



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. MOUNTAIN STATE FORD TRUCK SALES & THE USE OF REPLACEMENT COST FOR VALUING PARTS INVENTORIES.

In a nutshell, this is still one of the most controversial unresolved LIFO issues. The Tax Court decision upholding the IRS is still on appeal. However, this appeal has been put on hold because the Treasury has said that it intends to issue an industry-wide resolution and guidance in the near future.

How soon? What will taxpayers have to do? Will they have to pay penalties for using improper methods in the past? Will prior year inventories have to be recomputed? If so, how far back in time? Stay tuned. We'll have something specific to report ... after the Treasury commits itself to a course of action on this.

#2. FORM 970 GETS A FACELIFT. The Form for making LIFO elections has been revised, although not substantially. If you are making new LIFO elections, be sure to use the revision dated September, 2001. For more on these changes, see page 4.

#3. LIFO IMPLICATIONS FOR DEALERSHIP

QSUB GROUPS. We've received many calls asking how to handle LIFO calculations for dealer groups that have elected S Corporation treatment. Unfortunately, there are many questions for these QSub groups, but not many answers.

Some questions involve dancing around with the elusive notion of *separate trades or businesses*. Others highlight uncertainties and pitfalls that you're either already up against or that are waiting for your clients when QSub elections are made. If you want more, see page 6. After you're done with the article, maybe you'll be sorry you did.

#4. AUTO DEALERS WHO WANT TO TERMINATE LIFO FOR USED VEHICLES ... AN IMPORTANT WARNING. Be careful about the timing of filing Form 3115 if you have both new and used vehicles on LIFO. If you want to terminate

LOOKOUT LOOKS INTO

LIFO UPDATE	1
FORM 970 GETS A FACELIFT	4
LIFO PITFALLS FOR S CORP QSUB GROUPS	6
YEAR-END ALERT: SPECIAL LIFO CHALLENGES: CONFORMITY REPORTING REQUIREMENTS & PROJECTIONS FOR YEAR-END PLANNING	11
QUICK YEAR-END INFLATION ESTIMATES FOR AUTO DEALERS - SUMMARY	23
DETAIL BY MAKE FOR QUICK YEAR-END ESTIMATES FOR AUTO DEALERS 2001-2002 NEW VEHICLE INFLATION SURVEY ASSUMING ENDING INVENTORY MIX OF ONE-OF-EACH ITEM CATEGORY	24

only the used vehicle LIFO election, you must obtain permission, in advance, from the IRS National Office. The Form 3115 requesting this change must be filed **before the end of the year of change** (i.e., before December 31, 2001 for a calendar year taxpayer).

On the other hand, if you want to terminate **both** LIFO elections for new and for used vehicles **at the same time**, this change does not require advance permission from the National Office. The Form 3115 to terminate all existing LIFO elections at the same time is not required to be filed with the National Office until the original of Form 3115 is filed as part of the income tax return for the year of change. This change is automatic under Rev. Proc. 99-49.

#5. AUTO DEALERS WHO WANT TO STAY ON LIFO FOR USED VEHICLES ... AN IMPORTANT REMINDER.

Calendar year dealerships that want to make an automatic change to the Used Vehicle Alternative LIFO Method must do so when they file their 2001 tax returns. Otherwise, this change in a later year cannot be made without advance approval from the IRS.

Section 5.02(1) of Rev. Proc. 2001-23 states that the change can be made automatically "*provided the change is made for the first or second taxable year ending on or after December 31, 2000.*"

The intention of the IRS was not to give calendar year taxpayers "three years of choice." Accordingly, a calendar year dealership may make the change to the R.P. 2001-23 Method without permission for either its calendar year 2000 or its calendar year 2001. So if you have not already made the automatic change, your 2001 tax return is your last chance even though, literally, "the *second* taxable year ending on or after December 31, 2000" for a calendar year would be calendar year 2002.

#6. DEALERS IN TRANSITION FACE LIFO RECAPTURE ISSUES. *For Some Olds Dealers, LIFO Reserves Go Down the Drain as GM Pulls the Plug.* One nasty result as GM starts to phase out Oldsmobile concerns the recapture of LIFO reserves by dealers who face the prospect of losing inventory that they can't replace for LIFO purposes before year-end.

Some say there may be an opportunity for Olds dealers to try to seek reimbursement from GM for the unexpectedly hastened repayment of their LIFO reserves. How successful they might be could depend, in part, on the actual results when LIFO layer penetrations are computed.

How Much LIFO Recapture? How much and how quickly can only be determined on a dealer-by-dealer basis. Single franchise Olds entities will face recapture consequences more drastically than dual or multiple franchise operations. Another variable is the method of LIFO being used because potential recapture will be different for dealers using the Alternative LIFO Method, than for dealers who are not.

Under the Alternative LIFO Method for new vehicles, dealers who have Oldsmobile *and* other franchises as well may be able to offset a decrease in the new autos pool caused by a drop in Olds inventory. This can be done by increasing, to some extent, the other make new inventories which are included in the new autos pool. After all, the Alternative Method provides that *all* new automobiles, regardless of manufacturer, *must* be included in the same single pool.

Recapture Arguments & Vulnerabilities. But, could there be a fly in the ointment? Might the Service argue that Rev. Proc. 97-36 should not be interpreted as limiting or preventing LIFO reserve recapture where the dealership no longer continues to hold the franchise? In some instances, the Service has attempted to treat the disposition of a franchise

of a particular make of vehicles as an event requiring the recapture of the associated LIFO reserve. It has even stated this in its *IRS Audit Guide for Auto Dealerships*.

On other occasions, the Service has attempted to recapture the LIFO reserve attributable to a specific franchise by requiring a vertical-slice approach ... instead of the horizontal-slice or LIFO approach which is generally applied. The IRS thought vertical-slice recapture was more appropriate in order to "*clearly reflect income.*"

Where a dealer's inventory at the end of the year has been significantly reduced (because of the reduction in overall operations) is vertical or horizontal slice treatment appropriate? By removing a portion of all of earlier costs proportionally, the vertical slice approach results in more recapture of the LIFO reserve. In contrast, the horizontal slice approach generally produces less recapture. For more information on vertical vs. horizontal slicing, see the write-up in the June, 1999 *LIFO Lookout*.

In some instances where we were involved, the issue was raised by the IRS auditor and a request for ruling was made to the National Office. In these cases, the agent dropped the issue when the National Office informally indicated that it would rule in favor of the taxpayer and not support the agent's position.

However, in another situation, this issue went through the entire ruling process. In Technical Advice Memo (LTR) 199920001, the IRS National Office had to decide whether the examining agent should require an accelerated recapture of the LIFO reserve where a sale of inventory occurred as part of the organization's overall downsizing.

The National Office rejected the agent's arguments and allowed the taxpayer to treat the sale of inventory as if it were made in the ordinary course of business. Although this case did not involve an automobile dealer, it has many similarities to what dealers are facing in their current transition environment.

For example, take the current GM Olds phase-out situation: Query: Might the IRS argue for LIFO recapture treatment on similar grounds in situations where automobile dealerships are "required" to sell off the inventories of a franchise in order to comply with the realignment or consolidation objectives of the manufacturer? Is the case made stronger or weaker because the liquidation of the dealer's inventory is really the result of an *involuntary* conversion?

Here's another case: What about voluntary sales or exchanges of franchises by auto dealers? →



Many large dealers have multiple franchises, and they sell and/or trade franchises in transactions like this on a regular basis.

For example, what if a dealer has five or six franchises at the beginning of the year, sells off one of them during the year, and acquires another franchise before the end of the year? No big deal, just getting rid of one franchise and replacing it with another. In this case, the overall or total dollar amount of investment in inventory (for all franchises combined) at the beginning of the year and at the end of the year might be about the same, despite the fact that one business component/franchise has been entirely eliminated and replaced by a completely different franchise.

We could sure use some answers here.

#7. LIFO CONFORMITY: WATCH THOSE YEAR-END FINANCIAL STATEMENTS. There is no reason to expect the IRS to be lenient if it finds any violations of the LIFO conformity requirements on year-end financial statements. Such violations allow the IRS to take the position that the LIFO election must be terminated, although asserting that penalty is discretionary with the IRS Commissioner.

With this in mind, it's appropriate to review our annual reminders about year-end projections, estimates and the importance of placing proper LIFO inventory disclosures in the year-end financial statements. To this end, we have reproduced last year's article beginning on page 11 and urge you to read or re-read it as the case may be.

#8. DOCUMENT YOUR YEAR-END LIFO PROJECTIONS. Many businesses find it necessary to estimate LIFO reserve changes before the final amounts can be calculated, especially for income tax planning purposes. Knowing what is expected to happen before year-end is very important because these projected changes affect fourth quarter installments of estimated tax due Dec. 15 of this year or Jan. 15 of next year.

The conformity article discusses how to project LIFO reserve changes quickly and effectively. This begins on page 18. It also discusses strategies for managing year-end inventory levels beginning on page 20.

#9. YEAR-END PROJECTIONS FOR AUTO DEALERS BASED ON "ONE-OF-EACH" MIX ASSUMPTION. Most auto dealers are under great pressure to release their year-end financial statements before their actual LIFO calculations can be completed. To assist in making year-end projections, each year we provide a listing for new

vehicle LIFO inventories showing weighted average inflation (deflation) information for each model.

Our report compares everything in our SUPERLIFO database as of December 1, 2000...with intro-2002 model prices, unless the 2002 intro price was subsequently updated, and that information is also in our database for the end of the year. December 1, 2000 is the reference date for the equivalent of the calendar year 2001 beginning of the year date; i.e., December 31, 2000/January 1, 2001.

The summary on page 23 shows that for most new vehicles, the overall price increases are small again this year. This is due to competitive pressures among the manufacturers and currency pressures. Also, some manufacturers changed option packages either to or from standard base vehicles. There is some subjective language built into the tests under the Alternative LIFO Method for determining whether or not a vehicle is a "new" item or a "continuing" item. Our one-of-each inflation indexes for each manufacturer reflect all of these factors.

This year, there has been a significant number of model and item category increases for the 2002 Ford cars and trucks, particularly the *Crown Victoria*, *Escort*, *Focus*, *Taurus*, *Escape*, *Excursion*, *Explorer/Sport* and *Ranger*. Also significant are the price changes for 2002 Chevrolet *Tahoe* and *Suburbans* and Saturn models due to this year's models being more fully equipped than were last year's models.

The weighted averages we have computed are determined by taking all of the underlying item categories (for which information is currently available) and simplistically assuming that a dealer at year-end would have an inventory mix of one-of-each. These simplified, one-of-each inflation indexes may be used in year-end projections as a substitute for some other arbitrary or assumed inflation rate (like 1%, 2% or 3%) or by some other guesswork.

Warning. Our database is not entirely complete at this time because not all manufacturers have made their information available as we go to press. Notwithstanding this limitation, some readers have found our one-of-each results to be useful in estimating LIFO reserve changes or in comparing their results with ours. The detailed analyses for each make are on pages 24 to 31.

Reasonable Estimates. If you're going to reflect an *estimate* of the LIFO change for the year in a year-end Income Statement, that *estimate* should be a *reasonable* estimate in order to satisfy the IRS guidance found in Revenue Ruling 97-42. Unfortunately, no one really has any idea of what the IRS will

see LIFO UPDATE, page 10



FORM 970 FOR LIFO ELECTIONS GETS A FACELIFT

FORM
970

Taxpayers filing LIFO elections for calendar year 2001 tax returns should be sure to use the most recent revision of Form 970 which is now dated September, 2001.

It is generally understood that Form 970 must be filed in order to make the LIFO election in the first LIFO year. One very critical aspect of Form 970 involves the statement included in **Item B** in **Part I**. This statement emphasizes the fact that in filing the Form 970 and electing LIFO, the taxpayer agrees and/or consents ... "to make any adjustments that the IRS may require, on the examination of the taxpayer's income tax return, **to clearly reflect income** for the years involved in the change to or from the LIFO inventory method or due to the use of the LIFO inventory method." This statement binds the taxpayer to accept adjustments to inventory valuations involving all years **before, during** and **after** the use of the LIFO Method.

FORM 970 CHANGES

The revised Form 970 looks very much like its predecessor. The only differences are:

CHANGES

- The renumbering of Questions 4-12 on the old Form as Questions 4-13 on the new Form.
- The addition in Question 10 of a specific reference to the Used Vehicle Alternative LIFO Method as one of the methods that can be used in computing the value of dollar-value pools.
- The deletion of the "Penalties of Perjury" statement and the signature boxes from the bottom of the Form.

Question 7 asks for the description of the "method used to figure the cost of goods in the closing inventory over those in the opening inventory," i.e., how are annual inventory increments under the LIFO methodology going to be valued? Three specific possible entries are listed, along with the fourth entry as ... "Other." For auto dealers electing either of the Alternative LIFO Methods, it would appear that the appropriate response to Question 7 would be to check the "Other" box and write in either: "Rev. Proc. 97-36" for new vehicles or "Rev. Proc. 2001-23" for used vehicles. Under both methods, if an increment is computed for a year, that increment expressed in base dollars is required to be multiplied by the cumulative inflation rate as of the end of the year in

order to arrive at the proper LIFO valuation for that layer of increment.

Question 9 asks for the identification of the method for pooling the LIFO inventories. Six possible entries are listed, with the seventh entry as ... "Other." For auto dealers electing either of the Alternative LIFO Methods, it would appear that the appropriate response to Question 9 would be to check the "Other" box and write in: "Rev. Proc. 97-36" for new vehicles or "Rev. Proc. 2001-23" for used vehicles.

FORM 970 INSTRUCTIONS

The Instructions for Form 970 are still limited to one page of small print. However, the revised Instructions say that Form 970 ... *or a similar statement* ... should be filed with "your tax return for the first tax year you intend to use or expand the LIFO method."

In addition, some taxpayers will now get a break if they forgot to include Form 970 with the tax return. The Instructions state:

"If you filed your return for the tax year in which you wish to adopt and use the LIFO inventory method ... without making the election, you may make the election by filing an amended return within 12 months of the date you filed your original return. Attach Form 970 to the amended return and write '**Filed pursuant to Section 301.9100-2**' at the top of Form 970. File the amended return at the same address the original return was filed."

Be careful. The foregoing statement means only that if you already filed a tax return using LIFO, you can overcome the failure to include Form 970 by filing Form 970 as an attachment to the amended return. A taxpayer cannot amend a previously filed return that did not reflect LIFO by replacing it with an amended return that uses LIFO to value the ending inventory.

Consistent with the release in January, 2001 of the Used Vehicle Alternative LIFO Method, the Instructions refer to the Revenue Procedure (2001-23) where particulars on that method may be found.

Finally, the Instructions indicate that if the taxpayer previously filed Form 3115, *Application for Change in Accounting Method*, and received IRS consent to change for the current tax year, it is not necessary to attach a copy of the approval (grant) letter received from the IRS. Taxpayers are simply reminded to retain a copy of the letter for their records. *



Application To Use LIFO Inventory Method

OMB No. 1545-0042

Attachment
Sequence No. **122**

▶ Attach to your tax return.

