

# 2021 Machinery & Equipment Dealer

## LIFO Case Study

### Use of IPIC Method to Increase Tax Savings



# LIFOPro

Software & Turnkey Outsourcing Solutions

LIFO-PRO, Inc.

11620 Arbor St, Suite 100

Omaha, NE 68144

(402) 330-8573 office

(877) 848-6583 fax

[lifopro@lifopro.com](mailto:lifopro@lifopro.com)

[www.lifopro.com](http://www.lifopro.com)

# Table of Contents

Section	Slide(s)
Overview	3
2021 Tax Savings Opportunities	4
Machinery & Equipment BLS PPI Inflation	5 - 6
2021 After-tax Cash Savings Comparison	7
Other Considerations	8
Turnkey Outsourcing Solutions	9
Complimentary Tax Savings Analysis	10



# Machinery & Equipment Dealer LIFO Overview

- Many machinery & equipment dealers use LIFO because of the consistent long-term historical inflation
- Majority of machinery & equipment dealers on LIFO have use external indexes & Bureau of Labor Statistics Producer Price Indexes (BLS PPI), which is also known as the IPIC method
- IPIC method most predominantly used because it has historically provided much higher after-tax cash savings compared to the use of an internal index method which relies on actual current & prior/base year item costs to calculate inflation
- Many dealerships have what is referred to as a limited or selective LIFO election, which infers that less than 100% of goods are valued under LIFO
- Reasons for having limited LIFO election are as follows:
  - Minimal or negative tax savings from having used equipment & parts on LIFO if using internal indexes
  - Taxpayers are required to value inventories on LIFO at cost & are therefore not allowed to maintain LCM reserves on used equipment if they're on LIFO
  - Many dealerships also maintain lower of cost or market reserves for used equipment, which provides a form of tax savings since it reduces ending inventory balances, increases costs of goods sold & reduces taxable income
  - Some dealers leave used equipment off LIFO because they perceive the tax savings of maintaining LCM reserve on these goods to be greater than the tax savings of having these goods on LIFO

