1965

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T. Milton Kupfer

Recommended Citation
Haskins & Sells Selected Papers, 1965, p. 211-226

Tax Problems in Inventories

by T. Milton Kupfer
Partner, Executive Office

Presented before state society and AICPA audiences in Boston, Chicago, Columbus, Newark, and Washington, D.C. as part of the AICPA 1965 Tax Lecture Series

The Internal Revenue Service has taken an increasingly active interest in inventories over the past several years. This probably started before 1961, but it was brought to widespread attention in April 1961 when President Kennedy included a directive in his Tax Message to Congress to the effect that inventory matters were to be considered carefully by the Service.

The Service reacted publicly to this by including questions regarding inventories on the tax returns for 1961. These questions in substantially the same form appeared on the returns for all years until 1965. Although there is now only one rather innocuous question regarding inventories, I do not think that this indicates any lessening of Service interest in inventories. Certainly examining agents, and particularly the National Office, have been giving more and more attention to inventories.

All of this is of interest to us as accountants because in the past the Revenue Service has tended generally to accept inventory values shown in the books. In fact, inventories probably constitute the major area of taxation in which the rules developed by us as accountants have had the most influence. This, of course, is reasonable since the Code has long required only that inventories be taken on a basis that clearly reflects income in conformance with the best accounting practice of the industry. This lack of difference between book basis and tax basis should not, however, lead us to assume complacently that the best advantage is being obtained or that changes should not be suggested.

One facet of the National Office activity that should be kept in mind in considering what I have to say is that the National Office may inquire into all aspects of inventory accounting even though it may be asked to rule only on some limited aspect. The National Office has also required as a condition to changes granted to some categories of inventory accounting that changes be made in other categories that were not subject to the request.

WHEN MUST INVENTORIES BE RECOGNIZED?

Code

The basic rule regarding recognition of inventories has been in the Internal Revenue Code in substantially the same form for many years.

The rule is that "whenever in the opinion of the [Commissioner] the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer on such basis as the [Commissioner] may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income."

Regulations

The regulations implement this by requiring inventories in every case in which the production, purchase, or sale of merchandise is an income producing factor.

Court Rules

Even though the regulations use the phrase "income producing factor" without modification, court decisions over the years have established a rule that inventories are not required if only small amounts of inventoriable items are held by a taxpayer and if income is correctly reflected. The courts will not force the change as long as income is reasonably reflected. Minor deviations and errors in the treatment of certain items that do not play a large role in the computation of taxable income are not sufficient to warrant the requiring of inventories, so that either the cash method or the accrual method will reasonably reflect income.

Thus, one court decision related to a cash-basis partnership that began entering into government contracts when its previous business declined. Because of the change it began to accumulate inventories. However, they were not entered on the partnership books for several years and the partnership remained on the cash basis. Later, it attempted to change to the accrual basis and to show inventories. The Commissioner was upheld in refusing to allow the accrual method and in not recognizing the inventories on the ground that annual income was not distorted through continuing the cash method.

Increases in Later Years

Of course the situation could change in later years as inventories become more and more substantial. The gradual acquisition of inventories can result in a serious problem from bunching of income if their recognition is forced in one year. To the extent that the inventories were acquired before 1954, problems may be avoided, as we shall discuss later. However, as the years go by, this pre-1954 protection will tend to become less and less important so that taxpayers who have ignored inventories may find that they will be required to pay tax in one year on the entire inventory accumulation.

Taxpayers in this situation should give consideration to requesting permission to change their accounting practice under the provisions of a Revenue Procedure issued in early 1964. Although this change will not result in escaping tax, it should result in spreading the impact over a period of ten years. In this way the change can be planned for and taken care of on the instalment plan.

WHAT MUST BE INCLUDED IN INVENTORIES?

When we consider the question of what must be included in inventories, we again find that the basic rules follow our accounting concepts quite closely. The regulations include two general categories: (1) all finished or partly finished goods, and (2) raw materials and supplies—but only those that have been acquired for sale or that will physically become a part of the merchandise intended for sale.

Supply Items

This second requirement has given rise to confusion in the past and the result of the confusion may be the problems of today. This confusion arose with respect to so-called supply items, that is, items used in connection with the production process but not becoming a part of the final product. They might include small tools, lubricants for production machinery, coal, bricks, or chemicals used in the production process.