Name

Identifying number

Check one: ☐ First election ☐ Subsequent election

Part I Statement of Election

	Yes	No
A The taxpayer elects to adopt and use the LIFO inventory method provided by section 472. The taxpayer will use (or expand) the LIFO inventory method for the first tax year ending (month, day, year) ▶ for the following goods (see instructions):.....		
B The taxpayer agrees, as required by Regulations section 1.472-4, to make any adjustments that the IRS may require, on the examination of the taxpayer's income tax return, to clearly reflect income for the years involved in the change to or from the LIFO inventory method or due to the use of the LIFO inventory method.		
C Was the beginning inventory for the items specified in Item A above valued at cost (as required by section 472(d)) for the first tax year this application applies? If "No," attach an explanation		
D Will inventory be taken at actual cost regardless of market value? If "No," attach an explanation		

Part II Other Information

1 Nature of business ▶		
2 Inventory method used until now ▶		
3 Will any adjustment that resulted from the change to the LIFO method be included in income over a 3-year period? If "No," attach an explanation		
4 List goods subject to inventory that will not be inventoried under the LIFO method ▶		
5 Were the goods specified in Part I, Item A treated as acquired at the same time and at a unit cost equal to the actual cost of the total divided by the number of goods on hand? If "No," attach an explanation		
6a Did you issue credit statements or reports to shareholders, partners, other proprietors, or beneficiaries covering the first tax year to which this application relates?		
b If "Yes," state to whom and on what dates ▶		
c Show the inventory method used to determine income, profit, or loss in those statements ▶		
7a Check method used to figure the cost of the goods in the closing inventory over those in the opening inventory (see instructions): <input type="checkbox"/> Most recent purchases <input type="checkbox"/> Earliest acquisitions during the year <input type="checkbox"/> Average cost of purchases during the year <input type="checkbox"/> Other (attach explanation)		
7b The taxpayer selects the month of as the representative month used in selecting the index or indexes used to determine the current-year cost of the taxpayer's inventory pool(s) under Regulations section 1.472-8(e)(2)(ii) (see instructions). This applies only to taxpayers using the inventory price index computation method.		
8 Method used in valuing LIFO inventories: <input type="checkbox"/> Unit method <input type="checkbox"/> Dollar-value method (see instructions)		
9 If you use pools, check the box that indicates the pooling method. List and describe the contents of each pool in an attached statement. <input type="checkbox"/> By line, type, or class of goods authorized by Regulations section 1.472-8(c) (retailer, wholesaler, jobber, or distributor) <input type="checkbox"/> Pooling method authorized by Regulations section 1.472-8(e)(3)(iv) (retailer, wholesaler, jobber, or distributor) <input type="checkbox"/> Natural business unit authorized by Regulations section 1.472-8(b)(1) (manufacturer or processor) <input type="checkbox"/> Multiple pools authorized by Regulations section 1.472-8(b)(3)(i) (manufacturer or processor) <input type="checkbox"/> Raw material-content authorized by Regulations section 1.472-8(b)(3)(ii) (manufacturer or processor) <input type="checkbox"/> Simplified dollar-value method under section 474 (see instructions) <input type="checkbox"/> Other (describe and justify)		
10 Method used in computing LIFO value of dollar-value pools (see instructions and attach required information): <input type="checkbox"/> Double-extension (describe) <input type="checkbox"/> New Vehicle Alternative LIFO <input type="checkbox"/> Index (describe and justify) <input type="checkbox"/> Link-chain (describe and justify) <input type="checkbox"/> Used Vehicle Alternative LIFO <input type="checkbox"/> Other method (describe and justify) <input type="checkbox"/> Published price index (describe)		
11 Attach a statement briefly describing the cost system used.		
12 Did you receive IRS consent to change your method of valuing inventories for this tax year?	<input type="checkbox"/> Yes	<input type="checkbox"/> No
13 Did you ever use the LIFO inventory method before? If "Yes," attach a statement listing the tax years you used LIFO and explain why you discontinued it.	<input type="checkbox"/> Yes	<input type="checkbox"/> No

For Paperwork Reduction Act Notice, see instructions on back.

Cat. No. 17057T

Form **970** (Rev. 9-2001)



LIFO PITFALLS & PROBLEMS FOR S CORPORATION QSUB GROUPS

QSUB
LIFO

Many dealerships that have elected LIFO for their new and/or used vehicle inventories have also elected to be taxed as S Corporations. More recently, some of these dealerships have been operating for tax purposes under the more liberalized S Corp rules that permit wholly-owned S subsidiaries. These subsidiaries are technically referred to as QSubs (in the final regulations) or as QSSSs (in the temporary regulations).

Some CPAs have been involved with these QSub groups from as early as 1997 when they were first permitted. Others have more recently acquired dealer clients operating in this form, or may be contemplating the initial QSub elections of such groups for their clients.

BACKGROUND

Many dealerships are set up as corporations and, to avoid double taxation—first at the corporate level and again at the shareholder level—have elected to be taxed only once ... under the rules found in Subchapter S of the Internal Revenue Code.

Subchapter S has been around for more than 40 years. For almost the entire time, S Corporations generally were not allowed to be part of an affiliated group of corporations. In other words, they could not own 80% or more of the stock of another corporation. Also, S Corporations were not allowed to have another corporation as a shareholder.

All of this changed, effective for years beginning after December 31, 1996. The Small Business Job Protection Act, passed in August of 1996, allows S Corporations to own 80% or more of another corporation or 100% of a Qualified Subchapter S Subsidiary (QSSS or QSub). A QSub is any domestic S Corporation that is 100% owned by an S Corporation parent that has elected to treat the subsidiary as a QSub.

The QSub election results in a deemed liquidation of the subsidiary into the parent. Following this deemed liquidation, the QSub is not treated as a separate corporation. After the change in the law in 1996 and until the IRS issued a specific form that could be used to make the QSub election, the IRS required the filing of Form 966, *Corporate Dissolution or Liquidation*, in order to make a QSub election.

Initially, the IRS issued Proposed Regulations under Section 1361 and provided temporary procedures for making QSub elections in Notice 97-4. In January of 2000, in Treasury Decision 8869, the IRS

released the final Regulations on the treatment of corporate subsidiaries of S Corporations. At that time, it indicated that taxpayers should continue to follow Notice 97-4 in making QSub elections until a more specialized QSub election form would be published.

In September, 2000, the IRS finally issued Form 8869, *Qualified Subchapter S Subsidiary Election*, to be used by parent S Corporations wishing to make this election for their QSSSs. A parent S Corporation may elect to treat one or more of its eligible subsidiaries as a QSub.

The purpose of this article is discuss various LIFO issues faced by QSub groups. For those desiring detailed information on other aspects of QSub groups' operations, a list of selected references is included at the bottom of the "At A Glance" overview on the facing page.

For QSub groups with LIFO inventories, several basic questions arise. See "Some LIFO Implications and Problems" on page 9. Some of these are discussed in more detail below.

INITIAL LIFO ELECTIONS & FORMS 970

If each QSub entity were filing a separate return, it would seem to be required to file a Form 970 in order to elect to use LIFO. However, since the QSub is a "disregarded entity," is it still required to file Form 970 to elect LIFO for its own inventories?

Does each QSub have to make a separate LIFO election? Would it do this by filing Form 970? There are no clear answers. It would appear to be advisable ... or at least conservative ... to file a separate Forms 970 for each QSub initially electing LIFO. If the IRS eventually deems the filing of Forms 970 by QSubs unnecessary, what's the harm in having filed an extra piece of paper? On the other hand, if the IRS prefers or requires the filing Form 970 by each QSub, then that's already been handled.

To date, the IRS has not issued any specific guidance helpful in answering any of these questions. Informal discussion with the Service indicates that LIFO elections are to be made on a *trade or business* basis and that a QSub election probably should not prevent that QSub from being able to make a LIFO election.

POOLING

As previously mentioned, the QSub election results in a deemed liquidation of the subsidiary into

see **LIFO PITFALLS FOR S CORP QSUB GROUPS**, page 8

QUALIFIED SUBCHAPTER S SUBSIDIARIES

Sec. 1361(b)(3)(ii)	<ul style="list-style-type: none"> Provides that ... "except as provided in Regulations ... all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and items (as the case may be) of the S Corporation."
Reg. Sec. 1.1361-4	<ul style="list-style-type: none"> A corporation which is a QSub shall not be treated as a separate corporation. Repeats wording of Code Section 1363(b)(3) regarding treatment of assets of the QSub as assets of the S Corp. If an S Corp. makes a valid QSub election with respect to a subsidiary, the subsidiary is deemed to have liquidated into the S Corporation. Part of Final Regulations which became effective January 20, 2000.
Form 8869	<ul style="list-style-type: none"> Form to be used by an S Corp. to make a valid QSub election for a subsidiary ...
Notice 2000-58 Ann. 2000-83	<ul style="list-style-type: none"> Contains announcement of availability of new Form 8869, <i>Qualified Subchapter S Subsidiary Election</i>, dated Sept. 2000 ... supercedes Notice 97-4 use of Form 966.
TD 8869	<ul style="list-style-type: none"> Treasury Decision 8869, January 25, 2000 contains Final Regulations that relate to the treatment of QSubs and interpret the rules as amended in 1996. Discusses differences between Final Regulations and content of Proposed Regulations to the extent of their modification after consideration of comments expressed by practitioners.
Notice 99-6	<ul style="list-style-type: none"> Contains IRS temporary guidance on Employment Tax Reporting and Payment for Disregarded Entities, including Qualified Subchapter S Subsidiaries.
Rev. Proc. 98-55	<ul style="list-style-type: none"> Contains procedures for obtaining relief in certain late S Corp. election situations, including QSub elections which were not timely filed ... see Sec 5.02 and 5.03.
Notice 97-4	<ul style="list-style-type: none"> Requests comments from taxpayers and practitioners regarding certain issues arising under 1996 change in law for S Corporations. Provides temporary procedure for making QSub (referred to as QSSS) elections involving the filing of Form 966 until further guidance was issued.
Selected References	<p>Gibson, David. <i>The New & Improved S Corporation</i>. <i>Journal of Accountancy</i>, June 1997, pgs. 37-41.</p> <p>Herskovitz, Don, Michael Lux and Scot McLean. <i>QSSS Prop. Regs. Offer Planning Opportunities</i>. <i>The Tax Adviser</i>. October 1998, pgs. 684-701.</p> <p>Huizenga, David L. <i>Planning for a QSSS</i>. <i>The Tax Adviser... Tax Clinic</i>. May 1998, pgs. 313-316</p> <p>Lindholm, Nancy S. and Stewart S. Karlinsky. <i>The Benefits and Burdens of QSubs</i>. <i>The Tax Adviser</i>. July 1999, pgs. 490-514.</p> <p>Karlinsky, Stewart S. <i>The Brand New World of S Corporation Reorganizations</i>. <i>The Tax Adviser</i>. March 1998, pgs. 176-183.</p> <p>Panoutsos, Louis A. <i>S Corporations: Disposition of Stock by a QSST</i>. <i>The Tax Adviser... Tax Clinic</i>. September 1997, pgs. 555-556.</p> <p>Rose, Jordan P. and Michael G. Schinner. <i>Prop. Regs. For Qualified Subchapter S Subsidiaries - Almost Perfect</i>. <i>Journal of Taxation</i>. October 1998, pgs. 220-226.</p> <p>Schlesinger, Michael. <i>S Corporations Now Can Have Subsidiaries - But Proceed with Caution</i>. <i>Taxation for Accountants</i>. September 1998, pgs. 132-143.</p> <p>Schwartzman, Randy. <i>Traps & Pitfalls of the Final QSub Regs</i>. <i>The CPA Journal</i>. August 2000, pgs. 46-52.</p>



the parent. The Instructions for Form 8869 state that ... "Following the deemed liquidation, the QSub is not treated as a separate corporation; ***all of the subsidiary's assets, liabilities and items of income, deduction and credit are treated as those of the parent.***"

The italicized wording is also found in Code Section 1361(b)(3)(A)(ii). Reg. Sec. 1.1361-4(a)(ii) makes the same statement without providing any further expansion or illustration. The Instructions to Form 1120S for preparing Year 2000 tax returns provide no guidance on the treatment of "all of the subsidiary's assets... as those of the parent."

This second LIFO problem area relates to how QSub LIFO inventory computations should be made, particularly whether separate LIFO pools are required ... or are inconsistent with ... the language used in Code Section 1361.

There can be significant differences over time in the size of LIFO reserves depending upon whether a single pool or multiple pools are used. If a single pool is used, decreases in the amount of inventory of one type of goods can be offset by increases in the amount of inventory in other types of goods (so long as all of the goods are properly within the same LIFO pool), and liquidations involving the invasion of prior years' layers may be avoided.

At one time or another, many dealers in QSub groups may have been confronted with significantly lower year-end inventories. For some, the problem is particularly acute with the end of 2001 approaching. The implications of how they have treated their QSub LIFO pools may, or may not, allow them to offset inventory decreases experienced by some of the entities with inventory increases experienced by some of the other entities in the QSub group.

Would the Service take the position that the LIFO inventories of separate QSubs should not be combined into one overall pool for LIFO pooling purposes? From discussions with practitioners and with the IRS, it appears some S groups have combined all of their LIFO inventories while others have treated the LIFO calculations for each QSub as a separate pool ... or as a separate trade or business requiring a separate pool. ***There are three clearly different schools of thought on this issue.***

According to the Service, a critical factor in the analysis would involve a determination of whether a QSub was operated as a *separate trade or business*, as that term is used in Section 446. Resolution of this question is complicated by two factors. First, some of the critical elements or precedents found in the *trade or business* analyses under Section 446 don't

readily carry over to more complex, real world, dealership operating scenarios. Second, any resolution of the *separate trade or business* question is very much driven by the specific facts of the individual case. Much like dealership valuation issues, one will never be able to come up with a precise weighting for all of the factors involved.

Section 355 is another code section that involves determinations of *separate trade or business* activities ... and may shed some light on the question. Particularly relevant may be those portions of it that deal with divisive reorganizations such as spin-offs and requirements that *separate trades or businesses* either have been conducted in the past or will be continued in operation in the future.

HOW RELEVANT IS LTR 199911044?

LTR 199911044 provides some insight into how the IRS has evaluated the *trade or business* issue in the past. This LTR involved an auto dealer who had elected to use the Alternative LIFO Method for new vehicles.

The Revenue Procedure (97-36/92-79) requirement that relates to LIFO pooling for new vehicles under the Alternative LIFO Method provides that "***for each separate trade or business***, all new automobiles (regardless of manufacturer) must be included in one dollar-value LIFO pool and all new light-duty trucks (regardless of manufacturer) must be included in another separate dollar-value LIFO pool."

The dealer in this case held five franchises issued by two manufacturers. He conducted operations at three different locations, all within the same city. Not surprisingly, the applicable franchise requirements included conditions involving exclusivity and certification of personnel. The books and records, checking and payroll account activity were all centralized. There were some managerial employees, and there were other employees who worked when and as needed at all three of the locations. The dealer advertised each location and each franchise separately, and it also ran generic advertisements promoting the dealership as a whole. All of the inventory at all locations was financed through a "single line of credit ... secured by all of (the dealer's) vehicles."

The IRS examining agent was looking to break down the broader single pooling permitted by the Alternative LIFO Method for new automobiles into three separate pools, one pool for the new cars at each geographic location. In other words, the agent thought the dealer should maintain separate pools for each geographical location and tried to justify this result.

