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DEFENDER

The National Association of Dealer Counsel Newsletter FEBRUARY 2018

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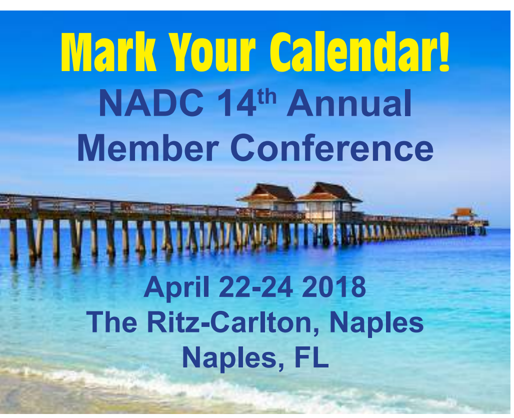

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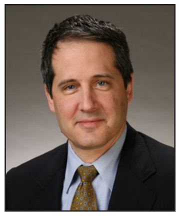
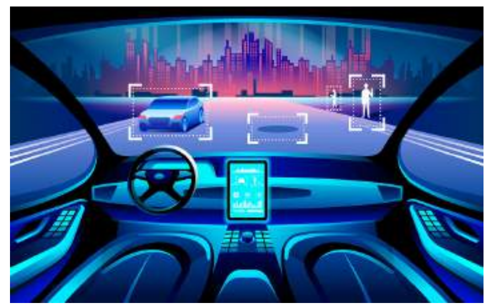


Dealerships in the Mobility Age

By Oren Tasini, Esq.
Haile, Shaw & Pfaffenberger, P.A.



The coming of autonomous vehicles is presaged by the technology that already exists in automobiles. This technology is growing daily and the race is on to see who will own the "tablets" that vehicles will become. Manufacturers are aware of the threat technology poses. Why else would GM have invested in $500 million in Lyft, or would Toyota and Uber have signed an agreement to cooperate on mobility services? But the challenge to be first is a difficult one. When competing with Google and Apple, you better bring your "A" game.

And how many of us believe the factory is going to create the ultimate customer experience? My wife's car requires a different 4-digit code to sync her Bluetooth than mine. There are too many calls and time wasted as a dealer fields calls from customers trying to decipher the inscrutable nature of blue tooth and NAV systems. The experience needs to be seamless, so it just happens, and customers say, "Wow, how did it do that?" and move on, enjoying the technology and their cars.

The example of PCs is instructive as to the first to market principle. Apple did this with the iPhone, creating a product that everyone wanted and still wants. Once third-party-owned software dominates the automotive space, the manufacturer will be weakened. Third parties may license their software to manufacturers or sell it directly to dealers as add-ons. In either case, the technology in a vehicle may create additional revenue streams for dealers, sold completely independently from the vehicles. That day is most likely still in the future, but the changes are already being felt.

But where do dealerships fit in? How can they be part of this mobility surge?

If you ask a dealer what his or her most important asset is, he or she will often mention "people" first. Next, the dealer will mention the brand. Perhaps the dealer will mention the real estate and then grumble about the monthly expense of rent, maintenance, and factory image upgrade costs. Inventory – the actual vehicles – is seldom mentioned. Inventory is just steel, glass, and rubber, burning money each minute it sits on the hot asphalt. As with any business, the faster inventory turns, the more money to the bottom line.

There is no doubt the OEMs want to be cutting edge. Technology is an opportunity to sell more cars by speeding up the sales process, which is infinitely too long. By the time a customer arrives at the dealership, he or she has made the buying decision. The only question is how long will it take. Dealerships should be able to initiate another conversation with a customer: Would you like to sign up for a "service" that makes your car a Wifi spot and syncs it to your phone and tablet and home? How about a software that will remind you of appointments as you drive and deliver texts to others automatically if you reschedule a meeting or, based on driving time due to traffic, you are going to be late. That software orders your groceries, too, so they will be waiting when you get to the store, or have them delivered the next day. It will turn on the lights in your wired home as you pull up the driveway.

