion Method", "Simplified Full Exclusion Method", "Partial Exclusion Method" and "Full Inclusion Method". The Full Exclusion Method and the "Simplified Full Exclusion Method", have detailed record keeping requirements in order to exclude from taxation the use of the demonstrator vehicle for full-time salespeople. There is no formal election to use a particular method. Since compliance with the required record keeping is very difficult, we recommend dealers adopt the Partial Exclusion Method for their sales employees.

To qualify as a full-time salesperson, the employee must be a full-time employee of the dealership, must spend at least half a normal business day performing the functions of a floor salesperson or sales manager, must be directly involved with the negotiation of sales to customers and must derive 25% of their gross income as a result of sales activities.

The Partial Exclusion Method enables dealers to tax full-time salespeople at an amount that is less than non-sales employees without maintaining any records on the use of the vehicles. Under this method, an amount is included in the full-time salesperson's wages, on at least a monthly basis, based on the number of days the demonstrator is used, payroll taxes are to be withheld (including federal and state withholding), and the amount of gross additional wages is then deducted and credited to demonstrator expense.

To be eligible for this method, the company must have a qualified written policy which:

- Prohibits use of the vehicle outside of normal business hours by individuals other than full-time salespeople.
- Prohibits use of the vehicle for personal vacation trips.
- Prohibits storage of personal possessions in the vehicle.

The qualified written policy must be communicated to employees by a posted notice, a letter or email or signed statements by the employees acknowledging receipt of the policy. Failure to comply with the written policy will result in the inability to use the reduced income amounts and 100% of the full lease value would be included in the income of the employee. A sample written policy is available in the revenue procedure can be found on the IRS website or sent to you upon request.

The income amount is based on the value of the vehicle found in the following table:

Table for Full-Time Salespeople

Value of the Demonstration Automobile	Daily Inclusion Amount
$0 - $14,999	$3
$15,000 - $29,999	$6
$30,000 - $44,999	$9
$45,000 - $59,999	$13
$60,000 - $74,999	$17
$75,000 and above	$21

To determine the value of every demonstrator vehicle used by the full-time salesperson, an employer may use any reasonable method, such as MSRP. Alternatively, the revenue procedure allows an "Annual Average Look Back Method" to value the vehicle based on the average sales price of all new vehicles sold in the prior year. The average sales price is used to determine the value of the demonstration vehicle and the corresponding daily inclusion amount under the table above. Once an amount is determined for the average sales price, that amount is used for all employees, regardless of the specific car they are driving. This amount is included in the employee's wages for each day the employee used a demonstration vehicle. The average sales price must be determined in January of each year and must be applied no later than February of that year. If salespeople are driving used vehicles, the same method applies; the value of a used car demonstrator is calculated based on the average sales prices of all used vehicles sold for the prior year.

There is no exclusion of income for non-salespeople driving demonstrator vehicles; 100% of the annual lease valuation table amount is to be reported, there are no exceptions. Employees subject to the full inclusion method include parts and service managers, office personnel, owners and their families, and those not qualifying for full-time salesperson status. The IRS has issued tables providing the daily inclusion amount under the annual lease value, and is used in the same manner as the table for full-time salespeople. The income inclusion amount for non-salespeople is based on the value of the demonstrator vehicle and is found on the annual lease value table. The value of new or used vehicles is determined in the same manner as it is for full-time salespeople.

The income for use of a demonstrator vehicle must be included in box 1 of Form W-2 *and* must be disclosed in **Box 14 - Other** with a code of "EPV" (EmployerProvidedVehicle).

Department of the Treasury
Internal Revenue Service

Publication 15-B
Cat. No. 29744N

Employer's Tax Guide to Fringe Benefits

For use in **2013**

Get forms and other Information faster and easier by:
Internet IRS.gov

Jan 18, 2013

Contents

Future Developments

For the latest information about developments related to Publication 15-B, such as legislation enacted after it was published, go to www.irs.gov/pub15b.

What's New

$2,500 limit on a health flexible spending arrangement (FSA). For plan years beginning after December 31, 2012, a cafeteria plan may not allow an employee to request salary reduction contributions for a health FSA in

A sample written policy as well as the full lease value tables can be sent on request or found in the revenue procedure at: http://www.irs.gov/pub/irs-pdf/p15b.pdf

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Questions: Erin Murphy, email: emurphy@dealercounsel.com

BE A CONTRIBUTOR!

We are always looking for submissions to publish in the Defender. Please send your contributions or proposals for articles to:

mike.charapp@cwattorneys.com

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