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# Truck Times

The Financial Side of the Trucking Industry

*In this issue:*

**Make Everyone in the Trucking Company Responsible for Profit**
*page 2*

**Managing Cash and Profitability in a Declining Freight Environment**
*page 3*

**New Excise Tax Exemptions on APUs**
*page 4*

**SAS 109 and the Impact on Trucking Companies**
*page 5*

**The ESOP Opportunity**
*page 6*

**Redefined "Commercial Motor Vehicle" Exempts Trailers from the URC Fees**
*page 7*

**Here and There in the Trucking Industry**
*page 8*



## Make Everyone in the Trucking Company Responsible for Profit

**By Tim Almack, CPA**
Partner
talmack@ksmcpa.com

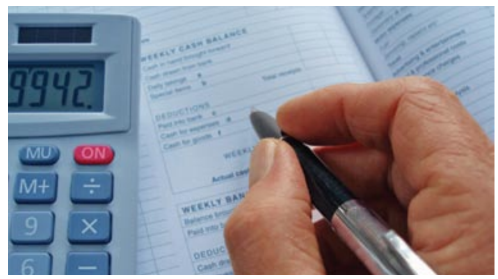
Profit is really a state of mind. In fact, it's the fuel that powers trucking companies.

The idea that the profitability of a trucking company depends solely on the owner or CEO is the traditional mindset and it, along with other ideas, has become antiquated, especially in this difficult economic environment. Profit should be the responsibility of the entire management team, properly called a "profit team." Without profits a business' opportunities are restricted. Most other business activities can be designed to achieve that goal. Should a company's goal be to run 2,700 miles per tractor per week? No. The goal is to utilize equipment efficiently and at a reasonable rate per mile to make a profit!

Business and financial goals are too often nondescript and arbitrary. Financial goals should be measurable, manageable, specific and understood by the management-profit team in order to relate them to the bottom line.

CEOs and managers alike share the fallacy that profitability belongs only in the hands of the CEO, and others should perform only the tasks in their job description. Wrong again. Every person on the management-profit team needs to be responsible and directly accountable for the profitability of the company. So what if a salesperson meets his goal of selling a certain dollar of freight revenue. The sales may have caused inefficiencies in the freight utilization. The question to be asked in assessing the success of a sales manager is not, "How much did your salespeople sell?" but "How much profit did they make for the company?"

Start working on changing the company mindset to reflect this profit philosophy. Then begin to filter that attitude down. Make sure the management-profit team accepts responsibility for contributing additional profitability to the company. Of course, attitudes and thought processes cannot be transformed overnight or by mandate. The management-profit team must be completely aware of the role they play in improving the organization's bottom line and should understand that the profit commitment must be developed. In this environment it becomes evident that "profits" are a state of mind.





*"Every person on your management-profit team needs to be responsible and directly accountable for the profitability of the company."*

Profit is not an unspeakable word - it is the reason organizations exists. Profits pay salaries, help expansion and make going to work fun. Obvious? Not always. There is an interrelationship between an organization's profits and a manager's success. The next step is to teach the management team to redirect their thinking so that profits are a state of mind. All other tasks support the profit goal.

Help managers and staff generate greater profitability by giving them this quiz. Doing so will determine whether the company has the all-important profit mentality.

Continued on page 7. See "*Profit.*"

## Managing Cash and Profitability in a Declining Freight Environment

**By Mark Flinchum, CPA**
Partner
mflinchum@ksmcpa.com

Freight volumes continued to decline through the end of 2008, and while available capacity and fuel prices also declined, possibly allowing for some recovery in rates among those trucking companies still standing, the freight volume declines outpaced retracting capacity. Industry experts are now looking to 2010 for a sustained recovery.

With economic uncertainty and the financial markets' lack of confidence to provide credit in the coming months, many operators are considering options for weathering the storm. While some have chosen to park equipment, others that have decided to sell underutilized equipment have met a declining price environment for used equipment. However, downsized fleets and dumping of unprofitable lanes have increased unit revenue.


Large carriers have focused on the more profitable areas of intermodal, dedicated, regional and brokerage business, leaving the less profitable conventional long-haul truckload market to those willing to compete in this rate challenged area.

The worldwide economic slowdown is likely to put financial strains on even the strongest and best run trucking companies. Historically, consumer spending has represented over 70% of the Gross Domestic Product. Tighter consumer lending standards and the move by people to increase savings in reaction to significant market losses will simply mean less consumer goods to ship. Bank financing to trucking companies, if available, is projected to be more expensive with only top tier borrowers of the highest quality obtaining credit. The aggressive lending practices of the past appear to be over. Trucking companies should be careful to monitor their accounts receivable exposure and be proactive on any slowing of collections, as the industry has experienced a large increase in losses due to bankruptcies.

