THE LIFO COALITION

1325 G Street N.W., Suite 1000, Washington, DC 20005   TEL: 202-872-0885

Fact Sheet on Last-in, First-out Inventory Accounting Method

Overview and Purpose of LIFO and FIFO inventory accounting:

1) To track product. A business always wants to have adequate inventory on hand to meet demand, whether manufacturing, distribution, or retail.

2) To track costs. A business must manage cash flow to maximize efficiencies. Since inventory items tend to be fungible, inventory conventions are a key part of tracking costs.

3) To determine income. The tax code requires taxpayers to use the best inventory accounting practice in the trade or business that most clearly reflects income. FIFO (First-in, First-out) is best suited to a business with falling prices. LIFO is best suited to a business with rising prices.

4) ***LIFO and FIFO achieve the same purpose: they most closely match the cost of goods sold with the cost of the replacement inventory the company must purchase in order to remain in business.***

5) Myth-buster: Tracking the flow of physical inventory and tracking costs are two different things. Both FIFO and LIFO track costs, not the flow of physical inventory.

6) Because hundreds of thousands of taxpayers use LIFO for these fundamental business and economic reasons, LIFO should remain in the tax code and not be repealed as part of any tax reform effort.

7) If LIFO were repealed, LIFO users would be uniquely and unfairly impacted compared to other taxpayers because they would face both an immediate, one-time retroactive tax increase from a punitive recapture tax and an ongoing, permanent tax increase from the loss of LIFO accounting in perpetuity.

LIFO is not a tax expenditure:

LIFO is a 78-year-old GAAP-approved inventory accounting system which does not meet the statutory definition of a tax expenditure. From its adoption in 1939 through 2008, LIFO was not included in the Joint Tax Committee list of tax expenditures, and is still not included on the Department of Treasury list of expenditures today. http://savelifo.org/wp-content/uploads/2017/06/LIFO-is-not-a-tax-expenditure.pdf.

LIFO repeal would slow the economy, cost jobs, and reduce revenue prospectively:

The economic dislocation that repeal of LIFO would cause would more than offset any new Federal revenue. A Tax Foundation study released in February, 2016, found that repeal of LIFO would reduce GDP by $116 billion per year, reduce federal revenue by $518 million annually, and cause the loss of as many as 50,300 jobs. *Click here for a Tax Foundation study on the impact of LIFO repeal: http://savelifo.org/wp-content/uploads/2016/02/TaxFoundation-FF501.pdf*

LIFO repeal would be uniquely and punitively retroactive:

LIFO repeal would require the retroactive recapture of all LIFO-related deductions that have been taken by LIFO taxpayers, sometimes over many decades. Under current law this recapture tax is paid only when the company reduces its inventory levels, experiences deflation, or goes out of business. To impose that tax in the absence of any of those triggering events would retroactively change the rules for LIFO taxpayers. For more on this click here: http://savelifo.org/pdf-2012/LIFO-Coalition-White-Paper-re-Retroactivity-Updated.pdf and here: http://savelifo.org/lifo-repeal-retroactivity-patrick-driessen-article-published-by-tax-analysts/

LIFO works the way it was intended to work:

LIFO is designed to react to price fluctuations. LIFO has a built in "toggle switch" that triggers tax when prices go down. For example: Crude oil has dropped in price in recent years, significantly reducing the LIFO reserves of oil and gas companies and bringing millions of dollars into current taxable income. Under current statute, the benefit from LIFO is recaptured when the taxpayer's inventory levels decline, prices fall, or the taxpayer goes out of business, in which case the taxpayer no longer needs tax treatment under LIFO.

LIFO is used by a wide cross-section of industries and not exclusively by large energy companies:

LIFO is used by more than a third of all U.S. companies, including hundreds of thousands of pass-through small and mid-sized businesses, including manufacturers, distributors and retailers of a wide variety of products. *Click here for a list of LIFO Coalition members: http://savelifo.org/about-lifo-coalition/ and here for a Georgia Tech study on LIFO usage:* http://savelifo.org/ga-tech-study/

Small businesses would be disproportionately harmed by LIFO repeal:

Small businesses that operate on tighter margins particularly rely on LIFO to ensure their ability to maintain inventory levels. Repeal could force many of them into debt not only to pay the recapture tax, but to replenish inventory – a backward spiral that will put them in a position of always trying to play catch up. Some may be forced out of business. *Click here for a Small Business Administration Office of Advocacy letter: http://savelifo.org/pdf-2011/SmallBusAdministrationLetter.pdf*

LIFO should not be repealed on a prospective-only basis:

LIFO was added to the U.S. tax code as an approved inventory accounting method in 1939 to address the corrosive impact of inflation on the ability of U.S. companies to maintain adequate levels of replacement inventory. The need for LIFO has not changed. If a company which sells a product that rises in price does not have sufficient after-tax profit to buy replacement inventory that company cannot remain in business.

LIFO should not be repealed in the context of tax reform or to offset tax rate reductions:

A reduction in income tax rates would not compensate LIFO users for repeal. Many companies have built up their LIFO reserves over many decades and their LIFO reserve is a multiple of one year's taxable income. A simple deferred payment scheme for the repayment of tax from LIFO repeal would not be sufficient to mitigate the harm that LIFO repeal would cause. Repeal would force some smaller companies out of business.

No factually accurate substantive arguments have been made to justify LIFO repeal:

While LIFO repeal has been discussed for nearly a decade, no *factually accurate* substantive argument for repeal has been made; rather, LIFO repeal has been proposed to generate revenue to fund other programs or tax cuts. *Click here for a letter on LIFO legislative history and purposes: http://savelifo.org/wp-content/uploads/2017/01/Camp-Letter-re-Comments-Draft-Tax-Reform-Act-03-31-14.pdf*