Minus capital loss carryovers to postacquisition part year (i.e., carryovers of $19,000 from X 3/31/60 and $5,900 from Y 1959)	24,900	
		0
Carryover to Y 1962		5,000
Less:		
Y's 1962 net capital gain (computed without regard to any capital loss carryovers)	$12,000	
Minus capital loss carryovers to Y 1962 (i.e., carryovers of $600 from X 3/31/60 and $5,900 from Y 1959)	6,500	
		5,500
Carryover to Y 1963		0

(iv) *Y Corporation's 1960 loss.* The carryover to 1963 is $5,500, computed as follows:

Net capital loss		$6,000
Less:		
Y's preacquisition part year net capital gain computed under subparagraph (5) of this paragraph	$18,100	
Minus capital loss carryovers to preacquisition part year (i.e., carryover of $24,000 from Y 1959)	24,000	
		0
Carryover to Y's postacquisition part year		6,000
Less:		
Y's postacquisition part year net capital gain computed under subparagraph (5) of this paragraph	$18,400	
Minus capital loss carryovers to postacquisition part year (i.e., carryovers of $19,000 from X 3/31/60, $5,900 from Y 1959, and $5,000 from X 3/31/61)	29,900	0
		0
Carryover to Y 1962		6,000
Less:		
Y's 1962 net capital gain (computed without regard to any capital loss carryovers)	$12,000	
Minus capital loss carryovers to Y 1962 (i.e., carryovers of $600 from X 3/31/60, $5,900 from Y 1959, and $5,000 from X 3/31/61)	11,5000	
		$500
Carryover to Y 1963		5,500

(f) *Successive acquiring corporations.* An acquiring corporation which, in a transaction to which section 381(a) applies, acquires the assets of a distributor or transferor corporation which previously acquired the assets of another corporation in a transaction to which section 381(a) applies, shall succeed to and take into account, subject to the conditions and limitations of sections 1212 and 381, the capital loss carryovers available to the first acquiring corporation under sections 1212 and 381.

[T.D. 6552, 26 FR 1985, Mar. 8, 1961, as amended by T.D. 6867, 30 FR 15094, Dec. 12, 1965; T.D. 7728, 45 FR 72650, Nov. 3, 1980]

§ 1.381(c)(4)–1 Method of accounting.

(a) *Carryover requirement*—(1) *General rule.* (i) Section 381(c)(4) provides that, in a transaction to which section 381(a) applies, an acquiring corporation shall use the same method of accounting used by the distributor or transferor corporation on the date of distribution or transfer unless different methods of accounting were used on that date by several distributor or transferor corporations or by a distributor or transferor corporation and the acquiring corporation. If different methods of accounting were used, the acquiring corporation shall use the method or combination of methods of accounting adopted pursuant to this section.

(ii) The acquiring corporation shall take into its accounts the dollar balances of those accounts of the distributor or transferor corporation representing items of income or deduction which, because of its method of accounting, were not required or permitted to be included or deducted by the distributor or transferor corporation in computing taxable income for taxable years ending on or before the date of distribution or transfer. The acquiring corporation shall similarly take into its accounts the dollar balances of those accounts of the distributor or transferor corporation which represents reserves in respect of which the distributor or transferor corporation has taken a deduction for taxable years ending on or before the date of distribution or transfer. The acquiring corporation shall also take into its accounts the dollar balance of that account of the distributor or transferor corporation which represents a suspense account established by the distributor or transferor corporation under section 166(f)(4) in taxable years ending on or before the date of distribution or transfer. Items of income and deduction shall have the same character in the hands of the acquiring corporation as they would have had in the hands of the distributor or transferor corporation or corporations if no distribution or transfer had occurred. This section shall have no application to items of income or deduction, or dollar balances, to the extent they are attributable to assets or liabilities not distributed or transferred, and shall have no application to items the tax treatment of which is specifically provided for in other paragraphs of section 381(c). In the case of an obligation of the distributor or transferor corporation which is assumed by the acquiring corporation and which gives rise to a liability (within the meaning of paragraph (a)(4) of §1.381(c)(16)–1) after the date of distribution or transfer, the deductibility of such an item is determined under this section if it is not deductible under section 381(c)(16) and the regulations thereunder. The amount of the adjustments necessary to reflect a change in accounting method pursuant to this section, the manner in which they are to be taken into account, and the tax attributable thereto shall be determined and computed under section 481 and the regulations thereunder, subject to the rules provided in paragraphs (c) and (d) of this section. Where such change is a change from the accrual to the installment method by a dealer in personal property, section 453(c) and the regulations thereunder apply.

