National Automobile Dealers Association
Office of Legislative Affairs
412 First Street, SE • Washington, DC 20003
1.800.563.1556 • 202.547.5500 • www.nada.org

April 14, 2015

The Honorable Orrin Hatch
Chairman, Finance Committee
United States Senate
Washington, DC 20510

The Honorable Ron Wyden
Ranking Member, Finance Committee
United States Senate
Washington, DC 20510

Re: Comments to Business Income Tax Working Group

Dear Chairman Hatch and Senator Wyden:

The National Automobile Dealers Association (NADA) appreciates the opportunity to provide its perspective on issues of importance to the automobile and truck dealer industry to the Senate Finance Committee's Business Income Tax Working Group. NADA represents nearly 17,000 franchised new car and truck dealers, employing more than one million Americans. NADA's member's sell all makes and models of vehicles, both domestic and international, including medium and heavy-duty trucks. Automobile dealers are a significant tax base for local communities, and the nation as a whole. In 2013, dealers provided $730.1 billion in sales, and $53.7 billion in payroll, as well as supporting other local businesses.

<u>The need for comprehensive tax reform</u>: NADA's diverse membership includes dealerships of all sizes, the majority of which are family-owned. NADA members operate in every congressional district in the country, and one-third of NADA's members sell fewer than 200 new vehicles per year. These dealers operate in a variety of entity forms, including sole proprietorships, partnerships, limited liability companies and subchapter S corporations, as well as some traditional subchapter C corporations. Therefore, NADA is concerned that tax reform should not be focused on a significant reduction in the corporate tax rate without providing, or at the expense of, any tax relief to entities that operate in non-corporate form and pay taxes at individual tax rates. These businesses, including many automobile dealerships, could lose the benefit of critical tax preferences (i.e., deductions, credits and exclusions) and gain none of the benefits of a lower corporate tax rate.

<u>LIFO and LCM</u>: A majority of automobile and truck dealerships use the LIFO (last-in, first-out) accounting method for new vehicles, used vehicles, and parts. For dealerships using LIFO accounting, preservation of the method is critical for inventory management as vehicles and parts increase in price over time. Previous tax reform proposals have recommended repeal of LIFO with the increase in income from LIFO reserves being taken into account ratably over a specific number of years. While the proposal offered by former Ways and Means Committee Chairman Dave Camp would repeal LIFO, it included a provision that provides that LIFO reserves of closely held businesses would be subject to a reduced tax rate of 7 percent to acknowledge the substantial effect repealing LIFO would have on cash flow for small and family-owned businesses. In addition, the LCM (lower of cost or market) accounting method is a related accounting practice that is primarily used by dealerships for used vehicles. Because the value of

used inventory can change rapidly based on market conditions, this is an important tool for dealers to account for the actual value of these vehicles. Repeal of the LIFO and LCM accounting methods, as suggested in previous tax reform proposals, would force dealerships to report an artificially increased tax liability, which would have a devastating impact on them and their employees, as the increased tax burden would threaten the continued viability of many dealerships.

Small Business Expensing and Bonus Depreciation: Section 179 small business expensing and bonus depreciation affect the investment decisions of many dealerships and small businesses. Having the ability to deduct the cost of qualified investments in the year that it is purchased, rather than being forced to depreciate the cost of the investment over time encourages dealerships to reinvest in their businesses. Both provisions fuel expansion, growth and jobs in local communities and across the country. The uncertainty of not knowing if small business expensing or bonus depreciation will be extended or for what period of time causes investment decisions to be postponed or eliminated entirely. NADA supports the permanent expansion of these provisions through tax reform to provide automobile and heavy-duty truck dealers the certainty needed to reinvest in their dealerships and to continue to create jobs and economic opportunity for their local communities.

Depreciation: Earlier proposals to replace the Modified Accelerated Cost Recovery System (MACRS) and Alternative Depreciation System (ADS) rules would effectively extend the depreciation period for all automobile and heavy-duty truck dealership assets. Such extended periods will negatively impact dealer cash flow and reduce the capital that dealers have available to operate and reinvest in their businesses. Also as previously proposed, treating all gain from the disposition of dealership assets as ordinary income would further negatively impact dealers resulting in less available capital to reinvest in their dealerships.

Amortization of Intangibles: The earlier Cost Recovery and Tax Accounting Reform Discussion Draft proposed increasing the amortization period for Section 197 intangible assets from 15 to 20 years. Under a transition rule, the extended 20-year amortization period would apply to intangible assets placed in service prior to the enactment of the provision. Sales of automobile and heavy-duty truck dealerships frequently involve a significant goodwill component (commonly referred to in the industry as "blue sky") such that the purchaser of a dealership is dependent on the 15-year amortization of such goodwill in order to finance the cash flow of the post-acquisition operations of the dealership. Extending the amortization period to 20 years will, therefore, make many dealership transactions uneconomic. To the extent that the working group is considering changes to existing cost recovery and/or tax accounting mechanisms in the Code that are not taxpayer favorable, we strongly urge the working group to consider making such changes in a manner that they are prospective only and do not immediately impose a retroactive tax increase on taxpayers with respect to prior investments in property, inventory or other assets.

Advertising Expenses: The Cost Recovery and Tax Accounting Reform Discussion Draft proposed allowing taxpayers to continue to currently deduct 50% of their advertising expenses in the year paid or incurred but would require that the remaining 50% of their advertising expenses be capitalized and amortized over a five-year period. Advertising has been an ordinary and necessary business expense just like salaries, rent and utilities for more than 100 years. It is an essential component of an automobile dealer's operations and its current deductibility is essential to the proper calculation of such dealer's net income tax liability. Current deductibility is particularly appropriate given that automobile dealer advertising is limited almost exclusively to the marketing of short-term sales (generally coinciding with a particular holiday or date) and other promotions of a limited duration.

Like-Kind Exchange Rules: The earlier Cost Recovery Accounting Reform proposal would repeal the well-established like-kind exchange rules. The like-kind exchange mechanism is frequently used in connection with the tax-efficient transfer of dealership real estate and franchise rights, which allows dealers to maintain their capital investment in dealership assets when relocating and/or becoming associated with a different franchise. Furthermore, the like-kind exchange mechanism is an integral part of a vehicle dealer's ongoing operations (particularly heavy-duty truck dealers) as it allows them to maintain their capital investment in inventory, particularly with respect to lease and rental fleets. Thus, the repeal of like-kind exchange would reduce the availability and affordability of vehicles to the general public.

Heavy-Duty Truck Excise Tax: Congress imposes a 12 percent federal excise tax (FET) on most new heavy-duty trucks. As a way to raise revenue for the depleted Highway Trust Fund, proposals have been made to increase the FET. An increase in the FET would depress new heavy-duty truck sales and delay the deployment of cleaner, safer, and more fuel economical trucks. Congress should oppose an FET increase, and instead consider lowering or eliminating the tax to address its detrimental impact on the environment and the trucking industry.

* * * * *

NADA appreciates the opportunity to comment on tax issues of importance to America's franchised new automobile dealers. If you have further questions, please have your staff contact Kathy Mason, our Director of Legislative Affairs at 202 547-5500 or kmason@nada.org.

Respectfully submitted,

Ivette E. Rivera
Vice President of Legislative Affairs

cc: The Honorable John Thune
The Honorable Benjamin Cardin