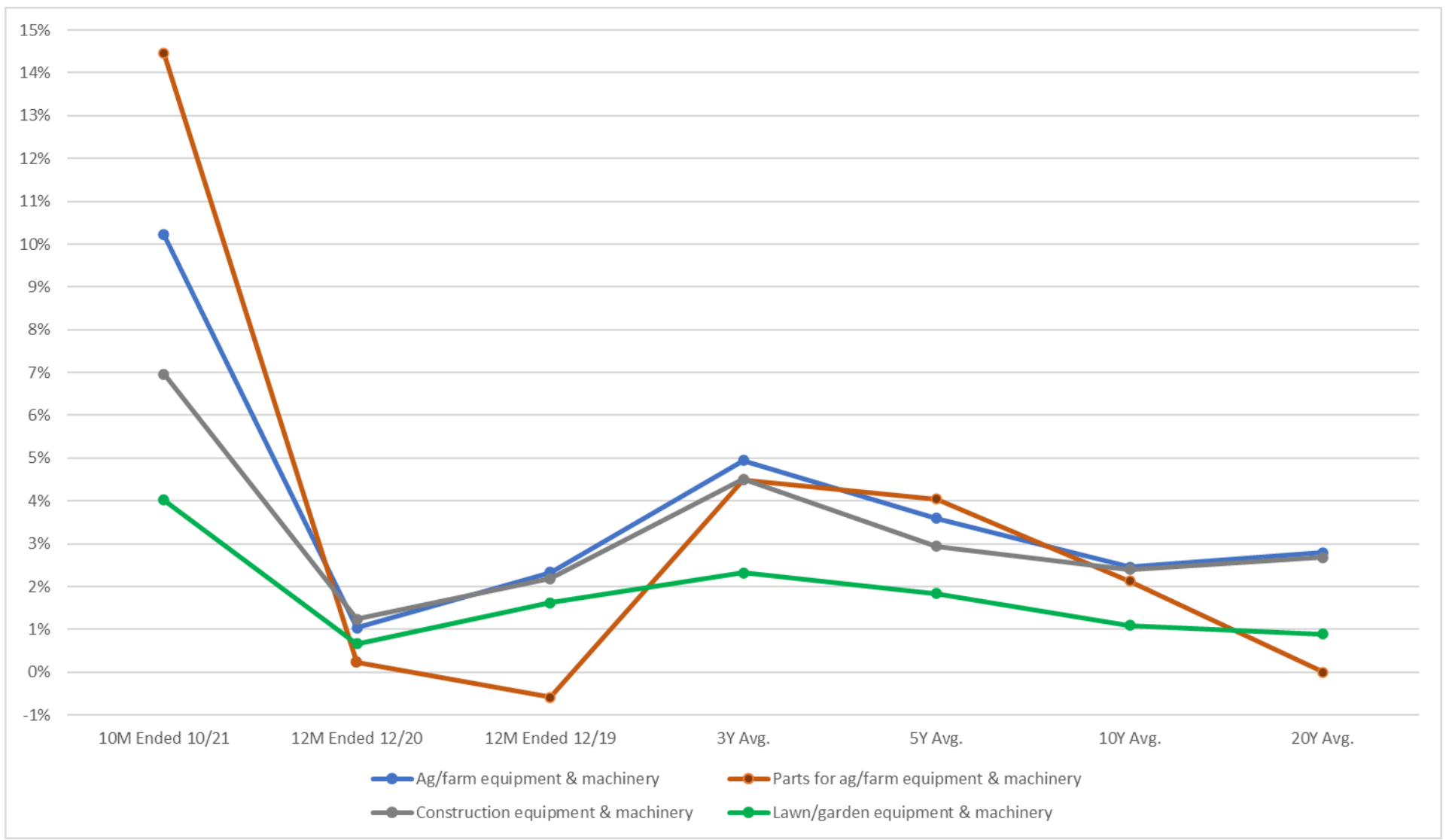


# 2021 Tax Savings Opportunities

- 2021 year to date IPIC PPI inflation for machinery & equipment are as follows (10M ended Oct. '21)
  - Ag/farm equipment & machinery: 10%
  - Ag/farm equipment parts: 15%
  - Construction equipment & machinery: 7%
  - Lawn/garden equipment & machinery: 4%
- Year to date averages are far above the historical averages for all machinery & equipment categories (see next slide)
- **Dealers on LIFO:**
  - Could substantially increase 2021 tax savings from LIFO by switching to IPIC PPI if they're currently using internal indexes or price book/list
  - Dealers with only new equipment on LIFO could capture even more 2021 tax savings by both switching to IPIC PPI & expanding LIFO election scope to include used equipment and/or parts
- **Dealers not on LIFO:**
  - Unprecedented inflation provides ideal opportunity for dealers not already on LIFO to elect for the 2021 year end
  - Tax savings from LIFO begins accruing in the year of election, meaning these benefits would be reported on 2021 year end tax return
  - 2021 tax savings from LIFO can not be retroactively recaptured by electing LIFO in a later period
  - LIFO should be elected in a period of inflation, and companies considering electing LIFO risk forfeiting substantial tax savings by opting not to elect in 2021



# Machinery & Equipment Dealer BLS PPI Inflation



Source: Bureau of Labor Statistics Table 9 Producer Price Indexes, Seasonally Unadjusted.



# BLS PPI Historical Average Annual Inflation Rates

PPI Code	1114	111409	112	1266
BLS Category Description / Inflation Measurement Period	Agricultural machinery and equipment	Parts for farm machinery, for sale separately	Construction machinery and equipment	Lawn/garden equipment
YTD '21 (10M Ended Oct. '21)	10.2%	14.5%	7.0%	4.0%
12 Months Ended Dec. '20	8.6%	13.8%	5.3%	3.5%
12 Months Ended Dec '19	10.2%	14.5%	7.0%	4.0%
12 Months Ended Dec '18	1.0%	0.2%	1.2%	0.7%
12 Months Ended Dec '17	2.4%	-0.6%	2.2%	1.6%
12 Months Ended Dec '16	3.5%	6.6%	3.4%	2.7%
12 Months Ended Dec '15	0.7%	0.2%	0.9%	0.1%
12 Months Ended Dec '14	1.2%	1.7%	1.0%	0.3%
12 Months Ended Dec '13	1.0%	-2.8%	0.9%	0.3%
12 Months Ended Dec '12	1.2%	1.7%	1.9%	0.8%
12 Months Ended Dec '11	1.7%	-1.2%	1.2%	-0.2%
12 Months Ended Dec '10	0.9%	1.0%	3.8%	0.6%
12 Months Ended Dec '09	3.3%	7.0%	4.3%	-0.1%
12 Months Ended Dec '08	2.3%	3.6%	0.7%	0.1%
12 Months Ended Dec '07	1.9%	0.3%	0.5%	-0.4%
12 Months Ended Dec '06	6.6%	0.1%	5.3%	4.2%
12 Months Ended Dec '05	2.6%	6.0%	2.4%	0.0%
12 Months Ended Dec '04	2.4%	0.1%	3.2%	2.1%
12 Months Ended Dec '03	3.3%	4.6%	5.0%	-1.4%
12 Months Ended Dec '02	5.5%	4.7%	6.0%	1.3%
<b>3 Year Annual Average</b>	<b>4.9%</b>	<b>4.5%</b>	<b>4.5%</b>	<b>2.3%</b>
<b>5 Year Annual Average</b>	<b>3.6%</b>	<b>4.0%</b>	<b>2.9%</b>	<b>1.8%</b>
<b>10 Year Annual Average</b>	<b>2.4%</b>	<b>2.1%</b>	<b>2.4%</b>	<b>1.1%</b>
<b>20 Year Annual Average</b>	<b>2.8%</b>	<b>3.8%</b>	<b>2.7%</b>	<b>0.9%</b>
<b>Years with Inflation: '02 - '21</b>	<b>20 of 20</b>	<b>17 of 20</b>	<b>20 of 20</b>	<b>15 of 20</b>