Dealers, however, may be slow to offer such software-based services, because there are so many vendors out there. It is dizzying. I will admit it. I am an early adopter. I bought one of the first Betamax players because it was much "better" than VHS. I have spent way too much money and time paying for technology that quickly becomes obsolete. I no longer do so. Dealers wanting to avoid this expensive trap may be paralyzed by indecision. The manufacturers are unlikely to rise to this challenge by neither developing their own solution, nor providing uniform solutions across all brands.

Truth be told, if the OEMs are not the owners and providers of technology, this may benefit dealers. OEMs will be in a weaker position to demand image upgrades, CSI compliance, or the imposition of stairstep incentives, because they do not control the most important asset in its product – the technology. What Microsoft did with software is instructive. It made personal computers a hunk of circuit boards which were worthless without Microsoft products. It forced manufacturers of PCs to engage in a race to the bottom, competing on price alone.

Dealers are in a bind. They do not want to fight the last "war," investing money and the precious time of their employees in outmoded technology that is quickly out of date, or worse, fails to provide the promised solution. They also cannot wait to see who will provide the best technology and then invest in a proven solution. Faced with this choice, dealers will spend likely less, in unproven stopgap solutions. Facing constant change, it is the only prudent choice. ■

Oren Tasini has over 25 years' experience representing automotive retail dealerships. He assists his clients in all aspects of their legal compliance, with a particular focus on mergers and acquisitions. Oren will be presenting at the Spring NADC meeting on the impact of technology on automotive retailers.

The Top 10 List of Provisions Included in the 2017 Tax Reform

Feature Article

By Adam Neporadny, *Dixon Hughes Goodman LLP*

The last major tax reform legislation was passed in 1986. Since then, the tax rules – Internal Revenue Code amendments, regulations, procedural guidance, and court case law – have morphed into a complex system for taxpaying dealers. The recently signed bill is a significant modification to the existing system, and the consensus is clear. Most businesses expect their income tax expense to decrease, including dealerships.

Though there are many moving parts in the new tax law with the potential to affect businesses and individuals to varying degrees, this article highlights what we consider ten of the most significant changes for dealerships.

1 - Individual tax rates and corporate tax rates

The final bill settled on keeping the same number of individual tax brackets as in current existence, seven. However, the new tax law reduces individual income tax rates to 10, 12, 22, 24, 32, 35, and 37%, and raises the income levels subject to each tax rate. These rates apply to tax years beginning after December 31, 2017 and beginning before January 1, 2026, unless subsequently extended by future legislation. On the corporate side, the current graduated tax rate was removed in favor of a flat 21% rate for tax years beginning after December 31, 2017.

2 - Alternative minimum tax

The original goal was to completely repeal the alternative minimum tax (AMT) for both individuals and corporations. Unfortunately, while the final bill removed the proposed full repeal of AMT for individuals, it replaced it with an increased exemption from $86,200 to $109,400, and the phase out threshold increased from $164,100 to $1,000,000 for married filing join taxpayers. The exemption amount for single taxpayers increased from $55,400 to $70,300, and the phase out threshold increased from $123,500 to $500,000.

On the other hand, corporate AMT is fully repealed under the final bill for tax years beginning after December 31, 2017, which is beneficial to dealerships taxed as a C corporation. Any AMT tax credit carryforwards will offset the taxpayer's regular tax liability and is refundable, within limits, starting in 2019.

3 - Pass-through income deduction

Aligning with a reduced corporate tax rate, Congress provided pass-through entities with a deduction for a percentage of their taxable income. Starting in 2018, a deduction will be allowed for taxpayers who have "qualified business income" (QBI) from a partnership, S corporation, or sole proprietorship, subject to limitations. The 20% deduction is limited to the lesser of: (1) 20% of their pass through business income; or (2) the greater of: (a) 50% of the W-2 wages paid in the qualified trade or business, or (b) the sum of 25% of W-2 wages, plus 2.5% of the unadjusted basis of all qualified property. This deduction applies for tax years beginning after December 31, 2017 and beginning before January 1, 2026.

