

# THE LIFO COALITION

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February 18, 2009

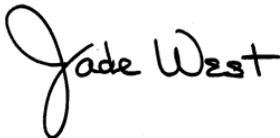
Florence E. Harmon  
Acting Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

**Re: File Number S7-27-08  
Comments with Respect to Roadmap for the Potential Use of Financial  
Statements Prepared in Accordance with International Financial Reporting  
Standards by U.S. Issuers**

Dear Madam:

I am writing on behalf of The LIFO Coalition (“The LIFO Coalition”), to submit the following comments in response to the above-referenced Securities and Exchange Commission (“Commission”) proposed rulemaking. The comments were prepared on behalf of the The LIFO Coalition by Mr. Leslie J. Schneider, Ivins, Phillips & Barker. We appreciate the opportunity to comment, and if you have any questions or need information about our Coalition, please contact either Mr. Schneider or myself.

Sincerely,



Jade C. West  
Senior Vice President-Government Relations  
National Association of Wholesaler-Distributors  
The LIFO Coalition Executive Secretariat

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Statements Prepared in Accordance with International Financial Reporting  
Standards by U.S. Issuers**

Dear Madam:

The following comments are being submitted on behalf of the LIFO Coalition (“The LIFO Coalition”) with respect to the proposal of the Securities and Exchange Commission (“Commission”) to provide a Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards (“IFRS”) by U.S. Issuers (“Roadmap”). The Commission issued its Roadmap and request for comments on November 14, 2008.

### **Who is the LIFO Coalition?**

The LIFO Coalition is an *ad hoc* group of over 120 trade associations representing hundreds of thousands of separate businesses reflecting a cross-section of industries in which inventories are a central part of business operations. This group includes both publicly-held companies which are U.S. issuers of financial statements and are subject to the jurisdiction of the Commission, as well as privately-held businesses that issue financial statements that are not subject to the jurisdiction of the Commission. A list of members of The LIFO Coalition is attached as Exhibit A.

The mission of The LIFO Coalition is to preserve the right of companies to value their inventories pursuant to the LIFO method for federal income tax purposes. This right is presently embodied in Internal Revenue Code Section 472, which has been a part of our federal income tax laws for 70 years.

### **What is the Nature of The LIFO Coalition's Interest in the Commission's Roadmap?**

As noted above, The LIFO Coalition is a group dedicated to preserving the use of the LIFO method of inventory valuation for federal income tax purposes. Since the interests of The LIFO Coalition relate primarily to the federal income tax treatment of inventories, actions proposed or taken by the Commission with respect to the financial accounting practices of companies subject to the Commission's jurisdiction would not normally be of concern to The LIFO Coalition. Accordingly, The LIFO Coalition takes no formal position with respect to the advisability of the Commission requiring issuers of financial statements in the United States to prepare their financial reports furnished to the Commission in conformity with IFRS. Likewise, The LIFO Coalition expresses no formal opinion regarding the Commission's proposed timetable for the adoption IFRS by U.S. issuers of financial statements, as set forth in the Commission's Roadmap.

Nevertheless, what is of vital interest to The LIFO Coalition is the fact that under IFRS, the use of the LIFO method of inventory valuation would be prohibited for financial reporting purposes. *See* IAS 2 "Inventories," ¶ IN63. The reason that this financial reporting prohibition is of interest to The LIFO Coalition is that, as noted on page 38 of the Roadmap, Sections 472(c) and (e)(2) of the Internal Revenue Code provide that a condition of the use of the LIFO method of inventory valuation for federal income tax purposes is that the taxpayer use no method other than the LIFO method of inventory valuation in reporting the results of its operations in its annual reports to shareholders, creditors, etc. (*i.e.*, so-called "LIFO conformity requirement").

Accordingly, as is acknowledged on page 38 of the Roadmap, if U.S. issuers were required to follow IFRS in their financial statements, such issuers would be prohibited from using the LIFO method to value their inventories for federal income tax purposes. Violation of the LIFO conformity requirement subjects the violator to termination of its LIFO election for federal income tax purposes.

