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Tax Accounting

BY JAMES E. SALLES

This month's column presents the second half of a two-part discussion of Notice 2001-76,[1] which permits some smaller businesses to use the cash basis of accounting despite selling "merchandise."

JUDICIAL DEVELOPMENTS

As discussed in last month's column, the Regulations require a taxpayer to keep inventories and accrue purchases and sales if sales of "merchandise" are a "material income-producing factor" in its business. *Wilkinson-Beane* [2] and its immediate successors established that goods could be "merchandise" even if they were only sold as part of a package with accompanying services. Thereafter, there slowly evolved a variety of approaches to determining when the sale of merchandise was an "material income-producing factor" in cases where goods and services were provided together.

Comparing Costs to Receipts

The earliest and most straightforward approach was based on a numerical comparison. In holding merchandise to be a material income-producing factor, the court in *Wilkinson-Beane* had noted that the cost of caskets was approximately 15 percent of the taxpayer's gross revenues. In *Surtronics, Inc. v. Commissioner*,[3]the Tax Court rejected the taxpayer's argument that it should not have to accrue sales because material costs accounted for only 5 percent of its billings.More recently, the Tax Court described "comparison of the cost of the merchandise to the taxpayer's gross receipts computed under the cash method of accounting" as the "recognized standard" to be applied in determining whether sales of merchandise were a material income-producing factor in the taxpayer's business.[5]

For a time, there was little guidance as to what ratio of costs to receipts might suffice to make sales of merchandise a "material income-producing factor." The IRS evidently contemplated publishing some sort of safe harbor,[6] but never did. Some inferential guidance appeared in 1993 with the issue of the final uniform capitalization ("UNICAP") regulations.[7] These regulations included an exemption for "property provided incident to services" so long as the property was both "*de minimis* in amount" and "not inventory in the hands of the service provider." [8] The regulations provide that if the "acquisition or direct material cost of the property" does not exceed 5 percent of the taxpayer's total charges, then the property will be deemed "*de minimis* in amount."

Strictly speaking, the UNICAP regulations do not address the "material income-producing factor" inquiry. Indeed, they at least contemplate the possibility that property might be "*de minimis*" but nonetheless still be "inventory in the hands of the service provider." However, in a 1997 technical advice memorandum, the National Office concluded that merchandise sales were not a "material income-producing factor" in the business of a medical clinic despite purchases totalling roughly 8 percent of revenues (although this figure included non-"merchandise" materials and supplies).[9] In another ruling issued later the same year, the IRS allowed a landscaper to use the cash method despite materials purchases of roughly 3 percent, 3 percent, and 6 percent of sales in the three years at issue.[10] Taking the regulations together with the rulings, practitioners and commentators began to regard the 5 percent neighborhood as relatively safe.[11]

"Ephemeral" Goods: *Galedrige Construction* and *Turin*

Comparing the cost of goods with revenues, however, is only useful if the goods are merchandise in the first place. The IRS, following long-standing regulations prescribing what goods are included in inventory[12] took the position that all property that was transferred (or physically incorporated into something that was transferred)

Jim Salles is a member of Caplin & Drysdale in Washington, D.C.

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in the transaction was merchandise. Thus a dentist's anesthetics, crowns, bridges, and dentures, or a medical clinic's medicine, serum and bandages were "merchandise," whereas such items as syringes, gloves, and disposable towels fell under the heading of "materials and supplies."[13]

The courts, however, began to challenge the assumption that any property whose ownership might pass to a customer was necessarily "merchandise." In *Galedrige Construction, Inc.. v. Commissioner*,[14] and *Jim Turin & Sons v. Commissioner*,[15] the Tax Court held that paving contractors were not required to inventory their stocks of emulsified asphalt because it was not their "merchandise." Unlike in *Asphalt Products*, the taxpayers themselves laid the asphalt, and "sold" it only as part of a finished road surface.

Both the Tax Court and the Ninth Circuit emphasized that the useful life of emulsified asphalt was measured in hours — if not laid promptly when it was heated, it hardened and had to be discarded.[16] To the Ninth Circuit in *Turin*, the asphalt's "ephemeral" status was the critical factor, because it meant that "there is no inventory that can be purchased late in one tax year and held over to the next."[17] Thus, whether or not the asphalt might be in some sense "merchandise," it was not as a practical matter an inventoriable good. This reasoning enabled the court to distinguish both the "drop shipment" authorities following *Epic Metals* and the earlier contractor cases such as *J.P. Sheahan Co.* on the grounds that they all involved goods which "were or *could be* stored in inventory."[18] For example, the taxpayer in *Epic Metals could* have stored the metal decking in a warehouse while it awaited sale.