(2) *Rules of application.* For purposes of section 381(c)(4) and this section, the term *method of accounting* shall have the same meaning as that provided under section 446 and the regulations thereunder. This section shall not be construed as preventing the exercise of any election which may be made by the acquiring corporation without consent of the Commissioner, or preventing the application of section 269 or 482, or the regulations thereunder. For provisions defining the date of distribution or transfer, see paragraph (b) of §1.381(b)–1. See other paragraphs of section 381(c) and the regulations thereunder for other rules regarding the treatment of the carryover of certain items specifically enumerated therein. See §1.460–4(k) for rules relating to transfers of contracts accounted for using a long-term contract method of accounting in a transaction to which section 381 applies.

(b) *Conditions for continuation of methods of accounting*—(1) *No differences in methods of accounting.* If all the parties to a section 381(a) transaction used the same method of accounting on the date of distribution or transfer, the acquiring corporation shall continue to use such method of accounting, unless the acquiring corporation has obtained the consent of the Commissioner in accordance with paragraph (e) of §1.446–1 to use a different method of accounting. This subparagraph may be illustrated by the following examples:

Example 1. X Corporation and Y Corporation use the accrual method as their overall method of accounting. Both corporations have established a reserve for bad debts under section 166(c). Pursuant to elections made by each corporation, they are amortizing trademark and trade name expenditures over a 60-month period under section 177, expensing intangible drilling and development costs under section 263(c), and accruing real property taxes ratably under section 461(c). It is assumed that there are no other items to which paragraph (a) of this section might apply. Y Corporation acquires all of the assets of X Corporation in a transaction to which section 381(a) applies. On and after the date of distribution or transfer Y Corporation must continue, without further election, to use the same overall method of accounting and the same accounting treatment of the specified items, unless consent of the Commissioner is obtained in accordance with paragraph (e) of §1.446–1 to change the methods of accounting. Thus, Y Corporation shall carry over the balance in X Corporation's reserve for bad debts account, shall continue to amortize and deduct over the remaining portion of the 60-month period the unamortized portion of the trademark and trade name expenditures carried over from X Corporation, and shall continue the same treatment of intangible drilling and development costs and of real property taxes.

Example 2. M Corporation and N Corporation use the cash receipts and disbursements method of accounting. N Corporation acquires all of the assets and assumes all the obligations of M Corporation in a transaction to which section 381(a) applies. M Corporation, immediately prior to the transaction, is entitled to receive $10,000 for unbilled services performed, and has billed but not received payment for services performed in an amount of $20,000. It has received but not paid invoices amounting to $18,000, and has received services in the amount of $5,000 for which no invoices have been received. Since M Corporation and N Corporation are both on the cash receipts and disbursements method, N Corporation must continue to use that method, unless consent of the Commissioner is obtained in accordance with paragraph (e) of §1.446–1 to change its method of accounting. Accordingly, N Corporation must include in income when received the unrealized receivables of M Corporation and may deduct the payment of those obligations of M Corporation which would have been deductible by such corporation if paid by it. Thus, N Corporation shall treat as ordinary income the receipt by it of M Corporation's $30,000 of receivables, and may deduct upon payment the amount of M Corporation's $23,000 of payables which would have been deductible by it.

