De Filipps' LIFO LOOKOUT

A Quarterly Update of LIFO - News, Views, and Ideas

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LIFO UPDATE

If you had called me personally to ask "what's happening lately with LIFO that I need to know about?"...Here's what I'd say:

1. REVENUE PROCEDURE 92-20

First off, a look at the table of contents tells you that Revenue Procedure 92-20 was the big happening during the last 90 days and will continue to be important for a long time to come. All taxpayers are affected regardless of whether they are **manufacturers** with special components-of-cost problems or *Hamilton Industries* bulk bargain purchase problems, or **wholesalers** or **retailers**. There are many LIFO methodology problems, specific index computation alternatives and potential pooling issues that affect every industry and exist across the board, depending on how they have been modified to fit into a given business situation.

This issue of the *Lookout* hits some of the high points of 92-20 and addresses some of the practical problems and implications everyone faces right now.

2. IRS WATCH: STORM SIGNALS

CHANGE TO WATCH FROM WARNING

For now, my overall **feeling** has moved to a somewhat more optimistic feeling (i.e., a storm watch) from a somewhat more pessimistic feeling last quarter (i.e., a storm warning). A number of readers have commented on the increasing pessimism that crept into recent UPDATE columns, especially in the March issue.

During the last week in April, NADA representatives (6 or 7) met with IRS officials and technicians (about 18) in a major meeting devoted specifically to the discussion of what most taxpayers perceive to be unfair and inconsistent practices taking place throughout the country in IRS auto dealer **LIFO** audit situations and in National Office interpretations on technical index computation matters.

At this meeting, the IRS requested additional information from NADA and further time in which to consider and evaluate whatever additional information NADA may be able to provide before it formulates a response. Just considering the enormous amount of time and resources invested by both NADA and the IRS and the progress made in addressing extended service contract issues, I am hopeful that some doors have been opened in the April 28th meeting that can lead to parallel discussions and possibly mutually satisfactory compromise and resolution of auto dealer LIFO issues. At this time it is too early to report any results or IRS feedback on the April 28 meeting.

Many are looking for, or hopeful for, a "simple solution" to these LIFO issues. But a simple solution may be hard to find for these complex and multifaceted practical problems now nearing the end of the second decade of vagueness. About the only thing that can be said for the IRS National Office policy that has evolved to date, is that it has consistently been anti-taxpayer. In contrast, however, many examining agents in the field have shown far more willingness and practicality in tempering strict but necessary examination requirements and expectations with "real world" business conditions and recordkeeping practices.

On the sideline, some of us are wondering how long Commissioner Peterson will continue to read speeches to meetings of business groups and professionals about how critical it is for the IRS in its Compliance 2000 to be realistic in dealing with businesses of all sizes. While she is making these speeches, some people in her own National Office seem to be totally ignoring everything she is saying. They seem to interpret "Compliance 2000" as

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a motto that taxpayers be required to spent at least *2000 hours trying to comply* with narrow interpretations of vague or silent regulations as a measure of how well they are doing their jobs. It's pretty hard to get this point across because LIFO issues are technical and complex and sheer size of the bureaucracy tends to be overwhelming.

I am encouraged by the activity within the IRS to address dealer extended service contract issues. I am also hopeful that some professionals in the National Office have had enough of others going around and telling people what the IRS does or does not want in LIFO computations. I am hopeful that the IRS will soon speak directly to the major question over whether or not there is - or ever was - a requirement that for all taxpayers, their LIFO calculations must be 100% accurate. Reality 2000 suggests that financial statements and tax returns can only be prepared if reasonable estimates are recognized as acceptable. Demands for 100% accuracy in inventory calculations seem to be incompatible with both Compliance 2000 and GAAP and out of touch with reality.

As the IRS now moves slowly on these LIFO issues in an environment of greater visibility and responsiveness, we need to be patient and understand that it may not be anxious to act quickly and bring upon itself a storm of criticism over unduly restrictive rules and retroactive application. That may be part of the reason why the rumored Technical Advice saying that an auto dealer cannot use sampling but must reprice every option and accessory still has not yet been made public. Update #3 below adds fuel to the fire!

I am expecting a real showdown on this issue in the near future! The Service is now getting more pressure from NADA and some CPAs to come out and say what it really means and what it will settle for. This "100% accuracy" issue may need to be litigated and several events and taxpayers are in various staging areas so that this issue, **on its own merits and undiluted by other technical distractions**, can be more cleanly addressed by the Courts, if necessary.

Most of us can adjust our computational approaches and software to adapt to the ultimate decision or outcome. So if the IRS will just say whatever it wants in black and white, we will have something "official" and in print to react to. Eighteen years of official silence on this key issue is hardly compatible with Compliance 2000 and a lot of objections raised on how the components-of-cost controversy has been handled (see Update #4) have equal validity in the auto dealer context.

3. ONE PROVIDER OF LIFO COMPUTATION SERVICES NOW CHANGING METHODS

One provider of LIFO computation services (whose method was written up in the September, 1991 *Lookout* as the "one size fits everybody" approach) apparently is backing off of its long-standing approach and requesting permission to change to a sampling approach in computing LIFO indexes for auto dealers. More Forms 3115 are being filed. It appears that the changed procedures will involve sampling approaches...and this, of course, is inconsistent with other claims that the IRS will be satisfied only if a dealer reprices **every** option and accessory. It will be interesting to see how this turns out: If the National Office permits change requests involving sampling approaches, won't that discredit statements previously attributed to it that acceptable repricing must be done taking into account all options?

And what about those dealers who are no longer using this firm to compute their indexes? For the CPA who has inherited a dealer client previously put on LIFO using the "one size fits all" method, this presents some transitional problems that must be addressed immediately and in light of Revenue Procedure 92-20. See also, in this issue, "Big 6" LIFO Practices Cut Down to 4 for Auto Dealers.

4. MANUFACTURERS' USE OF COMPONENTS-OF-COST INDEX METHODS

The AICPA Tax Executive Committee submitted its report dated April 13, 1992 to the IRS Chief Counsel on the components-of-cost method of computing LIFO price indexes. This lengthy report suggests a fundamental unfairness in the IRS' position against manufacturers' use of components-of-cost index methods and that "in no event should the application of any new rules be made retroactive."

The Report concludes that the IRS should not seek to prohibit the use of the components-of-cost method of developing an index for a variety of reasons: i.e., the components-of-cost method clearly reflects income, it represents the best accounting practice in many circumstances, the method has a long history of acceptability, its use was specifically provided for by the original drafters of the dollar-value LIFO regulations, and a disallowance of its use will require massive and very expensive systems changes for the many manufacturing companies that use the method.

The Report also states that "there is no single standard methodology for computing indexes under the components-of-cost method. If the IRS believes the diversity of practice in this regard should be narrowed for tax purposes, this issue should be addressed by way of a proposed revision of the LIFO regulations." The Tax Executive Committee report can be obtained from the AICPA as part of the preliminary agenda for the Tax Accounting Committee meeting June 17-19, 1992.

At the Tax Section's May 15 session on tax accounting, as reported in *Tax Notes* May 25, 1992, the IRS was criticized for "its failure to heed AICPA warnings before taking an adverse position on the use of cost component accounting methods" and that the IRS "failed to meet the AICPA and others half way." Practitioners voiced concern that "the Service had acted unwisely and unfairly by not opening a formal regulations project that would allow for extensive public comment before action was taken."