In the past the regulations indicated that supply items were a part of inventories subject to write-downs, and court decisions had upheld the right of taxpayers to write-downs. The regulations were revised to their present form in 1933. Nevertheless, many taxpayers continued to treat supply items as inventories without substantial problems arising. Others wrote them off as acquired, while some set up careful procedures to record the items as deferred charges in their balance sheets.

Permission to Write Off

A few years ago, the Internal Revenue Service adopted a liberal attitude toward the treatment of supply items. The Service now will grant permission to deduct cost of supplies currently as purchased rather than require them to be carried at cost. Our experience has been that this permission can generally be obtained. The principal requirement seems to be that the items actually be used within one year after being purchased. This might be demonstrated on the basis of turnover statistics for the entire account, although showing of the use of particular items is preferred by the Service. The other problem, of course, is to show that the items do not become a part of the product, although in a great many cases this should not be too difficult.

For taxpayers having a substantial amount of the supply items, the opportunity to write them off as acquired can present a real benefit. However, the possible effect on the financial statements should be considered since the Service will probably require that the change also be made on the books.

Title

Inherent in the rules regarding inclusion in inventories is that title must be vested in the taxpayer. This requirement presents some opportunities for tax planning in connection with sales in that year-end deliveries may be accelerated or deferred depending on the desirability of increasing this year's or next year's income.

Similarly, if there has been a market decline, it may be advantageous to accelerate purchases in order to obtain immediate benefit of a write-down to market.

Another facet of the title-vesting requirement relates to taxpayers on the LIFO method. It may be found before the end of the year that there will be a reduction in inventory quantities from those on hand at the beginning of the year. If so, there could be a loss of LIFO inventory base and a consequent increase in taxable income. On the other hand, if purchases can be accelerated so that there is no reduction in quantities at the year end, the effect will be that the excess of current cost over the LIFO cost will be deducted immediately and the LIFO base will be retained.

WHAT ARE ACCEPTABLE INVENTORY METHODS?

The Code and regulations provide two general criteria for determining whether an inventory method is acceptable. These are: (1) there must be a clear reflection of income; (2) the method must conform as nearly as possible to the best accounting practice in the trade or business.

In considering the first requirement, the fact that an inventory practice must be consistent from year to year is of the utmost importance. This is recognized in the regulations wherein it is stated that "greater weight is to be given to consistency than to any particular method of inventorying or basis of valuation so long as the method or basis used is substantially in accord with the regulations." This is because consistency prevents variations in the application of methods from resulting in income distortions that are not recoverable in future years. Thus, even though some practice may achieve substantially less than theoretical perfection, if it is done the same way each year the Service cannot raise a real objection unless in some year the practice results in distortion of income.

With regard to the requirement of conformity to the accounting practice of the trade or business, an accountant's opinion on the particular inventory method may be of great importance because the regulations provide that "an inventory that can be used under the best accounting practice in a balance sheet showing the financial position of the taxpayer can, as a general rule, be regarded as clearly reflecting his income." Thus, an exception to an inventory method in an accountant's opinion can well give rise to a tax problem.

The two methods most commonly used in valuing inventory are cost and the lower of cost or market.

INVENTORIES AT COST

There are two basic requirements for valuing inventories at cost:

The first relates to purchased items that are to be valued at invoice price plus freight and less trade discounts. Cash discounts may also be deducted if they are treated consistently.

The second basic rule relates to manufactured items. They are to be valued on the basis of the cost of raw materials and supplies entering into or consumed in production, the cost of direct labor, and the cost of indirect expenses incident to and necessary for production.

Inventory cost must include a reasonable proportion of management expenses, but should not include selling cost or profit.

Overhead

Of course, the major problems relate to the manner in which indirect overhead expenses are included or excluded from inventory. On the one hand we have problems caused by too much overhead in inventories. This includes items that are not incident to or necessary for production.

One such cost may be research and experimental expenditures. They generally should be excluded from inventories and deducted currently or deferred depending on the particular election made by the taxpayer.

Another category of costs remaining in some inventories is that of general and administrative expenses. For accounting purposes in some industries it has been the practice to include general and administrative expenses in inventories and the practice has carried over to the tax return. Because of the clear rule of the regulations that excludes general and administrative expenses from inventories the Internal Revenue Service has granted permission to remove those expenses even for taxpayers who are in the contracting business and use a long-term contract method.

