

Notice of Proposed Rulemaking and Notice of Public Hearing

Unit Livestock Price Method

REG-125626-01

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations relating to the use of the *unit-livestock-price method* of accounting. The proposed regulations affect livestock raisers and other farmers that elect to use the unit-livestock-price method. These proposed regulations provide rules relating to the annual reevaluation of unit prices and the depreciation of livestock raised for draft, breeding, or dairy purposes. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written or electronic comments must be received by May 6, 2002. Requests to speak and outlines of topics to be discussed at the public hearing scheduled for June 12, 2002, at 10 a.m. must be received by May 22, 2002.

ADDRESSES: Send submissions to: CC:IT&A:RU (REG-125626-01), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:IT&A:RU (REG-125626-01), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS Internet site at http://www.irs.gov/tax_regs/regsglist.html. The public hearing will be held in the room 4716, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, A. Katharine Jacob Kiss at (202) 622-4920; concerning submissions and the hearing, Sonya M. Cruse at (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 471 of the Internal Revenue Code (Code). The unit-livestock-price method, contained in § 1.471-6, provides for the valuation of different classes of animals in inventory at a standard unit price for each animal within a class. A taxpayer that elects to use the unit-livestock-price method must apply it to all livestock raised, whether for sale or for draft, breeding, or dairy purposes. Once established, unit prices and classifications selected by the taxpayer must be consistently applied in all subsequent years. Prior to 1997, § 1.471-6 did not allow a taxpayer to make any changes in the unit prices without first obtaining the consent of the Commissioner.

Following the enactment of section 263A, the IRS and Treasury Department published Notice 88-24 (1988-1 C.B. 491), which provided guidance to taxpayers regarding the application of the unit-livestock-price method to property produced in the trade or business of farming. Notice 88-24 indicated that forthcoming regulations would modify the rule contained in § 1.471-6 and require that taxpayers adjust their unit prices upward, from time to time as specified by those regulations, to reflect increases in costs taxpayers experience in raising livestock. Notice 88-24 also provided safe-harbor unit prices for the unit-livestock-price method with respect to female cattle raised or purchased by a taxpayer for purposes of breeding (beef cattle) or milk production (dairy cattle).

Contemporaneous with the publication of the section 263A temporary and proposed regulations on August 22, 1997, (T.D. 8729, 1997-2 C.B. 35), the IRS and Treasury Department modified the final regulations under § 1.471-6 to provide, for taxable years beginning after August 22, 1997, a taxpayer using the unit-livestock-price method must annually reevaluate its unit prices and must adjust the prices upward to reflect increases in the costs of raising livestock. The consent of the Commissioner is not required to make such upward adjustments, but no other changes in the classification of animals or unit prices may be made without the consent of the Commissioner.

On September 5, 2000, the IRS and Treasury Department published final regulations under section 263A (T.D. 8897, 2000-2 C.B. 234) in the **Federal Register** (65 FR 50638), which obsoleted Notice 88-24, relating to rules for property produced in a farming business. The preamble to these final regulations discussed comments received regarding the modification made to the unit-livestock-price method and indicated the IRS and Treasury Department's intent to study this method. These proposed regulations are promulgated in response to those comments.

Explanation of Provisions

Commentators expressed concern that if taxpayers are required to annually reevaluate their unit prices, they should be able to both increase and decrease the

unit prices to reflect all changes in the costs of raising livestock. The IRS and Treasury Department agree that to the extent the unit-livestock-price method requires an annual reevaluation of the unit prices, a taxpayer should be able to increase and decrease its unit prices without securing the consent of the Commissioner. Such a change is not a change in method of accounting, but an application of the unit-livestock-price method, similar to the application of a standard cost method. Consequently, the proposed regulations allow a taxpayer to both increase and decrease its unit prices without obtaining the consent of the Commissioner.

