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A Quarterly Update of LIFO - News, Views and Ideas

LIFO LOOKOUT

Volume 13, Number 4 | Publisher: Willard J. De Filipps, C.P.A. | December 2003

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. *As year-end closes in, TRADE DISCOUNTS & ADVERTISING EXPENSE CHANGES IN ACCOUNTING METHOD ARE STILL THE RIGHT ANSWER FOR DEALERS LOOKING FOR BIG, ONE-TIME TAX DEDUCTIONS.* As we pointed out in our year-end update last year, the big attraction is that these method changes, like the initial adoption of LIFO, result in the largest part of the benefit being deductible in the year of change. Like LIFO, it's one big beneficial *timing difference*.

The entire last issue of the *LIFO Lookout* discussed and illustrated many of the details. For auto dealers using LIFO, the benefits of making these changes can be significant. The Section 481(a) adjustments required to implement these changes will be ***negative*** adjustments. The great news is that the entire amount of the adjustment is 100% deductible in the year of change.

Even better is the fact that these deductions (i.e., the reductions of LIFO valuation of opening inventory in the year of change) are permanent deductions. They are locked into, or embedded, in the LIFO layer valuations. As a result, the amount of the Section 481(a) deduction for a LIFO taxpayer will only be paid back or offset in the future under certain circumstances, and then only to a limited degree.

Once the change has been made, only minor calculations need to be made at each year-end to determine the amount of cost reduction for trade discounts and advertising fees to be pulled out of ending inventory cost.

During 2003, we have already made these changes in accounting methods on a cost effective, turn-key basis for many of our clients.

We also felt this was important enough to contact all of our dealer clients and/or their CPAs to alert them in writing to this development/tax strategy. If you'd like to see how we worded our letter to our clients on this subject, see page 4.

LOOKOUT LOOKS INTO

Some dealers have indicated that they prefer to wait until next year to make the change. Their basic reason for putting off making the change was because their tax reduction strategies for 2003 are already in place ...and they don't need more deductions right now. However, they are planning to make the change next year, with 2004 as the year-of-change.

In some cases, the CPAs who we've spoken with about this just don't seem to get it. They think that it's foolish (some say even "unnecessary") to make the change because they can't "sell it" to their dealers. Is that stupid, or what? These CPAs are adamantly willing to continue to use an accounting method for trade discounts that is ***illegal***. They see nothing wrong with continuing to use a method that is not authorized by the Income Tax Regulations.

Our questions to them are: "What else are you avoiding or letting your dealer avoid because you don't like what the Regulations say?" Reminding them that they should be putting a Form 8275-R in the income tax returns falls on deaf ears.

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(Continued from page 1)

Don't expect the IRS to run around reminding taxpayers that Revenue Ruling 84-41 ... not to mention the Regulations under Section 471 ... requires trade discounts to be eliminated from inventory costs. After all, when has the IRS ever pushed tax deductions on car dealers?

But, consider this: If one really wanted to go to extremes, it could be argued that not eliminating trade discounts from inventory costs is a violation of the LIFO eligibility requirement that ending inventory be stated ***at cost***. Hmmm ... seems that the IRS just looks the other way when taxpayers overstate ending inventory. But, every once in a while, someone in the IRS gets excited over these technicalities. Remember *Mountain State Ford?* Everyone thought they were safe overstating ending inventories by using replacement cost for valuing parts inventories. What a mess that turned out to be!

#2. *"LIFO AT 30 ... LOOKING BACK, SIDEWAYS & FORWARD."* In October, I presented a review of the LIFO application over the last 30 years as it relates to auto dealers at the AICPA National Auto Dealership Conference in San Antonio. My presentation outline is included on pages 5 to 10.

#3. 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.

#4. 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.

#5. 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.

For 2003, new vehicle inflation indexes look to be among the smallest in years based on our one-of-each item category compilations.

Our report compares everything in our *SUPERLIFO* database as of December 19, 2003...with intro-2004 model prices, unless the 2004 intro price was subsequently updated, and that information is also in our database for the end of the year. December 1, 2002 is the reference date for the equivalent of the calendar year 2003 beginning of the year date; i.e., December 31, 2002/January 1, 2003.

The summary on page 23 shows that for most new vehicles, the overall price increases are small again this year. This is again 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.

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.

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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 accept as reasonable...or reject as unreasonable. So be careful, and save your projection calculations just in case the IRS ever wants to see them.

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.

#6. IF YOU'RE TERMINATING LIFO FOR USED VEHICLES, WATCH OUT FOR YOUR TIMING. After last year's used vehicle LIFO calculations were run, big deflation hit many dealers' used vehicle LIFO reserves. At that time, many dealers decided to terminate their used vehicle LIFO elections effective for the year 2002.

Other dealers, mainly those who had elected LIFO for their used vehicles long ago, still had large LIFO reserves ... though they were gradually being whittled down by deflation. These dealers decided to stay on LIFO at least through 2002 and wait and see what 2003 will bring.

Well, it looks like 2003 is bringing more deflation for used vehicle LIFO inventories. Consequently, those dealers who stayed on one more year are more likely now to terminate their used vehicle LIFO elections for 2003.

For these dealers, we should repeat the caution expressed previously regarding the timing of the filing of Form 3115 for permission to make this change.

There is some fine print you don't want to overlook if your dealer wants to terminate his LIFO election for used vehicles (while staying on LIFO for new vehicles) if that dealer recently elected to use the Alternative LIFO Method for Used Vehicles. Termination of the Used Vehicle LIFO Election cannot be made after the end of the year Under Rev. Proc. 2002-9. Instead, permission to make that change must be requested before the end of the year by the filing of Form 3115.

The problem lies in the limitations to the application of Rev. Proc. 2002-9 in certain situations. If the overall LIFO election were made within the last 5 years or if changes within the same method were made within the last five years, Rev. Proc. 2002-9 would not apply and the requirements of Rev. Proc. 97-27 would have to be followed.

If the dealer has been on used vehicle LIFO for more than 5 years, but the dealer recently changed to the Alternative Used Vehicle Method (say, in 2001 when this safe-harbor method first became available), it appears that the termination of the used vehicle LIFO election desired for the year 2003 cannot be made as an automatic change without advance approval *after* year-end. Instead, this change would have to be applied for by filing Form 3115 with the IRS in Washington, D.C. *before* December 31 under Rev. Proc. 97-27.

The second sentence of Sec. 4.02(6) of Rev. Proc. 2002-9 states that "a change in method ... does not include the adoption of a method of accounting ... in the first year in which the taxpayer has the *item* to which the method of accounting relates." Although the term *item* has a whole lot of meanings, and some of them are pretty broad or seem pretty strange, it may be difficult (or impossible) to interpret the term *item* under these circumstances in a way that would permit the dealer to automatically terminate the used vehicle LIFO election for the year 2003 under Rev. Proc. 2002-9 (i.e., without the advance filing before year-end and waiting for IRS approval).

For permission to make this change to terminate LIFO for used vehicles, it is our understanding that although the dealer has to file before the end of the year, the IRS is not requiring the payment of a user fee in connection with these change requests.

December __, 2003

Dear Dealer / CPA:

Re: ABC Dealership, Inc.
Possible Change in Methods of Accounting
For Trade Discounts and for Advertising Fees & Expenses
Effective for Calendar Year 2003

It appears that ABC Dealership, Inc., would benefit greatly by changing its method of accounting for trade discounts (floorplan assistance payments) and for advertising fees and expenses. The schedule enclosed, reflecting December 31, 2002 inventory information, estimates that the one-time, 100% fully-deductible-in-the-year-of-change, Section 481(a) adjustment for the dealership if it makes this change for 2003 would be at least in the range of $80,000 to $87,000.

You can obtain a better estimate of this potential Section 481(a) adjustment/deduction for 2003 by going to www.greenoutsourcing.com. It takes only a few moments to enter the basic data, and you will immediately have a more accurate projection ... at no cost. Alternatively, you can call me at the number above or Todd Boren at Green Financial Outsourcing Solutions at (214) 350-8197.

We have been actively involved with many dealerships and CPAs during the year assisting them in making the appropriate changes in accounting method. For dealers on LIFO, the most beneficial aspect of making these changes is the fact that they receive a significant income tax deduction in the year of change as a result of making these changes.

