De Filipps' DEALER TAX WATCH

A Quarterly Update of Essential Tax Information

Volume 3, Number 4 | Publisher: Willard J. De Filipps, C.P.A. | March 1997

DEALER TAX WATCH *OUT*

If you had called me personally to ask, "What's happening lately with IRS audits of dealers and dealerships that I need to know about?" ... Here's what I'd say:

#1. IRS AUDIT UPDATE ... HOT AND EMERGING <u>TAX ISSUES</u>. There's nothing new to report on our three major "hot topics:" Demonstrators (how far does the salesman's exemption extend and how should it be computed?), Factory incentive payments (who pays the "employer's portion" of the FICA taxes?) and LIFO conformity requirements for dealership financial statements (what is allowable and what is not, and what if it wasn't done in the past?).

One emerging issue combining LIFO and Project 2000 activities relates to what happens if a dealer disposes of all the inventory of one particular manufacturer and before year-end acquires another franchise and corresponding inventory to make up for the earlier disposition. If that dealer is using the Alternative LIFO Method, recapture of all LIFO reserves should be avoided under a literal interpretation of the requirement that dealers are required to put all new autos (including demonstrators)—regardless of manufacturer—into a single dollar-value LIFO pool. It appears that in some instances, the IRS doesn't think so.

Anyone at the NADA Convention Workshop in Atlanta hoping to pick up "the latest" on IRS issues came away empty handed. Peter Kitzmiller's update simply lamented the unchanged status of these topics.

#2. <u>RELATED FINANCE COMPANIES—STILL HOT</u>. Recently released Letter Ruling 9704002 involves used car dealers with "really bad facts" who ended up by having their purported sales of customer notes to the RFC ignored by the IRS because they had no economic substance.

We have compared this unfavorable letter ruling with a more favorable letter ruling we covered a year or so ago so you can see the emerging pattern of what is more likely to be acceptable to the IRS in structuring RFC activities.

We have also included material to give you a thorough idea of what to expect from the IRS in documentation requests, interrogations and adjustments if you have a related finance company. This information does<u>not</u> appear in the April, 1996 version of the IRS' Used Car Dealer's Audit Guide which contained only an overview of RFCs.

WATCHING OUT FOR

see **DEALER TAX WATCH OUT**, page 2

Dealer Tax Watch Out

#3. "AUDIT OF DEALER BY IRS THROWS CLOUD OVER INCOME FROM *SUBPRIME LOAN POOL*." This headline caught the eyes of many readers of the March 10 issue of *Automotive News*. This article is just one of many complaining about the IRS enforcement of a change in the Internal Revenue Code made 10 years ago by the Revenue Act of 1987. Hello! This change in Section 453 eliminated the ability of used car dealers to report income on customers' installment notes on the installment method.

It would appear these complaining dealers should have been advised of this change years ago by their CPA or tax attorney. This is not a case where the IRS is exercising judgment in an otherwise unclear or debatable area. The law is quite clear and specific ... and always has been since the change a decade ago.

These articles refer to anticipated action that used car dealers hope to take by going to Congress and trying to get changes made. We wish them well... although they may simply have to accept the way the law is and move on. We certainly wish them better luck than new car dealers had in trying to enlist Congressional help with the dealer LIFO financial statement conformity fiasco.

#4. SOMETIMES THE IRS JUST DOESN'T KNOW WHEN TO STOP. Just to keep the train of thought: Item #2 talks about actual IRS audits and the judgmental area of "economic substance" involving related finance companies/entities set up by used car dealers. Item #3 talks about belated moral outrage over a change in the law made 10 years ago that the IRS is finally getting around to looking at. Still another variation on these themes relates to the pounding dealers and others take during audits when the IRS gets heavy handed and carries its position too far.

A recent Tax Court case involves a taxpayer who sued the IRS for reimbursement of legal fees where the IRS went beyond a reasonable position and forced the taxpayer to defend itself. Although the *Dealer Tax Watch* normally covers only dealer-related tax cases and issues, the Tax Court Memo Decision awarding reimbursement of legal and other costs involves *Beaver Bolt*, a case we covered previously, and provides some good information on how Section 7430 operates.

#5. MORE FRUSTRATION WITH THE IRS. One reader has sent us copies of correspondence with the IRS requesting information under the Freedom of Information Act on the treatment of demonstrators and the "salesmen's exception." His CPA firm represents several hundred dealers and it is now in

(Continued from page 1)

its **4TH REQUEST** under the Freedom of Information Act on this subject. Without going into all the details, this CPA has received a runaround that rivals the Boston and New York marathons. His determination and persistence is marvelous to behold. But it is clear that he is getting the runaround, no less. Have any of you experienced similar problems?

With the retirement of Commissioner Richardson near at hand, some D.C. lawyers have been falling over themselves complimenting the Commissioner on the great things that have happened during her "reign." For a comprehensive, contrasting point of view, read "Some Thoughts on Commissioner Richardson's Tenure at the IRS," by Kip Dellinger. He clearly vocalizes the dissatisfaction and problems experienced by many practitioners in dealing with "Fortress IRS" and the "us vs. them" mentality found in many peering over the ramparts. Before reading Dellinger's article, perhaps you should take at least two blood pressure pills or tranquilizers.

#6. TRAP IN GIFT TAX RETURNS REPORTING GIFTS OF DEALERSHIP STOCK WITH VALUATION DISCOUNTS. If you've been diligently preparing gift tax returns to report gifts of dealership stock made in 1996, you probably noticed that you **CAN'T** use the "short form" gift tax return, Form 709-A, any longer. Gifts made during calendar year 1996 are to be reported using Forms 709, as revised December, 1996 ... and these revisions slipped taxpayers a mickey.

If any gifts are subject to valuation discounts, they may not be reported on the previous short form version of Form 709. For more, see page 3.

#7. TAX COURT ACTIVITY. In two recent petitions involving dealers and dealerships, the IRS in so many words told a dealership to quit horsing around with the Arabian show horses in its "Equine Assets" department. What is interesting is how the IRS ignored the "sale transaction" which the CPA had suggested to the dealer and his dealership and charged the dealer with a constructive dividend to the extent of the "horse" expenses paid.

In another recent case, the IRS took exception with the (lack of) adequate substantiation by a dealership sales manager for his meals and entertainment deduction. This will be discussed in our next issue.

#8. COMPARISON OF IRS & LIFO SOFTWARE VENDOR NEW ITEM LISTS. If you're interested in how widely the IRS and software vendors differed in determining "new item" treatment in connection with year-end—1996—LIFO calculations, the March 1997 issue of the *LIFO Lookout* contains extensive comparisons and commentary.

see **DEALER TAX WATCH OUT**, page 28

IRS CHANGE IN REPORTING VALUATION DISCOUNTS GIFTING DEALERSHIP STOCK ON FORM 709 GIFT TAX RETURNS

FORM 709

THE UNIFIED TRANSFER TAX & GIFT CONSIDERATIONS

Since 1976, our *unified transfer tax system* has resulted in taxable transfers being taxed according to a single tax rate schedule regardless of whether these transfers were made during a donor's lifetime or at death. The "old"- and previously separate $30,000 lifetime gift tax exemption and $60,000 estate tax exemption were replaced by a single unified credit which is $192,800 and exempts the equivalent of $600,000 of property transfers from the unified transfer tax.

This unified credit can be used to offset both gift and estate taxes and, since 1987, it has been fully phased in at the $192,800 credit or $600,000 exemption equivalent amount. Thus, the general result is that transfers of wealth are now subject to the same transfer tax whether or not the donor is alive at the time of the transfer. Rates for gift and estate taxes—as now *unified*—range from 18 percent to a maximum of 55 percent for transfers in excess of $3 million.

In 1981, the Economic Recovery Tax Act / ERTA, resulted in a major change when—in the name of "simplicity"—it removed from the unified rate structure the appreciation occurring on gifted property from the date of gift to the date of death for all gifts where the donor survived the gift by 3 years. Accordingly, despite the unified transfer tax, **lifetime gifts are almost always far more attractive** than deathtime transfers for several reasons.

1. There is a $10,000 annual gift tax exclusion which is available on a per donor, per donee basis.

2. This $10,000 annual exclusion is doubled so that spouses can together give $20,000 per donee, per year, whether or not they each own an interest in the asset being gifted.

3. The point in time at which lifetime gifts are valued is as of the date of gift and not the value as of the date of death. In other words, by gifting property that is likely to appreciate, the post-gift appreciation is eliminated from the donor's estate (if the donor survives the gift by 3 years).

4. Post-gift income generated by the gifted asset is removed from the donor's estate and therefore is not subject to a transfer tax.

5. By making gifts of minority interests in a non-publicly held entity, a donor may qualify for substantial discounts. Obviously, any valuation listed must be reasonable ...but there is a wide range of possibilities and even eminently qualified experts view the value of the same company's stock very differently.

THE BOTTOM LINE is that some of the most effective gift and estate plans have been accomplished by small, steady doses of annual gifts at or just below the minimum $10,000 per donee exception. Coupled with spousal consent, significant amounts of value, both current and future appreciation, can be—and have been—transferred over time to children and other donees and often with significant annual reduction in income tax burdens.

Lifetime gifts and the resulting special exclusions and treatments summarized above should not necessarily be taken for granted. They are available today—and current talk of "liberalization" or even repeal of the estate tax may not come to pass—or may come to pass with various adverse trade-offs.

VALUING DEALERSHIPS AND OTHER CLOSELY-HELD BUSINESSES

Even in the hands of qualified and experienced appraisers, the valuation of stock in a closely-held company is an inexact science. In one tax case, the Court quoted Winston Churchill's phrase "gross terminal logical inexactitude" to describe the usual result of efforts to value stock in a closely-held corporation.

Factors to be included in determining fair market value include:

1. Value of the business assets, including goodwill,
2. The company's net worth,
3. Prospective earning power,
4. Dividend paying capacity,
5. Economic outlook for the industry,
6. History of the business, and
7. Size of the block of stock to be valued (re: discount matters).

Lists like this are of limited help in coming to grips with the twin issues of valuing a company/dealership and arriving at discounts from that value for lack of marketability and minority position holdings. Just

see **GIFTING DEALERSHIP STOCK...**, page 4

about every AICPA Auto Dealership Conference and most other CPA gatherings include presentations on how to value dealerships and/or closely-held businesses.