It's too bad that auto dealers can't get this kind of Big 6/AICPA support to speak out on their behalf. (I've tried many times to get their attention.) If some of the arguments the AICPA advances for the retention of the components-of-cost method for manufacturers are legitimate and sound, then some of those same arguments can, and should, be made on behalf of auto dealers in questioning the "due process" that is supposed to be part of Compliance 2000 for everybody.

If "due process" **for all taxpayers**, big or small,

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contributes to taxpayer confidence in the System and voluntary compliance, then shouldn't these same procedures apply in resolving auto dealer LIFO issues? Commissioner Peterson has spoken about the need for applying different approaches to Fortune 500 companies and corner grocery stores. Some provision also needs to be made for businesses that fall within the size spectrum somewhere between the extremes.

5. IRS AUDIT ACTIVITY

For much of the last calendar quarter, IRS LIFO audit activity seems to have been pretty much reduced, partially due to the issuance of Revenue Procedure 92-20 with its 180-day special transitional rules for taxpayers already under audit. However, some IRS agents seem to clearly resent the taxpayer "break" granted by the 180-day transition rules in Revenue Procedure 92-20 for taxpayers under audit and could use various means to thwart taxpayers' requests for relief.

Most significant and troublesome in this regard is the argument raised by some agents that changes in LIFO methodology and computations they are questioning on audit are Category A method adjustments. If this Category A classification for LIFO computations is correct, it follows that taxpayers under audit cannot file Form 3115 and the agent will be able to make all adjustments as part of the IRS audit report (presumably using the earliest year under audit as the year of change and requiring Section 481(a) recomputation for all years with the full amount reported in income with no spread period).

The emerging LIFO audit scenario reported in the March, 1992 UPDATE in which I pointed out the "reasonable and practical" approach taken on audit by certain agents has been confirmed in several other discussions over the last few months with CPAs in different parts of the country. This "I'm okay...you're okay" approach seems to be one that certain IRS agents and offices are following where (1) adjustments for comparability/option-to-standard equipment adjustments have been made before base prices were compared for inflation and (2) the indexes computed by the taxpayer/CPA fall within the "parameters" of that particular IRS office's "computer."

One of my own specific experiences since writing the March, 1992 issue involves an IRS audit of seven dealerships that was settled with a "no change" for LIFO indexes computed with reference to base prices only (options and accessories were **not** repriced). The examining agent was understandably concerned that there might be some error in the indexes because none of the options were repriced. In the course of the audit, and with no harangue, we agreed upon several higher-dollar options whose beginning-of-the-year and end-of-the-year prices were checked against published prices and then factored into the overall index computation.

The six higher-dollar options selected for verification purposes were: (1) air conditioners, (2) automatic transmission, (3) rear window defroster (defogger), (4) power steering, (5) cruise control/speed control and (6) AM/FM radio and cassette tape players.

After testing three of the seven dealerships under audit and coming up with **minor** differences that, in the agent's opinion, were not significant enough to warrant adjustment, the agent accepted without change the method/results as being reasonable and the indexes and LIFO reserves, as computed by the CPA, for all seven dealerships.

Had these dealerships voluntarily locked themselves into repricing every option and accessory as part of their index computations, the annual compliance cost would have been more than $20,000 greater **every year**. Given the high overhead and low profit margins burdening most dealerships today, the practicality of less expensive annual LIFO computations seems obvious. This is a point NADA needs to continually stress in discussing LIFO computation alternatives with the IRS.

Look for considerably more IRS LIFO audit activity to resume now that June 28th is passed and the September 18 transitional deadline for certain taxpayers under audit is approaching. After September 18th, there will be even more LIFO audit activity.

6. WILL THE IRS NATIONAL OFFICE BE SWAMPED BY 3115 FILINGS?

It appears that the National Tax Office will be kept quite busy over the next several months. Will wave after wave of Form 3115 filings roll in? Will the waves be gentle Potomac River ripples or monsoon tidal waves?

First will come Forms 3115 that will be timely filed by the June 28(29) deadline for regular Calendar Year 1992 changes. Next will come those filed after June 28, i.e., late filings. Then will come Forms 3115 filed in connection with the extended service contract Announcement 92-93 which will instruct dealers in how to file for expedited changes for taxpayers not under audit on June 12.

After that are likely to come more Forms 3115 to be filed before the September 18, 1992 when the 180-day transition period for taxpayers under audit expires. Finally, there may be some taxpayers desiring to terminate their LIFO elections who will file under the expedited change provisions of Revenue Procedure 88-15 by the end of September.

The National Office will have its hands full since one of the major issues to be resolved before 3115's can be processed or audits can be completed is whether certain LIFO accounting methods are Category A or Category B methods. Also, examining agents will come under more pressure as their case loads both increase and age while change requests are being processed. The more sketchy the Form 3115, the more time needed for IRS followup requesting additional information. On the other hand, the more detailed the Form 3115 filed, the more time the National Office will have to take considering the submission.

It will be interesting to see how large the backlog really becomes and how much time it will take the National Office to process these forms and resolve these issues. Taxpayers may need answers in order to file tax returns for the years of change before the Service may be able to address all the issues and respond. The instructions for Form 3115 include a large box of information under the Paperwork Reduction Act Notice indicating the estimated average times for (1) recordkeeping, (2) learning about the law or the form and (3) preparing and sending the form to the IRS...what about a fourth category: estimated average time from submission of Form 3115 to IRS completion of the review process?

NEW PROCEDURES FOR CHANGING ACCOUNTING METHODS

Revenue Procedure 92-20 contains new rules intended to encourage taxpayers to voluntarily request permission to change from impermissible accounting methods before they are contacted by an IRS agent for an audit. The key word here is **impermissible**. In many instances, there is a significant difference between an impermissible method and a method that is simply one out of several acceptable alternative methods.

These new rules for accounting method changes modify and basically supersede Revenue Procedure 84-74. The June, 1991 *LIFO Lookout* contained several articles addressed to voluntary LIFO method change requests and other Form 3115 filing aspects, including requests to terminate LIFO elections. Those articles provide background for the "new" rules which now specifically mention and allow the use of a "cut-off" method under certain circumstances. Revenue Procedure 88-15 still remains a viable and preferable alternative to Revenue Procedure 92-20 for taxpayers desiring to terminate their LIFO elections.

Revenue Procedure 92-20 (I.R.B. 1992-12, March 2, 1992) is effective for accounting method change requests filed on Forms 3115 after March 23, 1992. The user fee for filing Form 3115 is $500 and the current Form 3115 bears a revision date of July, 1991, and includes a revised Schedule B for Changes Within the LIFO Inventory Method.

Although many LIFO situations are covered in the context of 92-20, this procedure was broadly written with no one particular type of accounting method, taxpayer issue or audit situation in mind. In this respect, it is broadly generic...although you may happen to have a situation that fits comfortably - or exactly - into its operation.