At the AICPA Auto Dealership Conference in San Antonio in October, I devoted a portion of my presentation on LIFO discussing the fact that many dealers are not properly recording trade discounts in accordance with the Regulations and Revenue Ruling 84-41. This holds true regardless of whether or not the dealership is using LIFO to value its new vehicle inventories.

I have written extensively on these changes in accounting method in the September 2003 issue of the *LIFO Lookout*. If you are not thoroughly familiar with the tax requirements and ramifications of this matter, you should find out more about it before December 31, 2003. You can see the information from the first page of the September 2003 LIFO Lookout on our web site at www.defilipps.com.

Here are two of the key client management issues that were included as part of the 2-page Practice Guide checklist in the *LIFO Lookout*.

1. Have the ramifications and benefits of the change in accounting method been explained to the dealer/client?
   - ☐ If possible changes in accounting method have been discussed, but dealer has decided not to make the changes, is there a memo in the file documenting discussion and rationale for not making changes at this time?
2. ☐ Regardless of how the client/dealer feels about the accounting for trade discounts, what is the Firm's position, liability and/or responsibility for not changing to the correct method/treatment for trade discounts? ***... It is clear that it is incorrect to include trade discounts as inventory costs. (Where do you stand ... and why?)***

Another related point is that if the dealer resists making this change ... despite the fact that he receives a significant benefit from doing so ..., you or your CPA firm may be signing an income tax return that reflects inventory values that have not been reduced for trade discounts in accordance with the Regulations. As a result, technically, the dealership's income tax return is required to include a special form, Form 8275-R, to indicate that the tax return reflects a method of accounting that is not authorized by the income tax regulations.

If your schedule permits, we should talk about this fairly soon since all of this requires action, and in some cases, certain filings with the IRS before December 31.

Sincerely,

Willard J. De Filipps, CPA

LIFO AT 30

Looking Back, Sideways & Forward

WILLARD J. DE FILIPPS, CPA

AICPA NATIONAL AUTO DEALERSHIP CONFERENCE
SAN ANTONIO, TEXAS - OCTOBER 23, 2003

I. ***Background & Perspective: Major Developments Along the Way***

A. Measuring and estimating inflation ... CPAs lead, IRS follows

B. The turbulent 80's

C. Alternative LIFO Method for New Vehicles

1. Compromise on computations all the way around ... IRS, NADA, dealers, CPAs
2. Originally, published as Revenue Procedure 92-79
3. Superseded by Revenue Procedure 97-36 ... identical in content, just removed all transition rules

D. Controversy over LIFO financial statement "conformity" for auto and truck dealerships

1. Various conformity requirements
2. Dealer financial statements required to be submitted each month in prescribed formats to the manufacturer / Factory ... held to be subject to year-end LIFO conformity requirements because they were statements submitted "for credit purposes"
3. The issue surfaces in 1994 ... at the first AICPA National Auto Dealership Conference
4. Eventual "resolution" in 1997
   a. Revenue Procedure 97-44
      (1) Penalty tax for past conformity violations
      (2) Penalty computed as 4.7% of LIFO reserve as of Dec. 31, 1996 (for calendar year taxpayers)
      (3) Paid in three equal installments
      (4) Subsequent IRS enforcement ... very disappointing
   b. Revenue Ruling 97-42
      (1) IRS guidance requires that an adjustment for LIFO must be reflected somewhere in the dealer's year-end income statement, but it does not mandate where the adjustment should be reflected (i.e., in *cost of goods sold* section ... or in *other income* or *other deductions*)
      (2) Reasonable estimate of change for the year may be used
      (3) Fiscal year dealerships only have to reflect LIFO change once per year

E. Parts & Accessories ... *Mountain State Ford*, and the use of replacement cost for valuing parts inventories

1. The use of the replacement cost method for valuing parts-type inventories was disallowed by the Tax Court in *Mountain State Ford Truck Sales, Inc. v. Comm.* 112 T.C. No. 7 (March, 1999)
   a. The taxpayer's appeal to the US Court of Appeals for the Tenth Circuit was rendered moot by the IRS issuance of Rev. Proc. 2002-17
2. Revenue Procedure 2002-17
   a. Generally, effective for taxable years ending on or after December 31, 2001
   b. Resulted, in part, from NADA efforts to try to compel IRS/Treasury to provide relief
   c. Provides safe harbor accounting method for dealers' parts and accessories inventories
      (1) Must be based on end-of-year quantities and mix (not interim)
      (2) Must include all items - not only a sample
   d. Allows dealers to approximate actual cost of parts inventory items by using replacement cost method based on end-of-the-year prices taken from manufacturers' price lists
   f. Automatic consent to change to this method was granted in almost all cases
   g. Rev. Proc. 2002-9 is modified to include this change as an automatic change in Appendix Sec. 10.02

(Continued)

I. ***Background & Perspective: Major Developments Along the Way (continued)***

E. Parts & Accessories ... *MSFTS*, and the use of replacement cost for valuing parts inventories ... (continued)

3. Action / Form 3115 filings necessary to conform
   a. In many situations, no action was required ... dealers would just continue doing what they had been doing in the past
   b. Other situations where filing Form 3115 was required (in contrast to "do nothing" situations)
4. For some dealers, easiest way out (or better advice) was to convert to IPIC method for parts and skip all of the Rev. Proc. 2002-17 requirements

F. Alternative LIFO Method for Used Vehicles ... Rev. Proc. 2001-23

1. Methodology (sub-elections and computations) patterned after Alternative LIFO for New Vehicles
2. Appropriate modifications are included to reflect difference in nature of used vehicles

G. LIFO develops its own legal vocabulary in the Courts

1. *Wendle Ford* ... definition of an "item" for LIFO repricing computation purposes
2. *Hamilton Industries* ... method of accounting implications with corresponding Section 481(a) adjustments negate statute of limitations by making adjustments in the earliest open year ... "clear reflection of income" standard ... Statute of limitations never runs on timing/methods of accounting
3. *Amity Leather Products* ... LIFO should not result in a deduction for factors other than inflation (such as technological change, inventory mix, etc.)
4. *Consolidated Manufacturing, Inc.* ... expanding reasons for terminating LIFO elections beyond those listed in Revenue Procedure 79-23
5. **"Link-chain, index"** methodology ... is it really necessary to be technically correct on this matter?
   a. "Repricing" versus "Double-extension"
   b. "Sample" vs. "Representative portion"

H. The real service - and practice opportunities - for dealers on LIFO

1. Projections of year-end changes in LIFO reserves and related planning
2. Understanding, reconciling and explaining (projected) LIFO reserve changes

II. ***New & Used Vehicles - Contemporary LIFO Issues***

A. New vehicles

1. Item categories - multiplying like rabbits
2. How far do you have to go in determining "item categories"?
3. Use of shared model codes by some manufacturers make reference to VIN numbers inappropriate ... must use most detailed level of description provided by manufacturer
4. ***"New Items"*** lists .... None of which are "Official"
5. Crossover vehicles ... should there be a third pool?