DISCOUNTS IN VALUING (DEALERSHIP) STOCK ...ARE THEY GETTING OUT OF HAND? IS 50+% TOO MUCH?

The IRS certainly has its hands full in auditing the valuation of closely-held businesses—and other entities—in estate and gift tax returns. Its loss last year in the *Mandelbaum* case (69 TCM 2852 (1995)), along with other recent developments—such as a barrage of technical advice requests involving Section 2703 as its latest attack on valuation discounts in family limited partnerships and the *Murphy* and the *Frank* cases—represent just the tip of the iceberg.

Basically, there are two discounts business appraisers take against the value of a business: one for the lack of marketability and the other for a minority interest holding. Some 15 years ago, one could easily claim, justify and settle with the IRS for a combined 25% discount. Over the more recent years, the range for the combined discounts has moved up to somewhere between 35% and 40%. If one was willing to persevere when resisted by the IRS on audit, even greater discounts could be obtained if one was willing to incur the legal costs to carry the fight further. Larger estates probably could get between 40% to 45% ...or even as much as 45% to 50%.

The *Mandelbaum* decision allowed the use of IPO (initial public offering) studies and the use of studies on restricted stock as discount valuation criteria. Without elaborating on *Mandelbaum* here, just consider its implications. If looking at IPO studies supports a 45% discount for lack of marketability and looking at restricted stock studies supports a 35% discount, why not add both these numbers together, divide by two and settle for a 40% (the average when 80% is divided by 2) discount for lack of marketability?

Now, for the minority interest discount. The IRS policy can best be described as one of "putting on the blinders" and looking solely at the property gifted, not taking into account who the donor is or who the donee is or whether or not the amount (of stock) gifted is a controlling interest. Discounts for minority interests typically range from a conservative 10% to a more aggressive 20%. Consequently, if one adds as conservative 40% for the lack of marketability plus a conservative 10% for minority interest position, then conservatively do we have a 50% combined discount?

(Continued from page 3)

If one subscribes to the above reasoning, then being *conservative* and claiming meager 35% discounts could result in leaving a lot of money/value on the table and adding years to the gifting process. You can see why the IRS has its hands full and is trying to get a handle on what is going on out there.

IRS FORMS FOR REPORTING GIFTS: LONG FORM & SHORT FORM

The annual form for reporting gifts and other transfers to the Internal Revenue Service is Form 709. This form requires reporting on a calendar year basis regardless of the taxpayer's regular income tax accounting period. It is due not later than April 15 of the year following the calendar year when the gifts were made. It is possible to obtain an extension of time to file Form 709 and this is "automatic" when extending the time to file the individual's Form 1040 income tax return.

Form 709-A, Short Form Gift Tax Return, can be filed instead in certain circumstances. Form 709-A can be used by most married couples instead of Form 709—the long form—to report nontaxable gifts if they consent to split gifts. The short form gift tax return (Form 709-A) may be filed if all of the following requirements are met:

1. The donor is a citizen or resident of the United States, and was married during the entire calendar year to one individual who is also a citizen or resident of the U.S. Both spouses must have been alive at the end of the calendar year.

2. The donor's only gifts (other than gifts for tuition or medical care) to a third party consisted of present interests in tangible personal property, cash, U.S. Savings Bonds, or stocks and bonds listed on a stock exchange. A "third-party donee" is any donee other than the donor's spouse.

3. The gifts to any one third-party donee (other than gifts for tuition or medical care) during the calendar year did not exceed more than $20,000. If the donee is a charity, no part of that gift may be given to a noncharitable donee.

4. During the calendar year, the donor did not make any gifts of terminable interests to his/her spouse.

5. During the calendar year, the spouse did not make gifts of terminable interests to the donor, did not make gifts (other than gifts for tuition or medical care) of over $10,000 to any other donee, and did not make any gifts of future interests to any other donee.

6. Both spouses agree to split all of the gifts either of them made during the calendar year.

7. Form 709 was not filed for the calendar year. →

TRAP FOR REPORTING DISCOUNTS ...DECEMBER, 1996 REVISIONS

Form 709-A was revised in December, 1996 for calendar year 1996 gifts and differs from the prior form in that it specifically says on its face that Form 709-A may not be used "to report gifts of closely-held stock, partnership interests, fractional interests in real estate, or gifts for which the value has been reduced to reflect a valuation discount."

For some of the previous, more pedestrian gift tax reporting where the value of the dealership stock, after reflecting one or two discounts, was below $10,000 ... no gift tax return might have been filed or the previous Form 709-A short form might have been used in a situation where the dealership stock was owned by the dealer who made gifts to donees in excess of $10,000 (but less than $20,000 per donee) so that the taxable gifts to each donee were under $10,000 and his spouse was consenting to split the gifts. The instructions are clear that where the gift exceeds $10,000 per donee, but when split it is less than $10,000 per donee, a gift tax return must be filed where the gifted property is owned by only one of the spouses.

TIGHTENING DISCLOSURE OF VALUATION DISCOUNTS

As indicated above, the IRS has been taking the matter of discounts quite seriously and now it wants to subject any gifts of corporate stock ... or other assets subject to similar discount techniques to even greater scrutiny by allowing only the filing of the long form Form 709. Schedule A on page 2 of gift tax Form 709 now specifically asks the following question: **"Does the value of any item listed in Schedule A reflect any valuation discount? If the answer is "yes," see instructions."** There are yes and no boxes, one of which is intended to be marked.

The instructions for Form 709, the long form U.S. gift tax return, also revised December 1996 contains the following language regarding the documentation of valuation discounts: **"If the value of any gift you report in either Part 1 or Part 2 of Schedule A reflects a discount for lack of marketability, a minority interest, a fractional interest in real estate, blockage, market absorption, or for any other reason, answer "Yes" to the question at the top of Schedule A. Also, attach an explanation giving the factual basis for the claimed discounts and the amount of the discounts taken."**

The instructions also require that balance sheets and statements of net earning or operating results and dividends paid for each of the five preceding years must be attached as "supplemental documents" to support the value of gifted property.

COMMENTS

Some preparers of gift tax returns spotted the change and hoped to get around it in reporting 1996 gifts by xeroxing copies of the "old Form 709-A" and reporting gifts on the old form. Query: Typically, spouses consent to split gifts in using this form. If the "wrong form" is used for reporting 1996 gifts, would that make the consent to split gifts invalid? At least one attorney I discussed this with indicated that he felt the Service would be put on notice by the filing of the old Form 709-A and that should not be a problem. Anyone considering this "strategy" should check with their own counsel before proceeding to file using the previous version of Form 709-A.

As a practical matter, is the IRS really going to be able to audit all these returns claiming valuation discounts? What audit incentive does the IRS really have if all that might happen is that the value of the dealership is increased or the amount of the discount claimed is decreased ... but all that happens is that (a little more of) the lifetime exemption will be used up? How will agents justify their time in examining these "non-productive" audits?

ONE FINAL TRAP FOR THE UNWARY: Any gift involving a valuation discount that must be reported on Form 709—the long form—must be reported even if the donor was married and, after splitting the gift's value, it would be less than $10,000 per donee. The instructions to Form 709 state clearly: Enter "... the entire value of every gift made during the calendar year while you were married, even if the gift's value will be less than $10,000 after it is split ..."

Practitioners should be aware that if gifts involving the transfer of dealership corporate stock or other assets (whether by transfers of corporate stock, interests in FLPs or otherwise) were reduced by valuation discounts, Form 709-A can no longer be used for reporting purposes. This may require filing amended gift tax returns if the changes in Form 709, mentioned above, were overlooked. Expect gifts involving valuation discounts to continue to receive a high level of scrutiny by the IRS in the future.

RELATED FINANCE COMPANIES
LETTER RULING 9704002 DENIES BENEFITS
HOW NOT TO DO THINGS & OTHER IRS CONCERNS

RFCs

Over the last two years, articles in the *Dealer Tax Watch* have covered many of the specialized tax problems facing used car dealerships. Some of these problems relate to the classification of salespersons as employees, as in the *Martin Springfield* case in California which the taxpayer won. Other articles have involved dealers who have set up related finance entities or companies to which they transfer their subprime used car customer installment notes. We have also critiqued the Used Car Dealer Manual issued in draft form by the IRS in April of 1995 and the more "finalized" Audit Guide for Independent Used Car Dealers when it was issued in April of 1996.

Over the past month, articles in the *Automotive News* have discussed several other problems that certain used car sellers are currently facing. For example, see March 10, 1997: "Audit of Dealer by IRS Throws Cloud Over Income from Subprime Loan Pool," March 31, 1997: "Dealers Battle IRS Over Taxes on Risky Loans," and April 7, 1997: "Used Car Sellers Seek Clout in IRS Battle." These articles relate to the fact that the IRS is enforcing Section 453 as it was amended by the Revenue Act of 1987 to prohibit dealers in personal property from using the installment sale method. It is surprising that dealers and their CPAs were not aware of this change in the law made so long ago. The issue of the ability to use—or more specifically, of being prevented from using—the installment sale method in connection with the sale of used cars is not a matter of debate or interpretation. Congress settled that 10 years ago as a matter of policy! So don't be confused, the more recent audit activity coming out of the National Office is dealing with the creation of related finance entities which were set up as a way to try to get around the decade-old change that prevents installment method reporting.

Apparently some dealers and CPAs have simply ignored the change in the law and continue to use the installment sale method. The continued use of the installment sale method by used car dealers—or any other dealers in personal property—is a Category A method of accounting meaning that it involves the use of a method of accounting now specifically prohibited by the Internal Revenue Code. Anyone currently using the installment method who is prohibited from doing so should seriously consider initiating a request for permission to change accounting methods by filing Form 3115 with the National Office in Washington, DC in order to obtain the more favorable terms and conditions for taxpayers who make voluntary changes in accounting methods before they come under audit by the IRS.

This article reports on the IRS activity involving the audits of Related Finance Companies in Letter Ruling 9704002 in which the IRS National Office held that the transfer of used car purchaser/customer notes by two dealers to another wholly owned company lacked economic substance and therefore, was to be ignored for tax purposes.

