***Frost v. Commissioner*, 28 T.C. 1126 (1957)**

Taxpayers who inventory breeding livestock using the unit-livestock-price method must consistently apply this method and cannot switch to depreciating the breeding livestock as capital assets without the Commissioner's prior approval.

Summary

The Tax Court held that taxpayers, who had consistently inventoried their breeding cattle using the unit-livestock-price method, could not remove the breeding herd from inventory and begin depreciating it without obtaining prior approval from the Commissioner of Internal Revenue. The court reasoned that switching from inventorying livestock to depreciating it constitutes a change in accounting method, requiring the Commissioner's consent under established tax regulations. Because the taxpayers did not seek or receive such approval, the depreciation deduction was disallowed.

Facts

Petitioners, Jack and Ruby Mae Frost, were farmers and ranchers who had been in the business since 1936. Since 1938, they had been breeding cattle. Prior to 1951, the petitioners consistently included all cattle used for breeding purposes in their inventory and valued them using the unit-livestock-price method. This accounting method was established by their accountants in 1936. In 1951, the petitioners removed a portion of their breeding herd from inventory and listed it on their depreciation schedule, claiming a depreciation deduction on their tax return. They did not request or receive approval from the Commissioner to make this change.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in the petitioners' taxes for 1951, disallowing the depreciation deduction. The Commissioner argued that removing the breeding herd from inventory and listing it for depreciation was an unauthorized change in accounting method. The petitioners challenged this determination in the Tax Court.

Issue(s)

1. Whether the petitioners could remove their breeding herd from inventory and depreciate it without prior consent from the Commissioner of Internal Revenue, given their consistent prior use of the unit-livestock-price inventory method.

Holding

1. No, because removing the breeding herd from inventory and depreciating it constitutes a change in accounting method requiring the Commissioner's prior approval, which the petitioners did not obtain.

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Court’s Reasoning

The court relied on Treasury Regulations (Regs. 111, secs. 29.22(c)-6, 29.41-2, 29.22(a)-7, and 29.23(l)-10) and the precedent set in *Elsie SoRelle*, 22 T.C. 459 (1954). The regulations provide farmers reporting on the accrual basis an option to either include breeding livestock in inventory or treat them as depreciable capital assets, but require consistent application of the chosen method. Regulation 111, sec. 29.22(a)-7 states that livestock acquired for breeding may be included in inventory “provided such practice is followed consistently by the taxpayer.” Regulation 111, sec. 29.23(l)-10 disallows depreciation for livestock included in inventory, as value reduction is already reflected in the inventory. The court quoted *Elsie SoRelle*, stating that taxpayers have an option, but if they include breeding stock in inventory, taking depreciation deductions is “expressly prohibited.” The court emphasized that these regulations have been in place since 1934 and statutory provisions have been reenacted without pertinent changes, indicating legislative sanction of this executive construction. Because the petitioners had consistently inventoried their breeding livestock and did not obtain the Commissioner’s approval to change methods, the court upheld the disallowance of the depreciation deduction. The court stated, “Since the Commissioner’s approval was not sought by petitioner before making the change in question…we think it is clear that respondent’s determination must be sustained.”

Practical Implications

Frost v. Commissioner underscores the importance of consistency in tax accounting methods, particularly for farmers and ranchers dealing with breeding livestock. This case clarifies that once a taxpayer elects to include breeding livestock in inventory (especially using the unit-livestock-price method), they are bound to that method unless they obtain prior approval from the IRS to change. For legal practitioners advising clients in agricultural tax law, this case serves as a reminder that changes in accounting methods, such as switching from inventory to depreciation for breeding herds, require formal consent from the tax authorities. This ruling impacts tax planning by requiring taxpayers to carefully consider their initial accounting method election and to formally request permission for any subsequent changes to avoid disallowance of deductions. Later cases and IRS guidance continue to emphasize the need for consistency and prior approval for changes in accounting methods, reinforcing the practical implications of the *Frost* decision.

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