Another cause of overstated inventories is costs that are allocated to inventory for accounting convenience. A good example of this is the rather common practice by which all costs allocated to a particular plant are considered to apply to the production of that plant even though many are not properly inventory costs. Costs are merely allocated to a particular location to satisfy our accounting tendency for neatly categorizing all items of cost. Although I am not aware of a request having been filed for permission to remove these costs from inventories, there seems to be no reason for the Service not to look favorably on one.

Idle Plant Costs

Another side of this question of too much overhead in inventories is that brought about by so-called idle-plant costs. These are unabsorbed fixed costs that arise when production in a particular period is, for one reason or another, low. It is not correct to regard all the fixed costs as allocable to the low number of units produced on a per-unit basis. Good accounting practice requires that these idle-plant costs be excluded from inventory valuation, and taxpayers have consistently taken this approach in the past. However, the official view of the Internal Revenue Service has been that inventory values should include a portion of all costs incurred in a period regardless of the level of production. The results of this approach are that amounts at which inventories are stated are higher in a period of low production because the fixed costs of the period are spread over a lesser number of units. This means that even though business is bad, profits may look good, and the balance sheet presents a misleading picture of solvency. However, a recent experience in connection with a request for technical advice indicates that this problem has been reconsidered and that the reconsideration has resulted in the logical conclusion that inventory costs are not properly stated if they include all idle-plant costs.

As usual, there are several unresolved problems.

Taxpayers will be required to show that something has occurred to cause their operations to be reduced. Thus, some identifiable factor probably will be necessary other than a general reduction in sales. This might be a strike, a casualty, or more important, the development of a new or improved product by a competitor.

Another problem is to measure extent of idleness. A determination based on the maximum capacity of a particular plant will not be recognized, nor will industry averages. The experience of the particular taxpayer will be important. An approach that could be adopted would be to base the computations on normal operations over a representative period, perhaps five years. The comparison might be made on the basis of production, such as tonnage or units, or on a factor such as labor-hours or labor-dollars. In the particular case, direct labor-dollars were used. If operations for a particular year are below the level of this base period, fixed costs not absorbed because of the reduced operations could be treated as costs of the period and not required to be included in inventory values.

Another problem relates to the nature of the costs subject to exclusion from inventory value. Although there is a general understanding that only fixed costs, and not variable costs, are eligible for exclusion, it may be difficult to determine whether a particular item varies with the level of production.

EXCLUSION OF OVERHEAD

We have been discussing the problems that arise when too much overhead is included in inventories. On the other side of the coin is the situation in which perhaps too little overhead is included.

Direct Costing

The first of these areas is that of the use of direct costing. As you probably know, under this method, only prime costs plus variable factory costs are used to value inventory. The remaining factory expenses (the fixed expenses) are charged-off currently to profit and loss. There has been a great deal of interest in the direct-costing approach for some time among accountants. While there is much to be said for its value for management information purposes, it has not achieved general acceptance for financial-statement purposes.

Another, and at least equally important, reason is the fact that the Internal Revenue Service also regards it as an incorrect method of tax accounting. Although there are a few reports of the Service's willingly accepting tax returns prepared on the basis of direct costing of inventories, the returns seem to relate to special circumstances. At the same time, the Service has been required to accept the use of direct costing unwillingly in some instances.

An outstanding example of this is found in the Geometric Stamping Company case in which consistent use by the taxpayer and prior acceptance by the Internal Revenue Service were sufficient to permit continued use of direct costing in the face of a different book method. The taxpayer was able to show that, because of the effect on beginning inventories, income actually was greater in some years than it would have been if an absorption-costing method had been used.

To summarize: It seems clear that, until the direct-costing method achieves more general acceptance from an accounting standpoint, it will not achieve such acceptance from a tax standpoint. Nevertheless, those taxpayers who have adopted it in the past have a strong argument for continuation.

Inadequate or Arbitrary Burden Rates

Somewhat allied to the question of direct costing, but having a different theoretical basis, is the problem of inadequate or arbitrary burden rates. This is distinguished from direct costing in that there is no attempt to eliminate specific items of overhead from the inventory. Rather, a-less-than-adequate portion of all items is included. Many taxpayers in the past have fallen into the use of these rates through inadequate attention to inventories. A burden rate that was realistic at one time was continued year after year and no thought given to changing circumstances; or perhaps no real thought was given to overhead at any time.

