HDMA
Healthcare Distribution Management Association

April 15, 2013

House Ways and Means Committee
Manufacturing Tax Reform Working Group
Small Business Tax Reform Working Group
1102 Longworth House Office Building
Washington, D.C. 20515

Dear Representatives Gerlach, Sanchez, Buchanan, and Schwartz:

I am writing to you on behalf of the pharmaceutical distribution industry to urge you to oppose any effort to repeal the last-in, first-out (LIFO) inventory method to address the U.S. deficit or tax reform. As the House Ways and Means Committee Working Groups convene to consider the elements of broader tax reform, we believe it is critical to maintain this well-established tax accounting method that has been used for decades to accurately reflect inventory costs for a broad spectrum of business sectors selling wide ranges of products across the country.

LIFO has been recognized as an accounting method in the United States since the 1930s and is the most accurate method of accounting in industries like pharmaceutical distribution, where inventory costs are increasing and subject to inflationary pressures. The impact of LIFO repeal on pharmaceutical distributors would be disproportionally burdensome because of the nature of LIFO usage in this industry.

The Healthcare Distribution Management Association (HDMA) represents primary healthcare distributors, the vital link between the nation's pharmaceutical manufacturers and healthcare providers. HDMA member companies ensure that nine million prescription medicines and healthcare products are delivered safely and efficiently to more than 200,000 pharmacies, hospitals, long-term care facilities, clinics and others nationwide. HDMA and its members work daily to provide value and achieve cost savings, an estimated $42 billion each year to our nation's healthcare system.

HDMA members will be uniquely impacted by LIFO repeal on their inventories of high-volume, high value medications. By maintaining large inventories of pharmaceutical and healthcare products, healthcare distributors minimize lags between the time an order is placed and the time it is fulfilled, create a buffer against uncertainties in supply and demand. They allow a pharmacy to purchase from over 1000 manufacturers daily, instead of the inefficiencies of buying direct. Under LIFO, taxpayers defer recognition of inflationary gains until inventory is drawn down. It is not a "tax expenditure" or "tax preference." LIFO subtracts the higher price of replacing inventory from the gross sale, resulting in a more accurate measure of a company's taxable income since it represents the replacement cost of that inventory.

According to a 2010 PricewaterhouseCoopers analysis, the tax increase resulting from LIFO repeal would raise annual federal income tax liability within the pharmaceutical distribution industry by an estimated 51.8 percent — nearly three times more than the average of other LIFO-

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using industries. Even more alarming, the retroactive "recapture" tax that would accompany LIFO repeal is estimated to be 400 percent of the industry's current federal income tax liability. This is particularly challenging for an industry that experiences exceptionally low operating margins (approximately one percent) while safely and efficiently delivering approximately 90 percent of prescription medicines sold in the United States.

While we support fiscal responsibility, eliminating LIFO would place significant financial pressure on the nation's healthcare distributors and only serve to further increase healthcare costs. I urge you to oppose any proposal to eliminate the LIFO accounting method. Please contact me at [redacted] if you have any questions or need additional information.

Sincerely,

Elizabeth A. Gallenagh, Esq.
Vice President, Government Affairs
and General Counsel