**Would the Adoption of IFRS by U.S. Issuers Subject to the Jurisdiction of the Commission  
have any Impact on Privately-held Companies?**

As noted above, the membership of The LIFO Coalition also includes a number of trade associations whose members consist of small and medium size businesses that are privately-held and are not subject to the jurisdiction of the Commission. While such businesses would not normally be affected by actions taken by the Commission, The LIFO Coalition believes that if U.S. issuers that are subject to the jurisdiction of the Commission are required to issue their financial statements in compliance with IFRS, that requirement would inevitably hasten the process by which generally accepted accounting principles (“GAAP”) for all issuers of financial statements operating in the United States would be conformed to IFRS and separate GAAP rules would disappear. Accordingly, The LIFO Coalition believes that a requirement by the Commission that U.S. issuers of financial statements subject to the jurisdiction of the Commission follow IFRS in preparing their financial statements would ultimately lead to the complete elimination of separate GAAP rules for all companies operating in the United States, regardless of whether the company was subject to the jurisdiction of the Commission.

Accordingly, The LIFO Coalition believes that the requirement that U.S. issuers of financial statements subject to the jurisdiction of the Commission follow IFRS rules would ultimately lead to the complete elimination of the use of the LIFO method of inventory valuation for federal income tax purposes because the LIFO conformity requirement would bar all taxpayers complying with IFRS from using the LIFO method for federal income tax purposes.

**What Would be the Economic Impact of the Complete Elimination of the LIFO Method of Inventory Valuation for Federal Income Tax Purposes as a Result of the Adoption of IFRS for Financial Reporting Purposes?**

The LIFO Coalition submits that the complete elimination of the LIFO inventory valuation method for federal income tax purposes by reason of the adoption of IFRS for financial reporting would have an immense adverse financial impact on taxpayers in the United States. While not every type of business maintains inventories and not every business with inventories employs the LIFO method of inventory valuation, a significant number of businesses with inventories use the LIFO method to value their inventories. Moreover, in a number of industries, LIFO is the predominant method of inventory valuation.

For example, in such basic manufacturing industries as textiles, chemicals, petroleum products, plastics, steel, aluminum, pharmaceuticals, food and beverages, tobacco products, automobiles and parts, heavy machinery, construction and farm equipment, and tool and die

making, the LIFO method of valuing inventories is used by a significant number of the members of such industries. Similarly, in the wholesale and retail industries, such as health care product distributors, automobile and equipment parts distributors and dealers, groceries and supermarkets, department stores, and specialty stores, a significant number of industry members use the LIFO method to value their inventories for federal income tax and financial reporting purposes.

When a company terminates its use of the LIFO inventory method for federal income tax purposes, whether as a result of a violation of the LIFO conformity requirement or by voluntary request, the company must report as taxable income in the year of termination of LIFO the accumulated difference between the value of its inventory under the LIFO method and under the inventory method to which the company is changing (referred to as a company's "LIFO reserve"). While limited administrative relief provisions are available to a company terminating its LIFO method, whereby the company may include the additional taxable income resulting from the termination of LIFO ratably over a period of years, the maximum length of such amortization period is currently only four years.

Moreover, LIFO has been a part of our federal income tax laws for 70 years, and many companies now using the LIFO inventory method for federal income tax purposes have used such method for many decades. As a result, a company's LIFO reserve is likely to be substantial in relation to its average annual taxable income. In fact, in many cases, a company's LIFO reserve may exceed the company's total net worth.

Notwithstanding that the term LIFO “reserve” is used to describe the cumulative reduction in taxable income that has resulted from a company’s use of the LIFO method, companies have not typically set aside or reserved funds to pay the additional tax that results from terminating the use of the LIFO method for federal income tax purposes. This circumstance is attributable to the fact that, while the LIFO method is viewed as conferring a temporary or timing benefit on a company, the company’s LIFO reserve tends to be recouped only when the company goes out of business or its assets are sold. Thus, companies do not ordinarily expect to incur the tax liability that results from the termination of the use of LIFO except when they go out of business.

Instead, in a going concern, as a company sells its products to customers, the company needs to replenish its stock of products in order to remain in business. In an inflationary environment, a company that sells its products for an additional profit due to an increase in the selling price of those products will ordinarily incur a correspondingly higher expense to replenish the product that is sold. In that circumstance, the taxpayer cannot be said to have profited from the higher selling price of its products when the proceeds from the sale of the product must be reinvested in the replenishment of the products. Thus, the theory of LIFO is that it matches current expenses with current revenue and avoids an impairment of a company’s capital that would otherwise result from paying current taxes on inflationary profits that are needed for reinvestment in inventory at the new, higher prices.