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In LTR 199911044, the IRS National Office ruled that the auto dealer could keep all new autos in one pool and all new light-duty trucks in a separate pool.

The National Office discussed three factors:

- separate geographical locations,
- one complete set of books and records, and
- separate sales force for new vehicle sales and service mechanics.

However, the National Office indicated that each factor **alone** was not a sufficient basis for requiring separate trade or business pooling treatment. For a more complete discussion of LTR 199911044, see "Automobile Dealer with Multiple Franchises & Locations Can Use One Pool for All New Cars," *LIFO Lookout*, June 1999, pages 8-11.

To illustrate just how problematic the *trade or business* concept can be, consider a further ramification present in the way many multiple dealership groups operate. Assume a QSub group consists of 10 separate QSubs: 4 are Ford, 3 are BMW and there is 1 Chevy, 1 Nissan and 1 Volkswagen. Assume further that all have elected LIFO. Could the LIFO inventories of the four Ford QSubs be combined? Similarly, could the LIFO inventories of the 3 BMWs be combined? Or would there be 10 separate

trades or businesses? Would the fact that some of the QSubs are in one city, town or state (i.e., different geographic locations) make any difference, notwithstanding the fact that different (or the same) manufacturers are involved? And what if the financing sources that the dealership uses for its new vehicles involve several different credit corporations?

A question of interpretation? How much weight should be placed on the interpretation of the *trade or business* (Section 446) or other pooling technicalities (Section 472) in light of the words used in Section 1361? The words of the statute say that **all of the assets of the QSubs are to be treated as those of the parent**. What do these words mean? In resolving questions of pooling for LIFO purposes, how should or can this unclarified statutory intent of Congress in Section 1361 be reconciled or weighed against assumptions the IRS may have to make regarding the intentions of the drafters of Revenue Procedures allowing simplified LIFO computation methods?

WHAT'S BEEN DONE, HAS BEEN DONE...

If the QSub S group initially has taken an aggressive position (in the tax return filed) by combining all of the LIFO inventories of all of the QSubs, could the

see LIFO PITFALLS FOR S CORP QSUB GROUPS, page 10

SOME LIFO IMPLICATIONS & PROBLEMS

1. **Initial LIFO elections.** Does each QSub have to make a separate LIFO election? If so, how should this be done? Who (i.e., which entity) should file the Form(s) 970?

2. **Pooling.** When the LIFO calculations are made for the QSub group, (1) is all of the LIFO inventory included in a single pool for the entire group (or the portion of the group that has elected LIFO treatment), or (2) are the LIFO calculations to be made with each QSub treated as a separate **pool**, or (3) are the LIFO calculations to be made with each QSub treated as a separate **trade or business**?

3. **Do all QSubs have to be on LIFO?** A parent S Corporation can elect to treat one or more of its eligible subsidiaries as a QSub. It would seem that within a group, some QSubs might make a LIFO election, whereas others might not. Since the making of a QSub election results in a deemed liquidation of the subsidiary into the parent, how are these complex rules to be applied? **Can a QSub not be on LIFO?**

Section 381(c)(5) and Reg. Sec. 1.381(c)(5) provide the rules for the carryover of inventory accounting methods in reorganization/liquidation situations. In the case of existing dealerships making new QSub elections, how are these requirements to be applied in situations involving LIFO inventories?

4. **Terminating LIFO elections.** If a QSub on LIFO wants to terminate its LIFO election, what are the ramifications? What are the mechanics for filing requests to terminate LIFO elections? If not all QSub members of the group are going off LIFO, who files the Form 3115? If the QSub is truly a disregarded entity and has no separate Employer Identification Number, is the filing under Rev. Proc. 97-27 required (because not all LIFO elections of all QSubs are being terminated) ... or can the filing be made under Rev. Proc. 99-49?

5. **Statutory intent vs. assumptions.** The words of the statute say that all of the assets of the QSubs are to be treated as those of the parent. What does this mean? In resolving questions of pooling, how should or can this unclarified statutory intent of Congress be weighed against assumptions the IRS may have to make regarding the intentions of the drafters of Revenue Procedures allowing simplified LIFO computation methods?



IRS compel that group to separate each sub's LIFO inventories into separate LIFO pools? There are some who might contend that there is nothing really "aggressive" in taking this position at all—that's what Code Section 1361 says you should do. Period!

If a QSub S group has not initially taken an "aggressive" position and treated each QSub as a separate pool, would the IRS allow it to subsequently combine all of the separate LIFO inventories into a single pool?

Are these questions for which there are either right (correct) or wrong (incorrect) answers? If the result is either it's "*right*" or it's "*wrong*," should amended tax returns be filed in order to correct the "errors" or "mistakes" that were made?

To date, the Service has not issued any guidance helpful in answering any of these questions.

These LIFO pooling issues might rise to the attention of the IRS for resolution under one of several scenarios:

- They could arise in an IRS audit if the taxpayer had combined all of the QSub LIFO pools, and on audit the IRS agent took the position that the single or combined pool should be split among the dealerships based on a *separate trades or businesses* rationale. This would probably be the more likely situation to occur.
- Alternatively, they could arise if an S Corp. QSub group may have previously filed tax returns treating each of the QSubs' LIFO inventories as separate pools. It might request the National Office to grant permission to change its LIFO accounting method to combine all of the pools into a single pool.
- Amended tax returns (Forms 1120-S and 1040s) could be filed to correct an "error" in the previous treatment and the Service might be forced to deal with the impact of these changes as they flow

through to the Federal ... and state ... income tax returns of the S-Corp shareholders.

CONCLUSION

Many CPAs have already made decisions regarding some of these QSub-LIFO aspects. Where they have, what are the implications now? Are courses of action taken either correct or incorrect, right or wrong, requiring the filing of amended returns? Or are there "method of accounting" implications which cannot be corrected by filing amended returns? And, most critical: what has been ... or will be ... the position of the IRS in dealing with these QSub LIFO questions and situations?

CPAs advising QSubs in advance of doing LIFO calculations for the first year may be in a much better position than those who have already filed tax returns committing themselves on some of these LIFO issues.

These LIFO questions should be considered carefully before the first income tax return is filed. Practitioners anticipating filing QSub group returns for the first time may wish to take a more aggressive approach in connection with these pooling issues given the plain language in Section 1361 and the absence of any clarification by the IRS at the present time.

After the first QSub income tax return has been filed, it will be harder to reflect the benefit of *new* thinking and/or to make any changes. These difficulties will be compounded due to "method of accounting" implications resulting from whatever action has been taken.

In dealing with many of the other QSub LIFO issues including making and breaking LIFO elections, practitioners should be aware that there is no real guidance from the IRS right now for any of them. In short, for all of these QSub LIFO questions, there are no certain or easy answers. *

LIFO Update

(Continued from page 3)

accept as reasonable...or reject as unreasonable. So be careful, and save your projection calculations.

When the year-end LIFO computations are made using all of the actual year-end invoices, the results based on detailed item categories may be significantly different from the projections based on one-of-each weighted averages. Also, a dealer's beginning-of-the-year average cost for an item category may be considerably lower than the intro dealer cost used in compiling the intro-to-intro averages, and this could result in a slightly higher inflation index.

The Best Way. A more accurate way to project LIFO changes is to input all of the dealer's invoices on hand as of a date close to the end of the year. By doing this, a more accurate weighted model mix is factored into the year-end LIFO reserve change projection. In addition, this process also factors in the actual average beginning-of-the-year item category costs for all of the continuing models. *



SPECIAL LIFO CHALLENGES: CONFORMITY REPORTING REQUIREMENTS AND PROJECTIONS FOR YEAR-END PLANNING

**YEAR
END
ALERT**

Taxpayers using Last-In, First-Out (LIFO) for valuing their inventories are often under great pressure to issue their financial statements as quickly after the year-end as possible. Whether under great time pressure or not, any taxpayer using LIFO must be sure that all year-end statements satisfy all of the LIFO conformity requirements. If they do not, the taxpayer risks the loss of its LIFO election.

There are many year-end LIFO conformity requirements, and there are many kinds of businesses using LIFO. All taxpayers using LIFO must comply with all of the year-end financial statement conformity reporting requirements in order to remain eligible to use the method.

As emphasized throughout the discussions on pages 14-16 of the special rules and IRS guidance for auto dealerships, taxpayers outside the scope of that guidance should be careful **not** to rely on that guidance as if the IRS had generalized or intended it to be applicable in their own different situations or industries. Similarly, auto dealerships—although benefiting from some clarification by the IRS on certain reporting issues—should be careful **not** to rely on that guidance as if the IRS had generalized or intended it to be applicable beyond the carefully worded "scope" sections in Revenue Ruling 97-42 and in Revenue Procedure 97-44.

see **SPECIAL LIFO CHALLENGES**, page 12

SPECIAL YEAR-END CHALLENGES FOR LIFO USERS

CONFORMITY REPORTING REQUIREMENTS

Basic LIFO Eligibility Requirements: "Conformity" Is Only One	12
Form 970 Questions Regarding Conformity	12
Conformity Requirements ... There Are Many	12
<i>Every Year</i> , All of the Conformity Requirements Must Be Met	13
Traditional Financial Statements in Annual Reports Issued by CPAs	13
Dealership Year-End Statements Sent to Manufacturers/Supplier/Creditors	14
Revenue Ruling 97-42: Disclosure Guidelines for Certain Dealers	15
Revenue Procedure 97-44: Limited Relief for Certain Dealers	16
Special Interpretations Clarified Only for Auto Dealers ... All Other LIFO Users Beware	16
Violations Cannot Be Corrected Once Year-End Financial Statements Have Been Released	17
How Some Businesses Get Around the LIFO Conformity Limitations	17
Interim Reports	18
Other Concerns: <i>Insilco</i> and Section 472(g)	18
Concluding Conformity Warnings	18

YEAR-END PROJECTIONS FOR PLANNING PURPOSES

Year-End Projections for Statement Conformity or for Income Tax Planning Purposes	18
Projection Mechanics	19
Understanding Why (Projected) LIFO Reserves Go Up or Down	20
Working Out of Anticipated Year-End Liquidation or Decrement Situations	20
Sometimes the Ever-Vigilant IRS Reverses Year-End Liquidation Avoidance Measures	22
A Warning About Aggressive Year-End Inventory Planning	22



**BASIC LIFO ELIGIBILITY REQUIREMENTS:
"CONFORMITY" IS ONLY ONE**

First: the bigger picture, of which conformity is only a part. The IRS can disallow a taxpayer's LIFO election if it finds a violation of any one of four eligibility requirements. The four requirements involve cost, conformity, consent, and the maintenance of adequate books and records.

TERMINATION SITUATIONS

1. Failure to value LIFO inventory at cost for tax purposes for the year preceding the year of LIFO election, the election year, and in all subsequent years (**Cost**).
2. Violation of the financial statement reporting conformity requirements for the election year and all subsequent years (**Conformity**).
3. Failure to properly elect LIFO, including the failure to file Form 970 (**Consent**).
4. Failure to maintain adequate books and records with respect to the LIFO inventory and all computations related to it (**Adequate Books & Records**).

During 1999, probably the most startling development involving these eligibility requirements came out of the Tax Court in *Mountain State Ford Truck Sales v. Commissioner*. In this case, the Tax Court held that the use of replacement cost for valuing parts inventories could not be employed as a substitute for actual cost in connection with LIFO inventories... nor for any other non-LIFO inventories.

If a violation of any one of the four eligibility requirements occurs, the Internal Revenue Service has the discretionary power to allow the LIFO election—if it can be persuaded to exercise that power in the taxpayer's favor. For example, Revenue Procedure 79-23 reflects the position of the Service that a LIFO election can be disallowed if the taxpayer fails to maintain adequate books and records with respect to the LIFO inventory and computations related to it. However, if a taxpayer is able to reconstruct the information necessary to calculate the LIFO inventory amount properly, it may be possible to avoid termination of the LIFO election for a violation of the "books and records" requirement.

Revenue Procedure 79-23 (1979-1 C.B. 564) states that in other circumstances where disputes with the IRS arise over computational errors, incorrect pool selection or item determination, or differences in the levels of costing inventories between financial statements and tax returns - the IRS is not authorized to terminate the taxpayer's LIFO election.

However, where the LIFO violations involve cost, conformity, Form 970 consent matters or "inadequate books and records," the Service usually looks to invoke this more dramatic measure.

Revenue Procedure 97-44, which allowed certain taxpayers with conformity violations to avoid termination of their LIFO elections by paying a 4.7% penalty amount, should be regarded as a very limited exception to the IRS general approach of terminating a LIFO election whenever it uncovers an eligibility violation.

**FORM 970 QUESTIONS
REGARDING CONFORMITY**

Form 970 is the LIFO election form which is required to be included with the tax return for the first LIFO year. One of the significant traps for the unwary is that Form 970 asks only whether the year-end financial statements *for the election year* have satisfied certain conformity requirements.

Question 5 on Form 970 does not warn taxpayers that these conformity requirements must be satisfied for every year-end statement for as long as the LIFO method is being used. This requirement is spelled out in Reg. Sec. 1.472-2(e)(1).

Worse yet, the relatively limited Form 970 instructions give no hint of the many troublesome interpretations that can arise under the regulations. As evidenced by the debacle that auto dealers and their CPAs floundered through for nearly a decade (and that resulted in Rev. Proc. 97-44), it would seem that many practitioners have never even looked at, much less attempted to study in detail, the regulations dealing with this critical issue.

**CONFORMITY REQUIREMENTS...
THERE ARE MANY**

There are many conformity requirements. They exist as restrictions on a taxpayer's general desire to pay lower taxes using a LIFO method for valuing inventories, while reporting more income to shareholders or banks and other creditors using a non-LIFO method. To prevent this from happening, the Treasury says that LIFO must be used in all reports covering a full year to insure that the use of LIFO for tax purposes conforms as nearly as possible with the best accounting practice in the trade or business in order to provide a clear reflection of income.

It is often stated that LIFO must be used to compute income in the year-end financial statements. However, it is more technically correct to state that the IRS only requires LIFO to be used in the primary presentation of income (i.e., in the Income Statement). For most taxpayers, the LIFO confor-

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mity requirements pose at least two general sets of requirements:

TWO SETS OF REQUIREMENTS

FIRST, they require that any year-end financial statements **issued in the traditional report form** by the business to creditors, shareholders, partners or other users must reflect the year-end results on LIFO.

SECOND, they also require all year-end **manufacturer-formatted financial statements** sent by certain dealers to a manufacturer/supplier/creditor (12th, 13th and any other fiscal year-end statements) to reflect LIFO results.

A taxpayer may adopt LIFO only if it has used no other procedure than LIFO in preparing an Income Statement or a profit or loss statement covering the first taxable year of adoption. As noted previously, for subsequent taxable years, similar restrictions are imposed. However, the Commissioner has the discretion to allow a taxpayer to continue to use the LIFO method even though conformity violations might have occurred.

Accordingly, a LIFO reserve, no matter how large, can be completely and abruptly lost if careful attention is not paid to the conformity requirements in year-end, manufacturer-formatted financial statements sent to the Factory/Manufacturer/Supplier... as well as in the more conventional year-end statements issued in report form by CPAs.