However, the IRS and Treasury Department also recognize a broader concern that the requirement to annually reevaluate unit prices may have eliminated much of the simplicity of the unit-livestock-price method. In this respect, the IRS and Treasury Department welcome comments on how the rules could be made simpler to apply. For example, the IRS and Treasury Department request comments on whether safe harbor unit prices similar to those announced in Notice 88-24 should be made available again to taxpayers using the unit-livestock-price method. If so, comments specifically are requested as to an index or measure those safe harbor unit prices should be based on and how often those safe harbor unit prices should be adjusted.

Commentators also suggested that the unit-livestock-price method should be clarified to allow a taxpayer to remove from inventory animals that have been raised for use in a taxpayer's trade or business (such as a breeding cow) and depreciate the cost of the animal based on its inventoriable cost. Under § 1.471-6(g), a livestock raiser who uses the unit-livestock-price method is permitted to elect to include animals *purchased* for draft, breeding, or dairy purposes in inventory or to treat those animals as property used in a trade or business subject to depreciation after maturity. In contrast, § 1.471-6(f) does not specifically permit a livestock raiser who uses the unit-livestock-price method to elect to treat animals *raised* for draft, breeding, or dairy purposes as property used in a trade or business subject to depreciation after maturity. There does not appear to be a

current rationale for distinguishing between animals *raised* versus animals *purchased* for draft, breeding, or dairy purposes. Accordingly, the proposed regulations clarify that a livestock raiser that uses the unit-livestock-price method may elect to remove from inventory after maturity an animal raised for draft, breeding, or dairy purposes and treat the inventoriable cost of such animal as an asset subject to depreciation.

Effective Date

These regulations are applicable to taxable years ending after the date final regulations are published in the **Federal Register**.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any electronic or written comments (preferably a signed original and eight (8) copies) that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for June 12, 2002, at 10 a.m. in room 4716, Internal Revenue Building, 1111

Constitution Avenue, NW, Washington, DC. Due to building security procedures, visitors must enter at the 10th Street entrance, located between Constitution and Pennsylvania Avenues, NW. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 15 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons who wish to present oral comments at the hearing must submit written comments and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and 8 copies) by May 22, 2002. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these proposed regulations is A. Katharine Jacob Kiss, Office of Associate Chief Counsel (Income Tax and Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.471-6 also issued under 26 U.S.C. 471. * * *

Par. 2. Section 1.471-6 is amended as follows:

1. In paragraph (c), the last sentence is removed.

2. Paragraph (f) is revised.

3. In paragraph (g), the first sentence is amended by removing the language "capital assets" and adding "property used in a trade or business" in its place.

The revisions read as follows:

§ 1.471-6 Inventories of livestock raisers and other farmers.

* * * * *

(f) A taxpayer that elects to use the "unit-livestock-price method" must apply it to all livestock raised, whether for sale or for draft, breeding, or dairy purposes. The inventoriable costs of animals raised for draft, breeding, or dairy purposes can, at the election of the livestock raiser, be included in inventory or treated as property used in a trade or business subject to depreciation after maturity. See § 1.263A-4 for rules regarding the computation of inventoriable costs for purposes of the unit-livestock-price method. Once established, the methods of accounting used by the taxpayer to determine unit prices and to classify animals must be consistently applied in all subsequent taxable years. A taxpayer that uses the unit-livestock-price method must annually reevaluate its unit prices and adjust the prices either upward to reflect increases, or downward to reflect decreases, in the costs of raising livestock. The consent of the Commissioner is not required to make such upward or downward adjustments. No other changes in the classification of animals or unit prices may be made without the consent of the Commissioner. See § 1.446-1(e) for procedures for obtaining the consent of the Commissioner. The provisions of this paragraph (f) apply to taxable years ending after the date that final regulations are published in the **Federal Register**.

* * * * *

Robert E. Wenzel,
*Deputy Commissioner of
Internal Revenue.*

(Filed by the Office of the Federal Register on February 1, 2002, 8:45 a.m., and published in the issue of the Federal Register for February 4, 2002, 67 F.R. 5074)