

POSITION PAPER: LIFO REPEAL

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The American Supply Association Opposes LIFO Repeal.

- On October 24, 2007, House Ways and Means Committee Chairman Rangel introduced tax legislation designed to be revenue neutral.
- The bill includes repeal of the last-in, first-out (LIFO) method of accounting for inventory.
- LIFO repeal was apparently proposed in part due to a mistaken belief that LIFO is a “tax loophole” or that it is set to disappear from use.
- In fact, LIFO is an established, widely-accepted inventory accounting method that has been used by large and small companies throughout the U.S. economy since the 1930s.
- Repealing LIFO would result in a massive tax increase for hundreds of thousands of large and small American businesses, and could force many smaller ones to close.
- Congress should reject any effort to repeal LIFO.

DISCUSSION

- **What is LIFO?** LIFO (which stands for “last in, first out”) is an inventory accounting method used by companies throughout the U.S. economy to determine both book income and tax liability. Book income is the amount of earnings shown on business financial statements. Tax liability is the amount of income tax owed to the government.
- **Why do businesses use LIFO?** If inventory costs are rising (i.e., there is inflation), LIFO is a more accurate way of measuring financial performance and calculating tax. LIFO takes into account the greater costs of replacing inventory, thereby giving both a more conservative measure of the financial condition of the business and the economic income to which tax should apply. Absent LIFO, phantom profits would be taxed.
- **Is the use of LIFO limited to a certain sector of the economy?** No. LIFO is used by manufacturers, mining companies, and energy producers, as well as by wholesaler-distributors, retailers, and other types of companies that sell every imaginable product. Literally hundreds of thousands of large and small American companies that maintain inventories use LIFO.
- **What would be the impact of LIFO repeal?** Repealing LIFO would force companies currently using the accounting method to report their LIFO reserves as income, resulting in a massive tax increase for large and small businesses spread across the economy. Additionally, repealing LIFO would mean potentially higher future tax bills and would make it harder for companies to manage inflation. Congress should reject any effort to repeal LIFO.

ASA is a member of the LIFO Reform Coalition.

