26 CFR 601.204: Changes in accounting periods and in methods of accounting.
(Also Part I, §§ 446, 471, 481)

Rev. Proc. 2014-48

SECTION 1. PURPOSE

This revenue procedure provides the exclusive procedures by which a taxpayer obtains the consent of the Commissioner under § 446(e) of the Internal Revenue Code to make certain changes within the retail inventory method to comply with final regulations under § 1.471-8 of the Income Tax Regulations.

SECTION 2. BACKGROUND

.01 Under § 1.471-8, a taxpayer may use the retail inventory method to compute the value of ending inventory at approximate cost (retail cost) or approximate lower of cost or market (retail LCM), by multiplying the retail selling prices of goods on hand at the end of the taxable year by a cost complement ratio. The cost complement is the value of beginning inventory plus the cost of purchases divided by the retail selling prices of beginning inventory and purchases. On August 15, 2014, the Internal Revenue Service (IRS) and Treasury Department published final regulations under § 1.471-8 (TD 9688) clarifying a taxpayer’s treatment of certain sales-based vendor allowances, margin protection payments, permanent markups and markdowns, and temporary markups and markdowns when determining the cost complement. The final regulations apply to taxable years beginning after December 31, 2014.

.02 The final regulations clarify that a taxpayer using the retail inventory method may not reduce the numerator of the cost complement by the amount of an allowance, discount, or price rebate that, under § 1.471-3(e), must reduce only cost of goods sold.

.03 The final regulations provide that a taxpayer using retail LCM generally may not reduce the numerator of the cost complement by the amount of an allowance, discount, or price rebate that is related to or intended to compensate for a reduction in the taxpayer's retail selling price of inventory (a margin protection payment).

.04 The final regulations clarify that a taxpayer using the retail inventory method generally must adjust the denominator of the cost complement for all permanent markups and markdowns, but may not reduce the denominator for temporary markups or markdowns. A taxpayer using retail LCM, however, generally does not adjust the denominator of the cost complement for markdowns.

.05 The final regulations provide an alternative method for a taxpayer using retail LCM to compute the cost complement by reducing the numerator by the amount of margin protection payments if the taxpayer also reduces the denominator of the cost complement by the amount of the reductions in retail selling price to which the margin protection payments relate (related markdowns).

.06 The final regulations provide a second alternative method for a taxpayer using retail LCM to account for margin protection payments when computing the cost complement. Under this method, a taxpayer that is able to determine the amount of its margin protection payments but cannot determine the amount of the related markdowns may compute the cost complement by reducing the numerator by the amount of margin protection payments and adjusting the denominator by the amount that, in conjunction with the reduction of the numerator, maintains what would have been the cost complement percentage before taking into account the margin protection payments and related markdowns.

.07 A taxpayer using one of the alternative methods described in sections 2.05 and 2.06 above must use that method for all cost complements.

.08 Sections 446(e) and 1.446-1(e)(2) state that, except as otherwise provided, a taxpayer must secure the consent of the Commissioner before changing a method of accounting for federal income tax purposes. Section 1.446-1(e)(3)(ii) authorizes the Commissioner to prescribe administrative procedures providing the limitations, terms, and conditions necessary to permit a taxpayer to obtain consent to change a method of accounting in accordance with § 446(e).

.09 Rev. Proc. 2011-14, 2011-1 C.B. 330, provides procedures for a taxpayer to obtain automatic consent of the Commissioner to change to a method of accounting described in the Appendix.

.10 Section 481(a) requires the adjustments necessary to prevent amounts from being duplicated or omitted when a taxpayer's taxable income is determined under a method of accounting different from the method used to determine taxable income for the preceding taxable year. *See* section 2.05(1) of Rev. Proc. 2011-14.

.11 When a change in method of accounting is made on a cut-off basis, in general, only the items arising on or after the beginning of the year of change are accounted for under the new method of accounting. *See* section 2.06 of Rev. Proc. 2011-14.

SECTION 3. SCOPE

This revenue procedure applies to a taxpayer using the retail inventory method that wants to change its method of accounting to comply with the final regulations under

§ 1.471-8.

SECTION 4. CHANGES IN METHOD OF ACCOUNTING

Rev. Proc. 2011-14 is modified to add new section 21.16 of the APPENDIX, to read as follows:

.16 *Retail inventory method.*

(1) *Description of change.* This change applies to a taxpayer using the retail inventory method that wants to make one of the following changes--

(a) From adjusting to not adjusting the numerator of the cost complement by the amount of an allowance, discount, or price rebate that is required under § 1.471-3(e) to reduce only cost of goods sold;

(b) From adjusting to not adjusting the denominator of the cost complement for temporary markups and markdowns;

(c) In the case of a retail LCM taxpayer:

(i) From adjusting to not adjusting the numerator of the cost complement by the amount of a margin protection payment;

(ii) From adjusting to not adjusting the denominator of the cost complement for permanent markdowns;

(iii) From using one method for computing the cost complement described in § 1.471-8(b)(3) to using a different method described in § 1.471-8(b)(3);

(d) In the case of a retail cost taxpayer, from not adjusting to adjusting the denominator of the cost complement for permanent markups and markdowns;

(2) *Certain scope limitations temporarily inapplicable*. The scope limitations in section 4.02 (1) through (4) and (7) of this revenue procedure do not apply for a taxpayer's first or second taxable years beginning after December 31, 2014.

(3) *Multiple changes*. A taxpayer that wants to make multiple changes under this section 21.16 of the APPENDIX for the same year of change should file a single Form 3115.

(4) *Manner of making change*. A taxpayer making a change under this section 21.16 of the APPENDIX for its first or second taxable year beginning after December 31, 2014 may use either a § 481(a) adjustment as provided in sections 5.03 and 5.04 of this revenue procedure or implement the change on a cut-off basis. If a cut-off basis is used, the change applies only to the computation of ending inventories after the beginning of the year of change. See section 2.06 of this revenue procedure for more information regarding a cut-off basis. A § 481(a) adjustment is neither permitted nor required if a change is made on a cut-off basis.

(5) *Designated automatic accounting method change number*. The designated automatic accounting method change number for changes in methods of accounting under section 21.16 of this APPENDIX is "204." *See* section 6.02(4) of this revenue procedure.

(6) *Ogden copy of Form 3115 required in lieu of national office copy*. A taxpayer changing its method of accounting under this section 21.16 of the APPENDIX must file a signed copy of its completed Form 3115 with the IRS in Ogden, UT, in lieu of filing the national office copy, no earlier than the first day of the year of change and no later than the date the taxpayer files the original Form 3115 with its federal income tax return for the year of change. *See* sections 6.02(3)(a)(ii)(B) (providing the general rules) and 6.02(7)(b) (providing the mailing address) of this revenue procedure.

(7) *Contact information*. For further information regarding a change under this section, contact Natasha M. Mulleneaux at 202-317-7007 (not a toll-free call).

SECTION 5. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 2011-14 is modified to add new section 21.16 to the APPENDIX.

SECTION 6. EFFECTIVE DATE

This revenue procedure is effective for taxable years beginning after December 31, 2014.

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Natasha M. Mulleneaux of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue procedure, contact Christopher Call at (202) 317-7007 (not a toll-free call).