While no one solution is the answer when dealing with these extraordinary economic times, steps should be taken to manage the impact on operations. To improve cash flow, implement a rigid cash management system that includes reducing or postponing capital expenditures. Preparing a weekly dashboard report of the expected cash outlays as well as expected receipts and updating the expectations daily will allow for proper prioritizing of expenses.

Understand the credit worthiness of shippers. Analyze customer segments and determine when credit should be extended and more importantly when credit shouldn't be extended due to the economic risk of their products being shipped (i.e. automotive related industries). Review traffic lanes and determine the profitability after factoring in back haul rates, dock delays, days outstanding on accounts receivable, and equipment demands to service. Evaluate whether operations have unnecessary redundancies that can be eliminated.

Know the strength of vendors. Remember, company suppliers are experiencing the same economy and are not immune to these same issues. Consider negotiating better payment terms with vendors to improve current cash flow. Have alternative suppliers available and ready to step in should a key vendor go out of business. As a vital partner, know how the bank views the industry and the company. Nothing can replace open, honest and frank discussions about the company's plans and outlook. Start renewal discussions in a timely manner and evaluate options such as debt restructuring as to term, interest rates and even debt forgiveness.

Consider an economic disaster team or crisis monitoring team to review early warning indictors in the company and measurement issues outlined above. Create a flexible financial model to review the impact on operations of a worst case scenario, a certain percentage decline in freight volume, and declines in pricing; use real world factors to measure the effects on operations.

Nothing lasts forever, and this economic slowdown too shall pass. Be prepared to take advantage of opportunities as freight volumes increase and determine the right timing of investment to add capacity.

## Carbon Footprints and the New Excise Tax Exemptions

**By Mark Reuter, CPA**
Manager
mreuter@ksmcpa.com

An obscure provision of The Emergency Economic Stabilization Act of 2008 (EESA) awarded The National Academy of Sciences (NAS) $1,500,000 to undertake a comprehensive review of the Internal Revenue Code to identify tax provisions having the largest effects on carbon and other greenhouse gas emissions, and report back to Congress no later than October 4, 2010. The transportation sector is a top carbon creating activity, and there's little doubt the Congress will be looking to the transportation sector as a place to reduce carbon emissions. Currently, many carbon reducing investments require capital equipment upgrades, and Congress could use tax credits and other tax code provisions to help transportation companies retool, as another provision of the EESA did.


In a move that provides immediate help to the transportation sector, the Congress exempted auxiliary power units (APU) and advanced refrigerated trailer insulation from the 12% federal excise tax on tractors and trailers for purchases after October 3, 2008. Congress recognized pushing for less pollution from transportation activities on one hand and taxing APU on the other hand was counterproductive.

The APU exemption called for the Administrator of the Environmental Protection Agency, in consultation with the Secretary of Energy and the Secretary of Transportation, to determine which APU reduce idling at rest stops or other locations where truck are temporarily parked or remain stationary. A Senior Revenue Agent in the IRS Excise Tax Division said no certification would be necessary and the exemption would be granted to any equipment that reduced idling. Based upon this explanation, the small engine auxiliary power units clearly qualify for the exemption, but it also seems likely the automotive shut-down/start-up systems, battery powered systems, fuel operated heaters and other equipment would qualify for the exemption.

*"The transportation sector is a top carbon creating activity, and there's little doubt the Congress will be looking to the transportation sector as a place to reduce carbon emissions."*

With the current economic climate, most truck and trailer manufacturers expect equipment purchases to be down for 2009, but purchases of equipment with quick pay-back periods, like APU, might still make sense. The 50% bonus depreciation officially ended on December 31, 2008, but many people expect the extension of the 50% bonus depreciation for 2009. There also seems to be some sentiment for allowing net operating losses to be carried back 5 years. We should know whether these provisions will make it into law in the next couple of months. With these provisions in place, equipment purchases and upgrades might make sense, and provide additional cash flow opportunities for transportation companies.

## SAS 109 and the Impact on Trucking Companies

**By Rick Lich, CPA**
Manager
rlich@ksmcpa.com

A year ago, implementation began on a new suite of audit risk assessment standards. Included in that suite of standards was the Statement on Auditing Standards No. 109 (SAS 109), Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement.

SAS 109 formalized the link between the risk of material misstatement in an entity's financial statements and the overall operating environment of an entity. SAS 109 requires the auditor to obtain an understanding of the risks associated with the entity's regulatory, legal and political environment, including environmental requirements and industry risks. When significant risks exist, the auditor is required to evaluate the design of the entity's related internal controls and determine whether the controls have been implemented.