Example 3. S Corporation and T Corporation are both publishers and use the accrual method as their overall method of accounting. Both corporations have elected under section 455 to defer prepaid subscription income to the taxable years during which the liability to furnish the newspaper, magazine, or other periodical exists. T Corporation, in a transaction to which section 381(a) applies, acquires all the assets of S Corporation and assumes the liability of such corporation to furnish or deliver the newspaper, magazine, or other periodical. On and after the date of the transfer, T Corporation must continue, without further election, to use the accrual method as its over-all method of accounting and to defer prepaid subscription income under section 455, unless consent of the Commissioner is obtained in accordance with paragraph (e) of §1.446–1 to change the method of accounting. T Corporation shall carry over the closing balance of S Corporation's prepaid subscription income account. The principles in this example would be equally applicable if both corporations had been deferring prepaid subscription income under a method permitted by subsection (e) of section 455.

(2) *Separate businesses.* If, after the date of distribution or transfer, the trades or businesses of the parties to a transaction described in section 381(a) are operated as separate and distinct trades or businesses within the meaning of paragraph (d) of §1.446–1, then the method of accounting employed by the parties to the transaction on the date of distribution or transfer with respect to each trade or business shall be used by the acquiring corporation, unless the acquiring corporation has obtained the consent of the Commissioner in accordance with paragraph (e) of §1.446–1 to use a different method of accounting, or unless the Commissioner prescribes a different method of accounting under paragraph (b)(1) of §1.446–1. However, if only a single method of accounting may be employed by a taxpayer with respect to a particular item regardless of the number of separate and distinct trades or businesses operated by such taxpayer, but different methods were employed by the several corporations on the date of distribution or transfer with respect to such item, then the acquiring corporation shall adopt the principal method of accounting determined under paragraph (c) of this section (see subparagraph (2)(iv) thereof) for such item, or the method of accounting determined in accordance with paragraph (d) of this section, whichever is applicable. This subparagraph may be illustrated by the following examples:

Example 1. M Corporation is engaged in a personal service business and uses the cash receipts and disbursements method of accounting. N Corporation is engaged in a retail furniture business and uses the accrual method of accounting. N Corporation acquires the assets of M Corporation in a transaction to which section 381(a) applies. In accordance with paragraph (d) of §1.446–1, N Corporation operates as a separate and distinct trade or business the personal service business formerly operated by M Corporation. Unless consent of the Commissioner is obtained in accordance with paragraph (e) of §1.446–1 to change the method of accounting, N Corporation shall continue to use the cash receipts and disbursements method of accounting with respect to the personal service business formerly operated by M Corporation, and shall use the accrual method of accounting with respect to the retail furniture business.

Example 2. Assume the same facts as in *Example (1)*, except that M Corporation has elected under section 171 to amortize bond premium with respect to fully taxable bonds. N Corporation has not made the election to amortize bond premium with respect to such bonds owned by it. N Corporation may not continue separate accounting methods as to amortizable bond premium but must consistently apply only a single method of accounting with respect to such bond premium since the election to amortize bond premium applies to all fully taxable bonds held by the taxpayer. N Corporation shall use the principal method of accounting determined under paragraph (c) of this section for such bond premium, unless it is determined in accordance with paragraph (d) of this section that a different method of accounting is to be used. However, if such principal or different method of accounting is not to amortize bond premium N Corporation is not precluded from making a new election to the extent permitted by section 171.

(3) *Integrated businesses*. (i) If, after the date of distribution or transfer, any of the trades or business of the parties to a transaction in section 381(a) are not operated as separate and distinct trades or businesses within the meaning of paragraph (d) of §1.446–1, then, to the extent that the same methods of accounting were employed on the date of distribution or transfer by the parties to the transaction with respect to any trades or businesses which are integrated or are required to be integrated in accordance with section 446(d) and the regulations thereunder, the acquiring corporation shall continue to employ such methods of accounting, unless the acquiring corporation has obtained the consent of the Commissioner in accordance with paragraph (e) of §1.446–1 to use a different method of accounting, or unless the Commissioner prescribes a different method of accounting under paragraph (b)(1) of §1.446–1.

