H. F. Campbell Company (Formerly H. F. Campbell Construction Company), Petitioner v. Commissioner of Internal Revenue, Respondent, 54 T. C. 1021 (1970)

A change in accounting method without the Commissioner's consent does not entitle a taxpayer to adjustments under Section 481(b)(4).

Summary

In H. F. Campbell Co. v. Commissioner, the Tax Court addressed whether a taxpayer could unilaterally change its accounting method for reporting income from long-term contracts without the Commissioner's consent. The petitioner, using the completed-contract method, attempted to change from using four criteria to two for determining contract completion in 1962. The court upheld the Commissioner's use of the original four criteria, denying the taxpayer's claim for adjustments under Section 481(b)(4) since the change was not approved. This case emphasizes that a taxpayer must obtain the Commissioner's consent before changing its accounting method, impacting how future cases involving similar issues should be approached.

Facts

H. F. Campbell Company used the completed-contract method of accounting, employing four criteria to determine when contracts were completed and income was reportable: physical completion, customer acceptance, recording of all anticipated costs, and computation of the final bill. In 1962, the company attempted to change this method by using only two of these criteria, leading to a dispute over the tax treatment of profits from several contracts. The Commissioner determined deficiencies based on the original four criteria, and the company contested this, arguing it had changed its accounting method and was entitled to adjustments under Section 481(b)(4).

Procedural History

The case was initially heard by the U. S. Tax Court, which issued an original report on December 23, 1969. A supplemental opinion was filed on May 18, 1970, addressing additional issues not considered in the original report, including the Commissioner's motion to amend the answer and the taxpayer's objections to the Commissioner's computation of deficiencies.

Issue(s)

1. Whether the Commissioner's motion to amend the answer to conform the pleading to the proof should be granted.
2. Whether the profits from two contracts (International Harvester Co. and Progressive Wholesale Grocery) are taxable in 1959 rather than 1960.
3. Whether the petitioner is entitled to elect, pursuant to Section 481(b)(4), to spread the income from five other disputed contracts over 1962 and the 9

succeeding years.

Holding

1. Yes, because the amendment merely conforms the pleading to the proof adduced at trial and is not untimely or prejudicial.
2. No, because the income from these contracts was correctly reported by the petitioner for 1960 under the four-criteria method.
3. No, because the petitioner's attempted change in accounting method was not consented to by the Commissioner, and thus, the petitioner is not entitled to adjustments under Section 481(b)(4).

Court's Reasoning

The Tax Court reasoned that the Commissioner's amendment to the answer was permissible under Rule 17(d) of the Tax Court Rules of Practice, as it aligned the pleading with the trial evidence. For the second issue, the court applied the four-criteria method consistently used by the petitioner from 1954 through 1961 and found that the contracts' income was correctly reported in 1960. Regarding the third issue, the court emphasized that a change in accounting method requires the Commissioner's consent under Section 446(e). Since the petitioner did not obtain this consent, the attempted change was invalid, and thus, the petitioner could not claim adjustments under Section 481(b)(4). The court cited relevant regulations and case law to support its stance that Section 481 relief is contingent on the Commissioner's approval of the change in accounting method.

Practical Implications

This decision underscores the importance of obtaining the Commissioner's consent before changing an accounting method. Taxpayers must adhere to their established methods unless formally approved to change, affecting how similar cases should be analyzed. The ruling clarifies that unilateral changes do not entitle taxpayers to Section 481 adjustments, impacting tax planning and compliance strategies. Businesses must carefully consider their accounting methods and seek approval for changes to avoid similar disputes. Subsequent cases have consistently applied this principle, reinforcing the need for Commissioner's consent in accounting method changes.