Beyond such materials as asphalt and liquid concrete,[19] the Ninth Circuit's analysis could call into question the IRS position that electricity is "merchandise,"[20] not to mention raising interesting (but unlikely to be litigated) questions about, for example, whether fast food chains are selling goods or a service. (Few fast food chains have much in the way of receivables to worry about.) However, the "ephemerality exception" has little application beyond such specialized situations because most materials are not incapable of being stored in usable form.

Osteopathic Medical

While the Ninth Circuit appeared to concentrate exclusively on the asphalt's "ephemeral" nature, the Tax Court was pursuing a broader distinction. Its reasoning appears most clearly in two reviewed decisions, *Osteopathic Medical Oncology and Hematology, P.C. v. Commissioner*,[21] and *RACMP Enterprises, Inc. v. Commissioner*.[22]

The question in *Osteopathic* was whether a cancer clinic's chemotherapy drugs were merchandise or supplies. The stage had been set in an earlier case, *Hospital Corp. of America v. Commissioner*,[23] which considered whether a hospital was selling services or providing goods when it furnished drugs and other items to its patients. The accrual requirement was not at issue in *Hospital Corp.* Through 1986, HCA had used a hybrid method under which it accrued purchases and sales, which the IRS had unsuccessfully tried to change to full-fledged accrual accounting.[24] Thereafter, Code Section 448 unquestionably required HCA to adopt an accrual method for all items of income and deduction. The issue concerned the application of Code Section 448(d)(5). That provision allows some taxpayers to avoid accruing accounts receivable "which (on the basis of experience) will not be collected," essentially providing a more tightly-constrained version of the old reserve for bad debts.[25] This "nonaccrual experience method," however, is confined to receivables from the sale of *services*, raising the question whether the hospital was selling goods, services, or both.

Many of hospital consumables are clearly supplies. The controversy before the court was how to classify items that found their way into, or on to, the patient in the course of medical treatment, such as casts, splints, sutures, skin staples, implants, and pacemakers as well as intravenous drugs.[26] The IRS contended that charges for such items represented proceeds from the sale of goods and were ineligible for the nonaccrual experience method under Code Section 448(d)(5). However, the court concluded that the medical supplies were "inseparably connected" to the services that HCA provided and therefore any income attributable to the supplies was still "income earned from the performance of services" that qualified for the nonaccrual experience method.

The court in *Hospital Corp.* did not have to decide whether the drugs were inventoriable "merchandise,"[27] but its reasoning strongly suggested that they were not. When the Tax Court faced the issue in *Osteopathic Medical*, it held the drugs were supplies, not merchandise, because they were "an integral, indispensable, and inseparable part of the rendering of medical serv-

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ices." The clinic's patients were buying a course of treatment, not a given quantity of drugs. The clinic did not, and indeed legally could not, furnish the drugs to the patients directly. After losing another memorandum case involving similar facts,[28] the IRS formally acquiesced in *Osteopathic Medical*. The acquiescence was only "in result," indicating disagreement with some aspects of the Tax Court's reasoning. However, the IRS did concede that "prescription drugs or similar items administered by healthcare providers" were not merchandise subject to inventory accounting, although the associated costs might still have to be capitalized under the rules for supplies.[29]

RACMP, Inc. v. Commissioner

RACMP was a reported and indeed reviewed opinion chronologically sandwiched between the memorandum holdings in *Galedrige* and *Turin*. The taxpayer in *RACMP* was a contractor that constructed driveways, sidewalks, and building foundations, a process that naturally required much sand, gravel, and poured concrete. The court held *Galedrige* squarely on point so far as the concrete was concerned: liquid concrete, like emulsified asphalt, has a useful life measured in hours, and much the same considerations apply. That left the other construction materials. Rock and steel are not ordinarily associated with ephemeral qualities, but the court held the other construction materials to be "indispensable and inseparable" to the services provided and consequently not inventory.[30]