EVERY YEAR, ALL OF THE CONFORMITY REQUIREMENTS MUST BE MET

To remain eligible to use LIFO, every year, the last monthly statement for the year sent to the manufacturer and/or any other credit source must reflect an estimate of the year-end change in the LIFO reserve if the actual change cannot be computed before the statement has to be released.

If a taxpayer is thinking about making a LIFO election for the year, then it should place an estimate of the year-end LIFO reserve ...or the actual amount if it has been calculated... in the year-end statements (including those issued to the Factory/Manufacturer or issued to any other party) in order to preserve its ability to elect LIFO when it files Form 970 as part of its Federal income tax return for the year at a later date.

Also, the expansion of the conformity requirements to other classes of goods should not be overlooked if a taxpayer is already on LIFO for one class of inventory (such as new vehicles or equip-

ment) and is considering extending LIFO to another class of inventory (such as used vehicles, equipment or parts). In this situation, the year-end Income Statements should also reflect an estimate of the LIFO reserve expected to be produced by extending the LIFO election(s) to the additional classes of goods under consideration.

TRADITIONAL FINANCIAL STATEMENTS IN ANNUAL REPORTS ISSUED BY CPAs

This section deals with reports issued by CPAs, where the CPA controls the release, content and format of the financial statements, notes and supplementary information. These are unlike monthly statements which may be prepared internally by the taxpayer's accounting department or controller and sent out to a manufacturer, supplier or other creditor without direct CPA involvement or review.

The LIFO conformity requirement as it relates to reports issued by CPAs requires that in the primary presentation of income (i.e., the Income Statement), the results disclosed must only be the net-of-LIFO results. The primary Income Statement *cannot* show results before LIFO, followed by either an addition or subtraction for the net LIFO change, coming down to a final net income or loss after-LIFO figure. This means that during a period of rising prices, a business using LIFO will usually be reporting lower operating results in order to comply with the conformity requirements. Very strict disclosure limitations existed with no room for deviation for many years.

The Regulations were liberalized in 1981 and they now allow LIFO taxpayers to disclose non-LIFO operating results in *supplementary financial statements*, as long as those supplementary non-LIFO financial statements satisfy two tests: **First**, they must be issued as part of a report which includes the primary presentation of income on a LIFO basis. **Second**, each non-LIFO financial statement must contain on its face a warning or statement to the reader that the non-LIFO results are supplementary to the primary presentation of income which is on a LIFO basis. Accordingly, in CPA-prepared year-end financial statements, a LIFO taxpayer's results on a non-LIFO basis can be fully disclosed as supplementary information if both of these requirements are met.

Alternatively, the Regulations permit disclosure of non-LIFO results in a footnote to the regular year-end financial statements, as long as the Statement of Income itself does not disclose this information parenthetically or otherwise on its face, and the notes are all presented together and accompany the Income Statement in a single report.

see **SPECIAL LIFO CHALLENGES**, page 14



Special LIFO Challenges

As a result of these "liberalizations" in the Regulations in 1981, these LIFO conformity requirements should not present any major reporting problems for reports issued by CPAs.

DEALERSHIP YEAR-END STATEMENTS SENT TO MANUFACTURER/SUPPLIER/CREDITORS

Many CPAs serving automobile dealerships are now aware that the Regulations contain several year-end LIFO reporting restrictions which apply to the specially formatted financial statements sent by auto dealerships and other businesses immediately after year-end to the Manufacturer/Supplier/Creditors. Some of those CPAs who were not had a rude awakening when their (former) dealer clients—through their attorneys—asked them to reimburse the dealers for their payments of the 4.7% penalty "settlement amounts" due under Revenue Procedure 97-44.

For automobile dealerships, and for any other LIFO users who have similar year-end reporting fact patterns or requirements, these restrictions on year-end dealership-issued statements pose fatal LIFO traps that are much harder to deal with than those for year-end reports issued by CPAs.

The Regulations provide that any Income Statement that reflects a full year's operations must report on a LIFO basis. This requirement applies regardless of whether the Income Statement is the last in a series of interim statements, or a December statement which shows two columns, one for the current month results and another for the year-to-date cumulative results.

The Regulations further provide that a series of credit statements or financial reports is considered a single statement or report covering a period of operations if the statements or reports in the series are prepared using a single inventory method and can be combined to disclose the income, profit, or loss for the period. See Reg. Sec. 1.472-2(e)(6). If one can combine or "aggregate" a series of interim or partial-year statements to disclose the results of operations for a full year, then the last Income Statement must reflect income computed using LIFO to value the inventory.

Literally interpreted, this wording applies to all franchised auto dealers' 12th statements (i.e., December unadjusted) as well as to their 13th statements. The 12th statement is usually issued on a preliminary basis, before accruals and estimates are refined by detailed adjusting entries. The 13th statement is usually issued several weeks after the 12th statement, and it reflects year-end accrual adjustments and other computations not otherwise com-

(Continued from page 13)

pleted within the tight time frame for the issuance of the December or 12th statement (usually by the 10th day of the following month).

The IRS National Office confirmed dealers' worst fears during 1995 in LTR 9535010. In this Letter Ruling, a calendar year dealership raised the conformity question in the context of what happens when the monthly statements, including the December year-end statement, are not on LIFO but the CPA prepares annual audited financial statements for the dealership which do reflect LIFO.

Here, the taxpayer's argument was that the CPA's audited statements reflecting LIFO were the primary financial statements, while the monthly statements sent by the dealership to the manufacturer and to the credit corporation were "supplementary statements." The IRS concluded that the dealer in LTR 9535010 had violated the LIFO conformity requirement because:

IRS TESTS

1. The dealership used an inventory method other than LIFO in ascertaining its income in the monthly financial statements,
2. The financial statements ascertained income for the "taxable year,"
3. The financial statements were "for credit purposes," and
4. The financial statements were not within any of the exceptions to the LIFO conformity requirements that are provided in the Regulations.

With respect to the use of the financial statements "for credit purposes," the IRS found that a debtor-creditor relationship did exist between the dealership and the manufacturer and the credit corporation. The IRS stated that if the taxpayer's "operations began to deteriorate, it is doubtful that Corp. X (the manufacturer) and Corp. Y (the Credit Corporation) would ignore these reports and continue to extend credit to T (the taxpayer) as though nothing has changed." The IRS noted that the taxpayer was unable to provide any explanation of what purpose other than credit evaluation the credit subsidiary might have for requesting the dealer's financial statements.

In a companion letter ruling, LTR 9535009, the IRS "officially" restated its position with respect to a dealer who reported for tax purposes using a fiscal year. The IRS employed the same four-step analysis as above to determine whether the fiscal year dealership had violated the LIFO conformity requirements. In connection with the second "test" related

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Special LIFO Challenges

to whether the dealership's financial statement to the Factory ascertained the taxpayer's income for the taxable year, the IRS noted that the year-to-date column information readily provides this computation for the reader. Even without year-to-date accumulations on the face of the monthly Income Statement, any series of months could simply be added together to reflect a complete 12-month period of anyone's choice.

LTR 9535009 states that the fiscal year dealer taxpayer issued a financial statement (in January, 19xx) that ascertained its income for the entire prior calendar year, and that calendar year statement is considered a statement covering the "taxable year" because it covers a 1-year period that both begins and ends in a taxable year or years for which the taxpayer used the LIFO method. This is the IRS' interpretation of Reg. Sec. 1.472-2(e)(2) which covers *one-year periods other than a taxable year*.

Warning. This would seem to be the position of the IRS for all taxpayers whose fact patterns fall under the Regulation. Only the special and limited relief afforded to certain dealers in Revenue Ruling 97-42 and Revenue Procedure 97-44 (discussed next) saved some taxpayers from the consequences of this narrow and harsh interpretation.

REVENUE RULING 97-42: DISCLOSURE GUIDELINES FOR CERTAIN DEALERS

On September 25, 1997, the IRS issued Revenue Ruling 97-42 which provides special interpretations allowing auto dealers to satisfy the LIFO conformity requirements. ***These special interpretations apply only to a year-end financial statement prepared in a format required by an automobile manufacturer on preprinted forms supplied by the automobile manufacturer.***

Placement in the Income Statement. LIFO adjustments must appear in the twelfth month Income Statement. However, they do not have to be reflected in the Cost of Goods Sold section through the inventory valuation accounts. As long as the LIFO adjustments are reflected somewhere in the determination of net income on the Income Statement, that conformity requirement will be satisfied.

Revenue Ruling 97-42 makes it clear that if a LIFO reserve adjustment is posted directly to the retained earnings account and reflected on the dealership's Balance Sheet, that treatment of the LIFO reserve change will not satisfy the conformity requirement. For years ending after October 14, 1997, it is thus imperative that the LIFO adjustment

(Continued)

be properly reflected in the Income Statement prepared for the last month of the year.

Use of estimates. A "reasonable estimate" of the change in the LIFO reserve for the year may be reflected instead of the actual change..., as long as that "reasonable estimate" is reflected somewhere in the year-end Statement of Income.

No one knows what the IRS will accept as a "reasonable estimate." Similarly, no one knows what procedures the IRS will accept as being "reasonable" in the preparation of an estimate of the change of the LIFO reserve for the year.

Fiscal year taxpayers. If an auto dealer employs a fiscal taxable year, and reflects the LIFO change in Cost of Goods Sold or anywhere else in the Income Statement, the LIFO conformity requirements can be satisfied in either of two ways: **First**, the dealer may make an adjustment for the change in the LIFO reserve that occurred during the calendar year in the month and year-to-date column of the **December** Income Statement.

Alternatively, the dealer may make an adjustment for the change in the LIFO reserve that occurred during the fiscal year in the month and year-to-date columns of the Income Statements provided for the **last month of the fiscal year**.

In other words, the IRS does not require the change in the LIFO reserve to be updated twice in the fiscal year-end... calendar year-end sequence. The IRS will permit a timing mismatch under these limited circumstances. For example, in a situation where a dealer has a September fiscal year-end and December (calendar) reporting year to the manufacturer: If the dealer reflects the (reasonable estimate) change in the LIFO reserve in the September monthly and year-end statement, that dealer does not need to recompute and update a LIFO change for the three month period from October 1 through December 31 and reflect a 3-month change in the December statement.

The dealer may simply carry through the annual LIFO reserve change effect reflected in the September fiscal year-end Income Statement without modification in the December Income Statement. Note that the December Income Statement must reflect the charge against income for the prior fiscal year-end LIFO reserve change and that prior September fiscal year-end LIFO reserve change should not be reversed so that the December Statement of Income does not reflect any LIFO reserve charge for the twelve month period ending December 31.

see SPECIAL LIFO CHALLENGES, page 16



Special LIFO Challenges

REVENUE PROCEDURE 97-44:

LIMITED RELIEF FOR CERTAIN DEALERS

Revenue Procedure 97-44 provided "relief" to auto dealers whose year-end Factory statements failed to satisfy the conformity requirements at any time during a six-year "look-back" period. These dealers were allowed to keep their LIFO elections if they paid a 4.7% penalty/settlement tax based on the amount of their LIFO reserves as of the last taxable year ended on or before October 14, 1997 (i.e., as of December 31, 1996 for most calendar-year auto dealers). These dealers were also required to satisfy certain other conditions as terms of the settlement.

In Revenue Procedure 98-46, the IRS extended this relief for similar conformity violations to all medium and heavy-duty truck dealers, providing them with a slightly different series of payments dates.

One of the major traps that practitioners and auto dealers now face is in the lack of synchronization between the language in Revenue Ruling 97-42 and the language in Revenue Procedure 97-44. Revenue Ruling 97-42 applies to the issuance of statements to a "credit subsidiary." In contrast, Revenue Procedure 97-44 contains broader language in its scope (Section 3) referring to the providing "for credit purposes" ... of an Income Statement in the format required by the franchisor.

See the analyses of Revenue Procedure 97-44 in the September, 1997 and December, 1997 issues of the *LIFO Lookout* for discussions of the settlement amount 4.7% penalty payment and many questions that still remain unanswered.

SPECIAL INTERPRETATIONS CLARIFIED ONLY FOR AUTO DEALERS... ALL OTHER LIFO USERS BEWARE

Different year-ends for book and tax purposes (fiscal years). LIFO conformity problems are multiplied where a taxpayer has a different year-end for reporting to a manufacturer, supplier, or creditor (calendar year-Dec. 31) than the fiscal year it uses to report for income tax return purposes and for other financial statement reporting purposes.

For these fiscal year taxpayers... other than auto dealers and light, medium & heavy-duty truck dealers... in order to satisfy another strict conformity requirement, the full-year Income Statements must reflect LIFO at the end of *both* twelve month annual reporting periods or years (Reg. Sec. 1.472-2(e)(2)).

This regulation states that the conformity rules also apply to (1) the determination of income, profit, or loss for a one-year period other than a taxable year, and to (2) credit statements or financial reports

(Continued from page 15)

that cover a one-year period other than a taxable year, but only if the one-year period both begins and ends in a taxable year or years for which the taxpayer uses the LIFO method for Federal income tax purposes. For example,...in the case of a calendar year taxpayer, the requirements...apply to the taxpayer's determination of income for purposes of a credit statement that covers the period October 1, 1981, through September 30, 1982, if the taxpayer uses the LIFO method for Federal income tax purposes in taxable years 1981 and 1982.

Placement of LIFO change in the year-end Statement of Income. In fighting with auto dealers over conformity, in 1994 the IRS informally indicated that on the last monthly (i.e., twelfth) statement, the LIFO adjustment had to be run through the Cost of Goods Sold section (via the beginning-of-the-year and the end-of-the-year inventory valuations), rather than through an other income/deductions account...or else dealers would not be in compliance with the LIFO year-end conformity requirement. The IRS subsequently retreated on this "placement" issue in Revenue Ruling 97-42.

For LIFO taxpayers other than those dealers indicated above, where and how the year-end LIFO adjustment is placed on the Income Statement is still critical. The IRS "only-through-Cost-of-Goods-Sold" interpretation could result in countless LIFO election terminations in situations where the (projected) change in the LIFO reserve at year-end was placed in some other section of the Income Statement, such as with an *Other Income* or *Other Deductions*. Fortunately, in Revenue Ruling 97-42, the IRS said (to certain dealers only) that the LIFO adjustment could be placed anywhere on the Income Statement.

Unfortunately, the IRS "guidance" for franchised auto dealers in Revenue Ruling 97-42 and the "relief" for prior conformity violations under Revenue Procedures 97-44 and 98-46 do not apply to any other types of taxpayers issuing what might be "similar" statements under "similar circumstances" to other manufacturers, suppliers or credit sources. No one can be sure what these other businesses with LIFO violations should do in light of what is now understood to be the IRS interpretation of these regulations.

WARNING

All taxpayers...other than auto and truck dealers...using LIFO who issue monthly statements to manufacturers, suppliers or creditors are not protected by the special rules in Revenue Ruling 97-42 which modify the Regulations only for special reporting situations faced by auto dealers.

→



Special LIFO Challenges

What should these businesses/taxpayers be told about their LIFO elections? Are they subject to retroactive termination of their LIFO elections at any time, literally at will, by the IRS? What responsibility does the CPA practitioner have as preparer of the tax return now that the IRS position has been more clearly set forth in Revenue Ruling 97-42? These are the questions that (should) haunt practitioners and their clients today.