(ii) If, after the date of distribution or transfer, any of the trades or businesses of the parties to a transaction described in section 381(a) are not operated as separate and distinct trades or businesses within the meaning of paragraph (d) of §1.446–1, then, to the extent that different methods of accounting were employed on the date of distribution or transfer by the parties to the transaction with respect to any trades or businesses which are integrated or required to be integrated in accordance with section 446(d) and the regulations thereunder, this paragraph shall not apply and the acquiring corporation shall adopt the principal method of accounting determined under paragraph (c) of this section or the method of accounting determined in accordance with paragraph (d) of this section, whichever is applicable.

(iii) The provisions of this subparagraph may be illustrated by the following examples:

Example 1. M Corporation and N Corporation both use the accrual method as an overall method of accounting. M Corporation has established a reserve for bad debts while N Corporation uses the specific charge-off method with respect to its bad debts. N Corporation acquires all of the assets of M Corporation in a transaction to which section 381(a) applies and integrates the business formerly operated by M Corporation into the business operated by N Corporation before the date of distribution or transfer. N Corporation shall continue to use the accrual method as its overall method of accounting, unless consent of the Commissioner is obtained in accordance with paragraph (e) of §1.446–1 to change its method of accounting. N Corporation shall use the principal method of accounting determined under paragraph (c) of this section with respect to bad debts, or the method of accounting determined in accordance with paragraph (d) of this section, whichever is applicable.

Example 2. X Corporation conducts two separate and distinct trades or businesses, a personal service business with respect to which the cash receipts and disbursements method of accounting is used and a manufacturing business with respect to which the accrual method of accounting is used. Y Corporation conducts a manufacturing business and uses the accrual method of accounting. Y Corporation acquires all of the assets of X Corporation in a transaction to which section 381(a) applies. After the date of distribution or transfer, Y integrates the manufacturing business formerly operated by X Corporation into the manufacturing business operated by it and continues to operate as a separate and distinct trade or business the personal service business formerly operated by X Corporation. Unless consent of the Commissioner is obtained in accordance with paragraph (e) of §1.446–1 to change the method of accounting, Y Corporation shall continue to use the accrual method of accounting with respect to the integrated manufacturing business and shall continue to use the cash receipts and disbursements method of accounting with respect to the personal service business.

(4) *Rules of application*. In any case where the method of accounting employed on the date of distribution or transfer is continued, it will be unnecessary for the acquiring corporation to renew any election previously made by it or by any distributor or transferor corporation with respect to such method of accounting. Also, the acquiring corporation is bound by any election previously made by it or by any distributor or transferor corporation with respect to such method of accounting which is in effect on the date of distribution or transfer to the same extent as though the distribution or transfer had not occurred. If, on the

date of distribution or transfer, any party to a section 381(a) transaction had no established method of accounting for any item, or came into existence as a result of the transaction, such party shall not be considered to be using a method of accounting for such item or having an overall method of accounting different from that used by the other parties to the transaction. Where under other sections of the Internal Revenue Code or regulations thereunder a taxpayer is permitted to elect a method of accounting on a project-by-project, job-by-job, or other similar basis (such as the election to charge taxes and carrying charges to capital account under § 1.266–1), that method elected with respect to each project or job shall be deemed to be an established method of accounting only for the project or job for which it is elected. Accordingly, unless two or more of the parties were working on the same project or job and were using different methods of accounting for such project or job before the date of distribution or transfer, the method of accounting previously elected for each project or job must be continued.

