LIFO Repeal Would Create Huge Tax Increases for Dealerships

Another repeal of the last in, first out (LIFO) inventory accounting method was proposed in October as part of the Tax Reduction and Reform Act of 2007. The elimination of LIFO would result in significant tax liabilities for thousands of small and large American companies including dealerships.

While this particular bill has little chance to pass in an election year, it's noteworthy because repealing LIFO was proposed separately by both political parties. So the risk of elimination exists regardless of which party gains power during the next election cycle.

Help stop the elimination of LIFO

Although, the bill won't be considered until the second session of the 110th Congress in 2008, industries are strongly urging Congress to reject any effort to repeal LIFO. On behalf of dealerships, the National Automobile Dealers Association (NADA) is fighting to maintain the use of LIFO. You can help protect LIFO by sending a message to Capital Hill.

Negative impact on dealerships

Repealing LIFO would bring substantial tax increases by requiring companies currently using the accounting method to report their LIFO reserves as income. It is assumed any elimination of LIFO would include a phase-out period that would ease the cash flow impact on a dealership. The most recent bill included a 10-year phase-out for LIFO, although the mechanics of the phase-out were not available.

Why is LIFO under attack again?

The assault on LIFO is fueled by two unrelated factors: the oil and gas industry and international accounting standards.

Oil and gas industry

the oil and gas industry is the largest beneficiary of LIFO. With record oil company profits and rising fuel prices, removing a perceived tax break for this industry will be viewed positively by the public.

International accounting standards

For years, there's been a push for conformity between international

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New Vehicle-Pool LIFO Method Could Cut Your Tax Bill

Highlights

- Auto dealers using LIFO could receive significant tax breaks by changing to the new Vehicle-Pool Method to group cars and light trucks into one pool.
- The revenue procedure generally becomes effective for tax years ending on or after December 31, 2007.

Dealerships that use the last in, first out (LIFO) inventory accounting method should consider switching to the new IRS Revenue Procedure 2008-23 (Vehicle-Pool Method). Grouping your car and light-truck LIFO pools into a single pool might result in substantial tax savings.

This revenue procedure provides an alternative dollar-value LIFO method for determining the proper vehicle pooling method for retail dealers of cars and light-duty trucks. It was issued by the IRS on March 7, 2008, and offers clarity on how to treat crossover vehicles for LIFO inventory purposes. The Vehicle-Pool Method generally becomes effective for taxable years ending on or after December 31, 2007.

How does the Vehicle-Pool Method work?

The new revenue procedure allows for resellers of new vehicles (cars and light-duty trucks) to establish one pool for all new vehicles in inventory. Resellers may also elect to have one pool for used vehicles. Vehicles with a gross vehicle weight that exceeds 14,000 pounds are excluded.

Who should consider making this election?

If you're on LIFO, your dealership should be analyzed to determine if this election makes sense for you. The new single pool LIFO revenue method could benefit auto dealers who:

- Have filed their 2007 tax return, but the benefits would be worth the effort to amend the return.

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financial accounting standards (IFRS) and U.S. generally accepted accounting principles (GAAP). And LIFO is not allowed under international accounting standards.

If the U.S. principles are changed to agree with international standards on LIFO, American companies would have to stop using LIFO in order to comply with GAAP. An existing requirement in the tax code requires all taxpayers using LIFO for tax purposes also use LIFO for financial statement purposes. This conformity requirement would force all companies changing from LIFO for financial statement purposes to terminate their LIFO election for tax purposes.

If this occurred, LIFO would be effectively eliminated without any action by Congress for any company issuing GAAP-based financial statements. Congress, however, would like this "revenue raiser" to be included in legislation to help keep any spending or tax bill "revenue neutral." So Congress will likely act in advance of any conformity initiative by the Financial Accounting Standards Board (FASB).

The issue could be solved if Congress eliminates the LIFO conformity requirement in the tax code, which would allow companies to remain on LIFO regardless of any action by FASB. But there appears to be little appetite for this in Congress. In the past, intense lobbying from affected industries, including NADA, prevented Congress from acting, but the tide is clearly turning.

For more information on how the elimination of LIFO would impact your dealership, please contact your local ATA representative.