B. There's also a "half-LIFO" for new vehicles ... i.e., use of Bureau of Labor Statistics / IPIC Method ... Short-changes the dealer ... BLS determines new vehicle inflation to be approximately 1/3 to 1/2 of amounts computed under regular calculations because it makes all kinds of "qualitative" adjustments

C. Used vehicles

1. Basic issue: LIFO in deflationary periods ... many dealers are terminating (or have recently terminated) these elections
2. Cost determinations ... specific rules are provided in the Rev. Proc. for determining cost of used vehicles

(Continued)

II. *New & Used Vehicles - Contemporary LIFO Issues (continued)*

C. Used vehicles ... (continued)

3. Use of *Official Used Vehicle Guides*, change in accounting method implications
4. Impractical requirements ... double-checking the *Official Used Vehicle Guides* for platform changes
5. Problematic language for "permitted" methods when terminating used vehicle LIFO elections

D. Determining "cost" of vehicles ... *To change or not to change?...* that is the question

1. Trade discounts/manufacturer financing incentives
2. LIFO implications of selectively changing accounting methods
   a. Section 481(a) adjustment is required ... negative Sec. 481(a) adjustment taken 100% in the year of change
   b. LIFO indexes as of the beginning of the year of change must be restated
3. Automatic change, can be made after year-end by filing Form 3115 with the tax return
4. Distinguishing CAMs for advertising fees and expenses (non-automatic changes) from changes for trade discounts

III. *Reserve Recapture Issues ... Minimizing Recapture of LIFO Reserves when Changing Entity Form*

A. Special problems for Oldsmobile dealers being phased-out by GM and for other dealers in transition

1. Different results depending on LIFO methods used: Alternative LIFO, IPIC, other methods
2. Vertical slice approach discussed in LTR 199920001 could be analogous
3. LTR 199911044 ... Although favorable to the auto dealer using the Alternative LIFO Method, the LTR involves a very simple fact pattern ... Leaves a lot of "wiggle room" in it for the IRS, but at the same time, also leaves a lot of "wiggle room" in it for certain dealer situations

B. Acceleration of repayment of LIFO reserves in other situations

1. Vertical slice approach ... LTR 199920001 doesn't involve an auto dealer, but it could be analogous

C. Section 1363(d) recapture of LIFO reserve where C corp. changes to S status

1. Revenue Procedure 94-61 provides guidance
2. Tax attributable to LIFO reserve is recaptured and repaid over 4 years ... basis is stepped-up
3. LIFO election is not terminated by change to S status ... LIFO election remains in effect
4. Special collapsed layer is created which combines all prior years' LIFO layers into a single layer ... Note: this does not involve a rebasing of all the prior year layer indexes
5. Tax versus financial accounting treatment for LIFO computations for S years
6. Other special problems

D. Section 351 Transfers and Section 721 Transfers

1. Regs (under IPIC) now allow the dealer to treat the year of transfer as a new base year ... This allows dealer relate (or index) the current year cost against the prior year's costs ... so that dealer does not lose all of the LIFO benefits realized before the Section 351 or Section 721 transfers.

E. Legitimate dealership restructuring not subject to LIFO recapture ... *Coggin Automotive Corporation*

1. $4.8 million LIFO reserve recapture issue upon restructuring of consolidated automotive group
2. Tax Court (115 T.C. 349 [2000]) upheld IRS and required recapture upon restructuring of consolidated automotive group
3. Appeals Court, reversing the IRS and the Tax Court, did not require recapture of LIFO reserves (89 AFTR2d 2002-2826 [CA-11, 2002])

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III. *Reserve Recapture Issues ... Minimizing Recapture of LIFO Reserves ... (continued)*

E. Legitimate dealership restructuring not subject to LIFO recapture ... *Coggin Automotive Corp.* ... (continued)

4. Letter Ruling 9716003 is precursor to the case in the Tax Court
5. Special cautions for current restructurings
   a. "Anti-abuse" of aggregation theory partnership regulation ... Reg. Sec. 1.701-2(e) ... effective for transactions after Dec. 29, 1994
   b. IRS may choose to contest similar transactions in jurisdictions outside of the 11th Circuit ... i.e., in states outside of Florida, Georgia and Alabama
   c. Best advice: Dealers should consider requesting a ruling from the IRS before undertaking restructuring transaction(s)

F. No LIFO reserve recapture where S Corporation contributes auto dealerships' LIFO inventories to a newly-formed limited liability company ... LTR 200123035

IV. *S Corporation QSub Groups ... Integrating LIFO Opportunities and Avoiding Pitfalls*

A. Tax returns, LIFO elections & election terminations

1. Overall combination of assets, per statute. Nothing in the instructions indicates what to do
2. No IRS formal guidance on how to combine all assets of Qsub group
   a. Initial LIFO elections ... Do all QSubs have to be on LIFO?
   b. Terminating LIFO elections for QSub members

B. LIFO calculations, pooling & reserve recapture implications

1. Should each Qsub's inventory constitute a separate pool?
2. Is each Qsub a "separate trade or business?"
   a. If so, separate pooling implications.
   b. Resolution may depend on whether the Qsub is operated as a "separate trade or business"
3. If, in initial return, all LIFO inventories of all Qsubs were combined, that approach obviously provides greater protection against reductions in inventory resulting in LIFO reserve recapture
   a. Method of accounting and change in method of accounting implications
4. How Qsub inventories have been treated in the initial S corp. return filed to include the Qsubs could have "method of accounting" implications
5. To date, the IRS has not issued any instructions or guidance on these LIFO/pooling inventory questions. Accordingly, there is no official IRS position requiring that Qsub inventories should be treated separately

C. It is important to consider all of this ***before*** filing the first income tax return for the S corp.

D. Under Reg. Sec. 1.1361-4, if S corp. makes a valid Q-Sub election with respect to a subsidiary, the subsidiary is "deemed to have liquidated into the S corp." ... Carryover of LIFO layers, merger of layers under Sec. 381(c).

V. *Changes in Accounting Methods: Rules & Guidelines Updated in 2002*

A. ***Voluntary Changes - Automatic***

1. Now covered by Rev. Proc. 2002-9 ... superseding Rev. Procs. 99-49, 98-60, 97-37
2. Basically, taxpayers making automatic changes are not under audit
3. Generally, a Section 481(a) adjustment is not required where the method changes involve LIFO inventories ... instead, use of the cut-off method is permitted
4. Form 3115 is filed after the year end as part of the income tax return for the year of change
   A copy of Form 3115 must also filed with the IRS National Office

(Continued)

V. *Changes in Accounting Methods: Rules & Guidelines Updated in 2002* *(continued)*

A. ***Voluntary Changes - Automatic*** ... (continued)

5. Special dealership applications
   a. Electing IRS-approved safe harbor LIFO calculation methods
      (1) New vehicles ... Rev. Proc. 97-36: Alternative LIFO Method for New Vehicles
      (2) Used vehicles ... Rev. Proc. 2001-23: Used Vehicle Alternative LIFO Method
   b. For voluntary LIFO election terminations see VI. below
   c. Certain IPIC (Inventory Price Index Computation) method changes
   d. Determining the cost of used vehicles purchased or taken as a trade-in
   e. Including and/or excluding certain other items or costs from inventory
      (1) Trade discounts, floorplan assistance, etc. ... Section 481(a) adjustment is required
   f. Changes in methods for determining inventory costs capitalized under Section 263A

B. ***Permission-Required Changes***

1. Now covered by Rev. Proc. 2002-19 ... Modifying Rev. Proc. 97-27
2. General rules & discussion ... see V.A.2. and V.A.3. above
3. Form 3115 must be filed with the IRS before year-end. Payment of a user fee is required
4. Special dealership applications
   a. Advertising fees and expenses ... Section 481(a) adjustment is required

C. ***IRS Audit-Initiated ... (Involuntary) ... Method Changes***

1. Involves changes in accounting methods that are made on audit by the IRS and whether the taxpayer - or the IRS - is bound / required to follow that accounting method in succeeding years.
2. Now covered by Rev. Proc. 2002-18
3. Superseding a proposed Revenue Procedure that was included in Notice 98-31 which would have required Section 481(a) adjustment to be picked up 100% in earliest open year
4. General rules & special dealership applications

D. ***Form 3115:*** Current Revision (as of October 21, 2003) is dated May, 1999

1. Form required to be filed when requesting IRS permission to make a change in accounting methods
2. General filing timing requirements ... automatic vs. changes requiring advance approval
3. Other filing experiences with the National Office

VI. *Voluntary Termination of LIFO Elections*

A. Terminating ***all*** LIFO elections at the same time

1. Does not require advance permission from the IRS
2. Does not require payment of user fee
3. Form 3115 is filed after the year end as part of the income tax return for the year of change
   A copy of Form 3115 must also filed with the IRS National Office
4. Rev. Proc. 2002-9 superseding Rev. Proc. 97-27

(Continued)