As auditors, the "control environment" is considered very important to the assessment of risk of material misstatement in the entity's financial statements. The control environment sets the tone of an entity and influences the control consciousness of the entity's employees. The control environment is also the foundation for all other components of internal control and provides structure and discipline throughout the entity.

What does this mean to trucking companies? SAS 109 puts an emphasis on the fact that documentation of a control procedure does not demonstrate that the control is actually operating as intended. Auditors, therefore, should go the next step and determine if the control has been implemented by performing inquiries, inspections and walkthroughs of the entity's key controls. Determining operational effectiveness of the control, however, is not a requirement of SAS 109.

SAS 109 has expanded the scope of auditors' internal control inquiry, inspection and walkthroughs. In order to obtain knowledge about an entity's business and the industry in which it operates, auditors will make inquiries of management and others within the entity, such as operating personnel not directly involved in the financial reporting process, employees involved in initiating, recording, or processing complex or unusual transactions, human resources and in-house legal counsel.

Auditors use the information obtained to tailor their audit procedures to address the specific risks of the entity. In determining what actions to take, auditors will examine not only controls such as segregation of duties, but also how managers monitor compliance, as well as the procedures organizations use to review and improve their internal controls. Accordingly, management should consider setting aside some time to discuss their organization's internal control environment and documentation requirements internally prior to meeting with outside auditors.

Developing internal control documentation may be difficult for some small to mid-size trucking companies. Documentation can come from many sources, and it is possible companies already have internal controls documented without realizing it. Companies should consider policies and procedures manuals, employee handbooks, job descriptions and the unwritten company culture. For example, smaller entities might not have a written code of conduct, but instead develop a culture that emphasizes the importance of integrity and ethical behavior through oral communication and management by example. The absence of documentation may or may not be a control deficiency but, it certainly does not hurt to have the documentation in place.

While SAS 109 has added a greater documentation requirement to financial statement audits, it has also assisted auditors in gaining a better understanding of the entity, its control environment and thus, becoming better auditors and advisors. SAS 109 has also assisted trucking companies in evaluating their internal controls and strengthening those controls where they can.



## The ESOP Opportunity

**By Andy Manchir, ASA, CMA**
Manager
amanchir@ksmcpa.com

Business owners can use Employee Stock Ownership Plans (ESOPs) as part of their succession planning strategy. As a tax-advantaged alternative to third-party sales, a sale to an ESOP should be considered by a business owner assessing their succession planning options.

**ESOP Sale Alternative**

Having key managers and employees take over operations when business owners retire is appealing. However, since many of these key employees have limited capital to fund a management buyout, using an ESOP as part of this buyout structure can make the transaction possible.

An ESOP can borrow funds to acquire company stock, thereby financing a buyout in a more tax-efficient manner, since the ESOP compensation expenses recorded for employees allows for repayment of loans with pre-tax dollars.

**Benefits of Sale to an ESOP**

Federal tax code contains provisions that favor the sale of company stock to an ESOP.

Shareholders who sell to an ESOP can defer capital gains tax payments on their proceeds, when following the guidelines set forth under Section 1042 of the Internal Revenue Code.

Additional tax advantages for companies exist, most notably for Sub-S corporations. The Sub-S corporation ESOP is not taxable on its share of corporate earnings. The taxes are deferred until employees take distribution from the plan upon retirement, death, disability or termination.

An ESOP can lead to the development of an employee-ownership culture, one that empowers and rewards employees for their efforts, by demonstrating the financial benefits of ownership and sharing company performance data in a way that emphasizes how each work group contributes to success.

**Indiana ESOP Initiative**

Indiana State Treasurer Richard Mourdock recently launched the “Indiana ESOP Initiative” (IEI) for the purpose of assisting Indiana businesses in becoming ESOP companies. Prior to running for statewide office, Mourdock served as an officer of an ESOP-owned company. This direct experience with the benefits of employee ownership served as the catalyst for his support of ESOPs as State Treasurer.

The Indiana ESOP Initiative will allow for a “Linked Deposit” program that will reduce the borrowing costs for an ESOP’s acquisition of company stock. Once a company has arranged for an ESOP loan with its local bank, the Treasurer’s office will make a ‘linked deposit’ in the form of a CD with that bank. The State will then take a reduced rate of interest on that CD, and in turn the bank will provide the ESOP loan at reduced rates of interest.