The court held that construction contracts should be treated as contracts for services, as they are in a variety of nontax contexts. If a taxpayer is actually selling services, the court remarked, "the cost of the materials is substantial is insufficient to transmute the sale of a service to the sale of merchandise and a service."[31]

The court's focus was on the nature of the transaction between the taxpayer and its customer rather than on the property itself. One taxpayer's inventory may be another taxpayer's supplies. The court in *RACMP* noted that paper and ink could not be inventory to an architect, even if the architect supplied clients with physical blueprints, because the "essence" of the architect's services is designing buildings,[32] but paper and ink *is* inventory to a newspaper.[33] While a contractor like *RACMP* might properly treat asphalt that it buys for immediate use as "supplies," asphalt is inventory to a dealer.[34] Similarly, the drugs in *Osteopathic Medical* were presumably inventory to the pharmaceutical companies that sold them to the clinic.

This point was vividly illustrated when Judge Vazquez, who joined in the majority opinion in *RACMP*, reached the opposite result in a memorandum case released the following day. *Von Euw & L.J. Nunes Trucking, Inc. v. Commissioner*[35] involved a trucker that sold sand and gravel — much like some of the "materials" in *RACMP* — to contractors. However, the only services that the taxpayer provided in such cases was transportation. The sand and gravel was thus merchandise. Moreover, because the taxpayer reaped larger profits when it bought the sand and gravel itself and sold it on a delivered basis than it did when it merely transporting its customers' materials, its sale was a "material income-producing factor." Thus, the accrual requirement applied.[36]

Applying the "Triple Eye" Test: *Vandra Bros.* and *Smith*

The IRS' string of losses in the Tax Court continued with two more memorandum cases that further fleshed out *Osteopathic Medical*'s "integral, indispensable, and inseparable" standard, which one writer refers to as the "Triple Eye" test.[37] Under the Triple Eye test, the key factor distinguishing supplies consumed in the course of supplying a service from "merchandise" provided in conjunction with a service is that the "supply" cannot usefully be provided without the service, and vice-versa.

The *Osteopathic* court explained that earlier cases requiring contractors to use the accrual method, like *J.P. Sheahan Associates v. Commissioner*,[38] all involved situations where "customers of the taxpayer also could have personally purchased the merchandise elsewhere and either installed the merchandise themselves . . . or contracted with a third party." For example, no one questions that automobile parts are "merchandise" to a repair shop. While normally the repair shop will install the parts in customers' cars, car owners can buy replacement parts and install them themselves, and some do.

Vandra Bros. Construction Co. v. Commissioner,[39] involved a contractor that specialized in laying concrete in public sites such as city streets and sidewalks. While most of its materials cost represented liquid concrete, the taxpayer also bought stone, reinforcing steel, and other items as needed. The Tax Court found the facts essentially indistinguishable from *RACMP* and held that

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the taxpayer was entitled to continue to use the cash method.

Smith v. Commissioner[40] involved a flooring contractor that would procure materials (for example, tile) to the customer's specifications. The contractor charged its customers what it paid for the materials, plus a fee. While the taxpayer did not stock flooring, the volume acquired in connection with a given job could be substantial, and several months might elapse before it received payment. The taxpayer nonetheless maintained no inventories — apart from a constant capitalized amount of $15,000 — and reported income on the cash basis.

Relying principally on *RACMP*, the Tax Court held that the flooring was not merchandise because its sale was incidental to the taxpayer's installation business. The court read *RACMP* as holding not only that the "ephemeral qualities" of liquid concrete precluded its status as merchandise, but also more broadly that materials could not be "merchandise" when they "were incorporated into the particular project to such a degree that they lost their separate identity." As in *Osteopathic Medical* and *RACMP*, the court appeared to focus not so much on what the taxpayer was selling as what its customers were buying. After the transaction, the taxpayer's customers did not have a pile of tiles; they had a floor.