VI. *Voluntary Termination of LIFO Elections (continued)*

B. Terminating ***less than all*** LIFO elections at the same time

1. No longer requires advance permission from the IRS, nor payment of a user fee ... now permitted by Rev. Proc. 2002-9 (Section 9.05) superseding Rev. Proc. 97-27, which previously treated this change as a change requiring advance permission from the IRS
2. Filing of Form 3115 is done ***after*** the end of the year of change as part of the income tax return for the year of change. A copy of Form 3115 must also filed with the IRS National Office
3. ***IRS relaxed the rules ...*** Issues where terminating used vehicle LIFO election where taxpayer has changed to the Alternative LIFO Method for Used Vehicles (Rev. Proc. 2001-23) or made other changes within the last 5 years
4. Section 481(a) adjustment & spread periods ... positive adjustments ... negative adjustments
5. Problematic / Troublesome language in definition of "permitted method" of accounting required to be used for inventory going off of LIFO

VII. *Looking Forward: What Lies Ahead?*

A. Basic considerations ...

1. Inflationary vs. deflationary price trends for new vehicles and for used vehicles
2. Changing value of LIFO interest-free loans/"permanent" deferrals due to lower interest rates affecting the time value of money

B. The real service - and practice opportunities - for dealers on LIFO

1. Projections of year-end changes in LIFO reserves and related planning
2. Understanding, reconciling and explaining (projected) LIFO reserve changes

C. Short term ... next 12 to 18 months or so

1. More terminations of used vehicle elections?
2. More changes in accounting methods to eliminate trade discounts and/or advertising fees from inventory costs?
3. LIFO elections for motorcycle dealers
4. Conversion of parts inventories on LIFO to the IPIC LIFO Method

D. Long term ... Will Congress ever repeal LIFO?

VIII. *Bibliography*

A. A comprehensive, topical index listing articles discussing all of the developments referred to in this outline can be accessed at www.defilipps.com (follow the "Publication" and "Index of Articles" links)

B. These articles have appeared in the *LIFO Lookout* from March 1991 through December 2002 ... Many of these articles also include additional selected bibliographies

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.

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SPECIAL YEAR-END CHALLENGES FOR LIFO USERS

CONFORMITY REPORTING REQUIREMENTS

YEAR-END PROJECTIONS FOR PLANNING PURPOSES

 (Continued from page 11)

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- →

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 equipment) 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-

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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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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 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

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

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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 <u>do not apply</u> 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.

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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 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.

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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.

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.

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 payback 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.

→

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 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

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 12/31/03**

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

	POOL #1 NEW AUTOMOBILES	POOL #2 NEW L-D TRUCKS
ACURA	0.12%	1.78%
AUDI	0.98%	0.00%
BMW	0.33%	2.63%
BUICK	2.09%	0.52%
CADILLAC	1.71%	1.03%
CHEVROLET	1.19%	2.26%
CHRYSLER	1.71%	2.30%
DODGE	2.15%	2.51%
FORD	0.57%	1.56%
GMC TRUCKS	0.00%	3.31%
HONDA	0.90%	0.43%
HUMMER	0.00%	1.50%
HYUNDAI	3.25%	1.98%
INFINITI	0.95%	0.00%
ISUZU	0.00%	(1.50)%
JAGUAR	(0.12)%	0.00%
JEEP	0.00%	2.13%
KIA	0.88%	3.17%
LAND ROVER/RANGE ROVER	0.00%	(11.87)%
LEXUS	(0.20)%	0.66%
LINCOLN	(0.29)%	1.25%
MAZDA	0.70%	4.16%
MERCEDES	1.40%	2.75%
MERCURY	1.30%	1.88%
MINI	0.12%	0.00%
MITSUBISHI	0.66%	0.79%
NISSAN	1.37%	1.51%
OLDSMOBILE	1.90%	1.26%
PONTIAC	1.18%	(1.23)%
PORSCHE	0.00%	0.00%
SAAB	(0.04)%	0.00%
SATURN	(0.39)%	3.87%
SCION	0.00%	0.00%
SUBARU	1.75%	0.62%
SUZUKI	1.05%	2.18%
TOYOTA	0.08%	0.48%
VOLKSWAGEN	2.83%	0.00%
VOLVO	(0.21)%	2.35%

Complete 2004 intro price information is not currently available for all models.
Accordingly, some inflation indexes exclude certain item(s) for which 2004 information is missing.
New items are repriced at current cost – i.e., no inflation.

Source: W. J. De Filipps' Make/Model Analysis Data Base Report, Preliminary Edition (copyright 2003)

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DECEMBER 19, 2003

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
ACURA								
NEW AUTOS - POOL #1								
NSX-T	2	0	2	158,426		158,426	0	0.00%
RL	2	0	2	78,621		79,114	493	0.63%
RSX	5	0	5	97,672		97,900	228	0.23%
TL	0	6	6		184,355	184,355	0	0.00%
TSX	0	4	4		100,228	100,228	0	0.00%
TOTAL NEW AUTOS	9	10	19	334,719	284,583	620,023	721	0.12%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MDX	5	0	5	176,830		179,980	3,150	1.78%
TOTAL NEW L-D TRUCKS	5	0	5	176,830		179,980	3,150	1.78%
TOTAL ACURA	14	10	24	511,549	284,583	800,003	3,871	0.49%
AUDI								
NEW AUTOS - POOL #1								
A4 SERIES	12	13	25	334,291	376,164	715,825	5,370	0.76%
A6 SERIES	6	1	7	218,383	39,095	266,252	8,774	3.41%
A8 SERIES	0	1	1		64,050	64,050	0	0.00%
ALLROAD	2	1	3	73,208	42,422	114,806	(824)	(0.71)%
RS6 SERIES	0	1	1		74,239	74,239	0	0.00%
S4 SERIES	0	4	4		168,688	168,688	0	0.00%
S6 SERIES	0	0	0				0	N/A%
S8 SERIES	0	0	0				0	N/A%
TT	4	2	6	128,532	74,768	205,526	2,226	1.09%
TOTAL NEW AUTOS	24	23	47	754,414	839,426	1,609,386	15,546	0.98%
TOTAL AUDI	24	23	47	754,414	839,426	1,609,386	15,546	0.98%
BMW								
NEW AUTOS - POOL #1								
3 SERIES	14	0	14	410,640		413,740	3,100	0.75%
5 SERIES	0	4	4		174,910	174,910	0	0.00%
7 SERIES	2	1	3	128,310	105,380	233,690	0	0.00%
M SERIES	2	0	2	91,910		92,275	365	0.40%
Z4	2	0	2	66,750		66,930	180	0.27%