CONFORMITY VIOLATIONS CANNOT BE CORRECTED ONCE THE YEAR-END FINANCIAL STATEMENTS HAVE BEEN RELEASED

What if year-end financial statements are issued (in a hurry) and the conformity requirements have been overlooked?

The position of the IRS is that once a year-end Income Statement has been issued or released on a non-LIFO basis, that statement cannot be recalled and corrected to reflect LIFO by the re-issuance of statements satisfying the conformity requirement. Furthermore, it then becomes discretionary with the IRS Commissioner as to whether or not the Commissioner chooses to terminate the taxpayer's LIFO election as a penalty for the violation.

The *William Powell Company* decision (81-1 USTC ¶ 9449) illustrates one taxpayer's success (or possibly good fortune) in avoiding termination of its LIFO election when it came down to "all-or-nothing" on this issue. This case, decided in 1981, involved what would have been the termination of a LIFO election made in 1973 because at the end of the first LIFO year, the taxpayer had issued non-LIFO statements and then later made a LIFO election when it filed its tax return.

In that case, the taxpayer recalled its previous non-LIFO statements and replaced/reissued LIFO statements to all the banks, creditors and shareholders before the income tax return for the first year was filed. The taxpayer probably would have lost its LIFO election if it had litigated the issue in the Tax Court, but the taxpayer chose to litigate this issue in the District Court in Ohio.

The taxpayer took the position that it had not "used" FIFO within the meaning of Section 472(c). Its position with respect to Section 472(c)(2) was that non-LIFO "worksheets" were not used for "credit purposes," since the credit had been extended prior to the delivery of the worksheets. The District Court accepted the taxpayer's arguments. With respect to Section 472(c)(1), Powell contended that *use* is determined at the time of the LIFO election and that

(Continued)

this election need not be made until the taxpayer files its return. At the time Powell elected LIFO, it was no longer *using* the FIFO statements, inasmuch as they had been recalled prior to the election and LIFO statements had been reissued.

The District Court, while agreeing that Powell's activities seemed to violate the plain language of Section 472(c)(2), was hesitant to strictly apply the "plain meaning rule" in this case. The Court said that it is the general rule that the words of a revenue statute are interpreted "in their ordinary, everyday senses," and a rigid application of this rule would not be consistent with the Commissioner's ongoing interpretation of the conformity requirement.

HOW SOME BUSINESSES GET AROUND THE LIFO CONFORMITY LIMITATIONS

Many businesses using LIFO—especially publicly-held companies reporting to the SEC—would like to reduce taxes by reporting lower taxable income/earnings in tax returns while at the same time reporting higher earnings/more income to their shareholders and creditors for financial and market valuation purposes. This can be done easily, thanks to loopholes conveniently provided in the Regulations. But one has to know they are there.

The Regulations allow taxpayers to legitimately avoid the intent of the conformity requirement by allowing them to use LIFO methods and sub-elections in their financial statements that are different from those LIFO sub-elections and methods that are used in their income tax return computations. That's right: ***Different LIFO methods may be used for book and for tax purposes.*** It is not necessary for the year-end financial statements to use the same exact LIFO sub-elections that are used in the tax return LIFO calculations. The Regulations simply require that both sets of financial statements (i.e., those included in the financial reports and those inherent in the income tax returns) must report using LIFO methods.

This allows some companies to use more pools ...in one case, several hundred more pools... for financial reporting purposes than for income tax purposes. Others use link-chain or link-chain, index (dollar-value) methods to lower LIFO income for tax purposes, while they use double-extension (dollar-value) LIFO methods for financial reports. Still others reconstruct long distant base prices for new items in their tax return LIFO calculations while they price new items at current cost in their financial statements. These companies enjoy the best of both worlds without violating the fine print of the "conformity" requirements.

see **SPECIAL LIFO CHALLENGES**, page 18



Special LIFO Challenges

Based on the foregoing, we continue to question the wisdom of the *advice* given by Wall Street to dealer groups going public in connection with terminating their LIFO elections. How many millions of dollars of LIFO deferral tax savings have been thrown away needlessly in exchange for the perceived benefit of higher earnings per share and hopefully higher market valuations? The significant—if not Draconian—penalties the investing marketplace exacts from businesses that miss their earnings per share projections by even a penny suggest that sacrificing real millions of LIFO tax deferral dollars “just for show” can be costly, if not almost unnecessary.

INTERIM REPORTS

Interim reports covering a period of operations that is less than the whole of a taxable year may be issued on a non-LIFO basis without violating the LIFO conformity requirement for tax purposes. The Regulations are completely clear and unambiguous on this point. Although generally accepted accounting principles may present some difficulties in this regard, the Income Tax Regulations clearly do not.

OTHER CONCERNS: *INSILCO* & SECTION 472(g)

For another example of how seriously the Treasury/IRS polices the LIFO conformity requirement, consider the origin of Code Section 472(g). This subsection was added because the IRS lost the *Insilco* decision in the Tax Court. This case involved a subsidiary using LIFO who reported to its parent corporation using LIFO, but the parent corporation reported its consolidated earnings (which included those of the LIFO-user subsidiary) to its own shareholders on a non-LIFO basis.

In upholding the taxpayer in *Insilco*, the Tax Court told the IRS that if it didn't like the result, it should get Congress to change the law. And that's exactly what the IRS/Treasury did! After its loss, the Treasury persuaded Congress to change the law (which it did by adding subsection (g) to Section 472) so that taxpayers in the future couldn't get around the conformity requirement the way *Insilco* had.

Section 472(g) provides that all members of the same group of financially related corporations shall be treated as one taxpayer for purposes of the conformity provisions of the Internal Revenue Code. For purposes of these provisions, affiliated groups are determined by using a lower 50% ownership threshold (than 80%). Furthermore, Section 472(g)(2)(B) provides that any other group of corporations which consolidate or combine for purposes of financial statements...shall be treated as one taxpayer for purposes of the conformity provisions.

(Continued from page 17)

CONCLUDING CONFORMITY WARNINGS

The *William Powell Company* and the *Insilco* decisions are the only recorded cases where taxpayers contested the IRS termination of their LIFO elections in court. The bottom line is that the IRS takes all of these conformity requirements seriously. On many audits, instead of assuming that the taxpayer has complied, the IRS asks for proof that financial statements at year-end were not in violation of the LIFO conformity requirements.

The first year of the LIFO election is very often the easiest one for the IRS to find a conformity violation in. This is because by the time the election is “officially” made in the tax return many months after year-end, the financial statements for the year are long gone out the door.

In these situations, the IRS asserts that there is no statute of limitations preventing it from inquiring as to a taxpayer's compliance with the conformity requirement ... and that the Service can look into this as far back as the initial LIFO election year. Furthermore, the burden of proof is on the taxpayer—not on the IRS—in these inquiries.

The IRS position is that there is no limit on its ability to go back to any prior year...no matter how far distant...to terminate a LIFO election because of a violation of any one of the many conformity requirements discussed above. The IRS supports its argument by reminding taxpayers that they have explicitly agreed to this result right on the Form 970 (in Part 1) that they included in their tax returns when they elected LIFO!

The only exception to this is the IRS' uncharacteristic and somewhat voluntary self-imposed limitation in 1997 for certain retail auto and truck dealers. Consequently, LIFO users cannot be too cautious or careful in dealing with conformity matters.

YEAR-END PROJECTIONS FOR STATEMENT CONFORMITY OR FOR INCOME TAX PLANNING PURPOSES

Projections for statement conformity purposes. When the pressure is great to issue the financial statements before detailed LIFO computations can be made, the conformity requirement should be satisfied by using a reasonable estimate of the change in the LIFO reserve in lieu of the actual amount. (Revenue Ruling 97-42 says so explicitly for auto dealers.) As mentioned previously, another alternative might be to use a different LIFO computation methodology for the financial statements than the one used for tax purposes.



Special LIFO Challenges

Projections for income tax planning purposes. It is unrealistic to attempt any serious planning for a business that uses LIFO without first projecting the change in the LIFO reserves for year-end.

Make projections early. These projections should be made early enough so that management can consider not only the financial impact of what is likely to happen, but also whether legitimate steps, motivated by sound business reasons, can be undertaken to produce a result different from that shown by the projections.

One thing is certain: After year-end, it will be too late to change the results that might have been avoided by proper planning with adequate timing.

Even if it is concluded that nothing can be done to avoid the LIFO reserve payback consequences, it is far better to know the extent of the impending "hit" so that other buffering actions can be taken, than it is to be caught entirely off-guard or without any idea of how large the LIFO reserve recapture is going to be.

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PROJECTION MECHANICS

Projecting year-end changes in LIFO reserves need not be too difficult nor time-consuming. Making these LIFO reserve change projections involves only two estimates: (1) the ending inventory level, and (2) the overall inflation percentage for the year.

All other necessary factors are known at the time the projections are made because they are "facts" related to the beginning of the year:

- Beginning-of-the-year inventory expressed in total dollars and in base dollars,
- Beginning-of-the-year LIFO valuation of the inventory,
- Method used for valuing current year increments, and
- Cumulative inflation index as of the beginning-of-the-year.

The computation of the projected change in a LIFO reserve is made by plugging in the estimates of (1) the year-end inventory level and (2) the current year's rate of inflation or inflation index ... and then "working backwards". These steps are detailed below.

PROJECTION MECHANICS

- (1) **Determine** the cumulative index as of the end-of-the-year—this is the estimated current year inflation index times (i.e., multiplied by) the beginning-of-the-year cumulative index,
- (2) **Divide** the end-of-the-year estimated (or, if known, actual) inventory dollars by the year-end cumulative index—to determine the end-of-the-year inventory stated or expressed in base dollars,
- (3) **Compare** the end-of-the-year inventory expressed in base dollars with the beginning-of-the-year inventory stated in base dollars to determine whether there is an increment or a decrement projected for the year,
- (4) **Value** the projected increment under the method already selected for valuing increments on Form 970, item 6(a).

Alternatively, if a decrement is projected for the year, carry back the decrement (expressed in base dollars) against prior years' increments (also expressed in base dollars) on a LIFO or reverse-chronological-order basis. This means that the most recent/last layer built up is the first one eliminated, and then prior years' layers are eliminated in reverse-chronological order. In other words, a decrement in 1999 is carried back first against any 1998 increment, then against 1997, then against 1996, then against 1995, etc. until the entire amount of the 1999 decrement (expressed in base dollars) has been fully accounted for. In some instances, a decrement may end up being carried all the way back to the original first LIFO year base layer.
- (5) **Add** all the resulting layers of inventory at their respective LIFO valuations to get the end-of-the-year inventory stated at its LIFO valuation,
- (6) **Subtract** the ending inventory at its LIFO valuation from the ending inventory at its actual or estimated current non-LIFO cost to determine the projected LIFO reserve as of the end-of-the-year,
- (7) **Subtract** the *actual* LIFO reserve as of the beginning-of-the-year from the projected LIFO reserve as of the end-of-the-year. The result determined in this final step is the estimate of the change in the LIFO reserve for the year.
- (8) **Reconcile and prove out** the projected changes to understand why the reserve is going up or down.

see **SPECIAL LIFO CHALLENGES**, page 20



Special LIFO Challenges

UNDERSTANDING WHY (PROJECTED) LIFO RESERVES GO UP OR DOWN

Taxpayers using LIFO are often surprised when they find out that even though their year-end inventory levels are projected to be lower than they were at the beginning-of-the-year, their LIFO reserves are expected to increase. And often these increases are very large.

In many instances, the net change in the LIFO reserve for a year is the result of complementing or offsetting price and inventory investment payback factors.

CHANGE FACTORS

Upward influences...causing increases

- Price increases ...inflation.
- Quantity increases, if a dual index methodology/approach is used.

Downward influences...causing decreases

- Price decreases ...deflation.
- Decreases in inventory investment levels—i.e., pay-backs of previously built-up LIFO reserves to the extent necessitated by the carryback of a current year quantity decrease (referred to as “decrements”) against increases (“increments”) built up in prior years. But see the qualification below where negative LIFO reserves are involved.

If year-end LIFO projections show that the dollar amount of the ending inventory (expressed in terms of base dollars) is projected to be lower than the beginning-of-the-year inventory amount (also expressed in base dollars), that means there is going to be a liquidation or decrement in a technical LIFO sense.

However, that liquidation or decrement may not necessarily cause, or result in, any pay-back of some or any of the LIFO reserve at the beginning-of-the-year. Whether or not there is a “pay-back” depends on how the prior year layers were built up over time and how they were valued for LIFO purposes.

For those who want more mechanical analysis, see: “Why Do Some LIFO Reserves Go Up Even Though Inventory Levels Go Down?” in the March, 1992 *LIFO Lookout* and “Another Rebasing Example - With Proofs: Why LIFO Reserves Go Up Even Though Inventory Levels Go Down and Despite Rebasing Indexes to 1.000 in Between” in the June, 1993 *LIFO Lookout*.

Also, for those who are interested in pay-back mechanics where negative LIFO reserves are involved, see “Strange...But Explainable...Results from the Wacky World of Negative LIFO Reserves,” in the December, 1998 *LIFO Lookout*. This article, with extensive supporting schedules, analyzes what might

(Continued from page 19)

otherwise be unanticipated results where negative LIFO reserves are involved, and even qualifies the generalization above that decreases in inventory investment levels cause or result in decreases in LIFO reserves.

WORKING OUT OF ANTICIPATED YEAR-END LIQUIDATION OR DECREMENT SITUATIONS

When a liquidation or decrement situation is anticipated, the starting point is to calculate the pay-back potential from a series of reduced inventory levels. In other words, as the year-end inventory drops, how much more (or less) is the LIFO reserve going to change? These calculations determine what the real LIFO recapture vulnerability will be as the anticipated current-year's decrement is carried-back on a LIFO basis against the prior LIFO layers that have been built up over the years.

This recapture potential will be different for every pool, since each pool has its own history and characteristics. For auto dealers, this recapture impact will be different for the new auto pool compared to what it will be for the new light-duty truck pool. The LIFO reserve repayment potential impact should be computed for each LIFO pool and expressed as a readily understandable dollar amount. For an example of this type of successive calculation, see “GM Dealers Low on LIFO Inventory May Face Stiff Recapture ... Planning May Lessen the Blow,” in the June 1998 *Dealer Tax Watch*.

Armed with this diagnostic information, taxpayers anticipating a liquidation may be able to lessen the anticipated LIFO recapture in at least three ways. The second and third considerations below are discussed in the June 1998, *Dealer Tax Watch* article referenced above.

ALTERNATIVES

1. **Manage inventory levels.** Attempt to increase or “manage” the inventory level through transactions that might not otherwise have been considered, but which still have some degree of business justification (other than solely attempting to minimize the impact of LIFO layer liquidations).
2. **Year-end change.** If eligible, change to a fiscal year-end that is prior to the year-end expected to be adversely affected by the significant inventory reduction.
3. **Switch to the BLS/IPIC method.** Consider changing to the BLS/IPIC method under the recent changes...and expeditious consent procedure ... available in Section 10.04 of the Appendix to Revenue Procedure 98-60.



Special LIFO Challenges

If a business using LIFO is trying to avoid a significant year-end reserve reduction, steps to increase the inventory level should be completed and documented before year-end. These actions should be considered only if they make sense from a business standpoint, after considering carrying costs, insurance, expected ability to sell the additional inventory and the possibility of challenge by the IRS.