(c) *Change of method of accounting without consent of Commissioner*—(1) *General rule.* If the acquiring corporation may not continue to use, under the provisions of paragraph (b) of this section, the method of accounting used by it or the distributor or transferor corporation or corporations on the date of distribution or transfer, the acquiring corporation shall use the principal method of accounting of such corporation (as determined under subparagraph (2) of this paragraph), provided that (i) such method of accounting clearly reflects the income of the acquiring corporation, and (ii) the use of such method is not inconsistent with the provisions of any closing agreement entered into under section 7121 and the regulations thereunder. If the principal method of accounting does not meet these requirements, or if there is no principal method of accounting, see subdivision (i) of paragraph (d)(1) of this section. If the acquiring corporation wishes to use a method of accounting other than the principal method of accounting, see subdivision (ii) of paragraph (d)(1) of this section. Whenever this paragraph applies, the increase or decrease in tax resulting from the change from the method of accounting previously used by any of the corporations involved shall be taken into account by the acquiring corporation. The adjustments necessary to reflect such change and such increase or decrease in tax shall be determined and computed in the same manner as if on the date of distribution or transfer each of the several corporations whose method or methods of accounting are required to be changed in accordance with this section had initiated a change in accounting method. In addition, the acquiring corporation shall take into account the portion of such adjustments which is attributable to pre-1954 Code years to the extent not taken into account by any of the other corporations in accordance with the rules provided in section 481(b)(4) and this paragraph. If the principal method of accounting is adopted under this paragraph, it will be unnecessary for the acquiring corporation to renew any election previously made by it or by any distributor or transferor corporation with respect to such principal method of accounting. Also, in such event, the acquiring corporation is bound by any election previously made by it or by any distributor or transferor corporation with respect to such principal method of accounting which is in effect on the date of distribution or transfer to the same extent as though the distribution or transfer had not occurred.

(2) *Principal method of accounting.* (i) The determination of the principal method of accounting shall be made with respect to each integrated trade or business operated by the acquiring corporation immediately after the date of distribution or transfer, except with respect to items for which only a single method of accounting may be used by any one taxpayer. See subdivision (iv) of this subparagraph. Such determination for an integrated trade or business shall be made by reference to the methods of accounting used immediately preceding the date of distribution or transfer by each of the component trades or businesses which now constitute the integrated trade or business of the acquiring corporation. The

method of accounting for items other than those for which special methods of accounting are provided under chapter 1 of the Code and the regulations thereunder (see §1.446–1(c)(1)(iii)) shall be governed by the principal overall method determined for such trade or business under subdivision (ii) of this subparagraph. The method of accounting for items for which special methods of accounting are provided under chapter 1 of the Code and the regulations thereunder shall be determined under subdivision (iii) of this subparagraph.

(ii) The principal overall method of accounting of an integrated trade or business is determined by making a comparison of—

(*a*) The total of the adjusted bases of the assets (determined under section 1011 and the regulations thereunder) immediately preceding the date of distribution or transfer, and

(*b*) The gross receipts for a representative period (ordinarily the most recent period of 12 consecutive calendar months ending on or prior to the date of distribution or transfer)

of the component trades or businesses which are integrated or are required to be integrated. If more than one component trade or business used the same overall method, then such total assets and gross receipts of each of the component trades or businesses shall be aggregated and compared with the aggregate of such total assets and gross receipts of other component trades or businesses which used a different overall method. If this comparison shows that the one or more component trades or businesses (using a common overall method of accounting) having the greatest total of the adjusted bases of assets also has the greatest amount of gross receipts, then the overall method of accounting of such one or more component trades or businesses shall be the principal overall method of accounting. If this comparison shows that the one or more component trades or businesses (using a common overall method of accounting) having the greatest total of the adjusted bases of assets does not also have the greatest amount of gross receipts, then there is no principal overall method of accounting, and the acquiring corporation shall request the Commissioner to determine the appropriate overall method of accounting for such integrated trade or business in accordance with paragraph (d) of this section.