Indiana has designated $50 million of state funds that may be used in this manner, with the belief that ESOP formation will help to preserve Hoosier jobs. “It’s not only critical that the state continues to bring in new jobs to Indiana, but it’s absolutely essential that Indiana keeps the jobs it currently has,” asserted Treasurer Mourdock in the IEI press release. “IEI’s mission is to encourage Indiana businesses to become ESOP companies and preserve Hoosier jobs.”

**Considering the ESOP Option**

Owners invest decades of effort to build the value in their businesses. A liquidity event will eventually occur to provide for their retirement and estate planning needs.

When owners are considering their succession plan options, an ESOP should be among the opportunities they consider. The ESOP opportunity could offer the “win-win” alternative for both owners and their employees.

## Redefined "Commercial Motor Vehicle" Exempts Trailers from the UCR Fees

**By Troy Hogan, CPA**
Manager
thogan@ksmcpa.com

On October 16, 2008 President Bush signed H.R.2095: Rail Safety Enhancement Act of 2008 into law. This Act redefines the term "commercial motor vehicle" and exempts trailers from the Unified Carrier Registration (UCR) fee calculation. This change will start with the 2010 registration; there is no change to how the 2009 fees are calculated.

The UCR program is a federal registration program enacted under the Unified Carrier Registration Act of 2005. The UCR replaced the Single State Registration System (SSRS) program on January 1, 2007. Unlike the SSRS program that applied only to interstate for-hire carriers, the UCR applies to all interstate motor carriers, interstate freight forwarders, brokers and leasing companies.

The UCR fees range from $39 to $37,500 and are based on the total number of commercial motor vehicles operated by the carrier. The fees are used to support motor carrier safety and enforcement programs and pay for UCR administration. The UCR is a base-state system and there are currently 41 participating states. Due to a shortfall in collections, increased enforcement is expected. This can be done by roadside enforcement checking online records to determine whether a carrier is current with its UCR obligations. It is also expected that the 2010 fee structure will change due to the shortfall in collections and the new trailer exemption. •

## Profit *(continued from page 2)*

### Profit Mentality Quiz

1. Is there a company-wide plan for profits?
2. Are managers held accountable for various tasks that contribute to profitability?
3. Is there an inventory of untapped ideas that will add to the bottom line?
4. Is the company profit-driven rather than sales-motivated?
5. Does the company have a policy regarding the types of customers it will serve?
6. Does the business take its long-term profit objectives into account in its hiring process?
7. Has the organization determined how the demand for services may change based on the environment, competition, and so forth?
8. Does the business keep tabs on its competition?
9. Does the organization assess customer service satisfaction levels?
10. Does the organization methodically and periodically reevaluate its strengths, weaknesses, opportunities, and threats?
11. Does the business survey the management team about their business goals and objectives?
12. Does the firm have formal profit goals and objectives?
13. Does management discuss profit objectives regularly?
14. Have the profit goals and objectives been communicated to the appropriate staff?
15. Is there a written profit plan in place to achieve the organization's profit objectives?
16. Does the business periodically evaluate its profit plan accomplishments and update it?
17. Is there a profit culture in the organization?
18. Is there a commitment by the management team for improved financial performance?
19. Does every manager know what additional profits would be used for?
20. Do the employees realize that profits are their responsibility?
21. Are employees and managers rewarded for meeting profit objectives?

Be proud of the "YES's." If there are any "NO's," there is room for improvement to the bottom line. •

## Here and There in the Trucking Industry

Tim Almack attended the Indiana Motor Truck Association's Board of Directors meeting in December 2008.

Tim Almack, Mark Flinchum, Troy Hogan, Jason Miller and Ed Stohlman presented Trucking Basics 101 in November at the KSM offices.

Andy Belser and Bruce Jones attended the Indiana Motor Truck Association's Annual convention in November 2008.

Tim Almack, Andy Belser, Jason Miller and Ed Stohlman attended the National Accounting and Finance Council Meeting in September 2008.

Mark Flinchum and Chris Felger attended the Ohio Trucking Association Convention in September 2008 and the American Trucking Association Convention in October 2008.

Bruce Jones moderated a panel discussion entitled "Growing, Restructuring or Surviving - What You Need To Know About Current Capital Markets" for the Truckload Carriers Association's Truckload Academy Webcast in September 2008.

KSM's Committment to the Trucking Industry:

- American Trucking Association
- Illinois Trucking Association
- Indiana Motor Truck Association
- Kentucky Motor Truck Association
- National Tank Truck
- Ohio Trucking Association
- Truckload Carriers Association
- Tennessee Trucking Association

For more information about Katz, Sapper & Miller, please visit www.ksmcpa.com.

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KATZ, SAPPER & MILLER, LLP
800 East 96th Street
Suite 500
Indianapolis, IN 46240