Despite cautions that inventory purchasing decisions should be based on sound business judgment and not solely on the desire to reduce projected LIFO pay-backs, some taxpayers may still wish to pursue more aggressive strategies and to take their chances in this regard.

As discussed in the next section, the IRS has been successful in challenging transactions that appeared to be motivated by the desire to avoid LIFO recapture impact. In these cases, the IRS ignored the last-ditch efforts that resulted in inventory on hand at year-end which was not "intended to be sold or placed in the normal inventory channels."

Ideas dealers might consider if faced with significant projected decrements. A dealer might attempt to increase or "manage" the year-end inventory level by considering some transactions that otherwise would not have entered his mind. These may be rationalized under the "Nothing ventured, nothing gained" generalization. However, they may not necessarily be justified if the IRS digs deeply into them and sees them as motivated solely by liquidation-avoidance. Therefore, these strategies should be regarded by dealers and their advisors as aggressive and not without the likelihood of challenge by the IRS. They are only generalized here, and they should be carefully and more fully evaluated by the dealer's advisors before any further action is taken.

1. After determining which pool (new automobiles or new light-duty trucks) has the greater LIFO repayment potential, a dealer may simply try to have more inventory dollars in the pool with the greater repayment potential.

In other words, if the dealer can have only \$1,000,000 worth of inventory, if the LIFO repayment payback potential is 30% on the dollar in the new automobile pool and 60% on the dollar in the new light-duty truck pool, the dealer should try to have more inventory dollars at year-end in the new light-duty truck pool than in the new automobile pool.

2. Attempt to purchase new vehicles of other makes (for resale to retail customers) to put into inventory.

Under the Alternative LIFO Method, all new automobiles, regardless of manufacturer, including those used as demonstrators, must be included in a

(Continued)

dollar-value LIFO pool, and all new light-duty trucks regardless of manufacturer, must be included in another separate LIFO pool. Thus, the Alternative LIFO Method would appear to contemplate all new automobiles being placed in one pool, regardless of manufacturer. Accordingly, a GM dealer who has other non-GM franchises in the same selling entity as the GM franchise(s) might try to stock up on the non-GM new vehicles to the extent possible.

3. Similarly, a dealer might simply attempt to purchase (for retail sale) some very expensive makes (Lamborghini or Rolls Royce) and put them in the new automobiles pool. ("A few will do.") Does a dealer have to have that franchise to sell those vehicles? What about creating a special joint venture, or flow-through type entity with another *franchised* dealer?

How far can the "retail resale" aspect be pushed? Will this pass muster with the IRS? One cannot be sure.

Caution: Section 4.02 of Revenue Procedure 97-36 does contain some troublesome language relating to LIFO pools. It states that "*for each separate trade or business*," all autos, regardless of manufacturer, must be placed in one pool. No one really knows what "*for each separate trade or business*" really means, and the IRS has yet to define or explain it. If these words don't mean anything, why are they there? Might the IRS assert some specialized interpretation for this term under these circumstances?

In TAM 199911044, the IRS gave some indication of its interpretation of the "for each separate trade or business" language. In this TAM, the National Office allowed an auto dealer to keep all new autos in one pool and all new light-duty trucks in a separate pool, even though that dealer was involved with two manufacturers, five franchises and three locations, all of which were in the same city. For more on this TAM, see "Automobile Dealer with Multiple Franchises & Locations Can Use One Pool for all New Cars," *LIFO Lookout*, June 1999.

4. A dealer might actively seek out another dealer with less of a LIFO recapture impact potential and attempt to purchase inventory from that dealer, perhaps paying a "premium" or offering that dealer some other considerations for that inventory that makes the transaction economically attractive to both parties.

5. Dealers with multiple franchises in different entities should make similar LIFO recapture impact calculations for all their LIFO pools in all entities... to determine whether a shifting of inventory from one entity to another, if feasible, might create a favorable recapture-avoidance result.

see **SPECIAL LIFO CHALLENGES**, page 22



Special LIFO Challenges

6. Finally, although it may seem heresy, a dealer might consider not closing sales until after the end of the year. For some dealers, what they hope to realize in gross profit and potential customer loyalty may be smaller than the real dollar outflow that *definitely* will result from the reduction of inventory by sales which will *definitely* trigger the LIFO recapture. Some dealers may simply be unable to make the right decision on this.

SOMETIMES THE EVER-VIGILANT IRS REVERSES YEAR-END LIQUIDATION AVOIDANCE MEASURES

In 1996, the Tax Court observed that taxpayers often "desire a higher base-year cost of ending inventory in a given year to avoid liquidating a LIFO layer, causing a match of historical costs against current revenues" (see *E. W. Richardson*, Tax Court Memo Decision 1996-368). The Court's observation was made in the context of three other cases and Revenue Ruling 79-188. All of these collectively stand for the proposition that the IRS may successfully overturn and even penalize year-end inventory transactions that are solely LIFO-benefit motivated.

1. ***Ingredient Technology Corporation*** (Su Crest Corporation, 83-1 USTC 9140, January 5, 1983). Tax fraud convictions by means of LIFO inventory overstatements.

2. ***Illinois Cereal Mills***, (86-1 USTC 9371 affirming T.C. Memo 1983-469, Dec. 40,342(M), 46 TCM 1001, August, 1983). Legal ownership of the goods did not justify inclusion in the taxpayer's inventory because the taxpayer did not intend to use the corn in its milling business.

3. ***Ballou and Company, Inc.***, (85-1 USTC 9290, U.S. Claims Court, No. 247-82T; March 29, 1985). The Court upheld the IRS' removal of year-end gold purchases from LIFO inventory calculations because the IRS adjustments removed only the amounts of gold that the taxpayer had purchased in order to temporarily inflate inventory levels solely for income tax/LIFO purposes at year end.

Revenue Ruling 79-188 can be given a positive spin and interpreted to indirectly suggest some planning considerations:

1. Attempt to document that sales during the year are at levels that justify the purchase of year-end inventory levels in the ordinary course of business.

2. It helps if the inventory acquired at year-end can be sold to regular customers in due course or to a third party, rather than back to original supplier. This helps to avoid the "cast" as a resale.

(Continued from page 21)

3. The inventory acquired at year-end should be paid for before its subsequent sale, again in an effort to demonstrate an intent to receive and use the goods in the ordinary course of the business.

4. The specific mechanics of taking possession and title prior to reselling the inventory should also be considered. But note, even doing all this legally did not stop the IRS in *Illinois Cereal Mills*.

TAM 9847003 provides more recent evidence of how closely the IRS scrutinizes year-end inventory levels and transactions. In this case, the IRS concluded that an affiliated group had engaged in inventory-level manipulation stating: "The Group simply used Y (one affiliated member) as a purchasing and holding company so that it could manipulate the quantity of goods in X's (another affiliated member) ending inventory, thereby artificially inflating X's cost of good sold ... This purchasing arrangement was designed to artificially reduce the Group's taxable income and avoid taxes; it had no independent purpose ... Although papers were drawn up to place formal ownership with Y, the objective economic realities indicate that X had effective command over the Y purchases." Accordingly, the IRS National Office concluded that X was the owner of the Y purchases and should have included them in its inventory.

In this TAM, the IRS pursued the adjustment to correct the year-end inventory levels through the Group's corporate restructuring, holding that (1) X's method of accounting for the Y purchases carried over to the taxpayer created in the merger process, (2) the treatment of the purchases in inventory constituted an unauthorized change in method of accounting, and (3) corrections could be made by changing the new taxpayer's method of accounting and making adjustments pursuant to Section 481(a).

A WARNING ABOUT AGGRESSIVE YEAR-END INVENTORY PLANNING

Any LIFO taxpayer aggressively planning to avoid year-end LIFO layer liquidations should realize that even satisfying the apparent "boundaries" set forth in Revenue Ruling 79-188 and these other cases may not be enough. Taxpayers' year-end transactions may not prevail if year-end purchases are structured to involve subsequent re-sales back to the same source shortly after year-end or just to otherwise look good on paper.

More recently, Letter Ruling 9847003 indicates that the IRS arguments are potentially more sophisticated and strengthened whenever the IRS brings Section 481(a) into the evaluation. The IRS' repeated use of the term *objective economic realities* may open the door to many subjective disputes. *



**MODEL/ITEM CATEGORY INFLATION SURVEY
FOR QUICK, ONE-OF-EACH, LIFO ESTIMATES
DEALER COST FOR THE YEAR ENDED 12/31/01**

**INFLATION ESTIMATE REPORT BY MAKE
BASED ON INFORMATION AVAILABLE**

	POOL #1 NEW AUTOMOBILES	POOL #2 NEW L-D TRUCKS
ACURA	0.80%	2.03%
AM GENERAL	0.00%	15.79%
AUDI	0.49%	0.00%
BMW	2.10%	0.00%
BUICK	2.16%	0.00%
CADILLAC	2.22%	0.27%
CHEVROLET	2.91%	3.20%
CHRYSLER	(1.54)%	0.66%
DAEWOO	6.55%	0.00%
DODGE	1.38%	0.53%
FERRARI	0.00%	0.00%
FORD	1.22%	1.77%
GMC TRUCKS	0.00%	3.02%
HONDA	1.49%	1.57%
HYUNDAI	1.71%	3.75%
INFINITI	0.00%	0.00%
ISUZU	0.00%	4.07%
JAGUAR	0.60%	0.00%
JEEP	0.00%	(1.88)%
KIA	0.33%	3.97%
LAND ROVER/RANGE ROVER	0.00%	0.36%
LEXUS	0.85%	1.75%
LINCOLN	0.45%	0.37%
MAZDA	1.02%	3.48%
MERCEDES	1.28%	0.34%
MERCURY	0.38%	(2.82)%
MINI	2.09%	2.55%
NISSAN	1.84%	0.01%
OLDSMOBILE	2.63%	0.37%
PLYMOUTH	0.28%	0.00%
PONTIAC	2.89%	(0.84)%
PORSCHE	1.37%	0.00%
ROLLS ROYCE	0.00%	0.00%
SAAB	0.09%	0.00%
SATURN	8.03%	0.00%
SUBARU	0.12%	0.01%
SUZUKI	1.59%	0.91%
TOYOTA	0.10%	0.32%
VOLKSWAGEN	1.10%	(15.83)%
VOLVO	1.01%	0.00%

Complete 2002 intro price information is not currently available for all models.

Accordingly, some inflation indexes exclude certain item(s) for which 2002 information is missing.

New items are repriced at current cost – i.e., no inflation.

Source: W. J. De Filippis' Make / Model Analysis Data Base Report, Preliminary Edition (Copyright 2001)

PAGE: 1

DECEMBER 21, 2001

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E. NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
ACURA								
NEW AUTOS - POOL #1								
CL	4	0	4	109,955		111,366	1,411	1.28%
NSX	2	0	2	147,840		148,026	186	0.13%
NSX-T	2	0	2	154,878		155,064	186	0.12%
RL	2	0	2	75,978		78,621	2,643	3.48%
RSX	0	5	5		97,354	97,354	0	0.00%
TL	2	2	4	53,273	58,745	113,210	1,192	1.06%
TOTAL NEW AUTOS	12	7	19	541,924	156,099	703,641	5,618	0.80%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MDX	4	0	4	130,672		133,328	2,656	2.03%
TOTAL NEW L-D TRUCKS	4	0	4	130,672		133,328	2,656	2.03%
TOTAL ACURA	16	7	23	672,596	156,099	836,969	8,274	1.00%
AM GENERAL								
NEW LIGHT-DUTY TRUCKS - POOL #2								
HUMMER	2	0	2	163,106		188,857	25,751	15.79%
TOTAL NEW L-D TRUCKS	2	0	2	163,106		188,857	25,751	15.79%
TOTAL AM GENERAL	2	0	2	163,106		188,857	25,751	15.79%
AUDI								
NEW AUTOS - POOL #1								
A4 SERIES	0	11	11		285,768	285,768	0	0.00%
A6 SERIES	3	3	6	114,689	100,418	217,271	2,184	1.92%
A8 SERIES	2	0	2	114,978		115,855	878	0.76%
ALLROAD	2	0	2	75,626		73,120	(2,506)	(3.31)%
S4	4	0	4	141,980		143,855	1,876	1.32%
S6	0	1	1		52,879	52,879	0	0.00%
S8	1	0	1	64,045		64,870	825	1.29%
TT	5	0	5	153,522		155,695	2,173	1.42%
TOTAL NEW AUTOS	17	15	32	664,820	448,065	1,118,315	5,430	0.49%
TOTAL AUDI	17	15	32	664,820	448,065	1,118,315	5,430	0.49%

PAGE: 2

DECEMBER 21, 2001

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E. NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/1/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
BMW								
NEW AUTOS - POOL #1								
3 SERIES	7	4	11	209,470	110,645	320,505	390	0.12%
5 SERIES	9	0	9	344,230		346,500	2,270	0.66%
7 SERIES	0	0	0				0	N/A
M SERIES	3	2	5	138,510	89,460	234,250	6,280	2.75%
Z3	3	0	3	96,650		96,210	(440)	(0.45%)
Z8	1	0	1	115,200		129,840	14,640	12.71%
TOTAL NEW AUTOS	23	6	29	904,060	200,105	1,127,305	23,140	2.10%
NEW LIGHT-DUTY TRUCKS - POOL #2								
X5	2	1	3	79,470	59,580	139,050	0	0.00%
TOTAL NEW L-D TRUCKS	2	1	3	79,470	59,580	139,050	0	0.00%
TOTAL BMW	25	7	32	983,530	259,685	1,266,355	23,140	1.86%
BUICK								
NEW AUTOS - POOL #1								
CENTURY	2	0	2	39,121		39,867	746	1.91%
LESABRE	2	0	2	48,406		49,666	1,260	2.60%
PARK AVENUE	2	0	2	63,775		64,572	797	1.25%
REGAL	2	0	2	44,780		46,221	1,441	3.22%
TOTAL NEW AUTOS	8	0	8	196,082		200,326	4,244	2.16%
NEW LIGHT-DUTY TRUCKS - POOL #2								
RENDEZVOUS	0	2	2		47,582	47,582	0	0.00%
TOTAL NEW L-D TRUCKS	0	2	2		47,582	47,582	0	0.00%
TOTAL BUICK	8	2	10	196,082	47,582	247,908	4,244	1.74%
CADILLAC								
NEW AUTOS - POOL #1								
CTS	0	1	1		27,149	27,149	0	0.00%
DEVILLE	3	0	3	122,186		125,203	3,017	2.47%
ELDORADO	2	0	2	76,847		79,481	2,634	3.43%
SEVILLE	2	1	3	82,642	40,053	124,785	2,090	1.70%
TOTAL NEW AUTOS	7	2	9	281,675	67,202	356,618	7,741	2.22%
NEW LIGHT-DUTY TRUCKS - POOL #2								