Revenue Procedure 92-20 provides a "gradation of incentives" to encourage prompt voluntary compliance. Under Rev. Proc. 92-20, a taxpayer generally receives better terms and conditions for any change in accounting method if the taxpayer voluntarily files its request to change methods before it is contacted for examination by the IRS. The Revenue Procedure allows taxpayers a limited 90-day window period during which the taxpayer coming under IRS audit may file a Form 3115 request to change an accounting method without first obtaining the approval of the District Director. However, a taxpayer receives terms and conditions during this 90-day window period that are **less favorable** than those available for method changes voluntarily requested prior to contact by the IRS, but those terms under the 90-day window are comparatively **more favorable** than the change adjustments required by the District Director/examining agent as part of the IRS audit report.

The terms and conditions surrounding an accounting method change involve (1) the year of change, (2) the computation of the Section 481(a) adjustment and/or the applicability of the cut-off method, and (3) the length of the adjustment period over which the Section 481(a) adjustment is reported in income. Each of these three "terms and conditions" has several different possibilities. This means there are numerous possible combinations of "terms and conditions" affecting any particular change request.

Why should a taxpayer consider making a voluntary change? Here are the incentives for a taxpayer not currently under IRS audit: **First**, the Internal Revenue Service presumably will not audit the methods changed in any years prior to the effective year of change. This prevents IRS adjustment for previous use of an erroneous method in prior years. Section 10.12 entitled "Protection for Years Prior to the Year of Change," states that if a taxpayer timely files a Form 3115 under this Revenue Procedure, an examining agent may not propose that the taxpayer change the same method of accounting for a year prior to the year of change.

However, this section provides a number of qualifications under which an enterprising IRS agent might successfully require a change in an earlier year. The most perplexing of these qualifications states that if a taxpayer is changing a sub-method of accounting that is within another method of accounting, an examining agent may propose that the taxpayer change the method (including, in appropriate circumstances, the sub-method) for a year prior to a year of change under this Revenue Procedure. It is difficult to determine exactly what this means.

The **Second** incentive for pre-audit change filing is that taxpayers may be allowed to spread the Section 481(a) adjustment reflecting the change over up to three or six years, depending on whether a Category A or a Category B method of accounting is being changed. **Third**, by being able to make the current year the year of change, the taxpayers avoid any interest on the adjustment arising from the change in accounting methods. **Fourth**, taxpayer penalties (under Section 6662) and tax return preparer penalties (under Section 6694) will not be imposed when voluntary method changes are made under Rev. Proc. 92-20.

Section 446 of the Internal Revenue Code provides that a taxpayer must first secure permission or consent from the Internal Revenue Service before it makes a change in a method of accounting. The Regulations provide that Form 3115 should be filed for this purpose within 180 days after the beginning of the year for which the proposed change is to be made. When the date for filing falls on a weekend or holiday, the filing of Form 3115 will be considered timely if it is

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filed on the next succeeding business day. For calendar year 1992, June 28th is/was the 180th day, falling on a Sunday...so the actual due date for Forms 3115 intended to be effective for calendar year 1992 is/was Monday, June 29, 1992.

It would appear that if a Form 3115 is filed too late to be effective for calendar year 1992, the IRS may treat that Form 3115 as an "early" application for change with respect to calendar year 1993. One question is whether an early (or otherwise timely) filing for calendar year 1993 will protect the taxpayer's method of accounting against IRS changes to 1992 and prior years. It appears that such a Form 3115 filing, made after June 28, but before calendar year 1993, will still protect 1992 and prior years from accounting method adjustments. So if a taxpayer missed the June 28(29) filing deadline to make the year of change calendar year 1992, it would appear that the taxpayer can still protect years prior to 1993 by either (1) a **late** filing for calendar year 1992 before or after the 270th day/with or without an approved extension of time or (2) an early filing for 1993 during the remainder/last half of 1992. Is this too good to be true? What happens if the IRS initiates an audit in the interim?

Under the Regulations, the Commissioner may prescribe administrative procedures, appropriate limitations, terms and conditions to accomplish accounting method changes and to prevent the omission or duplication of items includible in gross income or deductions. Section 481(a) requires that those adjustments necessary to prevent amounts from being duplicated or omitted be taken into account when the taxpayer's taxable income is computed under a method of accounting different from the method used to compute taxable income in the preceding tax year. One of the significant considerations in evaluating the application of Revenue Procedure 92-20 to LIFO situations is the incentive to avoid this requirement to make Section 481(a) recomputations for LIFO computations under the new method spanning all the years the old method was used.

Revenue Procedure 92-20 clearly states the opportunity to use the cut-off method in LIFO change situations. The new Revenue Procedure indicates that under the cut-off method, only items arising **on or after** the beginning of the year of change are to be accounted for under the new method of accounting. Any items arising **prior** to the year of change will continue to be accounted for under the taxpayer's former method of accounting.

Other previous transition rules for method changes limited or prevented entirely the use of net operating loss and credit carryovers as offsets against the Section 481(a) adjustment to income. The new rules provide that net operating losses and credit carryovers may be used to offset a net positive Section 481(a) adjustment, except that the Service may limit the offset ability if it appears to the Service that the utilization of the expiring loss or credit is a principal purpose for making the change in accounting method.

The specific results for a taxpayer changing methods that are either available or prescribed by 92-20 depend upon the interaction of three major considerations:

1. Whether or not the request for change is being made voluntarily (i.e., at a time when the taxpayer is not under audit by the IRS/before an IRS audit starts).
2. Whether or not the method of accounting being changed is a Category A method of accounting or a Category B method of accounting. (There are also special rules for **Designated** Category A and/or **Designated** Category B methods of accounting.)
3. Whether or not the taxpayer was under audit on March 23, 1992, thus possibly involving the special 180-day transition rules which end on September 18, 1992.
4. Note: A fourth consideration is whether or not the net Section 481(a) adjustment is positive or negative (see below).

The first three major considerations or factors are discussed separately, but they all fit together in the process of understanding how Revenue Procedure 92-20 works. One article discusses taxpayers not currently under audit and the differences between, and the consequences of, changes made at one of **three** points in time: either (1) before an IRS audit commences, (2) during the first 90 days after the start of an IRS audit, or (3) after the 91st audit day. The second article deals with the transition rules for taxpayers under audit on March 23, 1992 and the 180-day transition period which also includes taxpayers who are contacted for examination before the expiration of the transition period ending on September 18, 1992. The differences between Category A and Category B accounting methods are discussed separately in a third article. (See box, page 9.)

In changing methods of accounting for inventories, more often than not the new method results in a **positive** Section 481(a) adjustment - meaning that the inventories have been understated by the previous method and there is some income that needs to be reported as part of the method change process. Alternatively, it is possible for there to be a **negative** Section 481(a) adjustment - meaning that inventories were valued higher by the old method than they would be by the new method, in which case the taxpayer is entitled to a corresponding reduction of its taxable income as part of the method change process. Revenue Procedure 92-20 provides rules which are often different depending on whether the net Section 481(a) is positive or negative; only those rules relating to net Section 481(a) **positive** adjustments are discussed in these articles. ✻

TAXPAYERS NOT CURRENTLY UNDER AUDIT: PRE-AUDIT (VOLUNTARY) VS. 90-DAY WINDOW CHANGES

This article discusses the taxpayer's three basic alternatives associated with either (1) voluntarily requesting a change before the IRS initiates an audit, (2) making a request for change during the "90-day window" after the start of an audit or (3) facing the alternatives if neither of these actions to initiate a change are taken before the audit reaches its 91st day. The special 180-day transition rule for taxpayers under audit on March 23, 1992 are not discussed in this article.