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DECEMBER 19, 2003

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
Z8	0	1	1		124,480	124,480	0	0.00%
TOTAL NEW AUTOS	20	6	26	697,610	404,770	1,106,025	3,645	0.33%
NEW LIGHT-DUTY TRUCKS - POOL #2								
X5	2	0	2	81,400		83,540	2,140	2.63%
TOTAL NEW L-D TRUCKS	2	0	2	81,400		83,540	2,140	2.63%
TOTAL BMW	22	6	28	779,010	404,770	1,189,565	5,785	0.49%
BUICK								
NEW AUTOS - POOL #1								
CENTURY	1	0	1	19,087		19,691	604	3.16%
LESABRE	2	0	2	51,487		52,398	911	1.77%
PARK AVENUE	2	0	2	66,337		67,581	1,244	1.88%
REGAL	2	0	2	47,324		48,422	1,098	2.32%
TOTAL NEW AUTOS	7	0	7	184,235		188,092	3,857	2.09%
NEW LIGHT-DUTY TRUCKS - POOL #2								
RAINIER	0	4	4		133,198	133,198	0	0.00%
RENDEZVOUS	2	0	2	48,770		49,721	951	1.95%
TOTAL NEW L-D TRUCKS	2	4	6	48,770	133,198	182,919	951	0.52%
TOTAL BUICK	9	4	13	233,005	133,198	371,011	4,808	1.31%
CADILLAC								
NEW AUTOS - POOL #1								
CTS	1	0	1	27,149		27,880	731	2.69%
DE VILLE	3	0	3	128,580		132,019	3,439	2.67%
SEVILLE	2	0	2	87,748		88,925	1,177	1.34%
XLR	0	1	1		69,731	69,731	0	0.00%
TOTAL NEW AUTOS	6	1	7	243,477	69,731	318,555	5,347	1.71%
NEW LIGHT-DUTY TRUCKS - POOL #2								
ESCALADE	4	0	4	191,771		194,547	2,776	1.45%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
SRX	0	2	2		77,973	77,973	0	0.00%
TOTAL NEW L-D TRUCKS	4	2	6	191,771	77,973	272,520	2,776	1.03%
TOTAL CADILLAC	10	3	13	435,248	147,704	591,075	8,123	1.39%
CHEVROLET								
NEW AUTOS - POOL #1								
AVEO	0	6	6		61,244	61,244	0	0.00%
CAVALIER	6	1	7	86,890	9,578	98,582	2,114	2.19%
CLASSIC	1	0	1	16,273		17,161	888	5.46%
CORVETTE	3	0	3	126,617		127,798	1,181	0.93%
IMPALA	2	1	3	40,873	25,012	67,166	1,281	1.94%
MALIBU	0	3	3		56,374	56,374	0	0.00%
MALIBU MAXX	0	3	3		61,123	61,123	0	0.00%
MONTE CARLO	2	1	3	40,186	24,829	66,064	1,049	1.61%
TOTAL NEW AUTOS	14	15	29	310,839	238,160	555,512	6,513	1.19%
NEW LIGHT-DUTY TRUCKS - POOL #2								
ASTRO VAN	6	0	6	128,872		133,388	4,516	3.50%
AVALANCHE	4	0	4	119,542		126,407	6,865	5.74%
BLAZER	5	0	5	105,410		108,501	3,091	2.93%
COLORADO	0	32	32		601,040	601,040	0	0.00%
EXPRESS CARGO VAN	13	1	14	298,939	21,153	322,398	4,306	1.35%
EXPRESS CUTAWAY VAN	6	0	6	123,797		127,338	3,541	2.86%
EXPRESS PASSENGER VAN	6	0	6	144,883		147,880	2,997	2.07%
S10 PICKUP	1	0	1	21,706		22,272	566	2.61%
SILVERADO 1500	21	12	33	494,395	274,364	798,232	29,473	3.83%
SILVERADO 2500	5	6	11	127,802	168,563	301,536	5,171	1.74%
SILVERADO 2500HD	28	10	38	757,670	247,321	1,033,979	28,988	2.88%
SILVERADO 3500	14	16	30	396,007	453,494	862,526	13,025	1.53%
SILVERADO 3500 CHASSIS CABS	12	6	18	286,029	141,955	439,981	11,997	2.80%
SSR	0	1	1		38,681	38,681	0	0.00%
SUBURBAN	4	0	4	135,555		137,463	1,908	1.41%
TAHOE	2	0	2	61,522		62,300	778	1.26%
TRACKER	8	0	8	144,795		151,807	7,012	4.84%
TRAILBLAZER	6	2	8	162,044	56,146	223,297	5,107	2.34%
VENTURE	7	1	8	162,497	30,331	192,330	(498)	(0.26)%
TOTAL NEW L-D TRUCKS	148	87	235	3,669,465	2,033,048	5,831,356	128,843	2.26%
TOTAL CHEVROLET	162	102	264	3,980,304	2,271,208	6,386,868	135,356	2.17%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
CHRYSLER								
NEW AUTOS - POOL #1								
300M	2	0	2	56,601		57,321	720	1.27%
CONCORDE	3	0	3	71,846		72,926	1,080	1.50%
CROSSFIRE	0	1	1		31,158	31,158	0	0.00%
SEBRING	8	1	9	174,520	21,144	199,931	4,267	2.18%
TOTAL NEW AUTOS	13	2	15	302,967	52,302	361,336	6,067	1.71%
NEW LIGHT-DUTY TRUCKS - POOL #2								
PACIFICA	0	2	2		56,129	56,129	0	0.00%
PT CRUISER	4	0	4	73,595		77,839	4,244	5.77%
TOWN & COUNTRY	4	3	7	118,156	78,913	200,326	3,257	1.65%
TOTAL NEW L-D TRUCKS	8	5	13	191,751	135,042	334,294	7,501	2.30%
TOTAL CHRYSLER	21	7	28	494,718	187,344	695,630	13,568	1.99%
DODGE								
NEW AUTOS - POOL #1								
INTREPID	3	0	3	64,641		65,532	891	1.38%
NEON	3	1	4	41,739	18,970	61,859	1,150	1.89%
STRATUS	6	0	6	112,297		115,598	3,301	2.94%
VIPER	1	0	1	72,471		73,791	1,320	1.82%
TOTAL NEW AUTOS	13	1	14	291,148	18,970	316,780	6,662	2.15%
NEW LIGHT-DUTY TRUCKS - POOL #2								
CARAVAN	5	3	8	105,328	78,335	187,753	4,090	2.23%
DAKOTA	18	0	18	342,992		353,982	10,990	3.20%
DURANGO	0	6	6		164,340	164,340	0	0.00%
RAM PICKUP	40	0	40	944,221		979,219	34,998	3.71%
SPRINTER	0	13	13		361,380	361,380	0	0.00%
TOTAL NEW L-D TRUCKS	63	22	85	1,392,541	604,055	2,046,674	50,078	2.51%
TOTAL DODGE	76	23	99	1,683,689	623,025	2,363,454	56,740	2.46%
FORD								
NEW AUTOS - POOL #1								
CROWN VICTORIA	8	2	10	200,993	45,724	247,731	1,014	0.41%
FOCUS	11	2	13	158,191	34,476	194,118	1,451	0.75%
MUSTANG	12	2	14	283,253	68,281	352,521	987	0.28%
TAURUS	14	0	14	275,830		277,873	2,043	0.74%
THUNDERBIRD	2	1	3	67,663	39,696	108,607	1,248	1.16%
TOTAL NEW AUTOS	47	7	54	985,930	188,177	1,180,850	6,743	0.57%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
NEW LIGHT-DUTY TRUCKS - POOL #2								
CUTAWAY VAN	9	0	9	175,817		179,684	3,867	2.20%
E-SERIES	16	2	18	361,190	53,438	421,378	6,750	1.63%
ESCAPE	7	0	7	147,857		147,221	(636)	(0.43)%
EXCURSION	19	0	19	658,849		666,707	7,858	1.19%
EXPEDITION	16	2	18	500,780	58,676	562,420	2,964	0.53%
EXPLORER	32	0	32	929,466		944,960	15,494	1.67%
EXPLORER SPORT	6	2	8	139,854	50,575	193,727	3,298	1.73%
F150 HERITAGE	21	0	21	436,100		445,968	9,868	2.26%
F150 PICKUP	0	46	46		1,122,303	1,122,303	0	0.00%
F250 SUPER DUTY PICKUP	28	0	28	705,748		721,056	15,308	2.17%
F350 SUPER DUTY PICKUP	50	0	50	1,319,520		1,346,132	26,612	2.02%
FREESTAR	0	6	6		147,141	147,141	0	0.00%
RANGER	30	1	31	515,354	21,815	555,732	18,563	3.46%
SUPER DUTY CAB/CHASSIS	36	0	36	901,214		919,622	18,408	2.04%
TOTAL NEW L-D TRUCKS	270	59	329	6,791,749	1,453,948	8,374,051	128,354	1.56%
TOTAL FORD	317	66	383	7,777,679	1,642,125	9,554,901	135,097	1.43%
GMC TRUCKS								
NEW LIGHT-DUTY TRUCKS - POOL #2								
CANYON	0	26	26		495,494	495,494	0	0.00%
ENVOY	4	0	4	114,600		117,270	2,670	2.33%
ENVOY XL	4	0	4	122,021		124,328	2,307	1.89%
ENVOY XUV	0	4	4		125,982	125,982	0	0.00%
SAFARI	6	0	6	128,872		132,336	3,464	2.69%
SAVANA CARGO VAN	13	4	17	296,939	84,214	384,227	3,074	0.81%
SAVANA CUTAWAY VAN	6	0	6	123,797		126,630	2,833	2.29%
SAVANA PASSENGER VAN	6	0	6	144,883		147,288	2,405	1.66%
SIERRA 3500 CHASSIS-CABS	12	6	18	290,818	141,294	443,716	11,604	2.69%
SIERRA HEAVY-DUTY PICKUP	34	8	42	910,424	209,878	1,180,621	60,319	5.38%
SIERRA PICKUP	44	14	58	1,101,938	368,780	1,543,941	73,223	4.98%
SONOMA	9	0	9	149,761		153,024	3,263	2.18%
YUKON	8	0	8	287,691		291,402	3,711	1.29%
TOTAL NEW L-D TRUCKS	146	62	208	3,671,744	1,425,642	5,266,259	168,873	3.31%