Accordingly, if a company is required to terminate its LIFO method without having raised fresh capital from a sale of the business because the company continues in operation and

maintains its normal inventory levels, such as in the case of a termination of the LIFO method due to the violation of the LIFO conformity requirement, the adverse financial impact on a company could be devastating. On a nationwide scale, the complete elimination of LIFO could result in significant numbers of companies being unable to continue in operation, with the resulting loss of countless jobs.

**What Actions Could the Commission Take to Ameliorate the Potential Adverse Effects from the Adoption of IFRS on the Use of the LIFO Method for Federal Income Tax Purposes?**

There are a number of possible actions that the Commission could take, in concert with the Treasury Department, to eliminate the adverse effects on the use of the LIFO inventory method for federal income tax purposes resulting from the adoption of IFRS for financial reporting.

In the past, on several occasions, the Commission and other federal regulatory agencies have imposed various financial reporting requirements on companies which have conflicted with the LIFO conformity requirement and posed the risk that a company's compliance with the agency's financial reporting requirements would violate the LIFO conformity requirement in the tax law. For example, in the year of a company's adoption of the LIFO inventory method, financial statement disclosures required by the Commission would have resulted in the company violating the LIFO conformity requirement, but the Internal Revenue Service ("IRS") excused the violation in order not to create a conflict with the reporting requirements of another Federal

agency. *See, e.g.*, Rev. Proc. 77-33, 1977-2 C.B. 542, *amplifying* Rev. Proc. 75-10, 1975-1 C.B. 651, *revoking* Rev. Rul. 74-586, 1974-2 C.B. 156, *declared obsolete by* Rev. Proc. 88-19, 1988-1 C.B. 695. Similarly, compliance with requirements by the Commission that companies disclose in their financial statements the effect on income of valuing their inventory at replacement cost would have violated the LIFO conformity requirement, but the IRS excused the violation. *See* Rev. Proc. 77-7, 1977-1 C.B. 540. Also, in the past, compliance with financial reporting requirements imposed on companies adopting the LIFO inventory method by the Federal Trade Commission violated the LIFO conformity requirement, but the IRS excused the violation. *See* Rev. Proc. 75-30, 1975-1 C.B. 756.

On the basis of these past precedents, one action the Commission could take would be to meet with the Treasury Department and IRS and urge them to issue an administrative pronouncement excusing any violation of the LIFO conformity requirement caused by compliance with the Commission's IFRS reporting requirements.

A second possible approach would be for the Commission to approach the Treasury Department about modifying its income tax regulations relating to the LIFO conformity requirement (Treas. Reg. § 1.472-2(e)), so as to permit companies to continue to use the LIFO method for federal income tax purposes notwithstanding that the company's primary financial statements are issued in compliance with IFRS, provided the company also reports its results in those financial statements on a LIFO basis by including the information in a footnote to the financial statements.

As a result of regulations issued in 1981 (Treas. Reg. § 1.472-2(e)(3)), a company is held not to be in violation of the LIFO conformity requirement as long as its primary financial statements are issued on a LIFO basis. Thus, a company may report non-LIFO information in footnotes or in supplementary reports without violating the LIFO conformity requirement provided the primary financial statement information is reported on a LIFO basis. Obviously, compliance with IFRS would violate this requirement. However, the Treasury could reverse the foregoing presumption in the regulations and reissue the regulations so as to permit primary reporting of non-LIFO information, provided that supplementary reporting of LIFO information is provided in footnotes to the primary financial statements.

One obvious question would be whether the Treasury Department possesses the requisite authority to adopt either of the foregoing suggestions. The LIFO Coalition contends that the Treasury Department has broad authority to adopt these types of policies. This authority derives from the statute itself, as well as the legislative history accompanying the original enactment of the LIFO method in 1939.

In the current income tax statute, as well as in all predecessors to the current statute, it states:

A taxpayer may use the method [the LIFO method] provided in subsection (b) (*whether or not such method has been prescribed under section 471*) in inventorying goods specified in the application of such method . . . .

I.R.C. § 472(a) (Emphasis added).

The legislative history accompanying the original 1939 statute in which the LIFO method was first authorized by Congress states:

Under section 22(c) [the predecessor to section 471 under the present Internal Revenue Code], the Commissioner has the power to prescribe the method [LIFO], and section 219 of the bill reaffirms the power.

