



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

February 6, 2001

OFFICE OF
CHIEF COUNSEL

Number: **200121022**
Release Date: 5/25/2001
CC:IT&A:Br1
TL-N-5199-00

UILC: 472.15-00
472.09-00
472.19-00
9999.9800

INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR GRANT E. GABRIEL
INDUSTRY COUNSEL, INVENTORY TECHNICAL
ADVISOR PROGRAM CC:LM:MCT:DET

FROM: Heather C. Maloy
Associate Chief Counsel
(Income Tax and Accounting) CC:IT&A

SUBJECT: Request for Field Service Advice

This Field Service Advice responds to your memorandum dated November 9, 2000. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited as precedent.

DISCLOSURE STATEMENT

Field Service Advice is Chief Counsel Advice and is open to public inspection pursuant to the provisions of section 6110(i). The provisions of section 6110 require the Service to remove taxpayer identifying information and provide the taxpayer with notice of intention to disclose before it is made available for public inspection. Sec. 6110(c) and (i). Section 6110(i)(3)(B) also authorizes the Service to delete information from Field Service Advice that is protected from disclosure under 5 U.S.C. § 552 (b) and (c) before the document is provided to the taxpayer with notice of intention to disclose. Only the National Office function issuing the Field Service Advice is authorized to make such deletions and to make the redacted document available for public inspection. **Accordingly, the Examination, Appeals, or Counsel recipient of this document may not provide a copy of this unredacted document to the taxpayer or their representative.** The recipient of

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this document may share this unredacted document only with those persons whose official tax administration duties with respect to the case and the issues discussed in the document require inspection or disclosure of the Field Service Advice.

LEGEND

Taxpayer =
 Purchaser =
 Seller =
 Target =
 Date 1 =
 Date 2 =
 Date 3 =
 Date 4 =

ISSUE

Whether Taxpayer is required to take into account an adjustment under I.R.C. § 481(a) in connection with a change to the inventory price index computation ["IPIC"] method made pursuant to Rev. Proc. 97-37, 1997-2 C.B. 455.

CONCLUSION

By its terms, Rev. Proc. 97-37 alone governs the treatment of Taxpayer's change of accounting method. Therefore, Taxpayer is permitted to use a cut-off method when changing its accounting method, and was not required to make a section 481(a) adjustment prior to changing to the IPIC method. The Service may not require Taxpayer to change its LIFO method in a taxable year preceding the year of the change.

FACTS

On Date 1¹, Purchaser acquired the outstanding stock of Target from Seller. The parties elected to treat this transaction as a purchase of assets under

¹ Documents submitted by Taxpayer's representative and included with your request indicate that the purchase date was Date 3. Any factual question regarding the date of acquisition is irrelevant to this analysis.

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I.R.C. § 338(h)(10)², and valued Target's assets, including its inventory, pursuant to allocation rules contained in Treas. Reg. § 1.338(b)-2T. After the transaction was consummated, Target's name changed to Taxpayer. Taxpayer elected the "link-chain" LIFO inventory method by filing Form 970 with its tax return for Date 4, its first post-acquisition taxable year.

The temporary regulation's purchase price allocation mechanism resulted in Taxpayer's inventory on hand at acquisition being allocated a cost that was significantly lower than corresponding inventory manufactured subsequently. Nonetheless, Taxpayer treated pre-acquisition and post-acquisition inventory as the same "item" for purposes of LIFO inventory. The examining agent believes that Taxpayer's pre-acquisition inventory should be treated as a separate item under Hamilton Industries, Inc. v. Commissioner, 97 T.C. 120 (1991).

On Date 2, Taxpayer filed an application under the automatic consent provisions of Rev. Proc. 97-37, 1997-2 C.B. 455, to change its LIFO method of accounting to the IPIC method. Taxpayer made this change on a "cut-off" basis without first making an adjustment under I.R.C. § 481(a).

Discussion

In your request for advice, you recommend a determination that Rev. Proc. 97-37 does not apply because Announcement 91-173, 1991-47 I.R.B. 49, remains in force and requires a different result from Rev. Proc. 97-37. In Announcement 91-173, the Service determined that taxpayers requesting advance consent to change their method of accounting voluntarily to comply with the Tax Court's holding in Hamilton Industries must, inter alia, (1) file a current Form 3115, Application for Change in Accounting Method, and (2) for applications filed after November 6, 1991, make a section 481(a) adjustment in conjunction with the request. You reason that although Rev. Proc. 97-37 did not mention Announcement 91-173, section 5.02(1) of Rev. Proc. 97-27, 1997-1 C.B. 680, makes passing reference to the announcement as "an example of other published guidance that requires a section 481(a) adjustment." Further, you state that section 10.04(3), Appendix, Rev. Proc. 98-60, 1998-2 C.B. 761, the revenue procedure that superseded Rev. Proc. 97-37, takes the same position as that of Announcement 91-173. Therefore, you conclude that Rev. Proc. 97-37 does not apply to this case, and that Taxpayer is required under Announcement 91-173 to make a section 481(a) adjustment prior to changing its method of accounting. Furthermore, you conclude that by not making a section

² Unless otherwise indicated all citations refer to statutes, regulations, and Service pronouncements that were in effect at the time.

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481(a) adjustment prior to changing its accounting method, Taxpayer does not have audit protection for taxable years preceding the change.

Rev. Proc. 97-37 by its own terms is controlling in the case of a taxpayer qualifying for treatment under its provisions. See section 4.01 (“this revenue procedure is the exclusive procedure for a taxpayer within its scope to obtain the Commissioner’s consent”). The revenue procedure provides that a taxpayer changing its LIFO inventory method to the IPIC method will use the cut-off method in making the change. Rev. Proc. 97-37, Appendix, § 10.04(d)(2).

Rev. Proc. 98-60, which superseded Rev. Proc. 97-37, requires a taxpayer that improperly accounted for bargain purchase inventory to make a section 481(a) adjustment before changing its LIFO method of accounting to IPIC. However, Rev. Proc. 98-60 is effective, with certain exceptions not pertinent to this case, for taxable years ending on or after December 21, 1998. Taxpayer filed its application to change its accounting method on Date 2. Thus, the terms of Rev. Proc. 98-60 do not apply to Taxpayer’s change.

On the facts represented to us, Taxpayer meets the qualifications for treatment under Rev. Proc. 97-37. Accordingly, the Service will not require Taxpayer to make a section 481(a) adjustment prior to the change of accounting method in question.

Please call if you have any further questions.

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