The September 1995 *Dealer Tax Watch* discussed Letter Ruling 9534023 as an example of the structure and planning flexibility available to "creative" dealers and their advisors in setting up related finance companies and entities. It also showed that, if set up "properly," such entities could achieve significant tax benefits for the dealer. Letter Ruling 9704002 now illustrates a fact pattern to avoid if you want to achieve these favorable results. The September 1996 *Dealer Tax Watch* includes a "Checklist of Substance vs. Form Factors" to be considered in evaluating the "validity" aspect of related finance companies. That same *DTW* discussed seven good business and economic reasons for setting up related finance entities, as well as the tax issues created by their presence. Readers may wish to review that material for more background (or—if you're a new subscriber—call us and we'll be happy to send that material to you).

IRS IDEA OF AN *ABUSIVE* RFC FACT PATTERN

The IRS Used Car Dealer Audit Technique Guide—preliminary version dated April 1995—described an *abusive* factual pattern as follows:

"D is a retail business that sells used cars. D is a "tote the note" or "buy here/pay here" used car lot and is listed as the lienholder on the cars sold. D uses the "tote the note" concept for buyers who cannot pay cash for a used car or cannot qualify for bank financing. D finances these sales, usually for two years at the maximum legal interest rate.

"During 199X, finance company F is created with $1,500 in capital contributions to purchase notes receivable from car dealers selling "tote the note" cars. The notes are purchased at a discount. In essence, F is a factoring business. F is a S corporation, as is D. The same shareholders own both businesses in the same ownership

→

percentages. F is located in the office of D. F has no employees and does not have a business address or telephone listing of its own. D's employees maintain all of F's books and records and the address on F's return is that of the return preparer.

"F does not have any funds to purchase notes receivable from any dealership. Nor does it have a line of credit with any financial institution. It has not received any loans from shareholders or any financial institutions. F has never purchased notes receivable from any other dealer other than D. No other dealers are aware of its existence as F has no telephone listing or business address, does not advertise, and does not solicit business.

"F purchases 100% of D's notes at a 40% discount. There is no attempt to select the better performing notes. Neither party has any documentation of discount rates, the particular notes to be purchased, or other elements commonly found in factoring agreements. When D sells the notes receivable to F, the debtor/buyers are not notified that F is the new lienholder. The debtor/buyer is not instructed to make payments to F.

"D never receives cash from F at the time of the sale. Because F has no cash to pay D, intercompany accounts are set up to recognize the 60% due. D receives cash from F when F collects the notes receivable or when F factors the notes to an unrelated third party.

"F sells several of the notes receivable to unrelated entities at 40% discount. However, these entities take only the most current or best performing notes receivable. F receives cash and relinquishes its files when the sales are consummated. When D factors the notes receivable to F, D maintains control over the note files and recordkeeping for F.

"Since the law is well established that retail car dealers may not report car sales on the installment basis, D reflects all income from the car sales on the date of the sales and the losses on the sale of the notes when the notes receivable are sold to F. F, however, recognizes income as it is collected."

We shall see that the taxpayer in LTR 9704002 has many similar characteristics to this *"abusive"* pattern.

In connection with this example of an *"abusive"* RFC, the IRS identified these potential tax issues:

1. "Whether a loss incurred by a car dealer from the purported sale of notes receivable to a related finance company should be disallowed because the related finance company existed only in form and the transaction between the dealer and related finance company is a sham and lacks economic substance.

2. "Whether IRC Section 482 applies to the loss claimed by a dealer from the sale of notes receivable to a related finance company because the notes receivable were sold at less than the fair market value amount.

3. "Whether IRC Section 267 disallows a loss from the sale of notes receivable by a car dealer to a related finance company.

4. "Whether a dealer and related finance company are members of a controlled group for the purposes of IRC Section 267, thereby eligible for the special loss recognition rules of Temporary Treasury Regulation Section 1.267(f)-1T(e).

5. "Whether a car dealer is eligible for the special loss recognition rule of Temporary Treasury Regulation Section 1.267(f)-1T(e) where both the car dealer and related finance company are corporations and either or both are S corporations."

We shall see that the taxpayer in LTR 9704002 was hit with only the first challenge—a lack of economic substance—mentioned above.

ACCOUNTING METHOD CHANGE ISSUE AND REVENUE PROCEDURE 92-20

In its April 1995 Guide, the IRS indicated that the related finance company issue is a change in accounting method issue and that according to the National Office, the examiner and group manager do not have the authority to offer better terms and conditions than adjustments in the first year examined with no spread of the Section 481(a) adjustment. The Manual draft also said that "due to the **abusive nature** of this issue, examiners and group managers need to strictly adhere to the National Office's position. Examining agents are advised that as soon as examiners determine that they may have an RFC issue, they should furnish the taxpayer with a written notification of the issue because furnishing such written notification eliminates the 30-day and 120-day windows of Revenue Procedure 92-20."

The examining agent is advised to first notify the taxpayer as early as possible of all of the change in accounting method issues that will be the subject of the audit and then, after furnishing written notification, the examiner should not spend a significant amount of time on the accounting method change issues during the first 90 days of the examination. "This is because if the taxpayer files a Form 3115, Application for Change in Accounting Method, on a Category B method change during the 90-day window, the taxpayer obtains audit

see **RFCS: HOW NOT TO DO THINGS...**, page 8

protection. If, instead, the ... issue is a Category A method change, the taxpayer may be entitled to a 3-year spread of the Section 481(a) adjustment."

Agents are advised that whether a related finance company issue method change is a Category A method or a Category B method change has not been ruled on by the National Office ... yet. They are further advised that whether the change is a Category A or Category B method change only affects an agent's case processing if the taxpayer has timely filed a Form 3115 under Revenue Procedure 92-20. "If the taxpayer does not file a timely Form 3115 and you (i.e., the IRS examining agent) conclude that an RFC issue method change is appropriate, then the year of change is the first year examined and there is no spread of the Section 481(a) adjustment regardless of whether it is a Category A or Category B method change."

Examining agents are provided two other tactics to consider. First, they are told that Section 10.01 of Revenue Procedure 92-20 provides that the Service can decline to process a taxpayer's Form 3115 if to do so "would clearly and directly frustrate compliance efforts of the Service in administering the income tax laws." The agent is told that "if the examiner thinks it is not in the best interests of the Government for the National Office to process a taxpayer's Form 3115," they should contact their District's accounting method issues contact person.

Also, examining agents are alerted to give careful attention to the sequence in which examinations are commenced:

"We are identifying some used car dealers that set up RFCs by identification of the RFC return filed based on PIA codes and other techniques. This may result in the RFC return being assigned to you without the car dealer's return being forwarded or already under examination.

"If the RFC return identifies the car dealer's return, the examiner can order and obtain the car dealer's return using regular related return requisition procedures before taxpayer contact. However, the recommended procedure is to advise the taxpayer when contacted for purpose of scheduling the examination that the car dealer is also under examination. Have the taxpayer furnish the name, address, and EIN of the car dealer in the initial phone contact. Mail the appointment letter of both the RFC and car dealer at the same time and schedule the initial appointment to cover both examinations.

"The above procedure is recommended to avoid the situation of our examining an RFC and then a Form 3115 is filed for the car dealer before the car dealer return is placed under examination. If this occurs the examiner may not be able to raise the examination issue.

"This procedure only applies if the examiner has the RFC return but not the car dealer return. It does not apply if the examiner has the car dealer under examination but not the RFC. A decision to pick up the RFC return for examination can be deferred until it is determined whether the RFC issue is present."

DOCUMENT REQUEST AND ISSUE DEVELOPMENT

Examining agents are advised that if they identify a possible RFC (related finance company) issue during their audit preplan activity, a special RFC Issue Information Document Request (IDR) should be mailed to the taxpayer with the initial appointment letter. Examining agents are told that if they are not sure whether or not an RFC issue might be involved, they should "consider ascertaining this during the initial phone contact so that the RFC Information Document Request (IDR) can be mailed with the appointment letter."

Examining agents also are coached that "more so than other examinations, the examination needs to be conducted at the taxpayer's place of business. Only by observing actual business operations during the course of the examination can the examiner be assured that the relevant facts and circumstances have been adequately considered. Keep in mind our focus is substance, not form!"

WHAT TO EXPECT FROM THE IRS IF YOU'VE GOT AN RFC

A copy of the IRS' special *INFORMATION DOCUMENT REQUEST* for RFCs is on pages 12 and 13.

In addition, the IRS has developed a special questionnaire to be completed by the examining agent—not by the taxpayer or taxpayer's representative. It contains numerous questions that are to be asked by the examiner during the initial interview. The IRS *RFC ISSUE DEVELOPMENT SUMMARY QUESTIONNAIRE* is on pages 16-22.

IMPOSITION OF ACCURACY RELATED PENALTIES

Worst of all, examining agents are advised that "in cases where the facts indicate the discounting has no economic substance, strong consideration should be given to the applicability of the accuracy related penalty of Section 6662. In addition, if the facts and circumstances... indicate that the return preparer *knew* that the RFC discounting lacked economic substance, consideration should be given to the return preparer penalties of Section 6694."

→

In this regard, the IRS' Issue Development Summary instructs agents to ask during the initial interview:

1. "Taxpayer's and/or representative's opinion on the applicability of the accuracy related penalty of Section 6662 due to the RFC issue,
2. Representative's opinion on the applicability of preparer penalties due to the RFC issue."

YOU'RE IN THE CLEAR IF...

In its manuals, the IRS has indicated that a related finance company issue is based upon the facts and circumstances of the particular used car dealership or activities and the discounting of the related receivables. In the April 1995 Manual, the statement is made: "The RFC issue does not appear to apply to all 'buy-here, pay-here' plans." That guide draft indicates that the arguments identified do not apply to a used car dealer's discount transactions if... "the dealer discounts its receivables to its RFC for:

1. Legitimate business reasons,
2. At their fair market value, and
3. Perfected the form of the transactions and the RFC (i.e., title transferred and RFC legally incorporated under state law)."

All of this leads to the taxpayer in recent Letter Ruling 9704002 who was found not to be favorably situated.

THE "FACTS" IN LTR 9704002

In addition to owning several incorporated car dealerships, the taxpayer has two divisions, Division Y and Division Z (referred to as the Dealers), which operate used car dealerships. Most of the used car customers are people who are *credit-challenged;* i.e., they are unable to obtain bank financing. Dealers finance all of their sales. Payment on the notes executed by customers of Dealers was secured by the cars sold, which Dealers retained the right to repossess. Dealers included in income the total sales price as stated on the sales invoice.

