

Lender Services

Supporting Financial Institutions in
Managing Automobile Dealership Portfolios for Optimum Return





Introduction

The complexity of problems facing Lenders today is greater than ever. Dealerships have consolidated into groups – small and large. Strategy and planning, management, information, customer relations, marketing communication, and finance have all been centralized. This consolidation, current economic and credit crises, and domestic auto company bankruptcies have caused complex problems to emerge as multi-brand, cross-collateralized dealership organizations struggle to weather the storm.

Some retail owners and their management teams are experienced with downturns, while others are new to this environment. Some are progressive business leaders, while others only know what their fathers taught them. Some are losing their businesses because of market conditions, while others are losing dealerships because their OEMs are taking them away. In these situations dealership owners—salespeople at heart—more often than not remain optimistic, sincerely believing they can sell themselves out of any predicament... even when the real issue is cash flow and additional sales exacerbate their financial condition.

After several months of losses, many dealerships become undercapitalized and create “patches” for cash flow that become a slippery slope to out of trust situations – or worse. Lenders react by instituting strict payoff and curtailment policies, often employing a “keeper” to be on-site at the dealership. While this seemingly protects the Lender’s investment, it often results in the impairment of dealership assets; loss of employees and brand reputation; bankruptcy; and the burden of costly legal action. Everybody loses.

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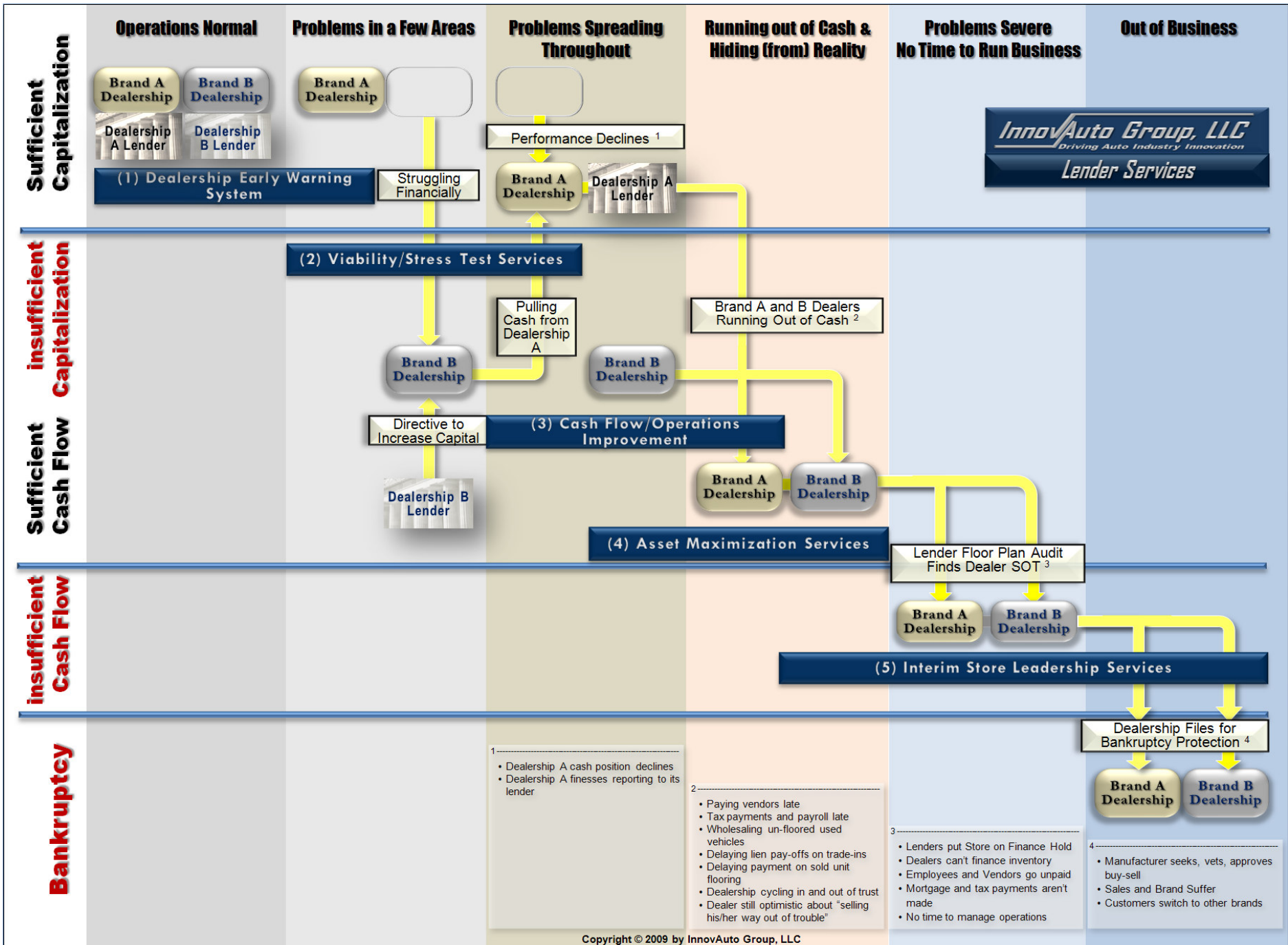
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InnovAuto Group, LLC