A few taxpayers have successfully argued that the use of these burden rates represents an accounting method. On the other hand, the view of the National Office of the Service is that they represent an erroneous application of inventory procedure. Until the issue is resolved, your clients will be well advised to move cautiously in making voluntary changes if they are unwilling to accept a tax change also. If they are, a change in practice that would spread this impact over ten years should be considered.

The ultimate in exclusion of overhead from inventory of course is the so-called prime-cost method. Under this method, only direct labor and direct material costs are included in inventories. All overhead, including variable expenses, is excluded. A 1964 Tax Court decision held that this method did not clearly reflect taxable income and could be changed by the Commissioner. This taxpayer did not have the protection of consistency as the method had been used for only about two and one-half years before the year of examination.

STANDARD COSTS

Another problem area, related to overhead in inventory, is that of the use of standard costs. The Service takes the position that standard costs are not an acceptable method of inventory determination and therefore cannot be used unless year-end adjustments are made to show actual costs.

At the same time, variances that develop out of a standard cost system should not be applied to inventory willy-nilly. For example, volume variances may well arise from idle plant and it should not be necessary to include all this variance in inventory. On the other hand, it may be more difficult to support the exclusion of price variances from inventory costs since they are more likely to represent actual cost.

This is not intended in any way to say that standard costs should not be used. They are a very useful tool for purposes of giving information to management. In dealing with the Service, however, it will be necessary to show that costs have been properly allocated to inventories. From a practical standpoint, it would seem that the maintenance of current standards will do much to alleviate possible questions. No doubt many problems in the use of standard costs have arisen where standards were not kept up-to-date. This, of course, also destroys their usefulness to management so that it is in the interest of everyone to keep them on a current basis.

There is a ray of sunshine in all this. Because the Service holds that standard costs are not acceptable without adjustment, it is not necessary to file an application for permission to use the method for book purposes. The required adjustment to actual cost effectively means that there is no change in inventory method when standard costs are adopted. This assumes, of course, that substantially the same elements of costs are recognized under the standard cost system as were recognized under the actual cost approach.

BY-PRODUCT COSTING

Another area of current interest is that of by-product costing.

A year or so ago we asked the Service to rule on an inventory valuation practice under which all costs would be assigned to the principal product up to the point at which separate processing starts. The Service refused to accept this as a proper practice. The client's request was rejected even though the proposed method would have resulted in higher total inventory valuation because, under the current method, there is usually a market write-down at the end of the year on some of the by-products. The principal reason for rejection was the failure to include raw material cost in the inventory value of the by-product. The Service of course will recognize an allocation based on the relative sales values of the products, the method mentioned in the regulations. A method that allocates none of the pre-separation costs to the by-product will not be approved even though the principal product would be produced in any event, and even though income from sale of the by-product is sufficient to absorb only the costs incurred subsequent to the splitting-off of production.

As in most other aspects of inventory problems, where there has been a consistent use of a method that does not assign to by-products any of the cost before split-off, a taxpayer has strong support for its continued use. This would be particularly true when there is a general practice in the industry to allocate the pre-separation costs to the principal product only.

WHAT ARE INVENTORIES AT MARKET?

Once the cost of inventories has been determined, the next major problem, at least for most taxpayers, is to determine the market value so that it can be compared with cost in order to determine the lower figure to be used in the financial statement.

The general rule for determining market value is that it should be the replacement or bid price at the date of the inventory for the quantity normally purchased by the taxpayer. This is subject to two exceptions.

First, if goods have been offered for sale at prices lower than the current prevailing replacement prices, they may be valued at the prices at which offered for sale, less the direct cost of disposition. These prices should accord with actual prices during a reasonable period before and after the inventory date.

The other exception relates to goods that are subject to a firm fixed-price contract under which the taxpayer is protected against loss. In these cases, market value is considered to be equal to cost.

Contract Losses

On the other hand, where it is apparent that there will be a loss on a contract, even though the work may not have been completed, the Court of Appeals for the Fifth Circuit has held that there can be a write-down to market in the year in which the loss becomes apparent rather than after the last item has been delivered. The government attempted to contend that a write-down to market applies only to finished goods that have actually been offered for sale and not to goods in process. In an extremely well-reasoned decision, the Court upheld the taxpayer's write-down to market.