S. Rep. No. 648, 76<sup>th</sup> Cong., 1<sup>st</sup> Sess, 6 (1939).

The background for this delegation of power to the Treasury Department derives from the fact that, in Section 22(c) of the Internal Revenue Code of 1939 (the predecessor to Section 471 of the present Internal Revenue Code), Congress did not prescribe which particular inventory valuation methods would be permissible for federal income tax purposes. Instead, Congress delegated the authority to prescribe which inventory valuation methods are permissible to the Treasury Department. The Treasury Department implemented this delegation of authority through the issuance of regulations.

However, at the time of enactment of the Internal Revenue Code of 1939, the LIFO method was relatively new and was not commonly used by companies. As a result, the Treasury Department opposed the use of such method for federal income tax purposes. In the 1939 statute, Congress overrode the Treasury Department's opposition to the use of the LIFO method for federal income tax purposes by expressly authorizing the use of the LIFO method in its own separate Code section. However, the statute and legislative history quoted above indicate that, if the Treasury Department's opposition to the use of LIFO for federal income tax purposes dissipates and LIFO becomes a generally accepted inventory valuation method, Congress intended to preserve the Treasury Department's authority to prescribe the use of the LIFO method for federal income tax purposes under the general inventory provisions in the Internal Revenue Code. This would mean that the Treasury Department could modify, or even completely eliminate, the existing financial reporting conformity requirement for users of the LIFO inventory method in Section 472 of the Internal Revenue Code, as such requirement does not now apply to inventory valuation methods other than LIFO that are employed for federal income tax purposes.

Based on the foregoing, The LIFO Coalition submits that the Treasury Department has considerable latitude to accommodate any financial reporting requirements imposed on U.S. issuers of financial statements subject to the jurisdiction of the Commission without such requirements causing the termination of companies' LIFO inventory methods for federal income tax purposes. Accordingly, The LIFO Coalition urges the Commission to proactively discuss this

problem with the Treasury Department in an attempt to reach an accommodation that does not result in the termination of the use of the LIFO method for federal income tax purposes.

### **What Are the Consequences if the Commission Takes no Action?**

If the Commission fails to take action to remedy the problem that exists for users of the LIFO inventory method, the Commission is likely to experience two possible responses from companies under its jurisdiction. First, with respect to the timetable proposed in the Roadmap, it seems highly unlikely that any companies using the LIFO inventory method would volunteer to be early adopters of IFRS, as such action would likely significantly increase their federal income tax liability.

Second, failure of the Commission to act on the LIFO problem may well induce companies to pressure the Commission and the FASB to create an exception in IFRS for U.S. issuers of financial statements, so that financial statements could be issued using the LIFO inventory method. The LIFO Coalition understands that the Commission is hoping to avoid having to create exceptions from IFRS in the United States, as the existence of such exceptions would undercut the goal of adopting a single, world-wide set of financial accounting standards. However, the financial reality is such that, if companies will experience a significant increase in their federal income tax liability if IFRS is adopted in the United States in an unmodified form, there will undoubtedly be considerable pressure on the Commission to modify IFRS so as to accommodate the use of the LIFO inventory valuation method in the United States.

For the foregoing reasons, The LIFO Coalition urges the Commission to pursue an accommodation on the LIFO issue with the Treasury Department at the earliest possible date.

Sincerely yours,

The LIFO Coalition  
(See attached membership list)

Attachment

Prepared by Mr. Leslie J. Schneider  
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Fax: 202-393-7601