In 1992, the individual owner formed Finance, which was incorporated under State law, of which he is the sole shareholder. Finance was capitalized with $1,000 in equity and a $24,000 loan from the individual. Dealers transferred to Finance their installment notes from recent sales, and employees of Taxpayer transferred the notes from Dealers' books to Finance's books. Finance never acquired any notes from any car dealer other than Dealers. Dealers did not receive any cash payment from Finance when they transferred notes to Finance. There was no fixed payment schedule for Finance to pay Dealers.

On its returns for FYE 1992, Taxpayer deducted losses that resulted from the transfers by Dealers of notes receivable to Finance. The notes were transferred for face value less imputed interest. Since the notes show no stated interest, they were discounted for an imputed interest amount. Finance acquired all of Dealers' notes, regardless of quality. Dealers have not provided the IRS with any written sales contracts for the transfers of the notes from Dealers to Finance or the terms of the sales. Finance had no employees or facilities. Employees of Taxpayer performed all administrative tasks for Finance. Taxpayer made all collections and recordkeeping functions.

The vehicle buyers were not informed that the notes were assigned to Finance. The notes were not marked that they had been assigned. The vehicles' certificate of title continued to show Dealers as the lienholders. If a vehicle was damaged in an accident Dealers, as the lienholders, and not Finance, had the right to any insurance proceeds and transferred the proceeds to Finance. Even after the notes were transferred to Finance, the customers continued to make payments to Dealers. Dealers' employees recorded the payments and performed necessary repossessions. A percentage of Dealers' administrative expenses was allocated to Finance, and Finance reimbursed Dealers for the allocated amounts.

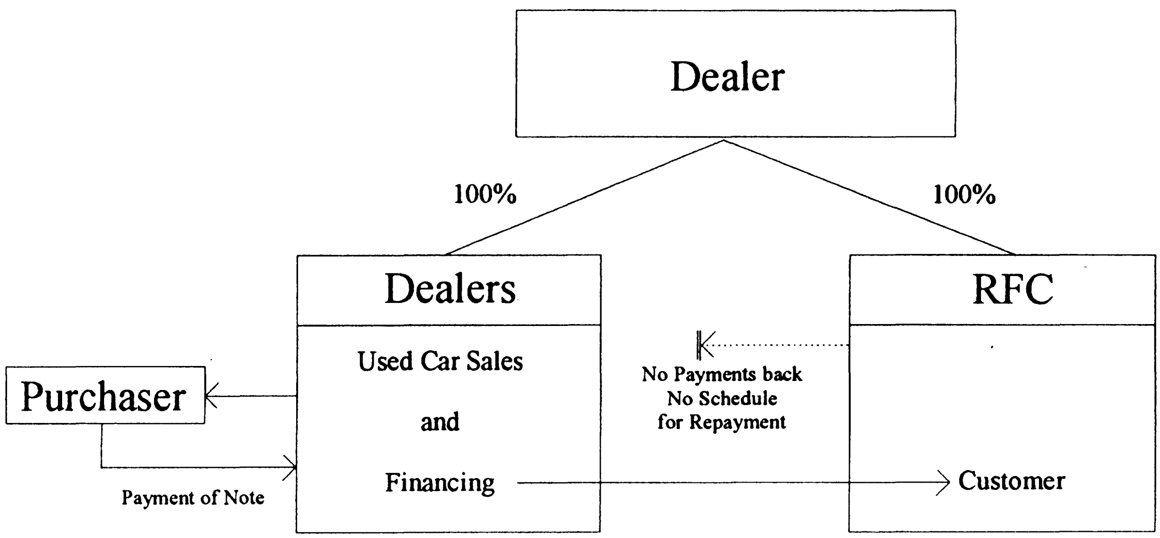
Any repossessed vehicle was recorded in Dealers' used vehicle inventory at a value shown in the NADA used vehicle guide. The transaction was treated as if Dealers purchased the vehicle from Finance.

Any profit of Finance was lent by Finance to related businesses of Finance and Dealers. Since Dealers were listed as the lienholders, Finance could not have sold the notes that it acquired from Dealers.

Dealers and Finance operate in a State which has adopted the UCC. Comment 1 to Paragraph 9-308 of the UCC states that in the automobile field, when a car is sold to a consumer buyer under an installment purchase agreement and the resulting chattel paper is assigned, the assignee usually takes possession; the obligor is notified of the assignment and is directed to make payments to the assignee.

see **RFCS: HOW NOT TO DO THINGS...**, page 23

TRANSFER OF NOTES TO RFC LACKS ECONOMIC SUBSTANCE



* Didn't notify customers
* Remained listed as lienholder on vehicle titles
* Employees performed all administrative tasks for RFC

* Had no employees
* Made no collections on notes
* Had no facilities
* Was not listed as lienholder on vehicle titles

IRS Holdings

1. No bona fide sale or disposition of notes under Section 1001.
2. Dealership could not deduct losses from transfer of notes to the RFC. Notes were transferred at a discounted amount representing imputed interest.

IRS Rationale

1. Transfer of notes lacked economic substance.
2. Dealership did not reduce its risk exposure arising from the (lack of) credit worthiness of the used car purchasers/customers.
3. Dealership did not receive cash any more quickly by transferring notes to the RFC.

COMPARING WINNING AND LOSING RFC STRUCTURES

	LTR 9534023 (WINNER)	LTR 9704002 (LOSER)
Type of entity	Partnership	Corporation
Ownership of entity	Different individual owners	Same individual
Seller of Used Vehicles	Used car department of full line dealership	Used car sales made by separate divisions
Sales price to RFC of used car purchasers' notes	At a discount	At a discount ... imputed interest
Payee designated in customer's purchase notes	Dealership	Dealership
Entity approving customers' financing forms	RFC	Dealership
Entity collecting payments on notes after transfer of notes to RFC	RFC	Dealership
Entity handling repossessions if customers defaulted	Dealership	Dealership
Initial capitalization	Not disclosed	$1,000 stock & $24,000 loan from sole shareholder

Points of comparison and reference.
Some are just informative background and not necessarily influential in the LTR holdings.

INTERNAL REVENUE SERVICE
INFORMATION DOCUMENT REQUEST
FOR RELATED FINANCE COMPANIES

FORM 4564 PAGE 1 OF 2

We plan on pursuing a substance versus form review of the transactions issue on the discounting of your finance contracts to your related finance company. For the purposes of applying the provisions of Revenue Procedure 92-20, 1992-1 C. B. 685, this Information Document Request is your written notification that we plan on pursuing this change in accounting method issue during our examination.

If you agree to this issue and file a Form 3115, Application For Change In Accounting Method, within 90 calendar days after the day I first contacted you for scheduling this examination (during the 90-day window of Revenue Procedure 92-20, Section 6.02), you will receive the most favorable terms and conditions of this revenue procedure.

If after considering the facts and circumstances of your case we determine this issue is appropriate and you did not file a Form 3115 during this 90-day window period, a change in your method of accounting will be made during my examination. In this instance, the year of change is your first tax year I have under examination (which contains this issue) and you will not be entitled to a spread of the Section 481(a) adjustment. Please give me a call if you have any questions on the provisions of Revenue Procedure 92-20.

In addition to providing the documentation requested below, please ensure that the managers (or other persons knowledgeable on the detailed day-to-day activities) of both the car company (CC) and the related finance company (RFC) are present at our initial interview.

PLEASE PROVIDE THE FOLLOWING:

1. Copies for our records of each federal income tax return filed by the used car company (UCC) and the related finance company (RFC) for the periods beginning with the year in which the RFC was formed and ending with the most recently filed federal income tax returns.

2. Please have available for inspection the complete set of books of the UCC and the RFC for the tax years beginning with first year examined and ending with period for which the last federal income tax return has been filed or is due. Please include bank account records for both entities.

3. Please have available for inspection the minute and stock record books of both the UCC and RFC.

4. A copy for our records of any Forms 3115, Application for Change in Accounting Method, filed by the UCC, RFC, or any related party since the filing of the tax return preceding the year in which the RFC was incorporated.

5. Copies for our records of the employment tax returns (Forms 940, 941, W-2's) filed by the UCC and the RFC since the formation of the RFC.

6. A copy for our records of any intangible tax returns filed with the State of ___________ by the UCC and/or RFC since the formation of the RFC.

(continued)

INTERNAL REVENUE SERVICE

INFORMATION DOCUMENT REQUEST

FOR RELATED FINANCE COMPANIES

FORM 4564 PAGE 2 OF 2

7. Copies for our records of <u>all</u> agreements to date among: the RFC and UCC, the RFC and its shareholders, and the RFC and all other related parties.

8. Copies for our records of <u>all</u> agreements (not covered above) on the formation of the RFC.

9. A copy for our records of a finance contract which has been discounted which is representative of other contracts. If the form of finance contracts has changed since the inception of the RFC, please provide a copy which is representative of each form or format used along with the period of time in which it was used.

10. If the UCC has discounted or still does discount its finance contracts to third party finance companies, please furnish a copy for our records of the discount agreement and a copy of a sample discounted contract for the last third party finance company utilized.

11. A copy for our records of a completed loan application form which is representative of the forms used since the RFC formation.

12. A copy for our records of a sample file actually kept by the RFC on a discounted contract during the calendar year 1991.

13. A copy for our records of any credit policies, collection policies, or repossession policies in effect immediately before creation of the RFC and since the formation of the RFC.

14. A copy for our records of all notes and or written loan agreements among the RFC and the UCC, among the RFC and its shareholders, and among the RFC and any other related party.

15. Available for inspection the dealer license from the State of ____________ Division of Motor Vehicles for the UCC and the RFC.

16. Available for inspection occupational or other licenses or permits from your county and/or city for the UCC and/or RFC.

17. A copy for our records of all promotional literature, brochures, or other information furnished to the owner, manager, and/or key employees in conjunction with the decision to form a RFC.

18. Copies or available for inspection all other documents and information you and/or your representative consider relevant in ascertaining whether the discounting of finance contracts to your RFC has substance or should otherwise be accepted for federal income tax purposes.