Bid Price

The bid price to be used is the one current in the taxpayer's own market and not a price existing in some distant market into which he would not normally be expected to enter.

Quoted market prices need not be used if it can be shown that they have been artifically determined or that transactions at different prices were completed outside the regular market in a volume equal to that of the transactions recorded for determining market prices. On the other hand, if market conditions at the end of the year are such that material can be obtained only by paying a premium, this premium market must be recognized. This could have real meaning in a year such as the current one in which a serious steel strike almost occurred. When a strike is prolonged and steel is in short supply, it may be necessary, in order to obtain a supply, to purchase steel at what are euphemistically referred to as "premium prices." If this condition exists at the year end, market value will include the premium.

Obsolete Goods

Special rules apply to damaged, imperfect, shopworn, or out-of-style goods, and to odd or broken lots. These are to be valued at bona fide selling prices less direct cost of disposition.

A point to be emphasized here is that the method of valuation is the same regardless of whether cost or the lower of cost or market is used in valuing normal goods. This should mean that a write-down should be permitted even though the LIFO method is used. However, the Internal Revenue Service has taken the position in at least one case that a write-down of LIFO inventories below cost, on the basis of their being obsolete or damaged, is not permissible.

The term "bona fide selling price" means the actual offering price during a period ending not later than thirty days after the inventory date. If literally applied, this requirement can cause problems for businesses such as used-car dealers. An artificially high trade-in value may be assigned to a car taken in trade and a real offering may not be made for some time. Revenue agents in some parts of the country have taken the position that the automobile cannot be written down to an amount lower than it has actually been offered for sale during the thirty-day period. The result may be an inventory valued at trade-in value. This does not seem correct. It would seem that blue-book or red-book prices should be good evidence, but careful records of the selling price of similar cars should be retained.

Write-Down by Items

Technically, write-downs to market are made for each item and not on an over-all basis. Actually, this is beneficial in that an item-by-item comparison of market with cost can result in a total inventory that is no more than it would be on an over-all basis and probably would be less. Of course, there are practical problems in applying and determining market on an item-by-item basis. Nevertheless, to the extent possible it should be done in order to avoid a possible contention that an arbitrary write-down has been used and that the inventory reported does not represent the market value of the entire inventory.

HOW ARE INVENTORY ITEMS IDENTIFIED?

In valuing inventory at cost we must, of course, know which items are being valued. There are three generally recognized methods for doing this.

Methods

First is specific identification. Each item in inventory is directly related to a particular acquisition. This method is, of course, impractical in most businesses of any size and, therefore, it has given way to methods that make assumptions concerning the inventory on hand. The two recognized approaches to these assumptions are the first-in/first-out, or FIFO, assumption and the last-in/first-out, or LIFO, assumption.

FIFO, of course, generally coincides most closely with the actual flow of goods. It was the method originally adopted by accountants and is still the most widely used. However, as prices increased, accountants came to realize that the FIFO method did not fully match costs currently being incurred with income currently being realized. It was on this basis that LIFO gradually came into more and more widespread use. It has been of substantial benefit to many taxpayers—those who were willing to make a decision at some point in time that prices of their inventory would continue to go up. Whether that conclusion is valid today is a question that each businessman must answer for himself. Because of the requirement for the use of LIFO that no write-downs to market are permitted, the decision is not an easy one. However, LIFO certainly is worth the consideration of any taxpayer.

LIFO In Bargain Purchases

I should like to point out, however, one particular situation in which the adoption of LIFO can be of great importance: It holds true when a large amount of inventory is obtained at a bargain, a frequent occurrence when a business is being sold out. If LIFO is adopted in the year of the bargain purchase, this low cost can be retained indefinitely in the inventory accounts and the higher replacement costs for current items can be used in determining taxable income.

When this approach is adopted, the election of the method for valuing increases in inventory must be made in a way that will cause the bargain acquisition to be included in the election. If a new corporation is formed to acquire the inventory and operate the acquired business, a short first year may be beneficial.

Different Methods for Different Businesses

In deciding on the method of identification to be used, it should be understood that different methods can be used for different businesses. Thus, in our bargain-purchase situation a separate division may be established for the newly acquired business and LIFO adopted for that business only. Similarly, a company may have different divisions for different businesses and may wish to value the inventory of one on the basis of cost and of another on the basis of the lower of cost or market.