4 - Standard deduction, charitable contributions, and the Pease limitation

Personal exemptions are removed in the bill in favor of a higher standard deduction effective for tax years beginning after December 31, 2017 and beginning before January 1, 2026. The new standard deduction amounts will be $24,000 for married filing joint or surviving spouse, $18,000 for an unmarried individual with at least one qualifying child, and $12,000 for single filers. Charitable contributions – which, under old law, were limited to 50% of a taxpayer's AGI – will now be limited to 60% of AGI effective for tax years beginning after December 31, 2017 and beginning before January 1, 2026. The bill will also repeal the current 80% deduction for certain contributions to universities made in connection with athletic seating rights.

5 - State and local tax deduction

A very impactful change included in the final bill is the limiting of the deduction available for sales, income, or property taxes paid to state or local tax authority to $10,000 ($5,000 for a married taxpayer filing a separate return) for tax years beginning after December 31, 2017 and beginning before January 1, 2026. This limitation does not apply to any of the aforementioned taxes paid or accrued in connection with carrying on a trade or business.

The bill specifically includes a provision that disallows prepaying state or local income tax for a taxable year beginning after December 31, 2017. Any amount paid in a taxable year beginning before January 1, 2018 shall be treated as being paid on the last day of the tax year for which the tax applies.

6 - Depreciation changes

The bill includes a provision that allows for 100% expensing through bonus depreciation of certain business assets placed in service after

September 27, 2017 through December 31, 2022. The amount of bonus depreciation allowed is then phased down over four years as follows starting: 80% in 2023, 60% in 2024, 40% in 2025, and 20% in 2026. The requirement that the property be new was also removed and replaced with a requirement that the property simply be new to the taxpayer–an impactful distinction.

However, in order to preserve full deductibility of floorplan interest expense, dealers received a trade-off. The ability to exclude floor plan interest expense from the interest expense limitation (discussed below) also means that qualified property for bonus depreciation purposes now excludes any property used in a trade or business that had floor plan financing indebtedness not subject to the interest expense deduction limitation.

Nonetheless, the bill includes some additional changes that have the potential to benefit many dealers. For example, Section 179 expensing limits will be increased to $1,000,000, with the phase out threshold being increased to $2,500,000 with both thresholds subject to inflation increases for tax years beginning after December 31, 2017. Furthermore, the definition of qualified property is expanded to include improvements to roofs, heating, ventilation, and air-conditioning property, fire protection and alarm systems, and security systems made to nonresidential real property if placed in service after the date such real property was first placed in service.

7 - Interest expense deduction limitation

The bill also includes a provision that limits the deduction for interest expense incurred by a trade or business to the sum of business interest expense, interest income, 30% of the adjusted taxable income, and the floor plan financing interest expense of a taxpayer for the year. For tax years beginning before January 1, 2022, adjusted taxable income will be computed without regard to depreciation, amortization, or depletion expense. Adjusted taxable income is otherwise generally defined as a taxpayer's taxable income without regard to any income, gain, deduction, or loss not properly allocable to the trade or business, any business interest expense or business interest income, and any net operating loss.

Real property trades or businesses, including rental property activities that qualify as a trade or business, may elect out of the interest deduction limitation if that trade or business uses the alternative depreciation system, which generally results in longer, slower depreciation deductions. Any interest not deductible for any tax year shall be carried forward indefinitely, and treated as business interest paid or accrued in the succeeding tax year.

8 - S corporation conversion to C corporation

Regarding the reduced corporate rates, Congress anticipated the possibility of S corporations looking to convert to C corporations.

To simplify this conversion, an S corporation that qualifies as an eligible terminated S corporation that pays distributions during the post-termination period is treated as having paid such distributions proportionately from any remaining S corporation accumulated adjustment account and any accumulated earnings and profits of the new C corporation. An eligible terminated S corporation is one that revokes its S corporation election within two years of the bill's enactment date and has the same shareholders with identical ownership percentages as of the date of the bill's enactment.

9 - Like-kind exchanges

Under the new law, like-kind exchanges are limited to only exchanges involving real property that is not primarily held for sale. This new limitation applies to exchanges completed after December 31, 2017; however, a transition rule allows like-kind exchange treatment for any property disposed of in an exchange on or before December 31, 2017, or for any property received by a taxpayer in an exchange on or before the same date. This exception generally allows for like-kind exchanges already in process to still take advantage of the current like-kind exchange rules.