(iii) The principal method of accounting for an item for which a special method or methods of accounting are provided under chapter 1 of the Code and the regulations thereunder is determined by comparing the amounts of such item and related accounts for the component trades or businesses in accordance with the principles of subdivision (ii) of this subparagraph. Thus, for example, in the case of bad debts, trades or businesses which are components of the integrated trade or business and which had been using the reserve method of accounting will be compared with the other component trades or businesses which had been using the specific charge-off method of accounting. In such a case, the following factors would ordinarily be used in determining the principal method of accounting for bad debts: (*a*) Sales on account for the most recent period of 12 consecutive calendar months ending on or prior to the date of distribution or transfer, (*b*) accounts receivable immediately before the date of distribution or transfer, and (*c*) the amount of debts which became worthless within the meaning of section 166(a) and the regulations thereunder during the most recent period of 12 consecutive calendar months ending on or prior to the date of distribution or transfer. If this comparison shows that the one or more component trades or businesses using the same method of accounting with respect to bad debts have the greater amounts of such sales, accounts receivable, and bad debts, then the method of accounting with respect to bad debts for such one or more component trades or businesses shall be the principal method of accounting. If such comparison shows that the one or more component trades or businesses using the same method of accounting with respect to bad debts do not have the greater amounts of all of such items, then there is no principal method of accounting with respect to bad debts, and the acquiring corporation shall request the Commissioner to determine the appropriate method of accounting for bad debts for such integrated trade or business in accordance with paragraph (d) of this section.

(iv) If a single method of accounting must be employed by a taxpayer with respect to a particular item regardless of the number of separate and distinct trades or businesses operated by the taxpayer, the principal method of accounting for such item shall be determined by comparing the aggregate amount of the item and related accounts for all the parties to the transaction using a common method, with the aggregate amount of the item and related accounts for those parties to the transaction which use a different common method. The method of accounting of the party having the greatest aggregate amount of such item and related accounts shall be the principal method of accounting for such item.

(3) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

Example 1. M Corporation, which commenced business in 1955, uses the cash receipts and disbursements method of accounting, while N Corporation uses the accrual method. On June 30, 1961, N Corporation acquires all of the assets of M Corporation in a transaction to which section 381(a) applies. N Corporation then integrates its own business with that of M Corporation. Immediately prior to the transfer the total of the adjusted bases of the assets of N Corporation was greater than that of M Corporation, and for the 12-month period ending on June 30, 1961, the gross receipts of N Corporation were greater than that of M Corporation. Under such circumstances, the accrual method of accounting is the principal overall method of accounting and N Corporation shall use such method for the integrated business, provided it clearly reflects income, unless consent of the Commissioner is obtained in accordance with paragraph (d) of this section to use a different method of accounting. Except as to items for which N Corporation had no established method of accounting and items for which a special method of accounting is provided under chapter 1 of the Code and the regulations thereunder, all adjustments necessary to place the accounts of M Corporation on the accrual method shall be made in accordance with section 481. Any increase or decrease in tax resulting from such adjustments shall be taken into account by N Corporation. Such adjustments and such increase or decrease in tax shall be determined and computed in the same manner as if M Corporation had initiated a change in method of accounting on June 30, 1961.

Example 2. Assume the same facts as in *Example (1)* except that the gross receipts of M Corporation were greater than those of N Corporation for the 12-month period ending on June 30, 1961. N Corporation must, under such circumstances, request the Commissioner to determine the appropriate overall method of accounting, in accordance with the provisions of paragraph (d) of this section. The necessary adjustments to be made by the corporation whose method of accounting is changed shall be made in accordance with section 481 to place the integrated business on the method so adopted. Any increase or decrease in tax resulting from such adjustments shall be taken into account by N Corporation. Such adjustments and such increase or decrease in tax shall be determined and computed in the same manner as if the corporation whose method is changed had initiated a change in method of accounting on June 30, 1961.

Example 3. Assume the same facts as in *Example (1).* Assume further that M Corporation's deduction for wages and salaries for the 12 calendar months ending on June 30, 1961, is larger than N Corporation's deduction for wages and salaries for such period. Since wages and salaries is not an item for which a special method of accounting is provided under chapter 1 of the Code or the regulations thereunder, the necessary adjustments shall be made in accordance with section 481 to place the wages and salary account of M Corporation on the accrual method of accounting, provided such accrual method clearly reflects income, unless consent of the Commissioner is obtained in accordance with paragraph (d) of this section to use a different method of accounting. Any increase or decrease in tax resulting from such adjustments shall be taken into account by N Corporation. Such adjustments and such increase or decrease in tax shall be determined and computed in the same manner as if M Corporation had initiated a change in method of accounting on June 30, 1961.