Average Costs

As long ago as 1919, the Internal Revenue Service took the position that an average-cost inventory method is not in accordance with the Internal Revenue Code. The particular average under consideration was an over-all moving average that had been built up over several years. This was held to violate the annual accounting concept. While the original rulings related to an annual accounting problem, the Service, over the years has taken the position that either a specific identification method or a FIFO method must be used.

The exact extent to which averaging can be limited by the Service is not clear. It would seem a practical impossibility to compute a large inventory without using some averaging. Further, averaging procedures have been commonly used by many taxpayers in various industries and probably register income clearly in many cases. Nevertheless, until very recently the National Office has taken a very narrow approach. We now understand that a change in attitude is taking place in this area also, and that at least one taxpayer has had an average method approved in connection with a change to machine accounting.

CHANGES IN INVENTORY PRACTICE

We often have occasion to suggest the desirability of changes in accounting practices. In many cases, the suggested changes would have the effect of substantially increasing taxable income if they were made for tax as well as for book purposes. Before we suggest changes in accounting, or before we approve changes suggested by the client, it is important that we be cognizant of the tax effects of the changes and of the ways in which tax increases might be avoided or held to a minimum.

The whole accounting method area has been subject to confusion and uncertainty ever since enactment of the changes in 1954 that were supposed to clarify matters. This uncertainty is caused in large part by the extremely narrow approach taken in the regulations to the definition of an accounting method. The Treasury holds that it includes not only the taxpayer's over-all method of accounting but also his accounting treatment of any item. This refusal to recognize any degree of materiality in defining an accounting method was, of course, intended to give the Treasury control of all changes. Although for a long time there was a large body of opinion to the effect that the Treasury's definition was improper, it seems clear now that it will be upheld in the courts.

When the accounting practice concerned relates to a deduction item such as vacation pay or accrued real estate taxes, this narrow definition has worked to the Treasury's advantage. For example, the courts have upheld the right of the Commissioner to refuse to allow a change to accrue a portion of the taxpayer's vacation pay, holding that the treatment of only a portion of vacation pay nevertheless represented an accounting method.

When the change results in an increase in income, however, such as is normally true when the Commissioner attempts to change inventory methods, the narrow regulation definition works to the taxpayer's advantage. A good example of the benefit received from the narrow interpretation is found in the recent Fruehauf Trailer Company case. Here the taxpayer had established the practice of valuing used trailers at $1.00 each, even though their actual value was substantially in excess of $1.00. Although the facts in the case were especially favorable to the taxpayer in that the Service had previously required the use of the $1.00 amount, the decision nevertheless is regarded as of great importance by the Service.

The Service now realizes that if it forces a change in inventory practice, it may have to give up the tax on the pre-1954 accumulations. As a result, it has issued instructions to hold up cases concerning inventory practices that carry over from closed years. This, of course, has created more uncertainty and confusion on the part of taxpayers. The AICPA has suggested strongly that, in the light of the Fruehauf case, the Service take steps to establish procedures to clear up the log jam of inventory cases.

What are the difficulties the Service has if it forces a change? When a voluntary change is made, that is, one initiated by the taxpayer, all adjustments necessary to avoid the omission or duplication of income or deductions must be made. On the other hand, if the Service forces the taxpayer to make a change, only those adjustments attributable to post-1953 years need be considered. This means that if an erroneous inventory method was in use before 1954, the tax benefit of the error cannot be collected from the taxpayer.

Thus, it can easily be seen that care must be exercised to avoid a voluntary change. This can be a problem, particularly when an examining agent makes what is described as a suggestion to the taxpayer that certain practices be changed.

In one case, the revenue agent told the taxpayer's bookkeeper that, since the business maintained an inventory, the regulations require that the books be kept on the accrual basis and that a change must be made. The taxpayer had no knowledge of the tax consequences and relied on the statements of the agent. Under these circumstances, the change was held to be initiated by the Commissioner.

In other cases, however, the agents have merely suggested that the next year's return report income under an accounting method wherein inventories were to be utilized in full. The evidence did not lead to the conclusion that the agents pressured the taxpayers. Therefore, the changes made in the subsequent year were held to be initiated by the taxpayers and there was no exclusion of pre-1954 adjustments.

CONCLUSION

In summary, there are at least as many opportunities as problems in inventories. Do not become unduly alarmed about the problems Rather, keep the opportunities in mind.