# THE LIFO COALITION

American Apparel & Footwear Association  
American Chemistry Council  
American Forest & Paper Association  
American Gas Association  
American Institute of Certified Public Accountants  
American International Automobile Dealers Association  
American Road & Transportation Builders Association  
American Supply Association  
American Veterinary Distributors Association  
American Watchmakers-Clockmakers Institute  
American Wholesale Marketers Association  
Americans for Tax Reform  
API  
Arizona Automobile Dealers Association  
Arizona Food Marketing Alliance  
Associated Equipment Distributors  
Associated Industries of Massachusetts  
Association for High Technology Distribution  
Association for Hose & Accessories Distribution  
Association of Equipment Manufacturers  
Automobile Dealers Association of Alabama  
Brown Forman Corporation  
Business Roundtable  
Business Solutions Association  
California Grocers Association  
California Independent Grocers & Convenience Stores  
Centralia-Chehalis (WA) Chamber of Commerce  
Ceramic Tile Distributors Association  
Charlotte (NC) Chamber of Commerce  
City of Pinehurst (TX) Chamber of Commerce  
Clovis (California) Chamber of Commerce  
Copper & Brass Servicenter Association  
The Distilled Spirits Council of the U.S.  
Far West Equipment Dealer's Association  
Financial Executives International  
Food Marketing Institute  
FreedomWorks  
Gases & Welding Distributors Association  
Greater New Orleans (LA) New Car Dealers Association  
Hardin County (OH) Chamber of Commerce  
Healthcare Distribution Management Association  
Heating, Airconditioning & Refrigeration Distributors International  
Hobbs (New Mexico) Chamber of Commerce  
Independent Lubricant Manufacturers Association  
Industrial Supply Association  
International Foodservice Distributors Association  
International Franchise Association  
International Music Products Association  
International Sanitary Supply Association  
International Sealing Distribution Association  
Iowa Nebraska Equipment Dealers Association  
Iowa Nebraska Equipment Distributors  
Jackson Area (MI) Manufacturers Association  
Kansas Automobile Dealers Association  
Lawn & Garden Marketing & Distribution Association  
Louisiana Auto Dealers Association  
Lubbock (TX) Chamber of Commerce  
The Manufacturers Association of Central New York  
Maryland Retailers Association  
Metals Service Center Institute  
Minnesota Grocers Association  
Missouri Chamber of Commerce & Industry  
Missouri Retailers Association  
National Association of Chemical Distributors  
National Association of Electrical Distributors  
National Association of Manufacturers  
National Association of Sign Supply Distributors  
National Association of Sporting Goods Wholesalers  
National Association of Wholesaler-Distributors  
National Automobile Dealers Association  
National Beer Wholesalers Association  
National Electrical Manufacturers Association  
National Federation of Independent Business  
National Grocers Association  
National Marine Manufacturers Association  
National Paper Trade Association  
National Petrochemical & Refiners Association  
National Retail Federation  
National Roofing Contractors Association  
National RV Dealers Association  
National Truck Equipment Association  
Nevada Franchised Auto Dealers Association  
North American Equipment Dealers Association  
North American Horticultural Supply Association  
North American Wholesale Lumber Association  
Northeast Pennsylvania Manufacturers and Employers Association

Ohio Council of Retail Merchants  
Ohio Grocers Association  
Oklahoma Automobile Dealers Association  
Outdoor Power Equipment Aftermarket  
Association  
Pet Industry Distributors Association  
Petroleum Equipment Institute  
Plattsburgh-North Country (NY) Chamber of  
Commerce  
Post Card & Souvenir Distributors Association  
Power Transmission Distributors Association  
Printing Industries of America, Inc.  
Puerto Rico Chamber of Commerce  
Randolph (MA) Chamber of Commerce  
Retail Industry Leaders Association  
Rhode Island Food Dealers Association  
Roanoke (VA) Regional Chamber of Commerce  
Rochester (NY) Automobile Dealers Association  
S Corporation Association  
Safety Equipment Distributors Association  
Sand Springs Area (OK) Chamber of Commerce  
Security Hardware Distributors Association  
Small Business & Entrepreneurship Council  
SouthWestern Association  
Southeastern Equipment Dealers Association  
Southern Equipment Dealers Association  
The State Chamber-Oklahoma's Association of  
Business and Industry  
Texas Association of Business  
Textile Care Allied Trades Association  
U.S. Chamber of Commerce  
Vermont Grocers' Association  
Virginia Automobile Dealers Association  
Wholesale Florist & Florist Supplier Association  
Wine & Spirits Wholesalers of America  
The Wine Institute  
Wisconsin Auto & Truck Dealers Association  
Wisconsin Grocers Association  
Wood Machinery

March 20, 2009

The Honorable Florence E. Harmon  
Acting Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Dear Madam Secretary:

On February 18, 2009, the LIFO Coalition submitted to you, comments on the proposed rulemaking with respect to the “Roadmap for Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers.”

The LIFO Coalition’s letter described itself as an “*ad hoc* group of over 120 trade associations.” In an attachment to the letter, the group is identified as including the American Institute of Certified Public Accountants (“AICPA”). Please be advised the AICPA was inadvertently included in the group. We wish to advise you further that the AICPA has not expressed any formal opinion with respect to the recommendation contained in the LIFO Coalition letter of comments.

Thank you for your attention to this matter.

Sincerely,



Arleen R. Thomas, CPA  
Senior Vice President  
Member Competency and Development