

BENEFITS OF OPERATING A RELATED FINANCE COMPANY

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Related finance companies have been around for more than 30 years, yet many dealers still don't utilize them for fear that they increase the risk of an IRS audit or that they create an administrative burden. Use of a RFC is an IRS approved strategy and the IRS has issued a 26 point checklist for operating a RFC correctly and while a RFC does add some additional administrative work, the pros significantly outweigh the cons.

Benefits of operating a related finance company include:

- 1) Income tax – The most obvious reason for operating a related finance company is the deferral of income taxes. Under IRS rules, a dealership is required to file their taxes on the accrual basis which means that income taxes are paid upfront when the vehicle is sold even though a dealer may not have received any payments yet from the customer. By using a RFC and by discounting the receivables, income taxes are effectively spread out over the life of the receivables, improving cash flow.
- 2) Obtaining lines of credit – Banks don't like to offer lines of credit to dealers when the dealer already has floor plans in place. If that dealer were to fail, the bank would have to fight with the floor plan companies over the assets of the dealership. By putting the finance receivables in the RFC, banks are more likely to offer lines of credit because the bank knows they have sole access to the assets of the RFC in the event of default.
- 3) Better operating structure – By operating a separate finance company, dealers can be more effective when collecting on receivables. Collectors can differentiate themselves from the dealership so that mechanical issues or sales issues are kept separate from collection issues.
- 4) Estate planning – By maintaining assets in 2 separate legal entities, the dealership and the RFC, the dealer has more options when performing estate planning and succession planning.

Related finance companies have proven themselves time and time again but they must be setup and operated correctly and dealers should seek professional guidance when considering a related finance company.