Opinion

Eliminate Unnecessary Taxes

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With bonus depreciation having expired at the end of 2013, many trucking companies are staring down the barrel of some huge estimated income tax payments in 2014.

For years, bonus depreciation has provided trucking companies with significant tax relief because of the net operating loss, or NOL, environments that bonus depreciation helped them to generate. Without that option, coupled with an improving economy, trucking companies selling their fully depreciated used trucks will be generating taxable income they no longer will be able to offset with the purchase of new equipment.

Paying necessary taxes can be tough. Paying unnecessary taxes simply makes no sense.

Coupled with flat freight rates, a looming driver shortage and fluctuating fuel prices, this coming tax spike will only exacerbate an average fleet age already at historic heights.

What's more, the inability to replace aging fleets can trigger a host of expensive problems from maintenance and safety issues to difficulty recruiting and hiring the best drivers — who prefer newer and more modern equipment.

A daunting challenge for every CEO and chief financial officer is coming up with "extra" cash to purchase more efficient equipment more frequently. It may be time for trucking companies to revisit Internal Revenue Code Section 1031 — which might be termed the original "economic stimulus," with its narrow focus on reincesting cash in new equipment — for a refresher on the Like-Kind Exchange programs that have provided tax incentives for new equipment purchases since 1921.

A 1031 exchange program allows trucking companies to defer current taxable gain when assets — e.g., tractor-trailers — are sold and "like-kind" replacement assets purchases.

Consider the following example, which illustrates what happens when 100 trucks (purchased new for $120,000 each) are then sold used for $35,000 each:

	Without LKE	With LKE
Original equipment cost	$12,000,000	$12,000,000
Tax depreciation allowed	12,000,000	12,000,000
Tax basis at sale	0	0
Sales price of equipment	3,500,000	3,500,000
Gain on sale	3,500,000	3,500,000
Tax due on gain (40%)	1,400,000	0
Cash available for replacement equipment	2,100,000	3,500,000

With only 100 trucks, an LKE program would have provided $1.4 million "additional" dollars for the purchase of new tractors. The LKE program converted those tax dollars into extra cash to spend on new equipment. Trucking companies using LKEs are tapping into an interest-free source of capital to keep their businesses rolling. It is essentially a line of credit you control — and you decide when to pay back.

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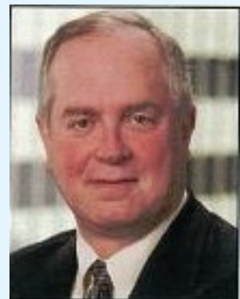
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The trucking industry is extremely competitive, and being able to reroute these deferred tax dollars back into the purchase of new tractors and trailers gives trucking companies a big advantage in remaining competitive.

However, while LKE programs certainly can enhance a company's cash flow, the importance of getting the details right cannot be overemphasized. IRS tax regulations stipulate that like-kind exchanges can be achieved only when the "form" of the LKE is accomplished pursuant to very detailed rules of administration. Adherence to these rules and regulations provides a company with a "safe harbor" that is acknowledged and honored by the IRS — if the exchange is done properly.

To that end, here are some important questions to ask yourself:

■ Do "trade-in" programs qualify for LKE treatment if cash is received from the dealer for trade-ins or the amount is held as a "credit" with the dealership for use in future purchases?

■ When do the regulations require a third party (i.e., a qualified intermediary) to hold proceeds and disburse funds?

■ Does the IRS really care if an LKE program does not follow the form of the regulations, as long as the trucking company eventually gets "like-kind" property in return for a trade and the right documents are filed with the trucking company's taxes?

■ Does "simultaneous" (i.e., same day) exchange negate the need for a qualified intermediary?

■ Can a truck dealer act as a qualified intermediary?

■ Do "multiple" exchanges require a master exchange agreement?

Consider exploring those questions and others with your tax advisers and a Qualified Intermediary's like-kind exchange program specialists. (A Qualified Intermediary is a professional provider of the mandatory mechanics of an exchange.) At a time when taxing authorities are looking under every rock for more revenue, extra care should be taken to ensure that exchanges are being done properly. "Business as usual" may not be acceptable for future audit scrutiny.

Over the years, Like-Kind Exchange programs have resulted in the deferral of tens of millions of dollars of taxable gains that have generated millions of dollars of additional cash flow that otherwise would not have been available.

Cash is king — period. Carriers with access to greater cash resources will have a distinct advantage in an already hypercompetitive trucking industry. If your company buys tractors and trailers and then sells them fully depreciated, you're going to pay 40% or more of those sales proceeds in income taxes. Wouldn't you rather keep that money and use it to buy new equipment?

Perhaps it's time for your company to identify unnecessary taxes that could be better invested in new equipment.

PricewaterhouseCoopers LLP, New York, and Accruit LLC, Denver, a personal-property Qualified Intermediary, are in a joint business relationship to provide trucking with integrated Like-Kind Exchange Program Services.