THE IRS RESPONSE

Pressure Builds for a "De Minimis" Rule

After *Vandra Bros.* and *Smith*, the IRS threw in the institutional towel, announcing that, pending further guidance, it would no longer press the issue of whether "construction contractors involved in paving, painting, roofing, drywall, and landscaping" are required to use accrual accounting because they sell "merchandise."[41] Indeed, it seems to have retreated from its litigation strategy on the whole "merchandise" question generally, stipulating successively to the dismissal with no or minimal deficiencies of pending Tax Court cases involving a paving contractor,[42] excavation contractor,[43] a building contractor with an "inventory" of bricks,[44] and even a slaughterhouse.[45]

The IRS had to take into account more than merely judicial developments. In the late 1990s, pressure had begun to build both on the IRS and in Congress to exempt small contractors, and other small businesses arguably selling property along with services, from the full rigors of accrual accounting. The issue achieved a higher profile on the Hill in part because of a revenue raiser slipped into the 1999 "extenders bill" that banned accrual taxpayers from using the installment method.[46]

The apparent intent was to target large, liquid publicly traded corporations that utilized the installment sales rules to defer tax on large, isolated capital transactions. However, the measure proved to have a larger-than-expected impact on small businesses, especially in the context of business dispositions. Many small businesses adopt accrual accounting because of the merchandise rule. After the 1999 amendment, if the sale of a business were structured as a disposition of assets by the corporation or other business entity, installment reporting would be unavailable and sellers could be taxed many years before they received the corresponding cash.[47]

The problem prompted hearings, and some lawmakers expressed the view that smaller businesses should be allowed to use the cash method regardless of whether they had inventories.[48] Congress eventually repealed the installment sales provision[49] without addressing the cash method issue. However, there remained interest in a more comprehensive "fix" of the rules governing sellers of merchandise, at least so far as they affected small taxpayers.

Even before the installment sales issue had come to the fore, Rep. Jim Talent (R-Mo.), Chairman of the House Small Business Committee, had introduced a bill to exempt sellers of merchandise with revenues under $5 million from the accrual requirement .[50] The counterpart Senate bill would also have permitted taxpayers to use the cash method if their cost of goods was less than 50 percent of revenues.[51] The Joint Committee staff simplification study included a similar proposal.[52] The legislative initiatives focused on the accrual requirement, evidently assuming that the cost of goods should be capitalized as supplies. However, the ABA Tax Section even suggested that outright expensing might be appropriate.[53]

Revenue Procedure 2000-22

The initial IRS response was Revenue Procedure 2000-22,[54] which was later refined in Revenue Procedure 2001-10.[55] Revenue Procedure 2000-22 generally allows taxpayers with average annual gross receipts of $1 million or less to use a modified version of the cash method, under which revenue from routine accounts receivable (due in 120 days or less) can be

deferred until the taxpayer is in receipt or constructive receipt of the cash. Other merchandise sales are reportable under Code Section 1001, which generally applies to sales of noninventory property.

Revenue Procedure 2000-22 also permits eligible taxpayers to opt out of inventory accounting. If inventories are not kept, then goods that would normally be inventoried must be treated as a "non-incidental" supplies under Regs. § 1.162-3, meaning that the associated costs must be capitalized. (Only "incidental" materials and supplied may sometimes be expensed.) However, the conventional inventory accounting and the uniform capitalization rules for inventories do not apply.

Revenue Procedure 2000-22 provides relief for most taxpayers that meet the $1 million threshold (computed under the rules applicable under Code Section 448). The revised procedure, however, added a specific exclusion for entities or arrangements that constitute "tax shelters" as defined under Code Section 448.[56] The referenced definition is broad, and can sweep in, for example, entities other than "C" corporations whose ownership interests offer limited liability and/or are registered under the securities laws.[57] Originally, relief had also been conditioned on a LIFO-style conformity requirement[58] requiring income to be reported to owners and creditors in the same manner as for tax, but the revised procedure eliminated this rule.

NOTICE 2001-76

Even after Revenue Procedure 2000-22 appeared, pressure continued for broader relief.[59] Proposals for a $5 million threshold were reintroduced in the new Congress.[60] Notice 2001-76 represents the IRS' attempt to address the demand for broader relief. With some minor wrinkles, the proposed revenue procedure incorporated in the Notice essentially expands the relief under Revenue Procedure 2000-22 to certain taxpayers with average annual gross receipts up to $10 million. While the procedure is in proposed form, the Notice provides that taxpayers may rely upon its terms for calendar 2001 and later years until further guidance is provided. The IRS has since followed up with an interim procedure providing automatic consent to necessary changes in accounting method.[61] Furthermore, the IRS promises not to disturb the taxpayer's method of accounting for past years if the taxpayer would have been eligible to use the cash method under the proposed procedure.[62]