# 2021 After-tax Cash Savings Comparison

## Inventory & Inflation Summary

Sample Machinery & Equipment Dealer 2021 Year End Inventory Summary				
Description	IPIC PPI Inflation	Inventory Balances at Cost		
		New Equipment	Used Equipment	All Goods
Ag/farm equipment & machinery	10.2%	\$10,000,000	\$4,444,444	\$14,444,444
Construction equipment & machinery	5.3%	\$750,000	\$333,333	\$1,083,333
Lawn/garden equipment & machinery	3.5%	\$500,000	\$222,222	\$722,222
Parts	13.8%	\$3,750,000	-	\$3,750,000
<b>Totals/Averages</b>	<b>9.5%</b>	<b>\$15,000,000</b>	<b>\$5,000,000</b>	<b>\$20,000,000</b>

## LIFO Calculation Summary

Description	New Equipment & Parts	Used Equipment Only	All Goods
2021 Inventory balance at cost	\$15,000,000	\$5,000,000	\$20,000,000
2021 Weighted Average Inflation Rate	10.9%	9.7%	10.6%
2021 LIFO Expense	\$1,629,390	\$485,770	\$2,115,160
2021 Tax Rate	40%	40%	40%
<b>2021 After-tax Cash Savings from LIFO</b>	<b>\$651,756</b>	<b>\$194,308</b>	<b>\$846,064</b>

### Notes

Above inflation rates use YTD PPI inflation for the 9M ended Sep. '21.

Above amounts are estimates. LIFO expense shown above uses current year inventory balance at cost multiplied by current year inflation rate.

Above example ignores layer erosion component of LIFO expense calculation that results when there are decreases in current vs. prior period inventory balances.



# Other Considerations

- IRS Form 3115 must be filed by return extended filing deadline to switch to IPIC method, but the switch is an automatic approval change
- Change is made prospectively on a cutoff basis, meaning prior year end LIFO reserve remains intact
- Must wait five years to switch back to alternative LIFO method
- Any preexisting lower-of-cost or market (LCM) reserves associated with used equipment inventories must be restored into income over a three year period beginning in the year of change if LIFO scope expansion is made to include used equipment
- LIFOPro offers turnkey outsourcing solutions to manage all aspects of your company's LIFO calculation, including:
  - Year end LIFO calculation & 3 interim estimates
  - LIFOPro PDF report package providing comprehensive calculation documentation
  - IRS LIFO election forms and/or IRS Form 3115 Change in Accounting Method preparation
- Estimated turnkey outsourcing solutions fee estimates are as follows:
  - First year, including IRS Form 3115/970 preparation: \$2,500 - \$5,000
  - Recurring annual service fee (optional): \$1,000 - \$3,000



Call us at 402-330-8573 Monday – Friday 8AM – 5PM CST  
Email us at [lifopro@lifopro.com](mailto:lifopro@lifopro.com)



# Turnkey Outsourcing Solutions

- LIFOPro offers turnkey outsourcing solutions to manage all aspects of your company's LIFO calculation, including:
  - Year end LIFO calculation & 3 interim estimates
  - LIFOPro PDF report package providing comprehensive calculation documentation
  - IRS Forms preparation, including:
    - IRS Form 970 Application to Use LIFO Method (for companies electing LIFO)
    - IRS Form 970/3115 Change in Accounting Method (for companies already on LIFO switching to IPIC CPI from ALM; both Forms 970 & 3115 are required to be filed & attached to 2021 year end tax return)
- Estimated turnkey outsourcing solutions fee estimates are as follows:
  - First year, including IRS Form 3115/970 preparation: \$2,000 - \$5,000
  - Recurring annual service fee (optional): \$1,000 - \$3,000



Call us at 402-330-8573 Monday – Friday 8AM – 5PM CST  
Email us at [lifopro@lifopro.com](mailto:lifopro@lifopro.com)

# Complimentary Tax Savings Analysis

- LIFOPro offers complimentary pro forma IPIC LIFO Benefit Analysis Report using your company's actual product mix to quantify the 2021 IPIC PPI tax savings
- For companies considering electing LIFO, report includes How LIFO Works Appendix & includes details on the practical application of LIFO for first-time users
- Only need a breakdown of current & prior inventories at cost by the following groups:
  - New ag/farm equipment & machinery
  - New construction equipment & machinery
  - New lawn/garden equipment & machinery
  - Parts
- Request your complimentary IPIC LIFO Benefit Analysis Report using one of the following methods:
  - Complete questionnaire online: [Machinery & Equipment Dealer Pro Forma IPIC Analysis Questionnaire](#)
  - Download & email completed questionnaire PDF file & to LIFOPro:
    - Dealers on LIFO: [Machinery & Equipment Dealer IPIC LIFO Benefit Analysis Questionnaire](#)
    - Dealers not on LIFO: [Machinery & Equipment Dealer IPIC LIFO Election Benefit Analysis Questionnaire](#)
- Turnkey outsourcing solutions fee quote included with analysis report
- Recipients will receive complimentary analysis PDF report & fee quote via email within one week of questionnaire submittal



Call us at 402-330-8573 Monday – Friday 8AM – 5PM CST  
Email us at [lifopro@lifopro.com](mailto:lifopro@lifopro.com)