The consequences to the taxpayer depend upon whether the accounting method issues involved are (1) non-LIFO Category A methods, (2) non-LIFO Category B methods or (3) LIFO methods. The rules and discussion of Designated Category A methods and Designated Category B methods are not covered in this overview.

NON-LIFO CATEGORY A

For non-LIFO accounting methods, if a taxpayer not under audit voluntarily requests a change in accounting method, the year of change will be the current year, i.e., the first year for which the Form 3115 is timely filed, thus allowing the change to be made on a prospective basis. For a taxpayer with a non-LIFO Category A accounting method voluntarily requesting permission to change, a Section 481(a) adjustment is ordinarily computed and the amount may be spread or taken into income one-third each year over each of the next three years.

If a non-LIFO Category A method of accounting is not changed before the IRS commences an audit, the taxpayer has 90 days from the start of the audit within which to file a Form 3115 requesting permission to make a change. If a change is made within this 90-day window, the year of change is moved back in time to be the earliest year under examination and the positive Section 481(a) adjustment is spread over three years. In this instance, the taxpayer loses some advantage or benefit by having the year of change moved to an earlier year, thus favoring the Internal Revenue Service.

If 90 days elapse after the start of the audit and Form 3115 has not been filed under the 90-day window, then the taxpayer cannot file Form 3115 at all, unless consent of the District Director is first obtained or unless certain other "windows" may be open under more limited special circumstances. As a consequence, the taxpayer may expect that the Section 481(a) adjustment will be computed and the full amount will be taxable, without any spread period, in the earliest or first year under audit.

Clearly the incentives to change before IRS contact are greater than those offered during the 90-day window; and the less attractive 90-day window incentives are comparatively less painful than the consequences if no action is taken. The only opportunity the taxpayer may have in the process for a better result will depend upon whether it is possible to negotiate a better deal at the Appellate level or hope to at least obtain the same results that would have been obtained had earlier filings been made. It is difficult to anticipate the likelihood of success under these circumstances.

NON-LIFO CATEGORY B

Revenue Procedure 92-20 provides a similar set of alternatives for taxpayers coping with non-LIFO Category B accounting methods. In this pre-audit, voluntary Form 3115 filing opportunity, the taxpayer is able to achieve a prospective or current year of change along with a spread period not to exceed six years for the Section 481(a) positive adjustment.

Should that taxpayer not request permission to change accounting methods before being contacted by the IRS for an audit, the 90-day audit window provides for the year of change to be the current year (consistent with Category B methods being less onerous in the eyes of the IRS than Category A methods) **but** the spread period for the net Section 481(a) adjustment vanishes and the entire Section 481(a) adjustment must be taken into account in the year of change.

Moving to the last, and worst, situation resulting where a Form 3115 has not been filed either pre-audit or during the first 90 days of the audit, the results are the same as those described for non-LIFO Category A situations above: namely, the examining agent will make the entire adjustment as part of his or her audit report...more likely than not making the earliest year under audit the year of change and not allowing any spread period. Again we see the progression from a more favorable combination of transitional terms and conditions to less favorable.

LIFO INVENTORIES

Where LIFO inventories are involved, the terms and conditions again sub-divide depending on the circumstances. Where the taxpayer has initiated the Form 3115 filing prior to any IRS audit contact, the year of change will be the current year for which the Form 3115 is timely filed. If the inventory accounting method change involves a *Hamilton Industries* type of bulk bargain purchase (see December, 1991 *LIFO Lookout*), the entire Section 481(a) positive adjustment →

must be taken into income entirely in the year of change. Section 9.01 of Revenue Procedure 92-20 provides specifically for this result by referring to IRS Announcement 91-173.

In all other situations, unless the Service has published guidance requiring a Section 481(a) adjustment, voluntary changes involving LIFO methods can be made using the **cut-off** method thereby avoiding any prior year recomputations. The allowance of the use of the cut-off method which avoids having to go back and redo all prior years can provide a significant benefit. Voluntary changes within the LIFO method should not necessitate Section 481(a) recomputations, except as indicated above.

If the LIFO taxpayer is audited and has not previously requested permission to change either an A or a B accounting method, again there is the opportunity under the 90-day window to file a Form 3115...but the year of change will be the earliest open year (i.e., the first year under audit) and, instead of the cut-off method, a Section 481(a) adjustment must be computed on a modified ten-year look-back basis (which may require reasonable estimates) and the resulting Section 481(a) adjustment will be spread over not more than six years. About the only taxpayer benefit in this approach is that if the LIFO election has been in existence for a very long period of time, there is a deferral of the repayment of any of the LIFO reserve built up before the tenth preceding year. This modified Section 481(a) computation is not available if the LIFO accounting method involves a *Hamilton* type of bulk bargain purchase...in which case the Section 481(a) adjustment must be recomputed for all years, although the taxpayer should be allowed the six-year spread.

The third alternative, that of not filing a Form 3115 either before audit or under the 90-day window, results in the Revenue Agent making the adjustment as part of the audit process, usually making the first year under audit the year of change and allowing no spread period whatsoever. Again, the progression of graded or graduated incentives for taxpayer-initiated "voluntary" Form 3115 filings is obvious. Also note that after the 90th day, examining agents may require a full Section 481(a) computation for all LIFO years, rather than allowing the taxpayer the more limited ten-year look-back computation available only under the 90-day window. ✻

EXCEPTIONS TO THE 3 AND 6 YEAR SPREAD PERIOD RULES

In a number of instances, Revenue Procedure 92-20 allows taxpayers to spread a net Section 481(a) computation adjustment over periods of up to three years or up to a maximum of six years. However, there are several exceptions and circumstances that will shorten the adjustment periods to less than 3 or 6 years.

1. If the entire net Section 481(a) adjustment is less than $25,000, either positive or negative, the taxpayer may elect to use a 1-year adjustment period instead of the adjustment period otherwise provided. This requires an affirmative statement attached to Form 3115 if the taxpayer wants this de minimis rule applied.
2. If 90% or more of the net Section 481(a) adjustment is attributable to the tax year immediately preceding the year of change, the taxpayer must take the entire net Section 481(a) adjustment into income in the year of change. Note that this requires the computation and comparison of the amounts of Section 481(a) adjustment for **two** years. If the 481(a) adjustment for the preceding year cannot be accurately computed, reasonable estimates can be used and a special statement regarding the use of estimates must be signed and attached to Form 3115. This condition replaces the previous test that required a reduction of the spread period if 67% of the Section 481(a) adjustment was attributable to any combination of the three years preceding the year of change.
3. In some instances, the number of taxable years that the method being changed has been used may be less than the number of years in the spread period. In these cases, the net Section 481(a) adjustment must be taken into account in computing taxable income ratably over the number of taxable years the present method has been used, if that number is fewer than the number of years in the adjustment period otherwise provided.
4. If the year of change or any year during the Section 481(a) adjustment period is a short taxable year, that short taxable year must be counted as a separate, full taxable year as if it had 12 months. Where this happens, the net Section 481(a) adjustment must be included in income as if such short taxable year were a full 12 months.
5. A significant reduction in inventory value will trigger an acceleration of the adjustment period, but exceptions are provided if the taxpayer can show that the inventory reduction was attributable to a strike, involuntary conversion or involuntary interruption of the availability of goods.
6. Ceasing to engage in the trade or business to which the Section 481(a) adjustment relates will also accelerate the spread period.
7. Certain other transfers to which Section 381(a) applies, or to which Section 351 in consolidated group situations applies, also have special rules.
8. Finally, a subsequent LIFO election will trigger the acceleration of some of the Section 481(a) adjustment. The amount accelerated is based on the unamortized balance attributable to the prior method change and certain other "catch up" timing factors.