TOTAL GMC TRUCKS	146	62	208	3,671,744	1,425,642	5,266,259	168,873	3.31%
HONDA								
NEW AUTOS - POOL #1								
ACCORD	43	5	48	900,778	101,472	1,016,762	14,512	1.45%
CIVIC	26	8	34	390,035	114,640	503,992	(683)	(0.14)%
INSIGHT	3	0	3	56,643		56,922	279	0.49%
S2000	1	0	1	29,325		29,505	180	0.61%
TOTAL NEW AUTOS	73	13	86	1,376,781	216,112	1,607,181	14,288	0.90%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
NEW LIGHT-DUTY TRUCKS - POOL #2								
CR-V	8	0	8	149,069		149,899	830	0.56%
ELEMENT	0	10	10		176,581	176,581	0	0.00%
ODYSSEY	5	0	5	125,948		126,363	415	0.33%
PILOT	5	0	5	136,050		137,354	1,304	0.96%
TOTAL NEW L-D TRUCKS	18	10	28	411,067	176,581	590,197	2,549	0.43%
TOTAL HONDA	91	23	114	1,787,848	392,693	2,197,378	16,837	0.77%
HUMMER								
NEW LIGHT-DUTY TRUCKS - POOL #2								
HUMMER	1	0	1	44,336		45,000	664	1.50%
TOTAL NEW L-D TRUCKS	1	0	1	44,336		45,000	664	1.50%
TOTAL HUMMER	1	0	1	44,336		45,000	664	1.50%
HYUNDAI								
NEW AUTOS - POOL #1								
ACCENT	3	7	10	30,614	74,706	106,080	760	0.72%
ELANTRA	6	3	9	77,296	40,665	122,011	4,050	3.43%
SONATA	7	0	7	108,218		113,229	5,011	4.63%
TIBURON	5	0	5	78,255		83,191	4,936	6.31%
XG350	2	0	2	44,361		44,361	0	0.00%
TOTAL NEW AUTOS	23	10	33	338,744	115,371	468,872	14,757	3.25%
NEW LIGHT-DUTY TRUCKS - POOL #2								
SANTA FE	4	4	8	71,888	88,667	163,733	3,178	1.98%
TOTAL NEW L-D TRUCKS	4	4	8	71,888	88,667	163,733	3,178	1.98%
TOTAL HYUNDAI	27	14	41	410,632	204,038	632,605	17,935	2.92%
INFINITI								
NEW AUTOS - POOL #1								
G35	4	0	4	108,847		109,992	1,145	1.05%
I35	1	0	1	26,225		26,360	135	0.51%
M45	0	0	0				0	N/A%
Q45	0	0	0				0	N/A%
TOTAL NEW AUTOS	5	0	5	135,072			1,280	0.95%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
NEW LIGHT-DUTY TRUCKS - POOL #2								
FX35	0	4	4		126,556	126,556	0	0.00%
FX45	0	2	2		80,018	80,018	0	0.00%
QX4	0	0	0				0	N/A%
TOTAL NEW L-D TRUCKS	0	6	6		206,574		0	0.00%
TOTAL INFINITI	5	6	11	135,072	206,574	342,926	1,280	0.37%
ISUZU								
NEW LIGHT-DUTY TRUCKS - POOL #2								
ASCENDER	2	0	2	53,951		54,166	215	0.40%
AXIOM	4	0	4	103,750		101,883	(1,867)	(1.80)%
RODEO	2	3	5	42,360	62,777	102,833	(2,294)	(2.18)%
TOTAL NEW L-D TRUCKS	8	3	11	200,051	62,777	258,882	(3,946)	(1.50)%
TOTAL ISUZU	8	3	11	200,051	62,777	258,882	(3,946)	(1.50)%
JAGUAR								
NEW AUTOS - POOL #1								
S-TYPE	3	0	3	139,172		141,064	1,892	1.36%
X-TYPE	2	0	2	59,704		57,020	(2,684)	(4.50)%
XJ SERIES	0	3	3		183,813	183,813	0	0.00%
XK SERIES	4	0	4	283,304		283,304	0	0.00%
TOTAL NEW AUTOS	9	3	12	482,180	183,813	665,201	(792)	(0.12)%
TOTAL JAGUAR	9	3	12	482,180	183,813	665,201	(792)	(0.12)%
JEEP								
NEW LIGHT-DUTY TRUCKS - POOL #2								
GRAND CHEROKEE	5	1	6	145,227	33,723	182,420	3,470	1.94%
LIBERTY	6	0	6	120,721		123,725	3,004	2.49%
WRANGLER	5	1	6	95,887	18,925	117,147	2,335	2.03%
TOTAL NEW L-D TRUCKS	16	2	18	361,835	52,648	423,292	8,809	2.13%
TOTAL JEEP	16	2	18	361,835	52,648	423,292	8,809	2.13%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
KIA								
NEW AUTOS - POOL #1								
AMANTI	0	1	1		22,655	22,655	0	0.00%
OPTIMA	5	0	5	80,285		80,285	0	0.00%
RIO	4	0	4	39,935		42,075	2,140	5.36%
SPECTRA	0	8	8		101,025	101,025	0	0.00%
TOTAL NEW AUTOS	9	9	18	120,220	123,680	246,040	2,140	0.88%
NEW LIGHT-DUTY TRUCKS - POOL #2								
SEDONA	2	0	2	38,000		39,065	1,065	2.80%
SORENTO	4	2	6	81,530	37,650	123,090	3,910	3.28%
TOTAL NEW L-D TRUCKS	6	2	8	119,530	37,650	162,155	4,975	3.17%
TOTAL KIA	15	11	26	239,750	161,330	408,195	7,115	1.77%
LAND ROVER/RANGE ROVER								
NEW LIGHT-DUTY TRUCKS - POOL #2								
LAND ROVER DISCOVERY	3	0	3	130,950		103,284	(27,666)	(21.13)%
LAND ROVER FREELANDER	3	0	3	78,862		73,592	(5,270)	(6.68)%
RANGE ROVER	1	0	1	64,792		65,142	350	0.54%
TOTAL NEW L-D TRUCKS	7	0	7	274,604		242,018	(32,586)	(11.87)%
TOTAL LAND ROVER/RANGE ROVER	7	0	7	274,604		242,018	(32,586)	(11.87)%
LEXUS								
NEW AUTOS - POOL #1								
ES 330	1	0	1	28,041		28,130	89	0.32%
GS 300	1	0	1	34,077		34,077	0	0.00%
GS 430	1	0	1	41,607		41,607	0	0.00%
IS 300	3	0	3	81,437		80,117	(1,320)	(1.62)%
LS 430	1	0	1	47,784		47,958	174	0.36%
SC 430	1	0	1	53,961		54,438	477	0.88%
TOTAL NEW AUTOS	8	0	8	286,907		286,327	(580)	(0.20)%
NEW LIGHT-DUTY TRUCKS - POOL #2								
GX 470	1	0	1	39,084		39,213	129	0.33%
LX 470	1	0	1	54,918		55,830	912	1.66%
RX 330	0	2	2		63,201	63,201	0	0.00%
TOTAL NEW L-D TRUCKS	2	2	4	94,002	63,201	158,244	1,041	0.66%
TOTAL LEXUS	10	2	12	380,909	63,201	444,571	461	0.10%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
LINCOLN								
NEW AUTOS - POOL #1								
LS	4	1	5	141,686	32,138	170,590	(3,234)	(1.86)%
TOWN CAR	9	0	9	364,401		366,070	1,669	0.46%
TOTAL NEW AUTOS	13	1	14	506,087	32,138	536,660	(1,565)	(0.29)%
NEW LIGHT-DUTY TRUCKS - POOL #2								
AVIATOR	4	0	4	154,883		156,224	1,341	0.87%
NAVIGATOR	6	0	6	269,569		273,521	3,952	1.47%
TOTAL NEW L-D TRUCKS	10	0	10	424,452		429,745	5,293	1.25%
TOTAL LINCOLN	23	1	24	930,539	32,138	966,405	3,728	0.39%
MAZDA								
NEW AUTOS - POOL #1								
MAZDA 3	0	3	3		43,923	43,923	0	0.00%
MAZDA 6	2	0	2	36,553		36,981	428	1.17%
MX-5 MIATA	5	1	6	108,974	21,458	131,503	1,071	0.82%
PROTEGE	0	0	0				0	N/A%
PROTEGE 5	1	0	1	15,379		15,793	414	2.69%
RX-8	0	2	2		47,933	47,933	0	0.00%
TOTAL NEW AUTOS	8	6	14	160,906	113,314	276,133	1,913	0.70%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MPV	2	1	3	45,078	19,930	67,507	2,499	3.84%
TRIBUTE	6	0	6	122,201		125,105	2,904	2.38%
TRUCK	16	0	16	278,821		292,821	14,000	5.02%
TOTAL NEW L-D TRUCKS	24	1	25	446,100	19,930	485,433	19,403	4.16%
TOTAL MAZDA	32	7	39	607,006	133,244	761,566	21,316	2.88%
MERCEDES								
NEW AUTOS - POOL #1								
C CLASS	13	3	16	413,376	92,861	519,834	13,597	2.69%
CL CLASS	0	0	0				0	N/A%
CLK CLASS	3	3	6	153,311	177,398	332,755	2,046	0.62%
E CLASS	0	1	1		70,680	70,680	0	0.00%
S CLASS	0	0	0				0	N/A%
SL CLASS	0	0	0				0	N/A%
SLK CLASS	3	2	5	130,294	81,701	211,995	0	0.00%
TOTAL NEW AUTOS	19	9	28	696,981	422,640	1,135,264	15,643	1.40%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
NEW LIGHT-DUTY TRUCKS - POOL #2								
G CLASS	2	0	2	152,055		157,031	4,976	3.27%
M CLASS	1	0	1	42,176		42,548	372	0.88%
TOTAL NEW L-D TRUCKS	3	0	3	194,231		199,579	5,348	2.75%
TOTAL MERCEDES	22	9	31	891,212	422,640	1,334,843	20,991	1.60%
MERCURY								
NEW AUTOS - POOL #1								
GRAND MARQUIS	4	0	4	99,265		100,421	1,156	1.16%
MARAUDER	1	0	1	30,858		30,968	110	0.36%
SABLE	6	0	6	122,054		124,070	2,016	1.65%
TOTAL NEW AUTOS	11	0	11	252,177		255,459	3,282	1.30%
NEW LIGHT-DUTY TRUCKS - POOL #2								