Example 4. Assume the same facts as in *Example (1).* Assume further that M Corporation used the specific charge-off method with respect to bad debts, and that N Corporation has established a reserve for bad debts. M Corporation's sales on account and bad debts for the 12 calendar months ending June 30, 1961, were larger than those of N Corporation. Also M Corporation's accounts receivable immediately prior to June 30, 1961, were larger than those of N Corporation. Since the method of accounting for bad debts is a special method of accounting under section 166, M Corporation's method of accounting for bad debts is the principal method of accounting for such item. Assuming such method clearly reflects income, appropriate adjustments shall be made in accordance with section 481 to the accounts of N Corporation to place N Corporation on the specific charge-off method with respect to all of its bad debts, as if N Corporation had initiated a change in method of accounting on June 30, 1961, and N Corporation shall include the amount of its reserve for bad debts in gross income, unless consent of the Commissioner is obtained in accordance with paragraph (d) of this section to use a different method of accounting.

Example 5. Assume the same facts as in *Example (1)* except that M Corporation commenced business in 1945. In addition assume that N Corporation is a calendar-year taxpayer and that of the total amount of the adjustments required by section 481 to place the accounts of M Corporation on the accrual method $40,000 is attributable to pre-1954 Code years as described in section 481(b)(4) and the regulations thereunder. Assume further that M Corporation does not elect, under section 481(b)(6), to take the $40,000 portion of the adjustments into account in the manner described in section 481(b)(1) or (2). In computing the increase in tax of M Corporation attributable to the $40,000 portion of the adjustment for the fiscal year ended June 30, 1961, only one-tenth, or $4,000, will be taken into account. The resulting increase in tax shall be taken into account by N Corporation. The remaining nine-tenths of the $40,000 portion of the adjustments, or $36,000, shall be taken into account by N Corporation in the amount of $4,000 in each of the calender years 1962 through 1970.

(d) *Change of method of accounting with consent of Commissioner*—(1) *General rule.* (i) If the acquiring corporation may not continue to use, under paragraph (b), the method of accounting used by it or the distributor or transferor corporation or corporations on the date of distribution or transfer, and may not under paragraph (c) use the principal method of accounting, or, if there is no principal method of accounting, then the Commissioner shall determine the appropriate method or combination of methods of accounting to be used.

(ii) If an acquiring corporation wishes to use a method or combination of methods of accounting other than the principal method of accounting which is required to be used by paragraph (c) of this section, it shall apply to the Commissioner for permission to use such other method or combination of methods of accounting. Permission to use such other method or combination of methods of accounting will not be granted unless the acquiring corporation and the Commissioner agree to the terms, conditions, and adjustments under which the change to such method or combination of methods will be effected.

(iii) The increase or decrease in tax resulting from the change from the method of accounting previously used by any of the corporations involved shall be taken into account by the acquiring corporation. The adjustments necessary to reflect such change and such increase or decrease in tax shall be determined and computed in the same manner as if, on the date of distribution or transfer, each of the several corporations that were not using the method or combination of methods of accounting adopted pursuant to subdivision (i) or (ii) of this subparagraph had initiated a change in accounting method.

(2) *Time and manner of making application.* Applications under subparagraph (1) of this paragraph for permission to use a method of accounting or requests for determination of the method of accounting to be used shall be filed with the Commissioner of Internal Revenue, Attention: T:R, Washington, DC, 20224, not later than 90 days after the date of distribution or transfer, except that in cases where the date of distribution or transfer occurs before August 5, 1964, such applications or requests shall be filed not later than November 3, 1964. The application shall be accompanied by a copy of the statement described in paragraph (b)(3) of §1.381(b)–1, and by a statement specifying the nature of the transaction which causes section 381 to apply; the difference in accounting methods used by the corporations concerned; the method or methods of accounting proposed to be used by the acquiring corporation; and the various amounts, if any, of items of income or deduction which will be duplicated or omitted in the computation of taxable income under such proposed method or methods. The Commissioner may also require such other information as may be necessary in order to determine the appropriate method or combination of methods of accounting to be used by the acquiring corporation.