(End)

IRS RECOMPUTATION ADJUSTMENTS FOR RFCs

Here's what your "adjusted" or recomputed/increased taxable income will look like after the IRS is finished with your RFC if it takes the position that the sale of the receivables is not to be recognized for tax purposes because the purported sale or disposition has no economic significance or substance:

Disallowance of the Losses/Deductions Claimed on the Sale of Receivables to Your Related Finance Company (RFC)

	Tax Years Ending		
	Dec. 31, X	Dec. 31, X+1	Dec. 31, X+2
Finance Contract Losses of Discount Deductions Claimed	$	$	$
Plus RFC Net Taxable Income			
Less Installment Collections Reported as Income			
Plus Section 481 Adjustment		N/A	N/A
Increase to Taxable Income	$	$	$

Unless the first year examined is the first year in which finance contracts were discounted to your related finance company (RFC), there is a Section 481(a) adjustment. The Section 481(a) adjustment is made in the first year, is examined and is computed as summarized below:

Prior Tax Years Ending	Discount Losses or Deductions Claimed		Installment Income Reported		Sec. 481(a) Adjustment
/ /	$		$		$
/ /					
/ /					
	$	Less	$	=	$

The above adjustments are made to the tax returns of the used car dealer. These adjustments are based upon the IRS position that the sale of receivables to the RFC should not be recognized for tax purposes because they lack economic substance. The Service is usually careful to indicate that its position is not that the RFC is a sham corporation or entity.

COMMENTS ON IRS RECOMPUTATIONS

Most car dealers allocate some indirect expenses to the RFC. If the sales of the receivables, subsequent gains on collections, the associated interest income, and the directly associated costs of the used car dealer are transferred back to the RFC but the indirect expenses allocated by the taxpayer to the RFC are left with the RFC, the RFC Form 1120 will have unusable net operating losses.

IRS agents are told to advise the taxpayer that all items of the RFC are being allocated back to the car dealer return in an attempt by the Service to fairly represent the actual economic substance of the taxpayer's business operations and not because of a sham corporation argument. If the taxpayer makes an issue of this, then consider leaving the RFC items not directly associated with the sale of the receivables on the RFC return.

Since in substance the taxpayer has one trade or business and not two separate and distinct trades or businesses, this entry transfers all income and expenses reported by the RFC back to the Used Car Company/ Dealer. For 1120 RFC returns this is the line 28 "taxable income before net operating loss" amount. For 1120S RFC returns this is the line 21 "ordinary income (loss)" amount. If an amount is positive it is added to the other column amounts in this column. If the amount is negative, it is subtracted from the other amounts in this column.

A separate report is to be prepared for the RFC. The RFC report will adjust the reported net income or loss to zero. Agents are told to label the adjustment "Use of the installment sales method—related finance company (RFC) issue". In the Form 4549 other information section state "All items of reported income and expenses are being adjusted to zero because these items are being allocated back to your used car company. Refer to the used car company's report explanation of items on the "Use of the installment sales method—related finance company (RFC) issue" for details.

If additional adjustments are warranted to the expenses claimed by the RFC, reflect and cover these adjustments in the car dealer report and not in the RFC report.

If the RFC reported any income on the finance contract <u>principal</u> collections, this amount is subtracted out here. This is necessary because the IRS is requiring the car dealer to use the accrual method and any income reported by the RFC subsequent to the date of sale is a duplication of income already reported.

<u>Any interest income reported on the finance contracts by either the RFC or car dealer is not backed out here. Interest income on the finance contracts remains fully taxable.</u>

Unless the first year being examined is the first year the car dealer discounted finance contracts to the RFC, there will be a Section 481(a) adjustment. This adjustment is in the first year examined. There is no spread forward of this Section 481(a) adjustment. However, the tax limitations of Section 481(b) may result in a lower tax liability for the taxpayer.

If the RFC files an 1120S tax return, the net ordinary income (loss) reported on the shareholder's Form 1040 income tax return needs to be adjusted to zero in the report for the shareholder. The same applies to any other items distributed from the 1120S to the shareholder.

Determine if the RFC (either Form 1120 or 1120S) made any cash distributions to the shareholder during the years under examination. If so, these amounts need to be treated as dividends from the Used Car Company (UCC) to the shareholder provided the UCC is not an S Corporation. The application of the basic rules of Section 301 will generally result in additional adjustments (taxable dividends) at the shareholder level.

GAINS & LOSSES ON REPOSSESSIONS. The IRS manual states that since there are innumerable improper ways gains and losses on repossessions may have been handled, specific up front guidance is not practical. Agents are told that the key is to ensure that gains and losses on repossessions of vehicles are properly computed and included in the car dealer's income and deductions. They are also told to specifically determine if the correct tax basis is used for vehicles repossessed and that interest income is properly included in income.

DIFFERING TAXABLE YEARS. If the RFC has a taxable year which differs from the taxable year used by the car dealer, the RFC's amounts will need to be allocated to conform to the taxable periods utilized by the car dealer in its tax year. These conversions can usually be readily made by inspecting the RFC's general ledgers. If due to the taxpayer's recordkeeping this conversion can not be readily made, taxpayer should be asked to furnish the allocations.

RELATED FINANCE COMPANY ISSUE DEVELOPMENT SUMMARY

Taxpayer ______________________ Examiner ______________________

This questionnaire is to be completed by the examiner (not the taxpayer or representative). The questions asterisked are to be asked by the examiner during the initial interview. If additional space is needed for answers add to back or separate page and cross reference.

A. Background

1. Date used car company (UCC) incorporated (refer to tax return) __________

2. Date related finance company (RFC) incorporated (refer to tax return) ______

3. Is the RFC corporate charter still active? ___________ (verify during inspection of minute book).

4. Type of income tax returns filed:

	UCC		RFC	
Form 1120	____		____	
Form 1120S (reflect election date)	____	________	____	________
Other	____		____	

5. * Date used car business started (refer to tax return) __________

6. * Date first car sold with taxpayer financing ________________

7. * Number of years car sales and financing treated as one business (same entity) ______________________________________

8. * Date first contract discounted to RFC ___________________

9. * Taxpayer's stated reasons for setting up the RFC (business, estate planning, family, tax planning, etc.) and the taxpayer's stated business reasons for discounting receivables to the RFC.

____

10. * Ownership of UCC (verify return reflection)

____

11. * Ownership of RFC (verify return reflection)

____

12. Initial Capitalization of RFC:

a. Amount of shareholder cash _______________________

b. Amount of shareholder formal notes (obtain copy) ___________

c. Amount of shareholder open loan account ___________

Source: Independent Used Car Dealers - IRS Audit Technique Guide
Exhibit II - April 6, 1995 Draft - Market Segment Specialization Program

B. General Operations

1. * Books & Records maintained by UCC and RFC (verify during exam):

	Separate for UCC	Separate for RFC	Combined for UCC & RFC
General Ledger	_____	_____	_____
Cash Receipts Journal	_____	_____	_____
Cash Disburs. Journal	_____	_____	_____
Trial Balances	_____	_____	_____
Journal Entries	_____	_____	_____
Financial Statements	_____	_____	_____
Checking Account	_____	_____	_____
Payroll Records	_____	_____	_____
Other General Records:			
______________	_____	_____	_____
______________	_____	_____	_____
______________	_____	_____	_____
______________	_____	_____	_____
Finance Contracts	_____	_____	_____
Sales Invoices	_____	_____	_____
Expense Receipts	_____	_____	_____
Credit Applications	_____	_____	_____
Credit Checks	_____	_____	_____
Proof of Insurance	_____	_____	_____
Title Records	_____	_____	_____
Tag Records	_____	_____	_____
Other Specific Records:			
______________	_____	_____	_____
______________	_____	_____	_____
______________	_____	_____	_____

2. * What method of accounting is used to report gross receipts (verify)

UCC		RFC	
Cash Method	_____	Cash Method	_____
Accrual Method	_____	Accrual Method	_____
Installment Method	_____	Installment Method	_____
Cost Recovery Method	_____	Cost Recovery Method	_____
Other	_____	Other	_____

3. * What method of accounting is used to report expenses (verify)

UCC		RFC	
Cash Method	_____	Cash Method	_____
Accrual Method	_____	Accrual Method	_____
Installment Method	_____	Installment Method	_____
Cost Recovery Method	_____	Cost Recovery Method	_____
Other	_____	Other	_____

* Questions asterisked are to be asked by the examiner during the initial interview.

4. * Has a Form 3115, Application for Change In Accounting Method, been filed by the UCC, RFC, or any related entity or party since the year preceding the year the RFC was incorporated? _________________________

5. * For the first year examined, name and describe the major duties of the UCC employees, including officers shareholders.

   Employee Name Duties

   _____________ ____

   _____________ ____

6. * For the first year examined, name and describe the major duties of the RFC employees, including officers & shareholders (specifically, determine who makes credit checks, credit decisions, who monitors, who collects, who repossesses, who manages the company, who does bookkeeping, etc.).

   Employee Name Duties

   _____________ ____

   _____________ ____

   If there are employees common to both the UCC and RFC determine the time allocation percentages for these employees.

7. * Has the RFC filed federal employment tax returns (940, 941) since it's inception? (If yes, copies are workpapers ___________________________________)

8. * Does the RFC share the same building as the UCC? ____________________

   a. * Who owns the building(s)?
   b. * What arrangements exist on rental?

   ____

   ____

   c. * Are there written agreements on this? __________
   d. * If yes, copies are in workpapers? __________
   e. * If same building are separate offices maintained? __________
   f. * Separate phone numbers and phone lines? __________

9. * How are common costs (utilities, supplies, overhead, etc.) shared or allocated?

   ____

   a. * Was this agreed to before or after the costs were incurred? __________
   b. * Are there written agreements on this? __________
   c. * If yes, copies of are workpapers __________

10. * Does the UCC have a dealer license from the state? __________
    Does the RFC? __________ If yes when obtained by RFC __________

11. * Does the UCC have a county or city occupational license or permit? ________
    Does the RFC? __________ If not, why not?

    ____

    If yes, when first obtained by RFC?

* Questions asterisked are to be asked by the examiner during the initial interview.

12. * Does the UCC file tangible tax returns with the state? __________
    Does the RFC? __________

13. Annual Cash Flow of RFC summarized <u>for each year</u> since business commenced (based on inspection of RFC cash general ledger accounts). For initial year include above A12 amount.