PAGE 3

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
ESCALADE	2	1	3	90,200	45,059	135,621	362	0.27%
TOTAL NEW L-D TRUCKS	2	1	3	90,200	45,059	135,621	362	0.27%
TOTAL CADILLAC	9	3	12	371,875	112,261	482,239	8,103	1.67%
CHEVROLET								
NEW AUTOS - POOL #1								
CAMARO	4	0	4	84,034		88,060	4,026	4.79%
CAVALIER	4	2	6	54,268	29,443	84,888	1,187	1.42%
CORVETTE	3	0	3	117,722		120,960	3,238	2.75%
IMPALA	2	0	2	38,772		40,272	1,500	3.87%
LUMINA	0	0	0				0	N/A%
MALIBU	2	0	2	33,233		34,107	874	2.63%
METRO	0	0	0				0	N/A%
MONTE CARLO	2	0	2	38,403		39,272	869	2.26%
PRIZM	2	0	2	28,130		28,758	628	2.23%
TOTAL NEW AUTOS	19	2	21	394,562	29,443	436,327	12,322	2.91%
NEW LIGHT-DUTY TRUCKS - POOL #2								
3500 CHASSIS-CABS	19	0	19	431,086		436,265	5,179	1.20%
ASTRO VAN	6	0	6	125,589		127,336	1,737	1.38%
AVALANCHE	0	4	4		114,432	114,432	0	0.00%
BLAZER	5	0	5	103,709		102,185	(1,524)	(1.47)%
COMMERCIAL CUTAWAY VAN	0	0	0				0	N/A%
EXPRESS CARGO VAN	10	0	10	211,490		220,387	8,897	4.21%
EXPRESS PASSENGER VAN	6	0	6	145,485		146,946	1,461	1.00%
S10 PICKUP	7	0	7	113,648		114,252	604	0.53%
SILVERADO 1500	20	5	25	422,084	135,754	574,946	17,088	3.06%
SILVERADO 2500	33	0	33	824,054		849,065	25,011	3.04%
SILVERADO 3500	14	0	14	370,981		381,243	10,262	2.77%
SUBURBAN	4	0	4	99,154		130,017	30,863	31.13%
TAHOE	2	0	2	46,198		59,276	13,078	28.31%
TRACKER	8	0	8	136,189		140,777	4,588	3.37%
TRAILBLAZER	0	6	6		161,176	161,176	0	0.00%
VENTURE	7	2	9	166,450	59,070	225,747	227	0.10%
TOTAL NEW L-D TRUCKS	141	17	158	3,196,147	470,432	3,784,050	117,471	3.20%
TOTAL CHEVROLET	160	19	179	3,590,709	499,875	4,220,377	128,793	3.17%
CHRYSLER								
NEW AUTOS - POOL #1								
300M	1	0	1	27,451		26,356	(1,095)	(3.99)%

PAGE 4

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
CONCORDE	2	1	3	45,489	25,753	69,704	(1,538)	(2.16)%
PROWLER	1	0	1	42,080		42,155	75	0.18%
SEBRING	7	0	7	148,293		146,397	(1,896)	(1.28)%
TOTAL NEW AUTOS	11	1	12	263,313	25,753	284,612	(4,454)	(1.54)%
NEW LIGHT-DUTY TRUCKS - POOL #2								
PT CRUISER	1	2	3	14,926	35,744	50,986	316	0.62%
TOWN & COUNTRY	7	1	8	198,065	22,374	222,059	1,600	0.73%
VOYAGER	2	1	3	39,453	15,498	55,185	234	0.43%
TOTAL NEW L-D TRUCKS	10	4	14	252,464	73,616	328,220	2,150	0.66%
TOTAL CHRYSLER	21	5	26	515,777	99,369	612,842	(2,304)	(0.37)%
DAEWOO								
NEW AUTOS - POOL #1								
LANOS	6	0	6	58,284		62,232	3,948	6.77%
LEGANZA	3	0	3	40,797		43,887	3,090	7.57%
NUBIRA	4	0	4	45,756		48,210	2,454	5.36%
TOTAL NEW AUTOS	13	0	13	144,837		154,329	9,492	6.55%
TOTAL DAEWOO	13	0	13	144,837		154,329	9,492	6.55%
DODGE								
NEW AUTOS - POOL #1								
INTREPID	3	0	3	63,232		64,379	1,147	1.81%
NEON	1	4	5	11,856	55,181	66,679	(358)	(0.53)%
STRATUS	4	1	5	71,030	16,195	88,834	1,609	1.84%
VIPER	2	0	2	128,290		130,665	2,375	1.85%
TOTAL NEW AUTOS	10	5	15	274,408	71,376	350,557	4,773	1.38%
NEW LIGHT-DUTY TRUCKS - POOL #2								
CARAVAN	8	2	10	189,202	37,571	228,867	2,084	0.92%
DAKOTA	5	11	16	83,855	197,204	285,368	4,309	1.53%
DURANGO	2	5	7	50,589	147,960	195,520	(3,009)	(1.52)%
RAM C&B & CHASSIS	6	0	6	120,157		120,607	450	0.37%
RAM PICKUP	10	8	18	217,835	153,494	372,079	750	0.20%
RAM VAN	12	0	12	220,293		223,275	2,982	1.35%

PAGE 5

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
RAM WAGON	3	0	3	63,531		63,756	225	0.35%
TOTAL NEW L-D TRUCKS	46	26	72	945,442	536,229	1,489,472	7,801	0.53%
TOTAL DODGE	56	31	87	1,219,850	607,605	1,840,029	12,574	0.69%
FERRARI								
NEW AUTOS - POOL #1								
360 MODENA	0	0	0				0	N/A%
456 GT	0	0	0				0	N/A%
550 MARANELLO	0	0	0				0	N/A%
TOTAL NEW AUTOS	0	0	0				0	N/A%
TOTAL FERRARI	0	0	0				0	0.00%
FORD								
NEW AUTOS - POOL #1								
CROWN VICTORIA	4	1	5	66,713	26,275	115,966	2,978	2.64%
ESCORT	2	3	5	23,709	39,916	64,874	1,249	1.96%
FOCUS	5	8	13	66,317	114,245	181,430	868	0.48%
MUSTANG	9	0	9	184,995	188,257		3,262	1.76%
TAURUS	5	5	10	91,721	102,958	197,458	2,779	1.43%
THUNDERBIRD	0	5	5		173,020	173,020	0	0.00%
TOTAL NEW AUTOS	25	22	47	453,455	456,414	921,005	11,136	1.22%
NEW LIGHT-DUTY TRUCKS - POOL #2								
CUTAWAY VAN	12	0	12	225,526		227,984	2,458	1.09%
E-SERIES	16	0	16	349,818		355,606	5,788	1.65%
ESCAPE	2	10	12	34,612	205,716	241,538	1,210	0.50%
EXCURSION	4	24	28	133,302	839,353	975,259	2,644	0.27%
EXPEDITION	4	0	4	123,105		124,375	1,270	1.03%
EXPLORER	8	0	8	219,124		219,154	30	0.01%
EXPLORER SPORT	4	8	12	83,341	186,739	270,997	917	0.34%
F150 PICKUP	37	2	39	804,539	53,791	860,453	22,123	2.58%
F250 SUPER DUTY PICKUP	28	0	28	670,956		689,900	18,944	2.82%
F350 SUPER DUTY PICKUP	50	0	50	1,256,464		1,290,574	34,210	2.72%
RANGER	34	13	47	575,188	204,861	787,695	7,646	0.98%
SUPER DUTY CAB/CHASSIS	36	0	36	852,367		876,358	23,991	2.81%

PAGE 6

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
WINDSTAR	7	1	8	170,660	24,777	198,389	2,952	1.51%
TOTAL NEW L-D TRUCKS	242	58	300	5,499,002	1,515,237	7,138,422	124,183	1.77%
TOTAL FORD	267	80	347	5,952,457	1,971,651	8,059,427	135,319	1.71%
GMC TRUCKS								
NEW LIGHT-DUTY TRUCKS - POOL #2								
ENVY	0	4	4		113,903	113,903	0	0.00%
SAFARI	6	0	6	124,604		127,336	2,732	2.19%
SAVANNA	20	0	20	430,776		447,236	16,460	3.82%
SIERRA 3500 CHASSIS-CABS	16	8	24	372,310	184,513	571,625	14,802	2.66%
SIERRA HEAVY-DUTY CHASSIS-CABS	3	0	3	65,881		67,351	1,470	2.23%
SIERRA HEAVY-DUTY PICKUP	20	12	32	497,354	298,482	819,424	23,588	2.96%
SIERRA PICKUP	35	18	53	806,177	412,785	1,265,310	46,348	3.80%
SONOMA	9	0	9	137,864		140,446	2,582	1.87%
YUKON	8	0	8	273,154		277,426	4,272	1.56%
TOTAL NEW L-D TRUCKS	117	42	159	2,708,120	1,009,683	3,830,057	112,254	3.02%
TOTAL GMC TRUCKS	117	42	159	2,708,120	1,009,683	3,830,057	112,254	3.02%
HONDA								
NEW AUTOS - POOL #1								
ACCORD	47	8	55	860,369	151,040	1,025,654	14,245	1.41%
CIVIC	28	0	28	384,078		390,330	6,252	1.63%
INSIGHT	2	0	2	36,985		36,767	782	2.17%
S2000	1	0	1	28,733		29,146	413	1.44%
TOTAL NEW AUTOS	78	8	86	1,309,165	151,040	1,481,897	21,682	1.69%
NEW LIGHT-DUTY TRUCKS - POOL #2								
CR-V	0	8	8		148,333	148,333	0	0.00%
INSIGHT	0	1	1		19,876	19,876	0	0.00%
ODYSSEY	3	2	5	70,025	52,180	125,284	3,079	2.52%
PASSPORT	8	0	8	192,200		196,696	4,496	2.34%
TOTAL NEW L-D TRUCKS	11	11	22	262,225	220,389	480,189	7,575	1.57%
TOTAL HONDA	89	19	108	1,571,390	371,429	1,972,086	29,257	1.51%

PAGE 7

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
HYUNDAI								
NEW AUTOS - POOL #1								
ACCENT	5	0	5	45,858		48,854	2,996	6.53%
ELANTRA	4	0	4	50,242		50,242	0	0.00%
SONATA	0	6	6		93,435	93,435	0	0.00%
TIBURON	0	0	0				0	N/A%
XG300	2	0	2	43,377		44,361	984	2.27%
TOTAL NEW AUTOS	11	6	17	139,477	93,435	236,892	3,980	1.71%
NEW LIGHT-DUTY TRUCKS - POOL #2								
SANTA FE	6	0	6	108,945		113,025	4,080	3.75%
TOTAL NEW L-D TRUCKS	6	0	6	108,945		113,025	4,080	3.75%
TOTAL HYUNDAI	17	6	23	248,422	93,435	349,917	8,060	2.36%
INFINITI								
NEW AUTOS - POOL #1								
G20	2	0	2	39,774		39,774	0	0.00%
I35	0	1	1		26,044	26,044	0	0.00%
Q45	0	1	1		45,672	45,672	0	0.00%
TOTAL NEW AUTOS	2	2	4	39,774	71,716	111,490	0	0.00%
NEW LIGHT-DUTY TRUCKS - POOL #2								
QX4	2	0	2	63,240		63,240	0	0.00%
TOTAL NEW L-D TRUCKS	2	0	2	63,240		63,240	0	0.00%
TOTAL INFINITI	4	2	6	103,014	71,716	174,730	0	0.00%
ISUZU								
NEW LIGHT-DUTY TRUCKS - POOL #2								
AXOM	0	4	4		103,610	103,610	0	0.00%
RODEO	10	0	10	213,497		219,020	5,523	2.59%
RODEO SPORT	7	0	7	113,608		120,841	7,233	6.37%
TROOPER	7	0	7	181,155		194,230	13,075	7.22%

PAGE 8

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
VEHICROSS								
	1	0	1	25,949		26,099	150	0.58%
TOTAL NEW L-D TRUCKS	25	4	29	534,209	103,610	663,800	25,981	4.07%
TOTAL ISUZU	25	4	29	534,209	103,610	663,800	25,981	4.07%
JAGUAR								
NEW AUTOS - POOL #1								
S-TYPE	2	2	4	83,708	89,104	172,808	(4)	(0.00)%
X-TYPE	0	4	4		122,220	122,220	0	0.00%
XJ SERIES	3	2	5	174,027	124,794	301,635	2,814	0.94%
XK SERIES	4	0	4	277,756		280,188	2,432	0.88%
TOTAL NEW AUTOS	9	8	17	535,491	336,118	876,851	5,242	0.60%
TOTAL JAGUAR	9	8	17	535,491	336,118	876,851	5,242	0.60%
JEEP								
NEW LIGHT-DUTY TRUCKS - POOL #2								
GRAND CHEROKEE	4	1	5	113,544	33,594	139,837	(7,301)	(4.95)%
LIBERTY	0	4	4		73,742	73,742	0	0.00%
WRANGLER	3	1	4	52,123	17,248	71,209	1,838	2.65%
TOTAL NEW L-D TRUCKS	7	6	13	165,667	124,584	284,788	(5,463)	(1.88)%
TOTAL JEEP	7	6	13	165,667	124,584	284,788	(5,463)	(1.88)%
KIA								
NEW AUTOS - POOL #1								
OPTIMA	6	0	6	93,849		89,961	(3,888)	(4.14)%
RIO	2	2	4	16,400	20,075	37,775	1,300	3.56%
SPECTRA	4	4	8	43,982	44,430	91,732	3,320	3.76%
TOTAL NEW AUTOS	12	6	18	154,231	64,505	219,468	732	0.33%
NEW LIGHT-DUTY TRUCKS - POOL #2								
SEDONA	0	2	2		38,295	38,295	0	0.00%

PAGE: 9

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
SPORTAGE	14	0	14	219,289		229,518	10,229	4.66%
TOTAL NEW L-D TRUCKS	14	2	16	219,289	38,295	287,813	10,229	3.97%
TOTAL KIA	26	8	34	373,520	102,800	487,281	10,961	2.30%
LAND ROVER/RANGE ROVER								
NEW LIGHT-DUTY TRUCKS - POOL #2								
LAND ROVER DISCOVERY	2	0	2	62,035		62,746	711	1.15%
LAND ROVER FREELANDER	0	3	3		77,553	77,553	0	0.00%
RANGE ROVER	1	0	1	60,180		60,180	0	0.00%
TOTAL NEW L-D TRUCKS	3	3	6	122,215	77,553	200,479	711	0.36%
TOTAL LAND ROVER/RANGE ROVER	3	3	6	122,215	77,553	200,479	711	0.36%
LEXUS								
NEW AUTOS - POOL #1								
ES 300	0	1	1		27,935	27,935	0	0.00%
GS 300	1	0	1	33,488		33,972	484	1.45%
GS 430	1	0	1	40,654		41,242	588	1.45%
IS 300	1	2	3	26,756	54,329	81,437	352	0.43%
LS 430	1	0	1	46,363		47,332	969	2.09%
SC 430	0	1	1		53,117	53,117	0	0.00%
TOTAL NEW AUTOS	4	4	8	147,261	135,381	285,035	2,393	0.85%
NEW LIGHT-DUTY TRUCKS - POOL #2								
LX 470	1	0	1	52,715		53,813	1,098	2.08%
RX 300	2	0	2	60,419		61,299	880	1.46%
TOTAL NEW L-D TRUCKS	3	0	3	113,134		115,112	1,978	1.75%
TOTAL LEXUS	7	4	11	260,395	135,381	400,147	4,371	1.10%
LINCOLN								
NEW AUTOS - POOL #1								
CONTINENTAL	1	3	4	36,412	108,331	143,270	(1,473)	(1.02)%
LS	3	6	9	93,380	200,599	296,524	2,545	0.87%