Modified Cash Method Provided

As under Revenue Procedure 2000-22, taxpayers eligible for relief under Notice 2001-76 are allowed to report income from routine receivables (due in 120 days or less) on the cash method: that is, upon receipt or constructive receipt. Income from other receivables is reportable under Code Section 1001, which applies to sales or exchanges of non-inventory property. Except in "rare and unusual circumstances,"[63] Code section 1001 generally requires current reporting of gain measured by the "amount received" (cash plus the fair market value of property) minus the taxpayer's basis in the property given up. The interaction of this principle with the regulations governing transactions ineligible for the installment method[64] will frequently produce a result similar to accrual accounting, because the buyer's obligation to make payment will be considered "property" to be taken into account at its fair market value. Thus, as a practical matter, the cash method is largely confined to ordinary accounts receivable meeting the 120-day test.

Eligible taxpayers may also choose not to keep inventories and to treat what would otherwise be inventoriable "merchandise" as non-incidental "supplies" under Regs. § 1.162-3; that is, capitalize the associated costs until the supplies are used, or in this case sold. The ordinary inventory accounting rules will no longer apply to merchandise reclassified as supplies. In the case of traditional supplies, taxpayers are generally permitted some flexibility in determining the cost flow assumptions (*e.g.,* FIFO, LIFO, or average cost).[65] Likewise, any reasonable method may be used for merchandise treated as supplies under the proposed revenue procedure, so long as it is used consistently.[66]

There will still remain some difference in treatment between merchandise that the taxpayer treats as supplies under the proposed revenue procedure and items that are properly "supplies" under general tax principles. As noted above, the proposed revenue procedure applies Code Section 1001 to the proceeds of sales that fall outside the 120-day safe harbor. If the items were true supplies, presumably the whole transaction would be treated as the provision of services and Code Section 1001 would not be implicated at all. Similarly, the cost of reclassified merchandise must always be capitalized under the proposed revenue procedure, whereas it is sometimes possible to expense true "supplies" upon purchase "provided the taxable

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income is clearly reflected by this method."[67] However, these distinctions are likely to be significant only in relatively unusual circumstances.

Eligible Taxpayers

Taxpayers required to use an accrual method under Code Section 448 — generally, C corporations with average annual gross receipts above $5 million — cannot use the proposed revenue procedure. Other taxpayers with average annual gross receipts (computed on a similar basis) between $1 million and $10 million are eligible for relief if they meet any of several alternative rules.

- A taxpayer may use the revenue procedure for any of its businesses so long as the North American Industry Classification System (NAICS) code for its principal business activity (that is, the activity accounting for the largest proportion of its gross receipts) is *not* one of a specified group of "ineligible codes."Ineligible codes generally indicate core production or reselling operations: mining, manufacturing, wholesale and retail trade, and "information industries."[68]
- A taxpayer may also use the revenue procedure for any of its businesses, even if its principal business activity falls under an ineligible code, if that business activity consists of the provision of services or "the fabrication or modification of tangible personal property upon demand in accordance with customer design or specifications."[69] A taxpayer is not considered to be engaged in "the fabrication or modification of tangible personal property upon demand" if the customer merely chooses among pre-selected options or the modifications are minor.[70] For example, a sofa manufacturer that upholsters to suit would not fall under this exception, but a custom toolmaker would.[71]
- Even if a taxpayer is not eligible to use the revenue procedure for all of its businesses (because its principal business activity falls under an ineligible code and does not involve the provision of services or custom production), it may still use the procedure for one or more trades or businesses that, standing alone, would qualify for relief.[72] For example, a taxpayer that sells plumbing (ineligible), but does some installation work (the provision of services) can use the revenue procedure for the installation business if it qualifies as a separate trade or business.[73] The standard is the same as for determining whether the taxpayer has two or more "separate and distinct" trades or businesses entitled to use their own method of accounting.[74] A "complete and separable" set of books must be kept for each business.

1. 2001-52 I.R.B. 613.

2. 420 F.2d 352 (1st Cir. 1970).

3. 50 T.C.M. (CCH) 99 (1985).