    Sources of Cash: YEAR ENDING: __________

    a. From Shareholder(s) ____________
    b. From UCC ____________
    c. From Other Related Parties ____________
    d. Third Party Financing ____________
    e. Collections on Finance Contracts ____________
    f. Other (Describe) __________ ____________

    Total Source of Cash Year Ending __________ ____________

    Uses of Cash:

    a. To RFC ____________
    b. To Shareholder(s) ____________
    c. To Other Related Parties ____________
    d. Total Salary & Expenses Paid Directly (Not Through UCC) to Third Parties ____________
    e. Other (Describe) ____________

    Total Cash Outflow for Year Ending __________ ____________

14. Summary of RFC's Related Party Loan Accounts

    a. Year end account balances

	YE _____	YE _____	YE _____	YE _____
UCC	$ _______	$ _______	$ _______	$ _______
Shareholder	_______	_______	_______	_______
Other Related	_______	_______	_______	_______

    b. Total loan repayments (total vs. net) during year ending

	YE _____	YE _____	YE _____	YE _____
UCC	$ _______	$ _______	$ _______	$ _______
Shareholder	_______	_______	_______	_______
Other Related	_______	_______	_______	_______

* Questions asterisked are to be asked by the examiner during the initial interview.

c. * Identify which loans and amounts, if any, are covered by notes (refer to applicable workpaper for retained copies).

d. * For each loan ascertain if there are written or oral agreements on the payment of interest.

e. * For each loan reflect the yearly amount of interest if any accrued on either the UCC's or RFC's books.

f. * Yearly amounts of interest actually paid:

	YE _____	YE _____	YE _____	YE _____
UCC	$ ________	$ ________	$ ________	$ ________
Shareholder	________	________	________	________
Other Related	________	________	________	________

g. * Any unique aspects of related party loan accounts

____

15. * Describe all other business activities of any kind of the RFC other than it's discounting of UCC contracts.

____

C. Financing Operation Details

1. Since the RFC was created:

   a. Has the amount of dealer financing increased? ___________
   b. If yes, how much? ________________________________
   c. Has the taxpayer modified the level of customer credit risk he or she would self-finance? __________
   d. Has the taxpayer modified collection procedures? __________
   e. Has the taxpayer modified repossession procedures? __________
   f. Describe any significant changes in business practices:

   ____

2. * Before the RFC was formed did the UCC discount finance contracts to third party finance companies? __________

3. * Since the RFC was formed has the UCC discounted contracts to finance companies other than the RFC? __________

   If yes: Identify finance companies, obtain copy for workpapers of sample contract(s), and compare and contrast with the RFC's contract terms, conditions, & procedures (include comparison of discount percentages and customer credit risks)

   ____

   ____

* Questions asterisked are to be asked by the examiner during the initial interview.

4. * Has the RFC discounted notes for anyone other than the UCC? __________
(if yes, fully develop)

    a. * If not, why not? ____

    b. * What actions, if any, has the RFC taken to obtain contracts to discount other than those of the UCC?

    ____

5. * Does the RFC discount all of the UCC finance contracts? __________
If not who determines for each company which are to be discounted and under what criteria? ____

6. * Were the receivables sold at fair market value? __________

    a. * How was FMV determined?

    ____

    b. * Is the discount percentage the same for all contracts? __________

    c. * Please reflect discount rate or range used. If this has changed over time reflect changes and reasons for.

    ____

7. * If not all contracts are discounted, or different discount rates are given on a contract by contract basis who has authority to make these decisions for:
    a. * The UCC? ________________________
    b. * The RFC? ________________________

8. * With respect to the terms and conditions of the discount agreements among UCC and RFC, who negotiated the agreements
On behalf of UCC? ______________________
On behalf of RFC? ______________________

9. * What percentage of finance contract customers are unable to obtain financing elsewhere due to poor or no credit? __________

10. * Who is recorded as the lien holder with DMV, UCC or RFC?
(verify from taxpayers records) __________

11. * Which company retains the original car title and tag records?

____

12. * Other than the discount price paid what fees, if any, are paid by either the RFC to UCC or UCC to RFC such as acquisition fees per contract, collection service fees, repossession fees, etc.

13. * Are any purchasers required to purchase road insurance (such as Road American) or credit life insurance? __________

* If so, which entity receives and reports the commissions earned?

* Questions asterisked are to be asked by the examiner during the initial interview.

14. * Who makes the decision when to repossess a car? __________

15. * If a vehicle is repossessed who reports the gain or loss on the finance contract UCC or RFC? __________

16. * How is the transfer of the vehicle back to UCC (from RFC handled in the books and for tax purposes?

____

D. Miscellaneous Information

1. * Since the formation of the RFC, has either the UCC or RFC obtained outside third party financing? __________

   a. * If yes, a copy of the financial statement submitted is workpaper _______

   b. * Are the assets & activity of the other company also?

2. * Is the UCC or RFC a member of the state Independent Auto (Dealers Assn.)?

3. * What other dealer organizations is the UCC or RFC a member of?

______________________ ______________________

______________________ ______________________

4. * Whose idea was it to set up the RFC? ______________________
How did this individual learn of the use of RFCs?

____

____

5. * Taxpayer's and/or representative's opinion-on the applicability of the accuracy related penalty of Section 6662 due to the RFC issue.

____

____

6. * Representative's opinion on the applicability of preparer penalties due to the RFC issue.

____

____

7. * What other information in the opinion of the taxpayer or taxpayer's representative is relevant in evaluating the substance versus form of contracts discounted to the RFC?

____

____

8. What other information in the opinion of the examiner is relevant in evaluating the substance versus form of contracts discounted to the RFC?

____

____

(End)

* Questions asterisked are to be asked by the examiner during the initial interview.

RFCs: How NOT To Do Things...

(Continued from page 9)

NATIONAL OFFICE ANALYSIS IN LTR 9704002

In analyzing the above facts, the National Office observed that the courts have held that for Federal tax purposes, a sale occurs upon the transfer of the benefits and burdens of ownership. It indicated that, in the present case, it found little evidence that the benefits and burdens of ownership had been transferred between the buyer and the seller. Upon the transfer of notes, the used car dealers still had the burdens of ownership with their employees still having the administrative responsibilities of collecting the payments from the used car buyers and performing repossessions, when necessary. It recognized that a percentage of the used car dealers' administrative expenses were allocated to the RFC and that the RFC reimbursed the used car dealers for the allocated amounts. It concluded that: "Nevertheless, dealers continued to be responsible for these administrative burdens."

The National Office pointed out that the used car dealers also continued to bear the risks of the credit worthiness of the notes. The only change for the dealers after the transfer of the notes was that the RFC, instead of the car purchasers, was the dealers' debtor. It was pointed out that none of this improved the dealers' financial position. The RFC was thinly capitalized with only $1,000 in equity and a $24,000 loan from the sole shareholder. The only significant assets the RFC had were the notes it acquired from the related used car dealers. Because of this, whether the used car dealers ultimately received payment still depended on whether the customers of the dealers made their payments on the notes. Dealers also continued to bear burdens in the case of default by their customers because they were responsible for processing repossessions. Also, repossessions were treated as if Dealers purchased the vehicle from Finance.

Dealers continued to have the benefits of ownership after the transfers of the notes. The notes were not marked to show that they had been assigned. Also the certificates of title showed Dealers as the lienholders. In the event that a vehicle was damaged in an accident, Dealers, as the lienholder, had the right to any insurance proceeds.

Finance did not get the benefits of ownership of the notes. Since the notes did not show that they had been assigned and Dealers were still listed as the lienholders, Finance could not have sold the notes. Further, Finance would lend any profits to related businesses of Dealers and Finance.

Here, the form as well as the substance of the transfers make it questionable whether bona fide sales took place. Dealers have not provided the terms of the sales of the notes to Finance and have not provided any written sales agreement to the Service. Finance did not provide any cash up front when it acquired the notes. There was no fixed payment schedule for Finance to pay Dealers.

In many ways, Dealers and Finance did not act like arms-length buyers and sellers. Finance and Dealers had the same owner, employees, and facilities. Finance acquired all of Dealers' notes during the period at issue. Finance never acquired any notes from any car dealer other than Dealers. In the event that a vehicle was repossessed, the transaction was treated as if Dealers purchased the vehicle from Finance.

There are other ways in which Dealers and Finance did not act like arms-length sales had taken place. The notes were not marked to indicate that they had been assigned. Dealers continued to be listed as the lienholders on the certificates of title. The customers were not notified that the notes had been assigned and the customers continued to make payments to Dealers. According to comment 1 to Paragraph 9-308 of the UCC, this is not the usual procedure, in the automobile field, when a note is assigned.

The National Office commented further that the transfers of the notes lacked economic substance because the dealers did not receive any cash upon the initial transfer of the notes to the RFC. Consequently, the dealers did not receive cash any more quickly as a result of making the "purported sales" or transferring the notes to the RFC. The final conclusion was that, for purposes of Section 1001 of the Code, the transfers of the notes between the used car dealers and the RFC were not bona fide sales.

As a result of that holding, it was not necessary for the National Office to address the secondary challenges that typically are waiting in the wings if the "economic substance" challenge fails. These secondary arguments include using Section 482 to reallocate income between the related entities and Section 267 issues to either disallow or defer the recognition of losses on the transfers.

Letter Ruling 9704002 reflects a taxpayer who went far down the audit path ... to the point of requesting Technical Advice from the National Office. In other audit situations, examining agents have raised similar issues and they were thoroughly set aside at Appeals or else the IRS declined to go to the National Office for Technical Advice because the taxpayer had "better facts". Letter Ruling 9704002 clearly illustrates a taxpayer with "bad facts" and it should be contrasted with more favorable facts, as found in Letter Ruling 9534023 to get a better idea of the variations possible and/or permissible. See page 10 and 11 for that comparison. *

RECOVERING LEGAL FEES WHEN THE IRS IS *UNREASONABLE*

SECTION 7430

A few issues back, we covered the *Beaver Bolt* Tax Court Memo Decision 1995-549. In summarizing the extreme differences between the IRS value of the non-compete agreement at only $53,000 and the taxpayer's... at $324,000 (6 times more), we asked "Were They Talking About The Same Thing?" The taxpayer's position was sustained by the Tax Court. (See December 1995 *Dealer Tax Watch*, pages 16-17)

Recently, in Tax Court Memo Decision 1997-44, filed January 27, 1997, Beaver Bolt was successful in recovering attorneys' fees and related costs from the IRS under Section 7430. This case brings Section 7430 to life in a way anyone feeling overly stressed by the IRS can relate to. Sometimes the IRS just won't quit and, if it strays beyond taking action that was "substantially justified", the taxpayer can sue to recover the legal costs it incurred in defending itself.