MONTEREY	0	3	3		88,284	88,284	0	0.00%
MOUNTAINEER	12	0	12	360,387		368,841	8,454	2.35%
TOTAL NEW L-D TRUCKS	12	3	15	360,387	88,284	457,125	8,454	1.88%
TOTAL MERCURY	23	3	26	612,564	88,284	712,584	11,736	1.67%
MINI								
NEW AUTOS - POOL #1								
COOPER	2	0	2	32,434		32,474	40	0.12%
TOTAL NEW AUTOS	2	0	2	32,434		32,474	40	0.12%
TOTAL MINI	2	0	2	32,434		32,474	40	0.12%
MITSUBISHI								
NEW AUTOS - POOL #1								
DIAMANTE	0	0	0				0	N/A%
ECLIPSE	14	0	14	306,387		310,789	4,402	1.44%
GALANT	1	4	5	19,642	77,819	97,590	129	0.13%
LANCER	5	5	10	72,380	94,970	166,608	(742)	(0.44)%
TOTAL NEW AUTOS	20	9	29	398,409	172,789	574,987	3,789	0.66%
NEW LIGHT-DUTY TRUCKS - POOL #2								
ENDEAVOR	0	6	6		163,164	163,164	0	0.00%
MONTERO	0	0	0				0	N/A%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
MONTERO SPORT	4	0	4	94,157		94,157	0	0.00%
OUTLANDER	4	0	4	71,965		74,572	2,607	3.62%
TOTAL NEW L-D TRUCKS	8	6	14	166,122	163,164	331,893	2,607	0.79%
TOTAL MITSUBISHI	28	15	43	564,531	335,953	906,880	6,396	0.71%
NISSAN								
NEW AUTOS - POOL #1								
350Z	7	4	11	193,233	131,399	328,624	3,992	1.23%
ALTIMA	7	5	12	129,524	90,320	223,182	3,338	1.52%
MAXIMA	0	3	3		75,985	75,985	0	0.00%
SENTRA	12	2	14	161,311	31,436	196,534	3,787	1.96%
TOTAL NEW AUTOS	26	14	40	484,068	329,140	824,325	11,117	1.37%
NEW LIGHT-DUTY TRUCKS - POOL #2								
FRONTIER PICKUP	26	0	26	497,462		515,278	17,816	3.58%
MURANO	8	0	8	212,596		216,842	4,246	2.00%
PATHFINDER	4	0	4	109,549		112,089	2,540	2.32%
PATHFINDER ARMADA	0	6	6		203,196	203,196	0	0.00%
QUEST	0	3	3		76,348	76,348	0	0.00%
TITAN	0	12	12		303,362	303,362	0	0.00%
XTERRA	9	0	9	195,129		194,665	(464)	(0.24)%
TOTAL NEW L-D TRUCKS	47	21	68	1,014,736	582,906	1,621,780	24,138	1.51%
TOTAL NISSAN	73	35	108	1,498,804	912,046	2,446,105	35,255	1.46%
OLDSMOBILE								
NEW AUTOS - POOL #1								
ALERO	8	0	8	149,069		152,114	3,045	2.04%
AURORA	1	0	1	31,385		31,773	388	1.24%
TOTAL NEW AUTOS	9	0	9	180,454		183,887	3,433	1.90%
NEW LIGHT-DUTY TRUCKS - POOL #2								
BRAVADA	2	0	2	61,214		62,662	1,448	2.37%
SILHOUETTE	5	0	5	147,718		148,904	1,186	0.80%
TOTAL NEW L-D TRUCKS	7	0	7	208,932		211,566	2,634	1.26%
TOTAL OLDSMOBILE	16	0	16	389,386		395,453	6,067	1.56%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
PONTIAC								
NEW AUTOS - POOL #1								
BONNEVILLE	3	0	3	81,613		82,702	1,089	1.33%
GRAND AM	7	0	7	131,801		134,748	2,947	2.24%
GRAND PRIX	0	3	3		65,221	65,221	0	0.00%
SUNFIRE	1	1	2	13,792	10,187	23,997	18	0.08%
VIBE	3	0	3	51,944		52,084	140	0.27%
TOTAL NEW AUTOS	14	4	18	279,150	75,408	358,752	4,194	1.18%
NEW LIGHT-DUTY TRUCKS - POOL #2								
AZTEK	2	0	2	40,297		41,074	777	1.93%
MONTANA	6	0	6	156,330		153,139	(3,191)	(2.04)%
TOTAL NEW L-D TRUCKS	8	0	8	196,627		194,213	(2,414)	(1.23)%
TOTAL PONTIAC	22	4	26	475,777	75,408	552,965	1,780	0.32%
PORSCHE								
NEW AUTOS - POOL #1								
911	0	0	0				0	N/A%
BOXSTER	0	0	0				0	N/A%
CARRERA	0	0	0				0	N/A%
TOTAL NEW AUTOS	0	0	0				0	N/A%
NEW LIGHT-DUTY TRUCKS - POOL #2								
CAYENNE	2	0	2	126,422		126,422	0	0.00%
TOTAL NEW L-D TRUCKS	2	0	2	126,422		126,422	0	0.00%
TOTAL PORSCHE	2	0	2	126,422		126,422	0	0.00%
SAAB								
NEW AUTOS - POOL #1								
9.3 SERIES	2	3	5	52,739	108,559	161,649	351	0.22%
9.5 SERIES	4	2	6	137,554	65,072	202,129	(497)	(0.25)%
TOTAL NEW AUTOS	6	5	11	190,293	173,631	363,778	(146)	(0.04)%
TOTAL SAAB	6	5	11	190,293	173,631	363,778	(146)	(0.04)%
SATURN								
NEW AUTOS - POOL #1								
ION 1	2	0	2	22,333		20,419	(1,914)	(8.57)%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
ION 2	2	2	4	26,053	27,515	54,008	440	0.82%
ION 3	2	2	4	28,843	30,305	59,634	486	0.82%
L300	0	6	6		116,178	116,178	0	0.00%
TOTAL NEW AUTOS	6	10	16	77,229	173,998	250,239	(988)	(0.39)%
NEW LIGHT-DUTY TRUCKS - POOL #2								
VUE	5	0	5	90,612		94,121	3,509	3.87%
TOTAL NEW L-D TRUCKS	5	0	5	90,612		94,121	3,509	3.87%
TOTAL SATURN	11	10	21	167,841	173,998	344,360	2,521	0.74%
SCION								
NEW AUTOS - POOL #1								
XA	0	2	2		24,470	24,470	0	0.00%
XB	0	2	2		26,750	26,750	0	0.00%
TOTAL NEW AUTOS	0	4	4		51,220	51,220	0	0.00%
TOTAL SCION	0	4	4		51,220	51,220	0	0.00%
SUBARU								
NEW AUTOS - POOL #1								
IMPREZA	12	2	14	239,586	57,160	302,518	5,772	1.95%
LEGACY	21	1	22	468,623	24,555	501,258	8,080	1.64%
TOTAL NEW AUTOS	33	3	36	708,209	81,715	803,776	13,852	1.75%
NEW LIGHT-DUTY TRUCKS - POOL #2								
BAJA	0	5	5		107,371	107,371	0	0.00%
FORESTER	7	3	10	147,586	71,327	220,949	2,036	0.93%
TOTAL NEW L-D TRUCKS	7	8	15	147,586	178,698	328,320	2,036	0.62%
TOTAL SUBARU	40	11	51	855,795	260,413	1,132,096	15,888	1.42%
SUZUKI								
NEW AUTOS - POOL #1								
AERIO	14	0	14	203,420		206,964	3,544	1.74%
FORENZA	0	5	5		65,325	65,325	0	0.00%
VERONA	0	4	4		68,635	68,635	0	0.00%
TOTAL NEW AUTOS	14	9	23	203,420	133,960	340,924	3,544	1.05%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
NEW LIGHT-DUTY TRUCKS - POOL #2								
GRAND VITARA	4	2	6	70,652	39,760	110,256	(156)	(0.14)%
VITARA	4	4	8	65,068	67,300	132,720	352	0.27%
XL-7	10	0	10	206,490		216,096	9,606	4.65%
TOTAL NEW L-D TRUCKS	18	6	24	342,210	107,060	459,072	9,802	2.18%
TOTAL SUZUKI	32	15	47	545,630	241,020	799,996	13,346	1.70%
TOYOTA								
NEW AUTOS - POOL #1								
AVALON	4	0	4	100,154		100,686	532	0.53%
CAMRY	8	0	8	154,939		153,953	(986)	(0.64)%
CAMRY SOLARA	0	8	8		157,052	157,052	0	0.00%
CELICA	4	4	8	72,218	78,064	150,584	302	0.20%
COROLLA	6	0	6	80,124		80,488	364	0.45%
ECHO	4	0	4	40,659		41,016	357	0.88%
MATRIX	7	0	7	107,372		107,372	0	0.00%
MR2 SPYDER	2	0	2	45,373		45,509	136	0.30%
PRIUS	0	1	1		18,411	18,411	0	0.00%
TOTAL NEW AUTOS	35	13	48	600,839	253,527	855,071	705	0.08%
NEW LIGHT-DUTY TRUCKS - POOL #2								
4RUNNER	12	0	12	336,167		336,602	435	0.13%
HIGHLANDER	6	5	11	143,874	124,297	268,865	694	0.26%
LAND CRUISER	1	0	1	46,729		47,446	717	1.53%
RAV4	0	4	4		71,942	71,942	0	0.00%
SEQUOIA	4	0	4	133,724		134,967	1,243	0.93%
SIENNA	0	9	9		227,465	227,465	0	0.00%
TACOMA PICKUP	17	0	17	268,550		272,124	3,574	1.33%
TUNDRA	15	0	15	332,064		333,473	1,409	0.42%
TOTAL NEW L-D TRUCKS	55	18	73	1,261,108	423,704	1,692,884	8,072	0.48%
TOTAL TOYOTA	90	31	121	1,861,947	677,231	2,547,955	8,777	0.35%
VOLKSWAGEN								
NEW AUTOS - POOL #1								
GOLF	10	0	10	161,093		165,672	4,579	2.84%
GTI	3	0	3	55,815		56,399	584	1.05%
JETTA	23	4	27	421,509	69,192	502,683	11,982	2.44%
NEW BEETLE	17	0	17	322,753		333,546	10,793	3.34%
PASSAT	18	0	18	477,530		492,222	14,692	3.08%
TOTAL NEW AUTOS	71	4	75	1,438,700	69,192	1,550,522	42,630	2.83%

