Scofield v. Commissioner, 1947 WL 89 (T.C. 1947)

Farmers and livestock raisers have a special privilege under Treasury Regulations to change from a cash receipts and disbursements basis to an inventory basis for tax reporting without obtaining prior consent from the Commissioner, provided they comply with specific adjustment requirements.

Summary

Scofield, a farmer, changed his tax reporting method from cash to inventory basis without prior IRS approval, relying on a specific regulation for farmers. The IRS contested, arguing that any change in accounting method requires prior approval. The Tax Court held that farmers have a specific exception to this general rule, and therefore Scofield did not need prior approval, so long as they followed the regulation's adjustment procedures. This case clarifies the scope of the special accounting method rule for farmers and when IRS consent is required for such changes.

Facts

The petitioner, a grain and cotton farmer, changed his method of reporting income from the cash receipts and disbursements basis to an inventory basis for the tax year in question. He kept a record of his inventories using the "farm-price method." The petitioner made the required adjustments to his income for the three preceding taxable years and submitted them to the IRS. The Commissioner determined a deficiency based on the assertion that the petitioner did not obtain prior permission to change his "basis of accounting or method of reporting income."

Procedural History

The Commissioner assessed a tax deficiency against the petitioner. The petitioner appealed to the Tax Court, arguing that as a farmer, he was entitled to change his accounting method without prior permission under specific regulations. The Tax Court reviewed the Commissioner's determination.

Issue(s)

1. Whether a farmer or livestock raiser must obtain prior permission from the Commissioner to change the basis of their tax returns from a cash receipts and disbursements basis to an inventory basis, as generally required for changes in accounting methods.
2. What is the proper method to calculate community property income for the taxpayer and his wife?

Holding

1. No, because the applicable Treasury Regulation provides a specific exception

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for farmers and livestock raisers, allowing them to change to an inventory basis without prior consent, provided they comply with the regulation's adjustment requirements.
2. The court determined the percentage of income that was considered community income should be determined by the formula laid out in *Clara B. Parker, 31 B. T. A. 644*.

Court's Reasoning

The court reasoned that Section 19.22(c)-6 of Regulations 103 sets up farmers and livestock raisers as a special class of taxpayers. The court stated, "Farmers may change the basis of their returns from that of receipts and disbursements to that of an inventory basis," as long as prescribed adjustments are made. According to the court, the petitioner complied with the regulations by submitting adjustment sheets for the three preceding taxable years. The court emphasized that the petitioner did not make any change in his "method of valuing inventories," thus he did not have to seek the Commissioner's permission. The court found support in an administrative ruling, Office Decision 841 (4 C. B. 53), which stated, "It is not contemplated by Treasury Decision 3104 that farmers must obtain formal permission in order to change the basis of their returns from that of receipts and disbursements to that of an inventory basis." Regarding the second issue, the court determined that 7% was a fair return on the petitioner's invested capital and that $10,000 was the reasonable value of his services, and with these factors determined, a recomputation of the community income may be made, if need be, according to the formula established in the *Clara B. Parker* case.

Practical Implications

This case clarifies that farmers and livestock raisers have a distinct advantage in tax accounting, allowing them to shift to an inventory basis without the typically required prior approval from the IRS. This simplifies tax compliance for agricultural businesses. However, compliance with the specific adjustment requirements outlined in the applicable regulation is crucial. Subsequent cases and IRS guidance must be consulted to ensure the continued validity and application of this exception, especially in light of changes to tax laws and regulations. This case affects how tax advisors counsel farmers on accounting method selection and reporting requirements, ensuring they leverage available benefits while remaining compliant.

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