PAGE: 10

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
TOWN CAR	5	4	9	199,232	164,110	365,877	2,535	0.70%
TOTAL NEW AUTOS	9	13	22	329,024	473,040	805,671	3,607	0.45%
NEW LIGHT-DUTY TRUCKS - POOL #2								
BLACKWOOD	1	1	2	47,792	47,577	95,154	(215)	(0.23)%
NAVIGATOR	2	0	2	80,525		81,389	864	1.07%
TOTAL NEW L-D TRUCKS	3	1	4	128,317	47,577	176,543	649	0.37%
TOTAL LINCOLN	12	14	26	457,341	520,617	982,214	4,256	0.44%
MAZDA								
NEW AUTOS - POOL #1								
626	3	0	3	56,180		55,616	(564)	(1.00)%
MILLENNIA	2	0	2	53,944		54,548	604	1.12%
MX-5 MIATA	5	0	5	105,324		106,983	1,659	1.58%
PROTEGE	2	2	4	25,841	30,884	57,968	1,243	2.19%
PROTEGE 5	0	1	1		15,318	15,318	0	0.00%
TOTAL NEW AUTOS	12	3	15	241,289	46,202	290,433	2,942	1.02%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MPV	3	0	3	63,847		64,563	716	1.12%
TRIBUTE	8	0	8	150,722		160,228	9,506	6.31%
TRUCK	8	2	10	132,655	30,664	166,239	2,919	1.79%
TOTAL NEW L-D TRUCKS	19	2	21	347,225	30,664	391,030	13,141	3.48%
TOTAL MAZDA	31	5	36	588,514	76,866	681,463	16,083	2.42%
MERCEDES								
NEW AUTOS - POOL #1								
C CLASS	2	3	5	62,218	105,370	168,146	558	0.33%
CL CLASS	3	0	3	282,906		291,277	8,371	2.96%
CLK CLASS	5	1	6	245,893	73,470	322,851	3,488	1.09%
E CLASS	7	0	7	351,774		355,192	4,418	1.26%
S CLASS	4	0	4	336,428		341,078	4,650	1.38%
SL CLASS	2	0	2	197,858		197,858	0	0.00%
SLK CLASS	2	1	3	77,004	51,057	129,363	1,302	1.02%
TOTAL NEW AUTOS	25	5	30	1,554,081	229,897	1,806,765	22,787	1.28%
NEW LIGHT-DUTY TRUCKS - POOL #2								

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
M CLASS	2	1	3	94,581	41,804	136,850	465	0.34%
TOTAL NEW L-D TRUCKS	2	1	3	94,581	41,804	136,850	465	0.34%
TOTAL MERCEDES	27	6	33	1,648,662	271,701	1,943,615	23,252	1.21%
MERCURY								
NEW AUTOS - POOL #1								
COUGAR	2	3	5	31,460	51,399	82,275	(584)	(0.70)%
GRAND MARQUIS	1	7	8	21,595	175,095	197,440	750	0.38%
SABLE	4	2	6	78,038	39,364	118,728	1,326	1.13%
TOTAL NEW AUTOS	7	12	19	131,093	265,858	398,443	1,482	0.38%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MOUNTAINEER	2	0	2	54,274		54,231	(43)	(0.08)%
VILLAGER	3	3	6	69,016	67,241	130,922	(5,335)	(3.92)%
TOTAL NEW L-D TRUCKS	5	3	8	123,290	67,241	185,153	(5,378)	(2.82)%
TOTAL MERCURY	12	15	27	254,383	333,099	583,596	(3,886)	(0.66)%
MITSUBISHI								
NEW AUTOS - POOL #1								
DIAMANTE	2	0	2	48,945		50,207	1,262	2.58%
ECLIPSE	16	0	16	329,717		338,813	9,096	2.76%
GALANT	5	1	6	94,973	19,588	115,884	1,323	1.15%
LANCER	0	5	5		71,519	71,519	0	0.00%
MIRAGE	4	0	4	50,402		51,598	1,196	2.37%
TOTAL NEW AUTOS	27	6	33	524,037	91,107	628,021	12,877	2.09%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MONTERO	2	0	2	60,630		62,593	1,963	3.24%
MONTERO SPORT	8	0	8	201,798		206,519	4,721	2.34%
TOTAL NEW L-D TRUCKS	10	0	10	262,428		269,112	6,684	2.55%
TOTAL MITSUBISHI	37	6	43	786,465	91,107	897,133	19,561	2.23%

NISSAN

NEW AUTOS - POOL #1

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
ALTIMA	0	8	8		148,002	148,002	0	0.00%
MAXIMA	4	0	4	87,829		92,422	4,593	5.23%
SENTRA	5	0	5	62,141		63,022	881	1.42%
TOTAL NEW AUTOS	9	8	17	149,970	148,002	303,446	5,474	1.84%
NEW LIGHT-DUTY TRUCKS - POOL #2								
FRONTIER PICKUP	22	14	36	411,641	277,197	693,600	4,762	0.69%
PATHFINDER	5	0	5	136,459		130,415	(6,044)	(4.43)%
QUEST	3	0	3	66,637		67,088	451	0.68%
XTERRA	9	8	17	183,673	185,659	370,255	923	0.25%
TOTAL NEW L-D TRUCKS	39	22	61	798,410	462,856	1,261,358	92	0.01%
TOTAL NISSAN	48	30	78	948,380	610,858	1,564,804	5,566	0.36%
OLDSMOBILE								
NEW AUTOS - POOL #1								
ALERO	8	0	8	141,946		146,325	4,379	3.08%
AURORA	2	0	2	59,578		60,376	798	1.34%
INTRIGUE	3	0	3	66,849		68,727	1,878	2.81%
TOTAL NEW AUTOS	13	0	13	268,373		275,428	7,055	2.63%
NEW LIGHT-DUTY TRUCKS - POOL #2								
BRAVADA	0	2	2		59,913	59,913	0	0.00%
SILHOUETTE	3	2	5	81,396	62,445	144,587	746	0.52%
TOTAL NEW L-D TRUCKS	3	4	7	81,396	122,358	204,500	746	0.37%
TOTAL OLDSMOBILE	16	4	20	349,769	122,358	479,928	7,801	1.65%
PLYMOUTH								
NEW AUTOS - POOL #1								
NEON	1	0	1	11,856		11,931	75	0.63%
PROWLER	1	0	1	42,080		42,155	75	0.18%
TOTAL NEW AUTOS	2	0	2	53,936		54,086	150	0.28%
TOTAL PLYMOUTH	2	0	2	53,936		54,086	150	0.28%



PAGE 13

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
PONTIAC								
NEW AUTOS - POOL #1								
BONNEVILLE	3	0	3	78,265		79,788	1,523	1.95%
FIREBIRD	5	0	5	115,359		120,280	4,921	4.27%
GRAND AM	8	0	8	139,722		142,722	3,000	2.15%
GRAND PRIX	5	0	5	105,344		108,351	3,007	2.86%
SUNFIRE	3	0	3	41,533		42,953	1,420	3.42%
TOTAL NEW AUTOS	24	0	24	480,223		494,094	13,871	2.89%
NEW LIGHT-DUTY TRUCKS - POOL #2								
AZTEK	2	0	2	41,683		39,335	(2,348)	(5.63)%
MONTANA	3	3	6	71,613	82,129	154,439	697	0.45%
TOTAL NEW L-D TRUCKS	5	3	8	113,296	82,129	193,774	(1,851)	(0.84)%
TOTAL PONTIAC	29	3	32	593,519	82,129	687,868	12,220	1.81%
PORSCHE								
NEW AUTOS - POOL #1								
911	0	1	1		169,641	169,641	0	0.00%
BOXSTER	4	0	4	161,638		164,244	2,606	1.61%
CARRERA	8	4	12	591,142	273,974	878,852	13,736	1.59%
TOTAL NEW AUTOS	12	5	17	752,780	443,615	1,212,737	16,342	1.37%
TOTAL PORSCHE	12	5	17	752,780	443,615	1,212,737	16,342	1.37%
ROLLS ROYCE								
NEW AUTOS - POOL #1								
BENTLEY	0	0	0				0	N/A%
ROLLS-ROYCE	0	0	0				0	N/A%
TOTAL NEW AUTOS	0	0	0				0	N/A%
TOTAL ROLLS ROYCE	0	0	0				0	0.00%
SAAB								
NEW AUTOS - POOL #1								
9.3 SERIES	6	1	7	197,087	26,409	225,905	2,409	1.08%

PAGE 14

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
9.5 SERIES								
	2	4	6	74,971	137,554	210,512	(2,013)	(0.95)%
TOTAL NEW AUTOS	8	5	13	272,058	163,963	436,417	396	0.09%
TOTAL SAAB	8	5	13	272,058	163,963	436,417	396	0.09%
SATURN								
NEW AUTOS - POOL #1								
L100	1	0	1	13,666		15,106	1,440	10.54%
L200	2	0	2	30,581		33,515	2,934	9.59%
L300	1	0	1	17,351		18,832	1,481	8.54%
LW200	2	0	2	32,979		36,129	3,150	9.55%
LW300	1	0	1	19,010		20,608	1,598	8.41%
SC1	2	0	2	22,559		24,086	1,527	6.77%
SC2	2	0	2	27,970		29,810	1,840	6.58%
SL	1	0	1	9,619		9,982	363	3.77%
SL1	2	0	2	20,732		22,196	1,464	7.05%
SL2	2	0	2	23,186		24,870	1,684	7.26%
SW2	0	0	0				0	N/A%
SWP	0	0	0				0	N/A%
TOTAL NEW AUTOS	16	0	16	217,653			17,481	8.03%
NEW LIGHT-DUTY TRUCKS - POOL #2								
VUE	0	4	4		69,957	69,957	0	0.00%
TOTAL NEW L-D TRUCKS	0	4	4		69,957	69,957	0	0.00%
TOTAL SATURN	16	4	20	217,653	69,957	305,091	17,481	6.08%
SUBARU								
NEW AUTOS - POOL #1								
IMPREZA	0	10	10		192,377	192,377	0	0.00%
LEGACY	18	3	21	387,841	81,693	470,342	808	0.17%
TOTAL NEW AUTOS	18	13	31	387,841	274,070	662,719	808	0.12%
NEW LIGHT-DUTY TRUCKS - POOL #2								

PAGE 15

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
FORESTER	6	1	7	124,061	23,020	147,083	12	0.01%
TOTAL NEW L-D TRUCKS	6	1	7	124,061	23,020	147,083	12	0.01%
TOTAL SUBARU	24	14	38	511,902	297,090	808,912	820	0.10%
SUZUKI								
NEW AUTOS - POOL #1								
ESTEEM	10	0	10	442,056		144,308	2,252	1.59%
SWIFT	0	0	0				0	N/A%
TOTAL NEW AUTOS	10	0	10	442,056			2,252	1.59%
NEW LIGHT-DUTY TRUCKS - POOL #2								
GRAND VITARA	6	0	6	112,970		115,190	2,220	1.97%
VITARA	12	0	12	198,064		199,504	1,440	0.73%
XL-7	9	4	13	186,369	87,890	275,932	1,673	0.61%
TOTAL NEW L-D TRUCKS	27	4	31	497,403	87,890	580,626	5,333	0.91%
TOTAL SUZUKI	37	4	41	639,469	87,890	734,934	7,585	1.04%
TOYOTA								
NEW AUTOS - POOL #1								
AVALON	4	0	4	100,154		100,154	0	0.00%
CAMRY	0	16	16		328,209	328,209	0	0.00%
CELICA	4	0	4	70,708		71,070	362	0.51%
COROLLA	6	0	6	72,206		72,206	0	0.00%
ECHO	4	0	4	40,076		40,244	168	0.42%
MR2 SPYDER	1	1	2	21,342	22,185	43,664	137	0.31%
PRIUS	1	0	1	18,793		18,793	0	0.00%
TOTAL NEW AUTOS	20	17	37	323,279	350,394	674,340	667	0.10%
NEW LIGHT-DUTY TRUCKS - POOL #2								
4RUNNER	4	0	4	113,746		111,415	(2,331)	(2.05)%
HIGHLANDER	0	6	6		145,120	145,120	0	0.00%
LAND CRUISER	1	0	1	46,280		46,018	(262)	(0.57)%
RAV4	4	0	4	63,981		65,116	1,135	1.77%
SEQUOIA	4	0	4	130,070		131,670	1,600	1.23%
SIENNA	3	0	3	69,742		69,365	(377)	(0.54)%
TACOMA PICKUP	17	0	17	263,946		265,721	1,775	0.67%

PAGE 16

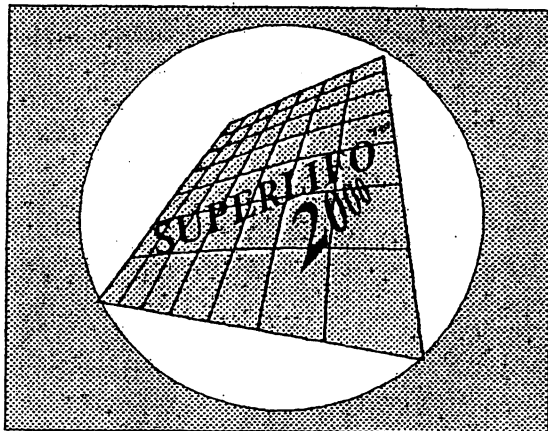
INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/01
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

DECEMBER 21, 2001

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/00 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
TUNDRA	11	0	11	227,233		229,035	1,802	0.79%
TOTAL NEW L-D TRUCKS	44	6	50	914,998	145,120	1,063,460	3,342	0.32%
TOTAL TOYOTA	64	23	87	1,238,277	485,514	1,737,800	4,009	0.23%
VOLKSWAGEN								
NEW AUTOS - POOL #1								
CABRIO	6	0	6	116,998		116,998	0	0.00%
GOLF	8	4	12	124,382	61,032	186,894	1,480	0.80%
GTI	0	3	3		53,999	53,999	0	0.00%
JETTA	14	15	29	253,360	291,234	547,807	3,213	0.59%
NEW BEETLE	10	0	10	174,166		175,138	972	0.56%
PASSAT	16	0	16	381,617		391,968	10,351	2.71%
TOTAL NEW AUTOS	54	22	76	1,050,523	406,265	1,472,804	16,016	1.10%
NEW LIGHT-DUTY TRUCKS - POOL #2								
EUROVAN	2	0	2	58,189		48,975	(9,214)	(15.83)%
TOTAL NEW L-D TRUCKS	2	0	2	58,189		48,975	(9,214)	(15.83)%
TOTAL VOLKSWAGEN	56	22	78	1,108,712	406,265	1,521,779	6,802	0.45%
VOLVO								
NEW AUTOS - POOL #1								
40 SERIES	4	0	4	96,880		97,734	854	0.88%
60 SERIES	3	3	6	82,814	93,081	178,248	2,353	1.34%
70 SERIES	8	5	13	273,912	171,455	448,434	3,066	0.69%
80 SERIES	3	1	4	118,718	46,952	168,364	2,694	1.63%
TOTAL NEW AUTOS	18	9	27	572,324	311,489	892,780	8,967	1.01%
TOTAL VOLVO	18	9	27	572,324	311,489	892,780	8,967	1.01%



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