(e) *Special rules applicable to distributions or transfers before August 5, 1964*—(1) *Statute of limitations bars assessment* *or refund.* If the date of distribution or transfer was before August 5, 1964, and if the assessment of any deficiency or the refund or credit of any overpayment for the taxable year of the acquiring corporation which includes the date of distribution or transfer or any subsequent taxable year is prevented by the operation of any law or rule of law, then this section does not authorize the Commissioner or the acquiring corporation to change any method or methods of accounting in any taxable year of the acquiring corporation. However, the Commissioner or the acquiring corporation may change such method or methods of accounting under the provisions of section 446 and the regulations thereunder or, where applicable, any section of the Internal Revenue Code (other than section 381(c)(4)), or the regulations thereunder, in accordance with which such changes may be made without the consent of the Commissioner.

(2) *Statute of limitations does not bar assessment and refund.* Except as provided in subparagraph (1) of this paragraph—

(i) If the date of distribution or transfer was before August 5, 1964, and the acquiring corporation has, for the taxable year which includes the date of distribution or transfer, (*a*) adopted or continued a method of accounting consistent with the rules of this section, (*b*) been granted permission by the Commissioner in accordance with paragraph (e) of §1.446–1 to use a method or combination of methods of accounting, or (*c*) adopted a method of accounting that under other sections of the Internal Revenue Code, or regulations thereunder, may be adopted without the consent of the Commissioner, then the method or methods of accounting adopted or continued in the manner described in (*a*), (*b*), and (*c*) shall not be changed, by reason of the rules contained in this section, by the Commissioner or the acquiring corporation for any taxable year ending after the date of distribution or transfer. However, the Commissioner or the acquiring corporation may change such methods of accounting for any such taxable year under the provisions of, and to the extent permitted by, section 446 and the regulations thereunder or, where applicable, any section of the Internal Revenue Code (other than section 381(c)(4)), or regulations thereunder, in accordance with which such change may be made without the consent of the Commissioner.

(ii) If the date of distribution or transfer was before August 5, 1964, and the acquiring corporation has, for the taxable year which includes the date of distribution or transfer, adopted or continued a method or methods of accounting other than in the manner described in (*a*), (*b*), and (*c*) of subdivision (i) of this subparagraph, then the acquiring corporation may—

(*a*) Continue to use the method or methods of accounting so adopted or continued if such method or methods clearly reflect income and if proper adjustments were made to reflect the adoption of such method or methods, or

(*b*) Adopt the method or methods of accounting prescribed by this section. Such method or methods of accounting shall be adopted by filing an amended return (which includes the proper adjustments required by this section) for the taxable year of the acquiring corporation which includes the date of distribution or transfer, and by filing amended returns for all subsequent taxable years of the acquiring corporation for which returns have previously been filed. Such amended return or returns shall be accompanied by a copy of the statement described in paragraph (b)(3) of §1.381(b)–1, and by a statement specifying the nature of the transaction which causes section 381 to apply; the difference in accounting methods used by the corporations concerned; the method or methods of accounting originally adopted by the acquiring corporation; the method or methods of accounting adopted on the amended return or returns; and the computation of the amount of the adjustments and the resulting increase or decrease in tax.

[T.D. 6750, 29 FR 11263, Aug. 5, 1964, as amended by T.D. 8071, 51 FR 2481, Jan. 17, 1986; T.D. 8995, 67 FR 34605, May 15, 2002]

§ 1.381(c)(5)–1 Inventories.

(a) *Carryover requirement*—(1) *General rule.* Section 381(c)(5) provides that in a