1289 Sylvandale Road

Mendota Heights, MN 55118

www.InnovAutoGroup.com



Solutions

(1) Dealership Early Warning System

To meet the need for a reliable, low-cost, and unobtrusive method of spotting unreliable financial reporting and conditions that could lead to a serious SOT situation, InnovAuto Group has developed a Dealership Early Warning System (DEWS) providing automated data capture, analysis, and alert capabilities as follows:

- ▶ At Lender direction **InnovAuto obtains** access to the DMS in the selected dealerships
- ▶ InnovAuto **provides the dealership guidelines on basic accounting and reporting requirements** vis-à-vis Lender and regulatory obligations

A Lender may also wish to install DEWS after an SOT situation has been alleviated and keeper tasks completed, but the Lender wishes to manage further risk via a "virtual keeper."

- ▶ The **DEWS application runs scheduled analyses**
- ▶ The analyses are downloaded to InnovAuto with **out-of-guideline conditions flagged**
- ▶ **Conditions indicating either inaccurate financial reporting, SOT risk, or both are communicated immediately** via e-mail to both the dealership and Lender

Lender benefits include:

- ▶ Being proactive, identifying negative trends early, and **avoiding large SOT situations**
- ▶ **Minimizing Lender risk, exposure, and losses**
- ▶ **Establishing dealership accountability** that prevents "information landscaping":
- ▶ **Freeing up Lender personnel to work on their primary duties** as analysts, consultants, and client service specialists, rather than putting them into the role of policemen or woman

The DEWS Philosophy

*AN OUNCE OF
PREVENTION IS WORTH A
POUND OF CURE...*

- Benjamin Franklin



(2) Dealership Viability/Stress Test Services

We also offer Lenders an **assessment of where individual dealerships currently operate within our basic performance continuum**, and where they are expected to fall based on expectations for economic, competitive, local market, and OEM realities.

This viability service **provides Lenders an objective analysis of which Dealer investments are solid, which need a tune-up, and which require more extensive intervention.**

InnovAuto Dealership Viability/Stress Test Services include **three levels of analysis:**

- 1. Lender Portfolio Analysis**
- 2. Individual Dealership Analysis – Remote**
- 3. In-Depth Individual Dealership Analysis – On-Site**

InnovAuto assessment services are handled by individuals who have significant backgrounds in operating and managing dealerships, including CFOs, Owners, General Managers, dealership CPAs, and attorneys.

(2) Dealership Viability/Stress Test Services (continued)

1. Lender Portfolio Analysis

This broad-based portfolio review can be **conducted for a variety of reasons:**

- ▶ To **validate the Lender's identification of adverse situations** within its dealership portfolio
- ▶ **To determine the relative level of operational risk** presented by multiple dealerships already identified by the Lender as problematic
- ▶ **To identify overall Lender risk in portfolios not yet evaluated**

The InnovAuto Lender Portfolio Analysis **includes remote assessments of** financial statements; inventory, manufacturer sales efficiency and market share targets; and consumer market, demographic, and customer satisfaction data.

