



## 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. IRS TAM ON COST CAP FOR DEALERS WILL IMPACT DEALERS' LIFO CALCULATIONS.

The inventory cost capitalization rules in Section 263A apply to all taxpayers with average annual gross receipts of \$10 million or more. On September 7, 2007, the IRS released a Technical Advice Memorandum in which it set forth several controversial interpretations relating to how these cost capitalization rules should be applied to the fairly complex service, repair and body shop operations of an automobile dealership.

This quarter's issue of the *Dealer Tax Watch* was devoted to an analysis of TAM 200736026, and it included *Can Your Dealership Get a Better Cost Cap Result?* as a *Practice Guide*.

Many auto dealers are looking at massive potential Section 481(a) adjustments ... hundreds of thousands of dollars ... as the IRS' interpretations in this TAM are being applied to dealerships across the country. What's more ... there are several very important issues relating to how automobile dealers using the LIFO method to value their inventories will be affected.

Unfortunately, the IRS did not address these LIFO implications. And, some of them remain to be more fully developed and could require restatement of the historical LIFO cost layers that make up a dealership's LIFO reserves. We will be reporting on these LIFO implications in a subsequent issue of the *Lookout*.

### #2. REBASING LIFO INDEXES TO 1.000 AFTER CHANGES IN LIFO METHODS.

To the extent that you are involved with LIFO elections over any extended period of time, you are likely to encounter situations where it is necessary to rebase the LIFO indexes to 1.000 after a change in LIFO method has been made.

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Sometimes this rebasing is necessary in connection with "automatic" changes in LIFO methods; sometimes it is required in connection with the LIFO changes that require advance approval from the IRS. In other cases, rebasing occurs after businesses merge and it is necessary to combine their LIFO pools.

Rebasing of LIFO indexes is an important, but sometimes misunderstood, process. For more information on this, see page 2.

### #3. THE DISADVANTAGE OF THE IPIC METHOD FOR AUTO DEALERS ... A CASE STUDY BASED ON OUR EXPERIENCE.

In our last issue of the *Lookout*, we took an in-depth look at the Inventory Price Index Computation (IPIC) LIFO Method. We examined many aspects of the IPIC method and the finer points of the various sub-elections that have to be considered.

We also specifically addressed the (potential) applicability of the IPIC LIFO method to auto dealerships' new vehicle inventories. In this context, our analysis in the June *Lookout* included several comparisons of the cumulative inflation results under the IPIC Method with the Alternative LIFO Method. Our comparisons in the June issue only took into

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