April 10, 2013

Mr. Kevin Brady, Chairman
Energy Tax Reform Working Group
U.S. House of Representatives Ways and Means Committee
Washington, DC

Re: Tax Reform and LIFO Repeal

Dear Chairman Brady:

Our company opposes any effort to repeal the last-in, first-out (LIFO) inventory method as part of any legislation to address the US deficit and/or tax reform.

Our company, Tube Forgings of America, is a closely held family business manufacturing steel pipe fittings used primarily in building out our country's energy infrastructure. We provide above average wages and benefits to approximately 175 employees in Portland, Oregon.

We have elected S corporation status. The income from our business is therefore taxed at the personal income tax rates instead of the corporate tax rates. These personal income tax rates exceed the corporate tax rates, which are widely acknowledged as being one of the highest corporate tax rates in the world.

Our company is one of the many small businesses using the LIFO method. The use of the LIFO method is not limited to large, publicly traded companies. As a legitimate method of accounting utilized by both large and small businesses across many different industries, LIFO is not a "special interest" issue.

It is not correct to characterize LIFO as a "tax expenditure". It is an appropriate method of accounting for inventories based on the accounting theory of matching revenues and expenses. It has been recognized by US GAAP (Generally Accepted Accounting Principles) for decades and our recently issued audited financial statements have been reported using the LIFO method.

It is interesting that LIFO has only recently been reclassified as a "tax expenditure". Internal Revenue Code Section 472 establishing LIFO for income tax purposes was enacted in 1939 and is in the portion of the Internal Revenue Code titled "Methods of Accounting". Congress and the IRS have recognized it as a method of accounting for more than 70 years. Congress shouldn't have it both ways.

LIFO has been criticized as an unwarranted deferral of income taxes. We disagree with this conclusion. LIFO recognizes the effects of inflation on inventories, which are real. The Internal Revenue Code

recognized the effects of inflation in many areas, such as the indexing of tax brackets and numerous other fixed dollar amounts embedded within the law. This indexing is intended to prevent the taxation of inflationary income as opposed to real income. Why should the taxation of inventory be any different?

LIFO is not a one-way street. It is also self-correcting. If inventory levels drop, or if deflation occurs, LIFO layers are liquidated and the prior benefits of LIFO are recaptured and reported as taxable income. What other "tax expenditure" does that? LIFO does not confer benefits beyond the impact of inflation.

Ultimately, the benefits of LIFO will be reported as income once the inventory is liquidated and the federal treasury will receive their due portion. The repeal of LIFO would be a retroactive tax increase which would in our case require multiple millions of dollars to pay without benefit of any additional revenue from the sale of inventory. These are dollars that would otherwise be used to finance inventory, fund employee benefits, or make capital investments in our business. Cash flow is crucial to a successful business and this would have a substantial negative impact on cash flow. For no other "tax expenditure" would its repeal result in additional income tax revenue from past year's activities.

It has also been said that the repeal of LIFO is justified in that it would "simplify" the income tax code. Given things that Congress has given us in the past such as the §199, "Income Attributable to Domestic Production Activities", the innumerable phase-ins and phase-outs, and regularly gives us (retroactive) changes in bonus depreciation and §179 limits, it is difficult to take this argument seriously given the negative impact the repeal of LIFO would have.

Should you have any questions, please contact me at 503-228-8691.

Sincerely,

Jay N Zidell
President
Tube Forgings of America, Inc.