InnovAuto Portfolio reviews are analyses completed through the eyes of experienced dealership operators.

Portfolio Analysis deliverables provided to the Lender include:

- ▶ Portfolio condition, risk, potential losses, patterns or consistency among dealership situations, and recommendations for alleviating portfolio distress
- ▶ Organization of individual dealership situations into performance/risk "segments," potential losses by segment, and general suggestions on remediating segment issues

InnovAuto's Lender Portfolio Analysis results and benefits include:

InnovAuto Portfolio reviews reduce Lender risk, losses, and management distraction

- ▶ Identification of immediate, mid-term, and long-term risks either for more aggressive monitoring or improvement action
- ▶ Improved understanding of common issues and challenges experienced within a Lender's dealership portfolio, thereby enabling the Lender to institute improvements across multiple client operations
- ▶ Identification of changes or trends indicating distress or imminent SOT situations



(2) Dealership Viability/Stress Test Services (continued)

2. Individual Dealership Analysis (Remote)

Individual Dealership Analyses are the next step in the Viability testing process. Remote Dealership Analyses are generally applied to individual dealerships exhibiting higher levels of risk within a Lender portfolio. InnovAuto dealership operations and financial specialists analyze underperforming stores for strengths, weaknesses, threats, and opportunities:

- ▶ Focusing on individual dealership profit centers, benchmarking performance against local market guidelines
- ▶ Identifying areas of concern and opportunity and providing a lens through which both the Lender and Dealer can focus on joint corrective action

InnovAuto's remote analyses include: dealership financial and bank statements, DOCs, and relevant correspondence between the Lender, manufacturer, and dealership.

InnovAuto's Remote Dealership analysis results and benefits include:

- ▶ Prompt, reliable dealership performance analysis and **improvement recommendations**
- ▶ **Vital and time-sensitive dealership financial evaluations without the Lender needing to staff up**

InnovAuto's Remote Dealership Analyses are completed by experienced dealership management and accounting professionals offering objective analysis and recommendations for joint Lender–Dealer implementation.

(2) Dealership Viability/Stress Test Services (continued)

3. In-Depth Individual Dealership Analysis (On-Site)

Recent InnovAuto research conducted among representatives of major dealership lenders indicated that **25% of dealerships were SOT outright or exhibiting signs of approaching SOT.** Among this 25% were **dealerships that might benefit from help, but further in-depth investigation was required to determine whether or not they can be saved.** To determine a dealership's capability and readiness for improvement, InnovAuto completes the following steps:

► Preparation

- If not already completed, InnovAuto conducts a **remote Individual Dealership Analysis** to identify likely problem areas and specific issues for on-site consultant investigation

► Day 1 in Dealership

- Complete interviews, process observation, documentation reviews, and root cause analyses; develop an accurate financial forecast; Review findings with InnovAuto senior management and the Lender, who decides whether or not to go ahead with on-site remediation planning.

► Days 2 – 3 in Dealership:

- Determine the top 5 to 10 top improvement opportunities; develop implementation plans with management team, Lender personnel, and where possible manufacturer field staff; develop financial forecast(s) reflecting the implementation of agreed-upon improvements; verify that implementation activities are begun and that Lender personnel (and manufacturer field staff, if involved) have all necessary information to effectively monitor dealership improvement progress

InnovAuto's On-Site Dealership Analysis and Improvement Capabilities

In addition to identifying improvement opportunities and solutions, InnovAuto's consultants are experienced in facilitating positive change by virtue of:

- Experience in wide-ranging dealership, field, Lender, and OEM projects
- A flexible consulting methodology capable of instituting minor change, process refinements, or process reengineering as needed.
- The availability of an internal reference library of best-practice business processes, job descriptions, and performance management techniques

InnovAuto's On-Site Dealership Analysis benefits include

objective understanding of specific dealership issues, an improvement plan understood and accepted by dealership management, and the implementation of change that reduces Lender risk and losses.