(***Tax Bill Cut** continued from page 1)*

- Have filed their 2007 return and don't want to amend, but do want to look into it for 2008.

Advantages

If right for your dealership, the single pool LIFO revenue method will:

- Decrease taxes by protecting prior year LIFO layers in a year where there is a decrease in one or both inventory pools.
- Eliminate confusion over whether a crossover vehicle should be categorized as a car or a truck.
- Alleviate the administrative burden of tracking separate pools for cars and light trucks.

Disadvantages

If a dealership is looking to reduce its LIFO reserve, using the single pool LIFO method could be counterproductive, but in certain situations could actually decrease your LIFO tax benefit.

How to make the single pool LIFO election

To comply with Revenue Procedure 2008-23, a dealership is required to file IRS Form 3115, Application for Change in Accounting Method, with the income tax return for the year of the change. Electing the vehicle pool method is an automatic change, which means there is no user fee due with Form 3115.

And for those auto dealers that have already filed your 2007 tax return, you may file an amended return with Form 3115 for 2007 (under relief provisions provided by the IRS to make this election).

For information on determining how the single pool LIFO revenue procedure would impact your dealership, contact (your ATA representative) or access the IRS bulletin on Revenue Procedure 2008-23.

TAX TIP

ABOVE-THE-LINE DEDUCTION AGAINST INDIVIDUAL INCOME TAX

Legislation was introduced on November 19, 2008 designed to create jobs and help the auto industry. The package includes two new "above the line" deductions for interest payments on auto loans and state sales/excise taxes on autos. Both would apply for new autos or light trucks purchased after Nov. 12, 2008 and before Jan. 1, 2010. There is no requirement that the auto or light truck be manufactured in the U.S. Both new deductions to arrive at adjusted gross income would phase out beginning at $125,000 of modified AGI ($250,000 for joint filers).

This legislation would save jobs in the American automobile industry and help consumers get the economy back on track. It is simple, it is straightforward, and it is bipartisan. The legislation is meant to stimulate demand in the automobile industry so people actually come into showrooms and buy cars, minivans, or light trucks. Why is this a good idea? Actually, if you buy a car, someone has to make it, someone has to sell it, someone has to service it, and someone has to provide administrative services. This is good for manufacturers, the dealers, and the suppliers. It could save considerable jobs in the auto industry. The bill is about jobs, jobs, jobs. Six million jobs are at stake in the American car industry. One out of ten jobs in America relies on the auto industry. Right now, the facts are gloomy. Sales are down. The auto industry has already cut over 100,000 jobs. The 30,000 American dealerships in this country are at risk of losing 37,000 jobs. We cannot let this happen. We cannot let the American automobile industry implode.

The bill is simple. If you buy a passenger car, minivan, or light truck between November 12 of this year and December 31 of 2009, you will get a tax deduction for your sales or excise tax and the interest on your loan. Families can save anywhere from $2,000 to $5,000.

This is a big deal because, next to the purchase of a home, the purchase of an automobile is the next big ticket item.

It is targeted at families with an income under $250,000 a year. It focuses on the middle-income and the middle-class family cars. It is also timely because we need to know that the biggest 6-week period for automobile sales is between Thanksgiving and New Year's Eve. They sell other cars during 6-week periods, but between Thanksgiving and New Year's Eve is the biggest 6-week sale. This bill also helps the environment because it gets more people in more fuel-efficient cars.

This bill is not limited to only American cars. It focuses on any car, recognizing that many automobiles are now made in southern States, as Texas does Toyotas; Kentucky does Toyotas; Tennessee does Nissans. Any way we look at it, even though it might have a foreign logo, it is American jobs doing the manufacturing.

By making interest payments and sales and excise taxes deductible, this program will help middle-class families afford the cars, SUVs, and light trucks they need to get to work and take their kids to school. This should mean real savings to middle-class families who are struggling to pay a mortgage or rent, buy groceries, and afford health care.

This proposal also helps the struggling auto industry and millions of jobs that are dependent on them: auto suppliers, steel and glass manufacturers, and the car dealers.

In this troubled economy you may wish to contact your Legislator to have him support this bill.