For dealers, this means that like-kind exchanges involving franchise rights are no longer available.

10 - Estate and gift taxes and generation-skipping transfer tax

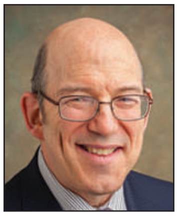
The law doubles the base estate and gift tax unified credit exclusion to $10 million, effective for decedents dying and gifts made after 2017 and before 2026. The bill also increases the GST exemption to $10 million. This effectively increases the inflation-adjusted exclusion and exemption amounts to $11.2 million ($22.4 million for a married couple) for 2018.

These increased exclusion and exemption amounts will provide planning opportunities for dealers looking to transition their estate in the coming years.

As there are far more elements to the tax reform than covered here, dealers may consider familiarizing themselves with the finer details of the changes. Looping in a trusted advisor and CPA is strongly recommended to ensure dealers are prepared for the oncoming effects – both favorable and complex – to their financial posture. ■

Adam Neporadny is a senior manager in the Birmingham office of Dixon Hughes Goodman LLP. He has more than 13 years of public accounting experience with a primary focus in the firm's national dealership practice. He provides a variety of tax and accounting services to dealership clients, including dealership tax compliance and planning services, and consulting and management advisory services.

President's Message



Andy Weill
Weill & Mazer
NADC President

PLEASE NOTE: OUT OF OFFICE
Executive Director Erin Murphy is out on maternity leave through April 2nd. Please contact Justine Coffey, Interim Executive Director, at jcoffey@dealercounsel.com or 202-868-4423 in Erin's absence.

Jim Collins famously wrote, "Good is the enemy of great." What he meant was that it can become tempting for an organization to become satisfied with its level of achievement and become unwilling to take the necessary steps to reach higher levels.

I have been mindful of Collins's point as we have been planning the April Conference along with the Planning Committee. Our conferences are one of our strong points, generating positive feedback, and are frequently cited as a primary member benefit. I remember my first attendance at an NADC Conference, and being amazed at the depth of knowledge, experience, and ability to effectively present information. I thought I would only be interested in a couple of topics; I found myself learning from every session, even in areas that did not have any apparent relationship to my practice.

I still feel that way about the conferences. At the same time, I feel the urge to hold up the old and comfortable ways for examination and see if there is room for improvement.

The starting point has been the feedback generated from you, the membership. Your comments and ideas matter. They are the first item on the agenda when the Planning Committee meets. We consider your points, especially when we see that several members raise similar issues. You also give us excellent ideas about topics, formats, scheduling, and much more. So, my first request is: keep doing it. For those of you who must run out the door at the end of the conference, please do not wait to the end; as an idea occurs to you, get it onto your feedback forms. Those ideas are often most clearly seen, and expressed, when fresh.

Our second step depends on you as well. We review proposals for presentations, and these come principally from members or member referrals. Perhaps you are not someone who wants to present, but you have heard a presentation at another venue that you think would be suitable for our membership. Let us know! There are a few people whom I have urged over the years to submit proposals, and it is very satisfying when one of those ends up turning into a quality presentation at our conference. While we have a wealth of excellent presenters who have appeared many times, it is essential to get fresh perspectives and different voices on the stage.

We also can use your input about presentation style. Are the panel presentations too crowded? Would you prefer more interaction with speakers? Are the slides effective? How valuable are materials to you when you take them home? We are willing to examine all of this.

I salute the hard work this Planning Committee and NADC staff have put into the Spring Conference process. And it is appropriate to note that we are standing on the shoulders of the excellent work of prior Planning Committees, speakers, and the support team. In my view, the best way to thank them is to continue to challenge ourselves to look at all aspects of our conferences and to be willing to question assumptions, be open to creative ideas, and make sure new voices get heard along with the old.

Please keep those feedback forms coming. Email me or other Board members with ideas or suggestions. Grab us for a few minutes at the conferences and let us know right then and there what thoughts you have. The Conferences are our most important product, and with all your input, attention, and energy, we will be solidly on another path, also encapsulated in a phrase by Collins: The Pursuit of Excellence. ■

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Volume XIV, Number 2
FEBRUARY 2018

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