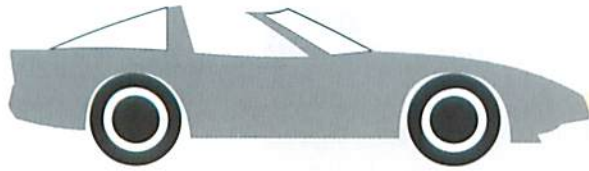




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# HEADLIGHTS

A PUBLICATION  
OF THE AutoCPAGroup

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## ANOTHER YEAR IS COMING TO AN END: ARE YOU READY?

**W**e are rapidly approaching another year-end. If you have not already been preparing, it is not too late to take advantage of some last-minute tax planning. It is also an opportune time to review your strategic goals and other operational issues.

**New- and used-vehicle LIFO:** The White House and Congress continue to suggest repealing the last-in, first-out (LIFO) method of inventory valuation as a way to generate revenue. So far, the lobbyists representing those on LIFO have won. Don't be surprised though if, at some point in the future, LIFO gets repealed. Until then, LIFO may be an effective tool for deferring income tax.

If you lost a franchise and were using the LIFO method, you will want to be sure to spend extra time with planning this year. The IRS has issued new guidelines allowing dealers to pay the tax on recapture over several years under certain circumstances. Consult your AutoCPAGroup adviser for the most advantageous method of dealing with this issue.



**Bart Haag,  
CPA  
Albin, Randall  
& Bennett**

Over the past several years, used-vehicle LIFO has not been as attractive due to declining used-vehicle prices. This year, however, with the Cash for Clunkers program, used-vehicle prices may make LIFO more attractive. It is certainly worth considering.

**Depreciation:** Fifty-percent bonus depreciation was extended this year. To qualify, equipment must be new, tangible property purchased in 2009. The amount available for Section 179 expensing was increased to \$250,000 for 2009. Companies with total purchases of \$1,050,000 of qualifying purchases cannot use Section 179. Only certain property qualifies. Your AutoCPAGroup adviser can assist.

**Tax incentives for your customers:** The American Recovery and Reinvestment Act of 2009

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### WINTER 2010

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**FRANCHISE  
TERMINATIONS  
AND LIFO**

includes tax incentives for your customers, too. In addition to the traditional depreciation benefits your customers can enjoy, they can also deduct the state and local sales and excise taxes they pay on qualified new vehicles. Certain restrictions apply, but this could be a marketing opportunity for you leading up to the end of the year.

**Estate-planning opportunities:** Even though this has been an especially tough year for many of you, it could create an opportunity to efficiently transfer your family-owned business, dealership, real estate or other assets. Business enterprise and tangible property valuations have significantly declined this year, making transfers to the next generation much more tax friendly. Also, it is unclear how much longer discounts for lack of marketability and minority interest will be allowed—politicians on Capitol Hill consider them a source of additional revenue. As of right now, though, the discounts can generate significant tax savings, combined with overall



lower valuations. Consult your AutoCPA Group adviser to learn how to transfer ownership to the next generation most efficiently. Or, if you are more charitably inclined, find out how to transfer significant assets to your favorite charity.

**Dividend tax rates:** President Obama has proposed increasing the dividend tax rate to 20% from its current

level of 15%. It appears that this change will not become effective, if ever, until sometime in 2010 or 2011. That means you still have time to consider distributing trapped earnings and profits from your S corporation. Doing so will result in a taxable dividend, but be sure and pay taxes at the lowest rate possible.

**Review estimated payments:** An often overlooked planning opportunity is simply paying your estimated payments in the most advantageous year. Generally, taxpayers must pay 100% to 110% of the balance owed from the prior year's tax return or 90% of the current year balance due at least quarterly. The American Recovery and Reinvestment

Act of 2009 allows certain taxpayers to instead pay 90% of the prior year or current year balance. Although this is potentially a cash-flow saver, it may not result in the most beneficial long-term result. Taxpayers should look at the amount they have paid and make sure it is still appropriate for their circumstances. For example, would prepaying a state estimated payment result in a larger deduction and lower federal income tax? Or, would prepaying a state estimated payment result in alternative minimum tax? At a minimum, all taxpayers should make sure to review the amount deposited with federal and state governments and do a little planning for their final estimate before the end of the year.

