AUTO TEAM AMERICA SUBMITS ITEMS TO IRS INDUSTRY ISSUE RESOLUTION PROGRAM

Auto Team America (ATA) and its member firms are always proactive in helping their clients maximize income and reduce taxes. This includes advancing tax issues in favor of the automotive industry. As part of this effort, ATA has recently submitted four items for possible selection by the IRS in the Industry Issue Resolution (IIR) Program.

The IIR Program resolves frequently disputed or burdensome tax issues that affect a significant number of business taxpayers. The IRS solicits suggestions for issues from taxpayers, representatives and associations for the IIR Program. For each issue selected for the program, the IRS works with industry personnel to understand the issue and relevant information. The Service then develops guidance to resolve the issue. Following are the four items ATA submitted to the IIR program:

1) Alternative LIFO method for used vehicles.

Certain vehicles do not appear in most official used vehicle guides, including items such as conversion vans and rare vehicles, because the publishers typically are unable to obtain sufficient data on such vehicles to publish a supportable value. The alternative LIFO method for used vehicles does not provide any guidance regarding the treatment of such items when computing LIFO for used vehicles.

ATA believes that in the interest of sound tax administration, the IRS should consider allowing a taxpayer computing LIFO under the Used Vehicle Alternative LIFO Method to exclude from the inflation index computation any items that are not listed in the official used car guide. In addition, the IRS should consider allowing taxpayers to determine the current-year cost for each used vehicle acquired via trade-in and not listed in the official used car guide, based on its actual cash value (ACV) trade-in value.

2) Optional simplified methods for automobile dealerships to use to determine the value of the use of demonstration automobiles provided to employees.

The IRS has provided guidance for the calculation of the amount that is includible in the income of automobile dealership employees who use demonstrator vehicles. However, ATA is proposing that additional clarification be provided regarding the tax treatment of dealer-provided fuel to employees whose demonstrator use is valued under one of the simplified methods.

Specifically, clarification is requested as to whether the value of employer-provided fuel is included as part of the working condition fringe for qualified automobile demonstration use, as well as included in the Daily Inclusion Amounts under the Partial Exclusion Simplified

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Method and the Full Inclusion Simplified Method.

The policy objectives and benefits of the revenue procedure could largely be undone if dealers must nevertheless ensure that their employees maintain mileage or other records to properly account for the value of dealer-provided fuel. The need to substantiate the value of this benefit would also greatly reduce the attractiveness of these methods.

3) A standardized methodology for dealers to determine the amount of interdepartmental profit that should be properly excluded in the overall computation of taxable income.

ATA is proposing a standardized methodology and also that a change to such methodology be allowed under the automatic accounting method change provisions.

New vehicle dealers operate and account for their businesses departmentally. It is an industry standard to account for transactions between departments at full or slightly reduced profit levels. This profit is then capitalized in the used vehicle inventory while reflected in the income of the parts and service departments.

ATA is proposing a methodology be established to reasonably estimate the amount of such internal profit. Such method might include factors for total internal sales, gross profit, and profit percentage for parts and service to determine an average profit percentage. Such average profit percentage could then be applied to the total amount of internal parts and service capitalized in ending inventory. The interdepartmental profit change would be common to most new vehicle automobile dealers and fit easily into the automatic provisions.

4) Allow dealers to use the Inventory Price Index Computation (IPIC) LIFO method for parts inventories while using the Alternative LIFO Method and/or the Used Vehicle Alternative LIFO Method.

The IPIC method is a simplified method for computing LIFO inflation based on Bureau of Labor Statistics data. The tax regulations provide for the use of the IPIC method but require that the taxpayer use the IPIC method for all items of inventory accounted for under the dollar-value LIFO method for a specific trade or business. However, this section states that the restriction can be avoided as provided for by exceptions in the regulations or other published guidance.

Various Revenue Procedures provide for the alternative new and used LIFO methods. However, according to these procedures, a taxpayer cannot use the IPIC method for parts and accessories inventory while using either of the alternative methods.

Most automobile dealers utilizing the LIFO method for vehicle inventories use the alternative methods due to the complexity and uncertainty of other methods. This limits the ability for these taxpayers to also use the LIFO method for their parts and accessories inventories. ATA is requesting that the IRS should consider permitting a taxpayer to use the IPIC method for parts and accessories while using either of the alternative methods.

Auto Team America and its member firms will continue to update clients and other dealerships on the status of these submissions to the IRS. For more information, please contact your local ATA member firm.

TAX TIP

MOVEMENT TO REPEAL ALTERNATIVE MINIMUM TAX NOW IN CONGRESS

The Alternative Minimum Tax (AMT) was created to ensure that all taxpayers pay a minimum tax because there was a growing trend in which some high-income taxpayers were able to significantly reduce or eliminate their regular tax. These high-income taxpayers took advantage of our tax laws, which give special treatment to certain types of income and which allow special deductions for certain expenses.

Initially targeted at the wealthiest taxpayers, the tax is now clipping even lower-middle income Americans. When the law was passed, the number of targeted taxpayers was very small—approximately 0.1 percent of all individuals.

Now the number of taxpayers facing potential AMT liability is expanding exponentially due to *bracket creep* caused by inflation, the growth in incomes, and by the classification of commonly used exemptions and deductions as *tax preferences*. While approximately 3.5 million individual taxpayers were subject to the AMT in 2004, estimates indicate that the AMT will affect 33 million taxpayers by 2010. Many dealers were, are and/or will be subject to the AMT.

Currently, H.R. 1186, The Alternative Minimum Tax Repeal Act of 2005, sponsored by Rep. Phil English (R-PA), is making its way through Congress with the aim at repeal of the AMT statutes. Endorsement of this bill by as many dealers as possible could influence a favorable outcome of repealing the AMT.

DEFROST YOUR FROZEN ASSETS: HOW YOU CAN FREE UP CASH QUICKLY

Did you make a profit but wonder what happened to your cash? Good question. Most of the time, *frozen assets* in your store are the culprit.

Frozen assets are store assets that do not turn to cash quickly. Owning these frozen assets is expensive—and will become even more expensive over the next few months should interest rates rise. When rates increase, excess inventory, slow moving receivables, and other dead weight balance sheet items will become much more expensive to own.

The first step in defrosting frozen assets is to uncover where they are hiding. A good first step is to analyze your store's cash flow. For example, which balance sheet items are turning to cash quickly? Which ones are eating it? This is actually a very easy process; unfortunately, most dealerships don't even have a cash flow report.

The next step in defrosting frozen assets is to review your schedules with a vengeance. Which assets are not turning to cash? Don't just look at the overall aging of receivables or inventory items—actually drill down to the detail schedule and highlight each old item.

For assets that are unscheduled, review the detail transactions comprising the balances. Once these problem assets are identified, get your "blowtorch" and start thawing-out—collect, sell, liquidate, or write-off—these assets as quickly as possible.

There are tools developed by dealer services accounting professionals that can help you immediately identify your frozen assets. A cash flow report will quickly tell you where your frozen assets (in total) are hiding. Additionally, there are means of drilling down electronically into your computer system to identify the detail transactions causing the problems.

For further information on this topic, contact your Auto Team America member firm.