TAXPAYERS CURRENTLY UNDER AUDIT:THE 180-DAY TRANSITION RULES

Many taxpayers were under IRS audit when Revenue Procedure 92-20 was published in March. These taxpayers are allowed to use special 180-day transition rules that include not only taxpayers under examination on March 23rd, but also taxpayers contacted for examinations before September 19, 1992. Note that the 90-day window period for filing Form 3115 after the start of an audit (discussed in relation to pre-audit contact change requests) may overlap and run beyond the September 18, 1992 deadline date in audit situations where the IRS audit date begins after the middle of June. Where the 90-day window period will run beyond the September 18, 1992 grandfather date, it seems to be desirable to complete Form 3115 filings before the end of the 180-day grace period on September 18, 1992.

CATEGORY A METHODS

The transition rules for taxpayers during the period ending September 18, 1992 are different depending on (1) non-LIFO Category A method situations, (2) non-LIFO Category B situations and (3) situations involving LIFO inventories. **WARNING**: Category A situations require a further breakdown differentiating between situations where the method had been audited to the point where the IRS had an **issue pending** evidenced by written notification to the taxpayer **on March 2, 1992**. For Category A method situations only, March 2, 1992 is a critical date. If a Category A method (LIFO or non-LIFO) issue was pending on March 2, 1992, the taxpayer will **not** be permitted to file a Form 3115 to change a Category A method. In this circumstance, the IRS agent will make the adjustment as part of the audit examination, presumably using the earliest open year as the year of change and with little incentive to offer any spread period for the required Section 481(a) adjustment.

For a non-LIFO Category A method, if an issue was not pending on March 2, 1992, the 180-day transition rule allows the filing of Form 3115 by the September 18, 1992 deadline to result in the year of change being made retroactive to the earliest open year under audit and a 3-year spread period for a Section 481(a) positive adjustment. It appears that this result follows even if an issue was not pending on March 2, 1992 but was raised by the examining agent in writing some time between that date and the September 18, 1992 deadline.

As indicated above, for a LIFO Category A method issue, the taxpayer is prevented from filing Form 3115 to change that method if there was an issue pending with written notification on March 2, 1992. This leaves the taxpayer with no guarantee of any spread period and the less attractive, but more imperative, need to attempt to settle or negotiate at Appellate for whatever can be obtained in the best manner possible.

With respect to LIFO Category A issues, if a LIFO issue was not pending on March 2, 1992, the 180-day transitional rule/September 18, 1992 deadline further subdivides depending on whether or not a method of accounting issue is pending AT THE TIME/ON THE DATE the Form 3115 is filed. If, on the date the Form 3115 is filed, an issue is pending with respect to the LIFO method, the year of change will be the most recent taxable year that is being examined by the IRS as of March 23, 1992, but not later than the most recent taxable year for which a Federal income tax return has been filed as of the date the examination (in which the issue is pending) began. The effect of this rule is to move the year of change to an earlier year to the disadvantage of the taxpayer, although the cut-off method will be allowed, thus avoiding a Section 481(a) computation, except for *Hamilton Industry* type bulk bargain purchase situations.

If AT THE TIME/ON THE DATE the Form 3115 is filed, there is no issue pending, then so long as Form 3115 is filed before the September 18, 1992 deadline, the cut-off method will be allowed and the year of change will be the taxable year in which the Form 3115 is filed, or the subsequent taxable year if the Form 3115 is filed more than 180 days after the beginning of the →

SOME CONCERNS AND QUESTIONS: IS 92-20 REALLY (MEANT TO BE) AN AMNESTY?

There are a number of concerns and questions regarding Revenue Procedure 92-20 for which time will tell whether the Service intends to administer this Procedure in the nature of an "amnesty."

1. As indicated elsewhere, many agents are aggressively taking positions that changes within the LIFO methodology and LIFO index computations should be treated as Category A methods. If this result stands, then taxpayers are prevented from filing 3115's to secure more favorable transitional treatment. How the National Office rules on these matters will be critical.
2. The 180-day transitional rules for taxpayers under audit seem to allow more aggressive IRS agents to hastily set up a LIFO "issue pending" before a Form 3115 can be filed, thus moving the year of change back to the taxpayer's disadvantage.
3. In Section 10.01, the IRS reserves the right to decline to process any application for change in accounting method under this Revenue Procedure in situations in which it "would not be in the best interests of sound tax administration to permit the designated change." Just exactly what does this mean? Is one interpretation: Throw down your guns, come out with your hands up... and **maybe** we won't shoot?
4. The Revenue Procedure elsewhere indicates that its provisions are not intended to prevent an IRS agent or Appeals Officer from settling a particular taxpayer's case involving an accounting method issue by agreeing to terms and conditions that differ from those provided in the RP 92-20 "when it is in the best interest of the Government to do so." No examples are provided as to when or under what circumstances such special deals might be appropriate. Is this a one-way street?

taxable year. Under this rule, the only current situation where the cut-off method could not be used would again be *Hamilton Industry* type bulk bargain purchase situations.

CATEGORY B METHODS

For situations involving Category B accounting methods, whether non-LIFO or LIFO methods, the essential point of focus is whether or not at the time the Form 3115 is filed - within the 180-day transitional deadline expiring September 18, 1992 - there was an issue raised in writing by the IRS relative to the accounting method being changed.

For non-LIFO Category B methods of accounting, if the Form 3115 is filed before September 18, 1992 and an issue was pending at the time of filing Form 3115, then the year of change under the Section 14.02 transition rules becomes the most recent taxable year that is being examined by the IRS (i.e., the latest year under audit). However, a maximum 6-year spread period is allowed for the Section 481(a) positive adjustment.

For non-LIFO Category B methods of accounting, if an issue was not pending on the date the Form 3115 is filed, and the Form 3115 is filed before September 18, 1992, then the year of change is prospective, allowing the year for which Form 3115 is timely filed to be the year of change. The same maximum 6-year spread period is allowed for the Section 481(a) positive adjustment.

In connection with LIFO Category B methods, the critical question also involves whether or not an issue was pending on the date the Form 3115 is filed. Again, in the context of filing before the September 18, 1992 deadline, if a LIFO Category B issue is pending, then the most recent year under audit (i.e., the latest year under exam) becomes the year of change and the cut-off method is allowed, except for *Hamilton Industries* type situations.

If on the date the Form 3115 is filed, an issue is not pending with respect to the LIFO Category B method, then filing Form 3115 before September 18, 1992 will result in the year of change being the taxable year in which the Form 3115 is filed, or the subsequent taxable year if filed more than 180 days after the beginning of the taxable year, and the cut-off method is allowed, except for *Hamilton Industries* type inventory situations.