The accompanying chart shows the different valuations bandied about by the IRS from its Engineering and Valuation Report showing the stock value at June 30, 1988 of Beaver Bolt at $739,000 (and the employee's non-compete agreement at 0) to its own expert witness' conclusion that the Company's stock value was $188,600 and its agreement with the taxpayer that within $1,000, that was the stock value. However, at trial, the IRS took the position that the non-compete agreement was worth only $53,000, and the IRS did not contend that the taxpayer had paid $513,000 to the former employee for anything other than the covenant not to compete and for her stock in the Company. In so doing, did the IRS take "action that was not substantially justified?" The Tax Court held it did.

A taxpayer who has substantially prevailed in a Tax Court proceeding may be awarded reasonable litigation costs if it satisfies five requirements.

TAXPAYER TESTS

SECTION 7430

1. It must exhaust administrative remedies,
2. It must substantially prevail with respect to the amount in controversy,
3. It must be an individual whose net worth did not exceed $2 million, or an owner of an unincorporated business or any partnership, corporation or similar entity whose net worth did not exceed $7 million at the time when the petition was filed,
4. It must show that the US/Internal Revenue Service took a position in the action that was not substantially justified, and
5. It must establish that the amount of costs and attorneys' fees claimed is reasonable.

The IRS conceded that the first three tests were satisfied, but it argued that it had taken a "substantially justified" position in the earlier litigation. The taxpayer has the burden of proof and it must satisfy each requirement before the Tax Court will order an award of litigation costs under Section 7430.

IRS POSITION "NOT SUBSTANTIALLY JUSTIFIED"

The standard of "substantial justification" requires that the IRS' position be justified "to a degree that would satisfy a reasonable person." To be substantially justified, the IRS' position must have a reasonable basis in both law and fact and there must be "substantial evidence" to support it. The fact that the IRS/Commissioner eventually loses or concedes a case does not, in itself, establish that the position taken was unreasonable. However, it is a factor to be considered. The taxpayer does not need to show that the IRS demonstrated bad faith in order to establish that the Commissioner's position was not substantially justified. Numerous cases are cited supporting each of these general statements.

WHEN DOES REASONABLE BECOME *UNREASONABLE?*

The IRS had taken the position that the covenant not to compete had no or minimal value. The issue the Court analyzed was whether that position "had a reasonable basis in fact and law." The taxpayer contended that the IRS' position was not substantially justified once the IRS received the valuation report of its own expert on August 22, 1994 which estimated that the stock in the company was worth $188,600. The taxpayer argued that from that time forward, the IRS position was unreasonable. (Note: not all legal costs are recoverable ... only those incurred after the point in time when the IRS takes an unreasonable position.)

In its defense, the IRS contended that:

1. The Company intended that the purchase price of $513,400 would be payment solely for the employee's stock. It was obligated to pay the former employee that amount even if she had not agreed not to compete and even if the fair market value of the stock was less than that amount.

2. The fact that the IRS and the taxpayer agreed to a fair market value for that stock on September 27, 1994 did not alter the fact that the allocation of any value to the non-compete covenant lacked economic reality.

3. The amount allocated to the covenant not to compete did not result from arms-length negotiations.

4. The taxpayer, and its employee, did not have adverse tax interests with respect to the allocation of $383,400 to the covenant.

→

	TAXPAYER TREATMENT IN RETURNS FILED	TAX COURT SUSTAINED TAXPAYER POSITION IN TAX COURT	IRS ENGINEERING AND VALUATION REPORT (JULY 31, 1992)	TAXPAYER'S EXPERT WITNESS REPORT DATED APRIL 18, 1994 AND RECEIVED BY IRS ON AUGUST 24, 1994	IRS EXPERT WITNESS (AUGUST 22, 1994)	IRS - TAXPAYER AGREEMENT (SEPTEMBER 27, 1994)	IRS POSITION IN TAX COURT
Total Payments	$513,400	$513,400	-	-	-	-	-
Stock Value as of 6-30-88	$130,000	$189,300	$739,000	$190,000	$188,600	$189,300	-
Non-compete Agreement	$383,400	$324,100	-	-	$52,669	-	$52,669

5. The employee was not concerned with the allocation of the purchase price—she was only concerned with the total amount she would receive when she terminated her employment.

The Tax Court stated that none of these five points established that the IRS had a reasonable basis in fact for continuing to contend, after August 22, 1994, that the covenant not to compete was worth only $52,669. The IRS had access to the taxpayer's expert witness report on the valuation of the company. And one month before trial, it had its own expert witness report on August 22, 1994.

Why didn't the IRS just hang it up there? The IRS did not concede that the covenant not to compete was worth $324,100—or any amount other than $52,669—despite the facts that:

1. The taxpayer's expert said that the corporate stock was worth $190,000, the IRS' expert said it was worth $188,600 and the parties agreed that the stock was worth $189,300, and

2. The IRS presented no facts or theory to support its position that the taxpayer paid the remaining amount of $324,100 (i.e., the excess of $513,400 over $189,300) to the terminated employee for anything other than the covenant not to compete.

At trial, the IRS did not offer any other reasonable theory for why the covenant not to compete was worth less than $324,100. Accordingly, the Court held that the Service's failure to reevaluate that position after August 22, 1994 was *unreasonable.* The Tax Court cited *Frisch v. Comm.* (87 T.C. 838, 1986) in which the IRS valuation position was held to be unreasonable where it had the taxpayer's appraisal for seven months before trial and it did not investigate further or reevaluate its own position as new facts came to light. The Court also cited—*Williford v. Comm.* (T.C. Memo 1994-135)—in which the Service valuation position was held to be unreasonable where it had been slow to seek an appraisal, did not contact the taxpayer's valuation expert and did not modify its position after receiving its own expert witness' report 42 days before trial. The Tax Court said that the IRS' position in *Beaver Bolt* was even weaker than the IRS position had been in the *Frisch* case because the IRS' expert witness substantially agreed with Beaver Bolt's expert witness regarding the valuation of the corporate stock. Based on all the foregoing, the Tax Court held that the IRS' failure to reevaluate its position after August 24, 1994 was unreasonable.

HAGGLING OVER THE AMOUNT RECOVERABLE

Beaver Bolt sought an award of litigation costs totaling almost $45,000—nearly 95% was for attorneys' fees, the rest for out-of-pocket expenses.

Section 7430 limits recoverable attorneys' fees to $75 per hour, adjusted for cost of living increases and special factors. Not surprisingly, the IRS also contested the amount of fee recovery claimed. The taxpayer did not argue that any special factors were present to warrant reimbursement for payment of attorneys' fees at a rate higher than $75. That meant the last element to be settled was the adjustment of the $75 per hour limit "for increases in cost of living." The Tax Court held that 1986 was the appropriate base year for measuring cost of living increases using the Consumer Price Index (CPI).

The Tax Court held that Beaver Bolt was entitled to be reimbursed for the hours billed to it by its attorneys for work performed from August, 1994 through March, 1995 and that the hourly rates applicable to these reimbursements were not to exceed $104 per hour for 1994 and $107 for 1995. Beaver Bolt had sought reimbursement at the hourly rates of $125, $150 and $180 per hour. The Court also allowed the reimbursement of litigation cost of almost $2,500 because the IRS did not argue that any amount of litigation costs claimed by the taxpayer was unreasonable, except for the hourly rate issue.

Although taxpayers have a limited remedy available in Section 7430, it may be a Pyrrhic victory. *

IRS TELLS DEALERSHIP TO "QUIT HORSIN' AROUND" WITH *EQUINE ASSETS*

Dealers and the IRS often have controversies over what constitutes a "separate trade or business." Recently, a new example was trotted out in petitions filed in the Tax Court by a dealer and by his dealership: the dealership operation of a separate "horse division" which breeds, shows and sells purebred Arabian horses and National Show Horses (shades of *The Black Stallion*).

In 1989, the dealer sold Arabian horses to his dealership and the IRS was auditing the 1989, 1990 and 1991 returns of the dealership and the dealer. The petitions filed in the Tax Court indicated that the dealership's decision to acquire the horses was made pursuant to the advice of (the dealership's) Certified Public Accountant. The sales price for the Arabian horses, it is contended, was a fair price determined by a third party appraisal of the assets.

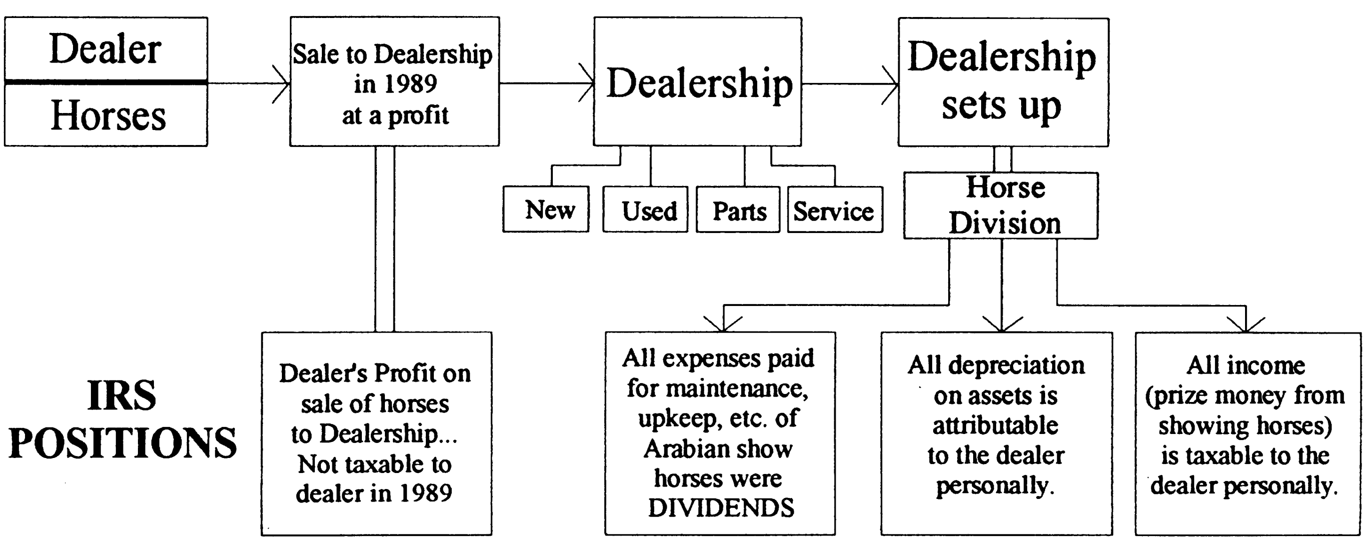
All income from prizes and awards earned by the horse division was deposited in the dealership's bank accounts and all expenses incurred in connection with maintaining, grooming and showing the Arabians were paid for and deducted by the dealership. The activities were duly blessed in the corporate minutes and separate books and records were maintained by the dealership for its "Northridge Arabian Division."