INFLATION ESTIMATE REPORT BY MAKE/MODEL/POOL
DEALER COST FOR THE YEAR ENDED 12/31/03
NEW ITEMS AT CURRENT COST - I.E., NO INFLATION

BODY STYLE	CONT. ITEMS	NEW ITEMS	TOTAL ITEMS	12/01/02 PRICE	NEW ITEMS	ENDING PRICE	DOLLAR CHANGE	PERCENT CHANGE
NEW LIGHT-DUTY TRUCKS - POOL #2								
EUROVAN	0	0	0				0	N/A%
TOUAREG	0	3	3		109,746	109,746	0	0.00%
TOTAL NEW L-D TRUCKS	0	3	3		109,746	109,746	0	0.00%
TOTAL VOLKSWAGEN	71	7	78	1,438,700	178,938	1,660,268	42,630	2.64%
VOLVO								
NEW AUTOS - POOL #1								
40 SERIES	2	2	4	45,872	55,234	102,674	1,568	1.55%
60 SERIES	3	2	5	85,886	62,920	149,157	351	0.24%
70 SERIES	6	2	8	205,367	66,373	267,172	(4,568)	(1.68)%
80 SERIES	2	3	5	75,565	114,030	190,775	1,180	0.62%
TOTAL NEW AUTOS	13	9	22	412,690	298,557	709,778	(1,469)	(0.21)%
NEW LIGHT-DUTY TRUCKS - POOL #2								
90 SERIES	2	1	3	68,925	31,349	102,630	2,356	2.35%
TOTAL NEW L-D TRUCKS	2	1	3	68,925	31,349	102,630	2,356	2.35%
TOTAL VOLVO	15	10	25	481,615	329,906	812,408	887	0.11%

The *De Filipps' LIFO Lookout* newsletter is a quarterly publication of LIFO News, Views and Ideas by Willard J. De Filipps, CPA, P.C., 317 West Prospect Avenue, Mt. Prospect, IL 60056. It is intended to provide accurate, general information on LIFO matters and it should not be construed as offering accounting or legal advice or accounting or legal opinion on any specific facts or circumstances. The contents are intended for general information purposes only. Readers should consult their certified public accountant, attorney and/or other competent advisors to discuss their own situations and specific LIFO questions. Mechanical or electronic reproduction or photocopying is prohibited without permission of the publisher. Annual subscription: $395. Back issues available for $70 each. Not assignable without consent. Any quoted material must be attributed to *De Filipps LIFO Lookout* published by Willard J. De Filipps, CPA, P.C. Editorial comments and article suggestions are welcome and should be directed to Willard J. De Filipps at (847) 577-3977; FAX (847) 577-1073. **INTERNET**: http://www.defilipps.com. © Copyright 2003 Willard J. De Filipps.
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De Filipps' LIFO LOOKOUT
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317 West Prospect Avenue
Mt. Prospect, IL 60056

First-class postage paid at Mt. Prospect, IL