Some IRS agents are aware that if they can activate and make pending LIFO issues before the taxpayer can file Form 3115, they have an opportunity to move the year of change back in favor of the IRS. If this is done, one can question whether there is intended to be any sense or spirit of amnesty for taxpayers under 92-20. *

CATEGORY A & B METHODS: UNCERTAINTY

The classification of a method of accounting as either Category A or Category B is important because it affects the number of years a Section 481(a) adjustment can be spread as well as determining whether a taxpayer under audit will be allowed to file Form 3115 to prevent or avoid or minimize an examining agent's adjustments.

CATEGORY A METHODS

Category A methods of accounting are methods of accounting that the taxpayer is specifically not permitted to use under the Internal Revenue Code, the Regulations or a decision of the U.S. Supreme Court. Note that only Supreme Court decisions, and not Tax Court decisions, qualify for Category A status.

A Category A method is also a method that differs from a method the taxpayer is specifically required to use under these three same sources. Category A methods used by taxpayers are those which the IRS polices more carefully and opposes more vigorously because they are specifically prohibited by the Code, Regulations or Supreme Court decisions. Consequently, Category A methods receive less favorable terms and conditions than do Category B method changes. Taxpayers using impermissible Category A methods are punished more severely.

Revenue Procedure 92-20 includes a list, not meant to be all-inclusive, of Category A methods of accounting. The only reference to LIFO in the list of examples of Category A methods included in Section 3.06 refers to the use of the LIFO method where there has been a termination event, as described in Revenue Procedure 79-23, that occurred during a year not barred by the statute of limitations. Apparently, this only applies where the taxpayer is in a voluntary LIFO termination request situation.

CATEGORY B METHODS

Category B methods of accounting are any methods other than those methods determined to be Category A methods. It's that simple: it's a B only if it's not an A.

DESIGNATED A & DESIGNATED B METHODS

Under Revenue Procedure 92-20, there are additional references to, and special rules for, "Designated A" methods of accounting and "Designated B" methods of accounting where the Internal Revenue Service in a document published in the Internal Revenue Bulletin identifies a method of accounting as falling within either of these two categories.

In its concern over taxpayers not changing accounting methods when they are required to do so by changes in the statute/Internal Revenue Code, the IRS has included Designated Category A methods as including those where changes have been required by statute or the Regulations. Apparently, the IRS does not plan to provide further information on what methods are Designated A methods and this has left some questions unanswered.

A MAJOR UNCERTAINTY FOR LIFO TAXPAYERS

One very significant aspect of the controversy or debate over whether a method of accounting is a Category A or a Category B method is found in the 180-day transitional period rules for taxpayers under audit on March 23, 1992. The transitional rules expiring September 18, 1992, provide that a taxpayer is not permitted to file a Form 3115 to change a LIFO Category A method if an issue was pending on March 2, 1992 with respect to the Category A method.

Many agents are taking the aggressive position that LIFO accounting computations and LIFO methods (sub-elections on Form 970) are Category A methods, thereby seeking to prevent taxpayers from filing Forms 3115 to obtain the more favorable terms and conditions under which to change their methods.

AUTO DEALER LIFO AMNESTY?...NOT! (FOR EVERYBODY)

BACKGROUND AND CONCLUSIONS

The ink was hardly dry on Revenue Procedure 92-20 when a number of commentators began interpreting it as if it were stone tablets containing the Ten Commandments for LIFO computations their way. Out went a clarion call for Form 3115 filings *en masse*. Many auto dealer associations distributed bulletins containing a number of statements about Rev. Proc. 92-20 that weren't even accurate and created misleading impressions. Several CPAs called the IRS and spoke to IRS technicians who were equally concerned over inaccurate statements and implications attributed to the IRS and/or to the Revenue Procedure.

On May 29th, I summarized my own reaction in an interim report conveying my thoughts and impressions at that time to *LIFO Lookout* subscribers. This is reproduced in full below.

Over the past weeks since then, I have received comments from many CPAs supporting and reinforcing the comments I made in that bulletin. Most CPAs who called had independently reasoned to many of the same general conclusions, which I will try to summarize below.

1. For those clients whom we had initially put on LIFO using methods we were comfortable and satisfied with, and which the IRS over the years had been satisfied with on audit, Forms 3115 were not being filed at this time.

2. Where newer clients, acquired in more recent years, had been put on LIFO by other CPAs using less desirable unit, averaging, otherwise messy or unjustifiable computational approaches, and especially where invoices for year-end inventories are no longer available, Form 3115 was being filed in advance of the 180-day deadline in order to make calendar year 1992 the year of change and to seal off pre-1992 years from a Section 481(a) adjustment.

3. In a number of instances, technically a single new vehicle pool might be split into two pools, one for new cars and one for new trucks, in accordance with *Fox Chevrolet*. However, where the dollar investments in new cars and in new trucks had remained fairly constant in relation to each other over the years, or where there might have been significant paybacks of LIFO reserves in prior years, many practitioners felt it was not necessarily advisable at this time to seek a method change to split the pools. In other instances, the decision to not split pools now was supported by documented prior IRS audit of the dealer's single pool arrangement, in which the IRS agent had concluded that the dollar amount of the adjustment based on splitting the pool was so small as to be unwarranted and an adjustment or change was not required as part of the audit.

TO THE AUTO DEALER ON LIFO; (INTERIM BULLETIN) MAY 29, 1992

A few weeks ago in March, the IRS issued Revenue Procedure 92-20 updating procedures and transition rules under Section 446 for requesting IRS permission to make changes in accounting methods. This Revenue Procedure applies to all accounting method changes and it includes special rules for taxpayers using LIFO and other special transition rules for taxpayers currently under audit.

This Revenue Procedure is a comprehensive document and it was not written with auto dealer LIFO applications in mind, although certain auto dealer LIFO issues and situations may fall within its scope.

Some state dealer associations have sent bulletins that are surprisingly erroneous and misleading in certain respects to all their dealers "explaining" this new Procedure. How some of these bulletins ever got out without being more carefully checked or edited is hard to understand given the more usual higher level of accuracy in important dealer communications. Nevertheless, these bulletins are creating more confusion and resulting in some CPAs being pressured and harassed unnecessarily by their understandably confused dealer clients.

CPAs who have called the Internal Revenue Service (at the number given in the Revenue Procedure), indicate that certain IRS personnel said they were astonished or surprised that anyone could interpret Rev. Proc. 92-20 the way some of these bulletins have. I have had such conversations with the IRS myself and also have corresponded with IRS Assistant Commissioner Hatcher urging some clarification.

One of the totally false statements and inferences in some bulletins is that R.P. 92-20 describes, refers to, or requires some kind of new, more exacting, method of LIFO computations for auto dealers. This is absolutely FALSE! The Revenue Procedure contains no discussion of - nor even any reference to - any "new method" that compels an individual analysis of every option and accessory on a new vehicle invoice.

Although more detailed LIFO computational approaches may be preferred by some IRS agents and conceded by some dealers, the fact is that auto dealers in many parts of the country are not being held to unnecessarily high standards. Many LIFO audits involving less detailed repricing are being settled regularly with little or no change. Today! Right now! All over the USA!...Why should any dealership be treated differently?