**Planning, planning, planning:** This has been one of the most turbulent years in history for auto dealers. Now is a perfect time to reflect on what helped you survive and possibly even prosper this year. It is also a perfect time to plan for next year. Some of the questions you should answer include the following:

- ✓ What volume do you expect to sell this year?
- ✓ Are your ordering procedures appropriate to maintain a proper supply of the types of vehicles you anticipate selling?
- ✓ Do your pay plans reflect the values or business objectives you are trying to promote?
- ✓ Is your staffing level adequate to meet your projected volume?
- ✓ How do you plan to advertise to meet your sales objectives for the upcoming year?
- ✓ Are there opportunities for expansion?
- ✓ How stable is your floor-planning source? Should you consider adding another source to diversify your lending relationships?
- ✓ Is your service department performing adequately?
- ✓ Should you consider hiring consultants to jump-start your business?

Planning can actually be enjoyable once you make time to do it and get started. The finished product can also be an excellent tool to hold employees accountable and reach your goals. Contact your local AutoCPA Group member to get started today. ☞

# FRANCHISE TERMINATIONS AND LIFO

Gregg Hamm, JD, CPA,  
Boyer & Ritter CPAs

**R**ecent franchise terminations will result in significant last-in, first-out (LIFO) reserve recapture for many dealers. To minimize the income taxes associated with this recapture, dealers need to understand their options and plan accordingly.

When a dealership on the LIFO method of inventory terminates LIFO, the recapture of the LIFO reserve is generally spread over four years. However, if the dealership ceases to operate its business, the remaining reserve is recaptured in the year the business ceases. For example, if a dealership terminates LIFO in 2009, a quarter of the LIFO reserve is included in income in 2009. If the dealership ceases to operate its business in 2010, the remaining three quarters of the LIFO reserve is included in income in 2010.

Recent Chief Counsel Advice (CCA) issued by the IRS provides guidance regarding franchise terminations and LIFO recapture. The CCA cannot be cited as precedent, but it does provide insight as to how the IRS will likely view this issue.

The CCA provides guidance on three franchise termination situations:

## 1. Loss of one of five franchises—Terminate LIFO for dollar-value pool that includes only new vehicles sold under the lost franchise

The dealership sold new vehicles at five franchises and maintained five dollar-value LIFO pools based on the vehicles sold under each franchise. One of the franchises was terminated in 2009, and all of that franchise's new vehicles were sold prior to the end of 2009. The dealership continued to sell the other four franchise brands, as well as continuing its used-vehicle and service businesses. The dealership elected to terminate its LIFO election for the dollar-value pool for the terminated franchise. The CCA provides that the dealership can spread the LIFO recapture over the four-year period, even though it does not have any inventory



items at the end of the year for the terminated franchise.

## 2. Loss of single franchise—Continue in used-vehicle and service business

The dealership had one new-vehicle franchise, which was terminated in 2009. All of the new vehicles were sold in 2009. After the termination, the dealership continued in the used-vehicle and service business.

The taxpayer elected to terminate LIFO for new vehicles in 2009. The CCA provides that the dealership can spread the LIFO recapture over a four-year period, since it is still operating its trade or business. However, if the dealership ceases to operate its trade or business, or terminates its existence, the recapture would be accelerated.

## 3. Loss of one of five franchises—Single pool method

The facts are the same as No. 1, except that the dealership elected to include all five franchises in a single vehicle pool for all new vehicles. The CCA provides that the dealership may not change from the LIFO method for a portion of the goods properly includible in a single dollar-value pool. The taxpayer may either (a) remain on dollar-value LIFO for all remaining franchises, which will likely preserve the oldest LIFO layers; (b) terminate the LIFO method for the entire dollar-value pool; or (c) change its pooling method from a single pool to a method of pooling based on the vehicles sold under each franchise agreement. The latter option would also involve changing from the LIFO method for the dollar-value pool that included the new vehicles sold under the terminated franchise. In all likelihood, converting from a single pool to multiple pools by franchise would not yield a result that makes economic sense.

## Conclusion

If a dealership has lost a franchise or will lose a franchise in the near future, the dealership should consider electing to terminate LIFO in 2009 in

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## FRANCHISE TERMINATIONS AND LIFO

(continued from page 3)

order to utilize the available four-year spread of recapture of the LIFO reserve. The facts and circumstances of each situation will need to be considered—the results can be materially different. If the dealership remains in the automobile business for four years, it will be able to utilize the entire four-year spread. However, if the dealership ceases to operate its automobile business or terminates its existence during the four-year period, the LIFO recapture will be accelerated. Please contact your AutoCPA Group member for more information. ↗

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