The petitions indicate that neither the IRS Examination Division nor the IRS Appeals Division disputed the profit-motivated nature of the Northridge Arabians. Thus, the entanglements of the hobby loss activity provisions of Section 183 are not involved in this conflict. The dealership contends that it has multiple divisions in various lines of business, that it is entitled to determine what lines of business it will operate, and that the IRS lacks substantial factual justification to ignore the sale.

The IRS took the position that the sale should be disregarded and it removed the profit from the sale of the horses from the dealer's 1989 return. All expenses paid by the dealership in connection with the horses were treated as deductible by the dealer and depreciation was allowed in his individual return. Consistent therewith, a modest amount of "horse income" was taxable in the dealer's individual return—rather than to the dealership—in the later two years. In the dealer's individual returns, the overall deficiency—about $20,000, including penalties—was relatively small.

The Service increased the dealership's taxable income by the amount of depreciation claimed and the amount of expenses for "horse activity" contending that those payments were not the dealership's expenses, but were those of the individual dealer and his wife. The disallowance of the horse expenses and the treatment of their payment as non-deductible dividend distributions created a deficiency of about $116,000 based on disallowed deductions of $306,000. That ain't hay!

The IRS completely disregarded the sale transaction and treated the parties as if the sale had not occurred ... except for making matters much worse by treating the expenses paid for the maintenance and upkeep of the horses by the dealership as non-deductible dividend payments. For more on constructive dividend exposure, see the December 1995 *Dealer Tax Watch*.



SAMPLE LETTER TO DEALERS ON ENROLLMENT FOR ELECTRONIC FEDERAL TAX PAYMENT SYSTEM

EFTPS

In 1993, as part of the NAFTA (North American Free Trade Agreement) legislation, Congress decreed that by 1999 the Internal Revenue Service must **electronically** collect 94% of all business taxes. To implement this mandate, Congress selected all employers with payroll tax liability of $50,000 or more in 1995 as "mandated business taxpayers" (MBTs). If your 1995 payroll tax deposits exceeded $50,000, you have been selected to participate in this EFTPS program.

In recent months, the Internal Revenue Service has been notifying all affected taxpayers that they must enroll in the Electronic Federal Tax Payment System (EFTPS) in order to avoid penalties when making deposits for Federal Income Tax purposes. For starters, there is a one time filing process that will result in changing the mechanics for making Federal Tax Deposits (i.e., Estimated Tax Payments and Tax Due on Form 1120 previously involving Forms 8109).

If your payroll taxes in 1995 were more than $50,000 and you haven't received your EFTPS Business Enrollment Form, Form 9779 from the IRS by now, please call us immediately.

After July 1, 1997, MBTs will no longer be able to make Federal deposits using the paper system directly to a bank without incurring an extra 10% penalty ... they must use the Electronic Federal Tax Payment System (EFTPS) to make deposits electronically for their Form 1120 U.S. Corporation Income Tax Liabilities and for all other Federal tax liabilities.

Accordingly, it will probably be necessary for you to independently enroll, since right now any authorization you may have granted to any outside payroll service to make direct deposits only relates to your payroll tax liabilities ... and it does not automatically cover your *income* or other tax liabilities.

ENROLLMENT DEADLINE: MAY 1, 1997

To independently enroll, it will be necessary to complete and mail in Form 9779 (EFTPS Business Enrollment Form) which you may have already received directly from the U.S. Treasury/IRS. This Form has some taxpayer information already preprinted on it. Be sure to check any preprinted information carefully.

Form 9779 offers two remittance methods choices: the ACH Debit Method ... and the ACH Credit Method.

Select the ACH Debit Method: forget about the ACH Credit Method. If you want to know the reasons why, please call and we can explain the differences between these two methods. In short, unless you're big like IBM and AT&T, the Debit Method will probably be better for you to select.

Under the ACH Debit Method, the company/taxpayer initiates payment of taxes by contacting the EFTPS Agent to withdraw the funds from the company's account.

The "ACH" prefix stands for the "Automated Clearing House" system which has overlaid the country to enable registrants to use their own 4-digit PIN (Personal Identification Number) in making transfers or deposits of taxes.

In choosing the ACH Debit Method, you may also wish to set a threshold amount by completing Item 21 on Form 9779. By setting a threshold, any payment larger than that threshold amount will be signaled as a potential problem.

YOU DO HAVE TO GO TO THE BANK

In choosing to use the ACH Debit Method, it is necessary to complete Items 30 - 33 on Form 9779. This further involves and requires a signature from one of the authorized agents at the financial institution/bank. What this all boils down to is that the IRS wants to be sure that you are not selecting a bank to handle your automatic transfers that is not already set up and acceptable to the IRS. Consequently ... the signature requirement in advance of sending in the enrollment form does make sense.

Take the original of Form 9779 to the bank and immediately have the person who handles your account complete and sign off in the authorization section. After that is done, sign and date Form 9779 and make a copy of it before mailing the original to the Internal Revenue Service.

Please send us a copy of the completed and signed Form 9779 so our files will be complete on this matter. If you have any questions on any of this, please call.

 (Continued from page 2)

Significant differences in new item determinations can result in significant differences in the changes in LIFO reserves... especially Olds, Ford, Subaru, Plymouth, Chevy and GMC dealers. The mostsignificant affected Ford dealers who might have been heavy in F150 pickups at the end of either 1995 or 1996.

Alternative LIFO really means alternative results, depending on whose LIFO software you are using.

#9. PROJECT 2000: THE NOOSE TIGHTENS ON DEALERSHIPS GOING PUBLIC. Further evidence of Project 2000 momentum may be found in the 1996 Annual Report for Cross-Continent Auto Retailers, Inc. Note 4, Major Suppliers and Franchise Agreements, states, in part: "In addition, the Company has agreed to comply with GM's Network 2000 Channel Strategy ("Project 2000"). Project 2000 includes a plan to eliminate 1,500 GM dealerships by the year 2000, primarily through dealership buybacks and approval by GM of inter-dealership acquisitions, and ***encourages*** dealers to align GM divisions' brands as may be ***requested*** by GM. The June 1996 agreements require that the Company (i.e., Cross-Continent Auto Retailers, Inc.) bring any GM dealership acquired after the Offering into compliance with the Project 2000 plan within one year of the acquisition. Failure to achieve such compliance will result in termination of the Dealer Agreement and a buyback of the related dealership assets by GM. The Company believes that this aspect of the June 1996 agreements does not present a significant risk to its business or future operating results."

GM and the other manufacturers seem to have significant leverage in pushing their Project 2000 intentions with the "major players" setting up public chains. It is interesting to see the verbs "*encourages*" and "*requested.*" That note also says: "The Company's ability to expand operations depends, in part, on obtaining the consent of the automakers to the acquisition or establishment of additional dealerships."

#10. PROJECT 2000 UPDATES. Some of the best updates on the manufacturers' Project 2000 activities were included in the daily *Automotive News* supplements distributed in Atlanta at the NADA Convention in February:

1. Tension Over Franchise System Increases; Conflicts & Legal Challenges Loom (February 4, 1997, page 9).
2. GMC Policy Kindles Florida Dealer Debate (February 4, 1997, page 16).
3. Dealer Consolidation Fuels a Seller's Market (February 3, 1997, page 4).
4. GM on Track with Project 2000 Changes (February 3, 1997, page 4).
5. GMC Dealers Adjust to Changes (February 1, 1997, page 20).
6. Dealerships Face New Restrictions (February 1, 1997, page 4).
7. Jeep/Eagle Dealers Look to Accelerate C-P Merger (February 1, 1997, page 14).
8. As C-P Changes, So Do Dealers and Their Council (February 1, 1997, page 16).

#11. EFTPS ELECTRONIC FILING REMINDER. Most dealerships are large enough so that they are already making all tax deposits electronically with the IRS. Smaller dealers, however, may fall into the category of "mandated taxpayers" now required to enroll to cease all non-electronic/paper payments after July 1. See page 27.

The *De Filipps' Dealer Tax Watch* newsletter is a quarterly publication of essential tax information by Willard J. De Filipps, CPA, P.C., 317 West Prospect Avenue, Mt. Prospect, IL 60056. It is intended to provide accurate, general information on tax matters and it should not be construed as offering accounting or legal advice or accounting or legal opinion on any specific facts or circumstances. The contents are intended for general information purposes only. Readers should consult their certified public accountant, attorney and/or other competent advisors to discuss their own situations and specific income tax questions. Mechanical or electronic reproduction or photocopying is prohibited without permission of the publisher. Annual subscription: $325. Back issues available for $70 each. Not assignable without consent. Any quoted material must be attributed to *De Filipps' Dealer Tax Watch* published by Willard J. De Filipps, CPA, P.C. Editorial comments and article suggestions are welcome and should be directed to Willard J. De Filipps at (847) 577-3977; FAX (847) 577-1073. **INTERNET**: http://www.defilipps.com.
De Filipps' Dealer Tax Watch format designed by *Publish or Perish, Inc.* (630) 627-7227.

De Filipps' DEALER TAX WATCH
Willard J. De Filipps, C.P.A., P.C.
317 West Prospect Avenue
Mt. Prospect, IL 60056

First-class