The Revenue Procedure also states that if there are eligibility problems underlying the LIFO election - like originally failing to file Form 970 or a financial statement LIFO disclosure violation (which are not the same as disagreements over how indexes should be computed) - there are more serious consequences and the more favorable terms in the Procedure are not applicable.

(Continued on facing page) →

Pity the poor dealer (or CPA) who thinks he is only requesting a change in accounting method but later is required to make a statement under oath that there has not been a LIFO terminating event! If the CPA or dealer has knowledge that a LIFO terminating event occurred in the past, and must be disclosed, this will present a major dilemma at an embarrassingly late stage.

IRS Appellate personnel are not necessarily bound to settle audit issues following the guidelines in the new Procedure...and certain IRS offices are now deliberately interpreting pending LIFO disputes aggressively in trying to prevent dealers under audit from receiving the benefits of its provisions. (Amnesty?) These aspects of Revenue Procedure 92-20 warrant further clarification - or at least uniform acceptance by the IRS field offices.

There is another reason for more reflection before making a knee-jerk reaction to these bulletins. As a result of a special meeting with NADA a few weeks ago, the IRS is considering the possibility of clarifying the appropriateness of various auto dealer LIFO practices. Although this may be a slow process, if clarification comes from the IRS, it may give dealers further insight into whether they really need to change anything. And if so, there may be more specific information or parameters for what an acceptable method will entail. I have had several recent conversations that now leave me more patiently optimistic.

Top level IRS personnel today are well aware that a dealer in one part of the country can get by not repricing options and still have an acceptable LIFO computation...while another dealer with identical inventories elsewhere in the country may be required to do the computations in far more detail and at far greater annual cost.

The IRS is also aware of, and seems concerned about, the scary stories and scare tactics following LIFO audits where agents have gone in and applied unrealistic requirements in a retroactive manner. Everyone from the Commissioner on down seems to be more tuned into these LIFO problems, issues, and inconsistencies, as never before.

Some CPAs, after considering their own LIFO practices, have concluded that since there really is no "new" method stated at the present time, there is no real reason to act under Rev. Proc. 92-20 to request IRS permission to change anything at this time.

On the other hand, certain double extension, averaging, unit, or unauthorized external index methods may already have significant exposure if they are far out of hand and present a more compelling reason for immediate change. But if, as the "price" of the change, a dealer has to agree to spend unnecessary dollars every year to compute LIFO indexes in unnecessary detail, that is also a factor to consider. And a factor for the IRS to address. This may be where making a change now might unnecessarily lock a dealer into more extensive annual computations in the future.

Some proponents of "change now" rattle the specter of "look what happens if you're caught on audit." Other CPAs are confident that their LIFO computation practices will not result in any material adjustments, especially if invoices are available and the dealer's LIFO computations are vigorously and intelligently defended. In view of the more substantial IRS interest and activity addressing dealer LIFO computational issues, waiting a little longer to see what happens may be reason enough for some dealers and CPAs to live a little longer with whatever risk already exists with their current LIFO computations.

The IRS seems - or may be - more willing to allow some flexibility in LIFO calculations as long as there is no abuse or distortion of income. If so, this will need to be communicated from the top. The IRS now seems to be more aware that hammering car dealers over the head with total or 100% accuracy requirements in LIFO calculations is TOTALLY INCONSISTENT with its own self-created and broadly announced Compliance 2000 goals and posture, with statements made by IRS Commissioners (past and present) about IRS willingness to be responsive to taxpayers' needs, and with thousands of audits in which less exact calculations were accepted with little or no change.

In jumping to a general conclusion that now is the time to make a change, some CPAs may be subordinating their judgement to others without adequate investigation of the issues. Any dealer contemplating filing a Form 3115 at this time might find that his or her current computational approach is not necessarily one that needs to be changed and ought to proceed with caution.

When you are in a crowded building and somebody shouts "Fire" and almost everybody runs for the exits, you can't help but wonder if you should get out first and think about why from a safe distance later. This stampede to the National Office with Forms 3115 is not one all dealers need to get involved with right now.

Remember, there is no new method! Call the IRS and you will hear this for yourself, as many other CPAs, including myself, have. Have your CPA call the IRS and ask a few questions on your behalf, and you may find out that some of the information about R.P. 92-20 in some bulletins or interpretations is not necessarily the whole story. Maybe you're being set up for something you might not need or might regret later. Consider obtaining an independent second opinion from a knowledgeable CPA and question the motivation of anyone trying to sell something that maybe isn't necessary or required at this time.

If it will help you to look before you leap, I can give you the names of several CPAs in your area or community who are not trying to sell LIFO calculations "their way" or fill up summer slack time with chargeable work. They will patiently take the time to help you through more of the details.

WILLARD J. DE FILIPPS, CPA (May 29, 1992)

"BIG 6" LIFO PRACTICES CUT DOWN TO 4 FOR AUTO DEALERS

In the September, 1991 *Lookout* I summarized six major LIFO computational "practices" used by auto dealers in "Theory, Practice & IRS Audit Issues: What's Going on Out There." See reprint of that article enclosed for your reference. These major LIFO practices, in the order listed, were:

1. Averaging approaches...whereby essentially the total dollar amount of general ledger cost or carrying value of the inventory is divided by the number of units in arriving at an average cost per vehicle. (Old number: #1 - new number: #_ gone! because in many instances the older the LIFO election, the greater the distortion -and the less supportable the results - caused by these cruder or unrefined averaging practices.)
2. Repricing approaches in which every ending inventory invoice and every option and accessory included on every invoice, plus all other capitalizable costs, are repriced in arriving at an overall weighted index for the inventory pool. (Old number: #2 - new number: #1)
3. Repricing approaches in which the index is determined by repricing a representative portion (some, but not necessarily all, invoices or base prices) and less than every option and accessory (in some cases none) listed on the invoice. (Old number: #3 - new number: #2)
4. The determination of a "prototype" index for each make, with that index applied to a dealer's ending inventory, without reference to specific invoices in the ending inventory, i.e., "one size fits all." (Old number: #4 - new number: #_ going fast, if not entirely gone...see UPDATE #3, on page 2 of this issue)
5. The use of acceptable external indexes developed from published price indexes, most notably Table 6 of the Producer Price Indexes. (Old number: #5 - new number: #3)
6. A variety of other approaches...this catch-all category includes anything not falling within the five major LIFO practice groupings listed above. (Old number: #6 - new number: #4, including now some averaging approaches not changed and some "prototype" or "one size fits all" indexes not changed)

It seems that one of the practical consequences of Revenue Procedure 92-20 activity is that the "Big 6" major alternatives may be cut down to (perhaps) the "Big 4": namely, numbers #2-#3-#5 have survived (with some more faint-of-heart types switching from number #3 to number #2). There will always be a final catch-all category. So that leaves four. The two more likely to be dropping out as a result of the Revenue Procedure 92-20 "amnesty" seem to be number #1 (harder to defend averaging approaches) and number #4 (the "one size fits all" approach).

One of the more notable LIFO computation methods included in the original #6 catch-all category is the unit method. Many dealers and CPAs took the opportunity presented by Revenue Procedure 92-20 to get off this dangerous unit method and switch to a link-chain, index method knowing full well the impossibility of otherwise defending LIFO reserves built up over the years through the unit method.

