

## Temporary, Targeted Relief Necessary to Avoid Unexpected LIFO Recapture Resulting From Global Interruption of Vehicle Production

### Issue

Government actions to contain the pandemic slowed or stopped production at motor vehicle assembly plants and suppliers across the globe, creating a major foreign trade interruption in the U.S. vehicle industry. Also, this foreign trade interruption severely upended the vehicle industry's supply of critical semiconductor chips, further reducing production. This precipitous decline in production has prevented franchised new-car and -truck dealerships from replenishing inventory. As a result, dealers using the last-in, first-out (LIFO) accounting method cannot acquire sufficient inventory to avoid additional taxable income and unexpected tax liability triggered by LIFO recapture.

[Congress has provided Treasury](#) the authority to grant a pending petition that would allow LIFO relief for dealers because actions in response to the pandemic triggered a "major foreign trade interruption" that makes inventory replacement difficult. *Members of Congress should urge Treasury to grant temporary LIFO relief for businesses facing difficulty replacing inventories due to government and other actions that created a major global interruption of vehicle production.*

### Background

New car and truck dealers cannot replace inventory due to actions to contain the pandemic which precipitated a foreign trade interruption. To reduce LIFO recapture, by the end of the tax year (December 31 for most dealer taxpayers) dealers generally restock inventory approximately equal to the cost of inventory at the start of the year, because shortfalls can be taxed as ordinary income.

NADA [petitioned](#) the Treasury Department last November to exercise authority under [Section 473](#) of the Internal Revenue Code to allow taxpayers to make an election to replace their new-vehicle inventories over a three-year period. Treasury can grant this relief when a "major foreign trade interruption" makes inventory replacement difficult, and the election would allow dealers to restock as factory production normalizes.

Since the petition was submitted, vehicle inventory constraints have worsened, compounded by the persistent semiconductor shortage further curbing factory production. And most dealers on LIFO will be powerless to replenish inventories sufficiently by year's end.

### Key Points

- Government and other actions to contain the pandemic triggered a major foreign trade interruption that caused unprecedented and completely unforeseen shortfalls in new-vehicle inventories for franchised dealers, rendering inventory replenishment difficult in 2020 and significantly worse in 2021. Some dealers have reported inventory drops exceeding 90%.
- Due to circumstances beyond dealers' control, LIFO recapture will trigger significant, unexpected tax liability, reducing cash flow and stripping much needed working capital from many small business family dealerships as they continue to be hit by inventory shortages.
- Treasury should exercise the authority Congress granted under Section 473 of the Internal Revenue Code to address such unforeseen circumstances caused by responses to the global pandemic.

### Status

[NADA recently met with the Treasury Department](#), but the Department has not responded formally to NADA's November 2020 petition. The [LIFO Coalition also sent a petition](#) in February seeking temporary LIFO relief. In [April](#) and [August](#) the trade association representing accountants (AICPA) submitted similar petitions to Treasury.