

## LIFO Repeal

### HDMA's Position:

HDMA opposes repeal of the Last-In First-Out (LIFO) inventory accounting method. Eliminating the ability to elect the LIFO method would have a grossly disproportionate impact upon pharmaceutical distributors with inventories of high volume, high value medications. Its repeal would unfairly reverse long-standing tax policy and result in an unprecedented tax increase for these companies.

- Repealing LIFO would force companies currently using this accounting method to report their LIFO reserves as income, resulting in a massive retroactive tax increase for companies without a corresponding economic benefit.
- According to a 2008 study on tax accounting for the pharmaceutical distribution industry developed for HDMA by PricewaterhouseCoopers, "Repeal of the LIFO election would increase annual federal income liability within the pharmaceutical distribution industry by 12 times more than the average industry." This is particularly challenging in an industry that has an exceptionally low net profit margin of only 1.06%.
- HDMA member companies distribute nearly 76% of all prescription medicines dispensed in the U.S. Repeal of the LIFO election would have a significant impact on their viability and would likely result in an increase in the cost of prescription drugs for Americans.

### Issue:

LIFO has been an established and recognized accounting method in the U.S. since the 1930s and is utilized for tax reporting purposes by a broad spectrum of business sectors that sell a wide range of products. In October 2007, House Ways and Means Committee Chairman Charles Rangel introduced H.R. 3970, the "Tax Reduction and Reform Act of 2007," which would repeal the LIFO accounting method. Moreover, President Obama proposed elimination of LIFO in his 2010 budget submission to Congress. Elimination of LIFO would raise business taxes and would be particularly punitive on distributors of high value products such as pharmaceuticals. Taxes would be increased in two ways:

1. Recapture Tax: This retroactive increase in taxable income is estimated to be the equivalent of 3.6 years of normal corporate tax payments for the pharmaceutical distribution industry, in comparison to an average of one-half year for other industries.
2. Ongoing Tax: The annual increase in taxable income liability for the pharmaceutical distribution industry is estimated to be 58%, an increase in excess of 12 times more than the average industry.

### Additional Information:

HDMA distributor members have found that LIFO provides a more accurate method to measure financial performance and calculate tax liability as inventory costs continue to rise. LIFO takes into account the greater costs of replacing inventory, thereby giving a more conservative measure of both the financial condition and the taxable income of a business.

### About HDMA

HDMA represents primary, full-service healthcare distributors. Each business day, HDMA member companies deliver more than eight million prescription medicines and healthcare products to more than 145,000 pharmacies, hospitals, nursing homes, clinics, physician offices, government and other providers in all 50 states. This essential public health function is provided with tremendous efficiency, saving the nation's healthcare system nearly \$32 billion each year. For more information, visit [www.HealthcareDistribution.org](http://www.HealthcareDistribution.org).

3/9/09