



Why an Internal Audit Function is Practical for Heavy Truck Dealers

David Wilkinson, CPA, Senior Manager | DHG Dealerships

Heavy truck dealers often ask, “Does our dealership really need internal audit?” Many dealers don’t have an internal audit function due to misconceptions about cost, practicality or understanding of the function. The internal audit function is to test compliance with the dealership’s policies and procedures and to identify potential areas of risk. However, internal audit can be key to helping heavy truck dealerships identify and managing potential risks to operate efficiently and minimize exposure to loss.

In this article, we discuss some of the common areas of risk for heavy truck dealers and simple steps to address them through the internal audit function.

Assessing Common Risks

The following are common risks within heavy truck dealerships that can be mitigated with effective policies and an effective internal audit function:

- **Small and remote locations.** For large group dealerships with multiple locations, there is risk that some locations may not follow all corporate policies as required.
- **Federal excise tax (“FET”) determinations and documentation.** Dealerships can face significant penalties and interest due to errors in FET determinations, or if the proper exemption forms for exempt sales have not been

completed and filed. The cost of an FET audit where FET determinations have been made improperly or appropriate documentation hasn’t been retained can result in significant interest and penalties.

- **Sales and use tax.** Dealerships must be able to determine which sales are exempt from sales tax and provide proper documentation for such sales. Additionally, they should have a process for identifying when use tax is applicable and properly accruing for it.
- **Aged open repair orders.** How efficiently does your service department close repair orders and promptly bill the customer? Open repair orders that are aged often have higher risk of policy adjustments or warranty adjustments. Worse yet, do you still have the truck at the dealership? If not, you have a receivable that is unbilled and aging!

- **Aged cash pay receivables.** Most dealerships will sell parts or service on cash accounts to customers unable to qualify for credit. The customer is required to pay at the time of delivery, and most dealers have the policy to not release the parts or trucks without payment. This is typically considered a low risk receivable; however, they become the *highest risk category of receivables* once the parts or truck are gone from the dealership. If a service writer or manager releases a truck prior to payment on cash tickets, the customer has essentially been granted credit contrary to the overall credit determination.
- **Cash handling procedures.** How does the dealership handle cash with customers and cashiers, including the application of cash and check payments to customer accounts? This is an area that requires robust processes and controls to mitigate risk of employee theft.
- **Cash disbursement controls.** As with cash handling, there is potential risk regarding the procedures for disbursing checks and other monetary items.
- **Use of unapproved vendors.** Proper vendor selection protocols should exist to mitigate the risk of department managers or others selecting vendors due to self-interest rather than the interest of the dealership. Such selection bias could be the result of family or personal relationships, or even kickbacks paid to the manager.
- **Accounts receivable credit memos.** Often dealers have conflicting duties for personnel authorized to issue to credit memos. Those conflicting duties can create the opportunity for employee theft.
- **Lease and rental.** Most dealers have access to and rely on pricing guidelines from the lease and rental groups affiliated with their make and have policies that require approvals (for example CEO, CFO or dealer principal approval) for deals that fall outside those guidelines as those deals can have higher risk or lower margins. Testing compliance with obtaining required approvals makes those policies more effective.

There can be other key risks unique to your dealership. Think through your operations as you contemplate the above risks for other areas that you may want to test.

Clear Policies and Procedures

Does your dealership have clear and appropriate policies and procedures to manage the above risks? Are there any holes or gaps? And most importantly, are they being followed? Policies and procedures can lay the foundation for mitigating the previously mentioned risks at the dealership. Policies and procedures should be documented, communicated to employees and regularly reviewed. With good processes you can improve efficiency and effectiveness as well as make sure your policies and procedures are scaled for any growth or turnover in the dealership. You can also identify which controls may or may not be fulfilling their purpose, and then make certain control recommendations for improvement.

Test the Compliance – Inspect What You Expect

Internal audit can help you test and measure your organization's compliance with the established policies and procedures. Such compliance can also help the dealership avoid hefty penalties and fines from compliance related testing. Trusting that policies are being followed without testing such compliance is a recipe for bad surprises. An effective internal audit function can be built through hiring an internal auditor (or team depending on dealership size) or through outsourcing the process to experienced consultants. Among the factors to consider are training, experience and flexibility to address your specific needs. In either scenario, it is important to design an internal audit program that addresses the key risks faced by the dealership in an efficient and cost-effective manner.

Conclusion

Implementing an effective and practical internal audit approach for your dealership can help you avoid and mitigate significant risks and identify potential problems early. For more information about how to implement a practical internal audit for your dealership, reach out to us at info@dhg.com.

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