4. *See also, e.g., Knight-Ridder Newspapers v. United States*, 743 F.2d 781, 790 (11th Cir. 1984) (noting a newspaper's costs of paper and ink exceeded 17% of revenues); *Von Euw & L.J. Nunes Trucking, Inc. v. Commissioner*, 79 T.C.M. (CCH) 1793, 1797 (2000) (merchandise cost at least 31% of revenues).

5. *Cross Oil Co. v. Commissioner*, 81 T.C.M. (CCH) 1682, 1685 (2001).

6. *See* Gen. Couns. Mem. 38288 (Feb. 21, 1980).

7. Reg. § 1.263A-1, 8482, 1993-2 C.B. 77, *superseding* Reg. § 1.263A-1T, T.D. 8131, 1987-1 C.B. 98, *amended by* T.D. 8148, 1987-2 C.B. 70

8. Reg. § 1.263A-1(b)(11).

9. TAM 9723006 (Feb. 7, 1997).

10. TAM 9808003 (Nov. 3, 1997).

11. *See, e.g.,* Raby and Raby, "Merchandise and Cash Method Taxpayers," 81 **Tax Notes** 1533 (Dec. 21, 1998), suggesting the critical threshold might be about 8%, citing TAM 9723006.

12. Reg. § 1.471-1.

13. PLR 9848001 (July 16, 1998); TAM 9723006 (Feb. 21, 1997).

14. 73 T.C.M. (CCH) 2838 (1997).

15. 75 T.C.M. (CCH) 2534 (1998), *aff'd*, 219 F.3d 1103 (9th Cir.2000).

16. *Galedrige*, 73 T.C.M. (CCH) at 2841, 2843; *Turin*, 75 T.C.M. (CCH) at 2535-36, 219 F.3d at 1105, 1107-09.

17. 219 F.3d at 1107.

18. 219 F.3d at 1109.

19. *See RACMP Enterprises v. Commissioner*, 114 T.C. 211, 225-27 (2000).

20. *See* IRS Industry Specialization Program Coordinated Issue Paper, "Customer Deposits," 1991-95 **IRS Positions** ¶ 175,785; PLR 9523001 (12/17/94).

21. 113 T.C. 376 (1999) (reviewed) *acq. in result*, 2000-23 I.R.B. 2.

22. 114 T.C. 211 (2000) (reviewed).

23. 107 T.C. 116 (1996).

24. *See Hospital Corp. of America v. Commissioner*, 71 T.C.M. (CCH) 2319 (1996).

25. Former Code § 166(c), *repealed by* Tax Reform Act of 1986, Pub. L. No. 99-514, § 805(a).

26. 107 T.C. at 123.

27. 107 T.C. at 143 n.18.

28. *Mid-Del Therapeutic Center, Inc. v. Commissioner*, 79 T.C.M. (CCH) 1875 (2000).

29. AOD 2000-05 (April 27, 2000).

30. 114 T.C. at 227-31.

31. 114 T.C. at 224.

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32. 114 T.C. at 224-25.

33. *See Knight-Ridder Newspapers v. United States*, 743 F.2d 781 (11th Cir. 1984).

34. *See Asphalt Products Co. v. Commissioner*, 796 F.2d 843 (6th Cir. 1986) *rev'd on another issue*, 482 U.S. 117(1987).

35. 79 T.C.M. (CCH) 1793 (2000).

36. 113 T.C. at 388.

37. Leo F. Nolan II, "Zen and the Cash Method," 87 **Tax Notes** 1771 (June 26, 2000).

38. 63 T.C.M. (CCH) 2842 (1992).

39. 80 T.C.M. (CCH) 125 (2000).

40. 80 T.C.M. (CCH) 701 (2000).

41. Chief Counsel Notice cc-2001-010 (Feb. 9, 2001); Tax Analysts Doc. No. 2001-4417; *see also* FSA 200125001 (Jan. 18, 2001) (recommending IRS not attempt to change drywall installer's accounting method).

42. *T.D. Whitton Construction, Inc. v. Commissioner*, Docket No. 5994-00 (2000) (petition available as Tax Analysts Doc. No. 2000-15699), *judgment per stipulation*, Aug. 29, 2000.

43. *A.D. Wilson, Inc. v. Commissioner*, Docket No. 5495-00 (2000) (petition available as Tax Analysts Doc. No. 2000-15698), *judgment per stipulation*, Feb. 5, 2001.