IN SUMMARY: My estimate is that Revenue Procedure 92-20 may have significantly reduced in number some of the more widely applied alternative LIFO methods used by auto dealers. But, of those remaining, there is clearly the need for some definitive statement now by the Internal Revenue Service, preferably by an amendment to the Regulations or in a Revenue Procedure, clarifying whether, in fact, there should only be one. And if so, what shall it be? As mentioned in this issue's UPDATE, what should be interesting is the justification or theory the IRS will have to come up with to rationalize the **ABSOLUTE CONFLICT** between (1) its allowance of the sampling methodologies requested by many 92-20 applications (including substantially all of those moving away from the "prototype" index approach) and (2) the so-called "100% accuracy" position attributed to it by advocates of new method number #1.

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DEALER EXTENDED SERVICE CONTRACTS: ANOTHER REV. PROC. 92-20 APPLICATION

In a Technical Advice Memorandum issued earlier this year, the IRS took the position that an automobile dealer who sold extended service plan contracts and purchased insurance from a third party to cover that risk was required to include in gross income the gross amount of the customer payment in the year of receipt, but the dealer could not deduct the full cost of the insurance purchased. Instead, the dealer was required to amortize the related insurance payment over the life of the insurance contract. This position results in a mismatch of income and deductions and, in some instances, creates severe cash flow problems.

IRS audit activity on dealer extended service contracts has been very intense, both before and after publication of the Technical Advice Memorandum.

Many dealers were unsure whether or not they should change their accounting method for vehicle service contracts by filing Form 3115. After considerable discussion between the NADA and the IRS, the Service concluded that it would issue a separate Revenue Procedure for certain dealers not under audit that would enable them to change extended service contract accounting methods without having to file a Form 3115 with the National Office by June 28(29), 1992.

This affects only those dealers who are considered as obligors on the contracts they sell. The Service plans to issue a Revenue Procedure to allow these dealers to expeditiously change their method of accounting with the automatic consent of the Commissioner.

This Revenue Procedure, when issued, will apply to manufacturers, wholesalers and retailers of motor vehicles that sell multi-year service warranty contracts on those vehicles and insure their risks under the contracts. The expedited procedure will **not** apply to taxpayers that cover their risks through arrangements that do not constitute insurance. Also, the expedited procedure will not apply to a taxpayer that has received written notification from the examining agent before June 12, 1992 citing the extended service contract issue. For further details, see Announcement 92-92 (I.R.B. 1992-27, June 17, 1992).

Apparently, the IRS is seriously considering what is referred to as a "dealer proxy" approach which the dealer could elect to apply in lieu of the rules in Technical Advice Memo 9218004. Both the IRS and NADA are still working out the details and eventually the Form 3115 accounting method change procedures and ramifications will be published.

1992 SEMINARS

REVENUE PROCEDURE 92-20
ANALYSIS...APPLICATION...AMNESTY(?)

A NEW SEMINAR FOR 1992

OBJECTIVE: Familiarization with accounting methods used for tax purposes that require change or modification to satisfy IRS requirements and with procedures to be followed in making and filing change requests with the IRS National Office in Washington, D.C.

◻ Aug. 03 - Indianapolis, IN	Holiday Inn Indianapolis Airport	2501 S. High School Road	(317) 244-6861
◻ Aug. 05 - Atlanta, GA	Holiday Inn Atlanta Airport South	5010 Old National Hwy.	(404) 761-4000
◻ Aug. 07 - Orlando, FL	Marriott Orlando Airport	7499 Augusta National Drive	(407) 851-9000
◻ Aug. 10 - Rolling Meadows, IL	Holiday Inn Rolling Meadows	3405 Algonquin Rd (Rt.62) at Rt. 53	(708) 259-5000
◻ Aug. 12 - St. Louis, MO	Holiday Inn St. Louis Airport (Oakland Pk)	4505 Woodson Rd.	(314) 427-4700
◻ Aug. 14 - Walnut Creek, CA	Holiday Inn Walnut Creek	I-680 & 2730 N. Main St.	(510) 932-3332
◻ Aug. 17 - Los Angeles, CA	Holiday Inn Los Angeles (Int'l Airport)	9901 LaCienega Blvd. at Century Blvd.	(310) 649-5151
◻ Aug. 21 - Dallas, TX	Holiday Inn Dallas/Ft. Worth Airport So.	4440 W. Airport Fwy (Hwy 183) (Irving)	(214) 399-1010
◻ Aug. 24 - Livonia, MI	Holiday Inn Livonia West	17123 Laurel Park Drive North	(313) 464-1300
◻ Aug. 26 - Pittsburgh, PA	Holiday Inn Pittsburgh (Int'l Airport)	1406 Beers School Rd.(Coraopolis)	(412) 262-3600
◻ Aug. 28 - Baltimore, MD	Holiday Inn Baltimore (Int'l Airport)	890 Elkridge Landing Rd. at Airport Rd.	(410) 859-8400
◻ Aug. 31 - New York, NY	Holiday Inn New York (LaGuardia Airport)	104-04 Ditmars Blvd. (East Elmhurst)	(718) 457-6300

Please use Registration Form on enclosed brochure.

LIFO for AUTO DEALERS 1992 Seminars

Surviving IRS ATTACKS and AUDIT ISSUES

OBJECTIVE: This full day seminar discusses LIFO eligibility requirements, practical computational techniques, IRS audit issues and LIFO practices you can successfully defend and others that are ticking time bombs now being set off in dealerships around the country by IRS auditors through its coordinated Motor Vehicle Industry Specialization Program.

◻ Oct. 02 - Walnut Creek, CA	Holiday Inn Walnut Creek	I-680 & 2730 N. Main St.	(510) 932-3332
◻ Oct. 06 - Los Angeles, CA	Holiday Inn Los Angeles (Int'l Airport)	9901 LaCienega Blvd. at Century Blvd.	(310) 649-5151
◻ Oct. 21 - Baltimore, MD	Holiday Inn Baltimore (Int'l Airport)	890 Elkridge Landing Rd. at Airport Rd.	(410) 859-8400
◻ Oct. 26 - Pittsburgh, PA	Holiday Inn Pittsburgh (Int'l Airport)	1406 Beers School Rd. (Coraopolis)	(412) 262-3600
◻ Oct. 28 - Livonia, MI	Holiday Inn Livonia West	17123 Laurel Park Drive North	(313) 464-1300
◻ Nov. 04 - Dallas, TX	Holiday Inn Dallas/Ft Worth Airport So.	4440 W. Airport Fwy (Hwy 183) (Irving)	(214) 399-1010
◻ Nov. 06 - St. Louis, MO	Holiday Inn St. Louis Airport(Oakland Pk)	4505 Woodson Rd.	(314) 427-4700
◻ Nov. 11 - Atlanta, GA	Holiday Inn Atlanta Airport South	5010 Old National Hwy.	(404) 761-4000
◻ Nov. 13 - Orlando, FL	Marriott Orlando Airport	7499 Augusta National Drive	(407) 851-9000
◻ Nov. 18 - Rolling Meadows, IL	Holiday Inn Rolling Meadows	3405 Algonquin Rd. (Rt 62) at Rt. 53	(708) 259-5000
◻ Nov. 20 - Indianapolis, IN	Holiday Inn Indianapolis Airport	2501 S. High School Rd.	(317) 244-6861

Please use Registration Form on enclosed brochure.