(3) Cash Flow/Operations Improvement Services

Dealership owners and managers have historically managed for profitability rather than for cash flow. Combining this tendency with the common retail belief that a dealership can “sell its way out of trouble”, **dealership management often—and needlessly—intensify their own financial problems with every additional unit sold.** So InnovAuto offers Cash Flow and Operations Improvement Services focused on preventing dealerships from going out of trust, while teaching dealership owners and managers to properly maintain adequate capitalization.

This **short-term consultancy** includes:

- ▶ **Teaching dealership management (owner, GM, department heads, office management) how to manage the dealership’s cash position;** steps include:
 - Accurate cash flow modeling and forecasting; educating the Dealer and his financial team on the cycling and movement of cash; and monitoring and revising assumptions on a daily, weekly, monthly, quarterly basis.

- ▶ **Preparing a strategic plan for dealership owners and managers to transform their financial management from a profit orientation to a cash flow orientation;** steps include:
 - Review of sales and income projections, expenses, and cash management processes
 - Identification of cash requirements (regular, infrequent, and one-time)
 - Prioritizing payables and cash outlays

- ▶ **Establishing appropriate systems, processes, and controls to ensure that cash flow is managed properly and with minimum effort** after the InnovAuto consultant departs; steps include:
 - Providing dealership management relevant material from InnovAuto’s library of process and management documentation, job descriptions, and process measurement and improvement

Lender Benefits of InnovAuto’s
Cash Flow/Operations
Improvement Services

By teaching dealership owners and managers how to convert their enthusiasm for profitability to an understanding of and focus on cash flow InnovAuto helps Lenders eliminate a key root cause of SOT situations. Or, in the words of Lao Tzu:

GIVE A MAN A FISH AND YOU FEED HIM FOR A DAY. TEACH A MAN TO FISH AND YOU FEED HIM FOR A LIFETIME.

(4) Asset Maximization Services

InnovAuto Asset Maximization specialists are experts in dealership operational and financial management. Their tasks include serving as dealership management's coach and advisor, rehabilitating and improving operational and financial management, assuring that risk is minimized, and protecting and maximizing asset value.

InnovAuto Group, LLC can provide **professional asset management services when the store is in or thought to be entering the "Problems Beginning to Spread" or "Running Out of Cash" stages**. These services include the basic activities of a keeper, but include **more advanced steps keepers and field personnel are generally unable to take**.

InnovAuto's Asset Maximization Services **institute systems and controls ensuring that dealership capitalization and cash positions are recognized, stabilized and maintained** at adequate levels so the **store avoids falling into a doom cycle** of being out of trust, paying off Lender obligations, and then becoming SOT again.

InnovAuto's Asset Maximization Services enhance traditional keeper services **with people and actions eradicating the root causes producing SOT conditions in the first place:**

- ▶ Evaluating and aging current assets to understand and document actual asset value
- ▶ Verifying and bolstering asset controls to stem leakage
- ▶ Assessing the dealership balance sheet for accuracy and to stop suspicious activity
- ▶ Reviewing purchasing policies and opportunities to assure that operations are lean
- ▶ Managing cash flow for adequate capitalization and liquidity
- ▶ Providing the Lender client continual written and verbal reporting on findings, plans, progress, and results

These services also preclude the need to pull Lender staff from their primary positions, thereby enabling **Lender personnel to stay on the jobs they do well while placing a more highly qualified person in the role of problem solver**.

Why supplement traditional keeper activities with more intensive analysis and improvement activity?

To solve root cause problems instead of temporarily easing symptoms likely to return later.