44. *Manor Concrete Construction Co. v. Commissioner*, Docket No. 9625-00 (Sept. 7, 2000), (petition available as Tax Analysts Doc. No. 2000-27270), *judgment per stipulation*, Apr. 23, 2001.

45. *DeYoung v. Commissioner*, Docket No. 8734-00 (2000), *judgment per stipulation*, Aug. 7, 2001.

46. Tax Relief Extension Act of 1999, Pub. L. No. 106-170, *codified at* I.R.C. § 453(a)(2).

47. *See* Notice 2000-26, 2000-17 I.R.B. 954 (Apr. 10, 2000), modified by Notice 2001-22, 2001-12, I.R.B. 911.

48. *See* "Mikrut Says Treasury Needs Time to Assess Cases Before Issuing Cash Method Guidance," Daily Tax Report, Apr. 6, 2000, at G-7; News Story, TNT Doc. 2000-10301 (Apr. 5, 2000).

49. Installment Tax Correction Act of 2000, Pub. L. No. 106-573, § 2(a), *repealing* former I.R.C. § 453(a)(2).

50. H.R. 2273, 106th Cong., 1st Sess. (June 17, 1999) by Messrs. Talent and English.

51. S. 2246, 106th Cong., 2d Sess. (Mar. 9, 2000) by Sens. Bond and Grassley.

52. JCS-3-01 "Study of the Overall State of the Federal Tax System and Recommendations for Simplification, Pursuant to Section 8022(3)(B) of the Internal Revenue Code of 1986," (Jt. Comm. Prt. Apr. 2001) ("2001 Simplification Study") VII.B at 328-32.

53. *See* Statement of Richard M. Lipton on behalf of the ABA Section of Taxation before the Senate Finance Committee, Apr. 26, 2001, *reprinted at* 617, 627-28 (Spring, 2001).

54. 2000-20 I.R.B. 1008.

55. 2001-2 I.R.B. 272.

56. Rev. Proc. 2001-10, § 3.

57. *See* I.R.C. § 448(a)(3), 461(i)(3), 1256(e)(3)(B).

58. *Cf.* I.R.C. § 472(c).

59. *See* Letter from Cong. Donald Manzullo (R-Ill.) to Joseph Mikrut, Tax Legislative Counsel (June 7, 2000) (Tax Analysts Doc. No. 2000-20507); W. Eugene Seago, "A New Revenue Procedure Makes the Cash Accounting Method More Available, But Does It Go Far Enough?" 93 J. Tax'n 12, 17 (July, 2000); Massey, "Practitioners Disappointed With New Cash Basis Revenue Procedure," 57 Daily Tax Highlights & Documents 906 (Apr. 28, 2000).

60. Cash Accounting for Small Business Act of 2001, H.R. 656, 107th Cong., 1st Sess. (Feb. 16, 2001), by Cong. Wally Herger (R-Ca.); Cash Accounting for Small Business Act of 2001, S. 336, 107th Cong., 1st Sess. (Feb. 14, 2001), by Sen. Christopher Bond (R-Mo.).

61. Notice 2002-14, 2002-8 I.R.B. 1.

62. Notice 2001-76, Prop. Rev. Proc. § 9.

63. *See* Reg. § 1.1001-1.

64. Reg. § 15A.453-1(d).

65. *See, e.g., Madison Gas & Electric Co. v. Commissioner*, 72 T.C. 521, 550-57 (1979), *aff'd on another issue*, 633 F.2d 512 (7th Cir. 1980) (utility's "inventories" of coal).

66. Notice 2001-76, Prop. Rev. Proc. 4.04.

67. Reg. § 1.162-3.

68. Notice 2001-76, Prop. Rev. Proc. § 4.01(1).

69. Notice 2001-76, Prop. Rev. Proc. § 4.01(2)-(3).

70. Notice 2001-76, Prop. Rev. Proc. § 4.01(3).

71. Notice 2001-76, Prop. Rev. Proc. § 6, Exs. 5-6.

72. Notice 2001-76, Prop. Rev. Proc. § 4.01(4).

73. Notice 2001-76, Prop. Rev. Proc. § 6, Ex. 3.

74. *See* Regs. § 1.446-1(d).