(5) Interim Store Leadership Services

For situations in which a dealership's financial performance has declined to a critical or near-critical state, **InnovAuto Group, LLC provides professional Interim Store Leadership Services to operate the dealership for maximum value during its slump, turnaround, bankruptcy, and/or buy-sell.**

These services can be implemented by InnovAuto immediately upon a lending institution identifying a dealership as nearing trouble, already out of trust, or scheduled for a buy-sell. InnovAuto's interim leadership team will be there to safeguard the Lender's collateral, turn around the operation where possible, and/or prepare the dealership for sale. **Our bottom-line goal is putting the store in optimal operating condition so the lender can generate maximum returns and/or get the highest possible acquisition price from the best possible purchase candidates.**

As former dealership operators, CFOs, turnaround consultants, and CROs, our interim dealership leaders understand the difference between liquidating assets and maximizing asset value...the difference between sitting in an office with spreadsheets and going out into the dealership to improve customer satisfaction and business performance.

InnovAuto Interim Store Leadership deliverables include:

- ▶ Efficient and rapid fact-finding and analysis to determine the scope and severity of the dealership's situation
- ▶ Identification of necessary changes in process, people, and operational and financial management
- ▶ Detailed improvement plan including specific actions, improvement targets, timeline, and assigned responsibilities
- ▶ Continuous written and verbal communication with the Lender

InnovAuto Group is also able to work in situations where the current owner and/or management are still in the store (e.g. during notice of termination periods).

Lender Benefits of InnovAuto's Interim Store Leadership Services

Objectivity in problem identification and solution ensure the shortest path between operational crisis and improvement or sale.

Though a combination of risk mitigation and strategic asset handling, InnovAuto's experienced CROs preserve maximum asset value for dealership re-launch or sale.

Expertise in dealership operations, financial management, and transformational consulting further accelerates needed change in people, process, and performance management.

InnovAuto's extensive experience and connections within the North American automobile industry enable it to—if and when needed—help debtors, Lenders, and OEMs find dealership buyers.



About InnovAuto Group, LLC

InnovAuto Group, LLC is a team of industry professionals whose mission is to aid the century-old North American automobile industry in successfully addressing the realities of both the present and future.

InnovAuto Group, LLC (www.InnovAutoGroup.com) provides solutions to the auto industry at large, including Manufacturer Distribution Organizations and their Field Representatives; Dealerships and their Suppliers; Lenders, CPAs and Law Firms; and to Municipal, State, and Federal Government Agencies.

Our team consists of practitioners representing the full breadth of auto industry operations: OEM product, marketing, and distribution executives; owners and managers of retail automotive operations; dealership CFOs, CPAs and attorneys; government relations specialists; and experts in supporting dealership facility, technology, marketing communication, human resource management, and business operations.

Because each of our members has decades of industry experience, InnovAuto Group LLC has been through multiple economic downturns and is capable of advising and handling the unique issues arising when the economy puts OEMs, dealerships, financial institutions, and the public interest at risk.

InnovAuto Group, LLC Lender Services Contacts

Mr. Don Ray, CPA, CSP
Treasurer and Board Member
InnovAuto Group, LLC
4710 Princeton Road
Memphis, TN 38117
917-359-5128 (mobile)
dray@innovautogroup.com

Ms. Barbara A. Jerich, JD
General Counsel and Board Member
InnovAuto Group, LLC
6604 Indian Hills Road
Edina, MN 55439
612-760-7900 (mobile)
bjerich@innovautogroup.com

Mr. Mark Rikess
Founder, Chairman of BOD
InnovAuto Group, LLC
6671 Sunset Boulevard
Los Angeles, CA 90028
916-715-8129 (mobile)
mrikess@innovautogroup.com

Mr. Brad Bowers, CPA
Partner and Lender Services Practice Leader
InnovAuto Group, LLC
2525 Topaz Dr
Boulder, CO 80304
(209) 261-7538 (mobile)
bbowers@innovautogroup.com

Mr. James F. Williams
Managing Director
InnovAuto Group, LLC
1289 Sylvandale Road
Mendota Heights, MN 55118
602-978-0578 (mobile)
jwilliams@innovautogroup.com

Please visit us on the web at www.InnovAutoGroup.com.

NOTE: InnovAuto does not provide tax or legal counsel.