or in part, or that the public interest so requires.

(1) This requirement shall not be deemed satisfied if a request is merely conclusory or otherwise fails to set forth by affidavit(s) specific facts demonstrating in detail:

(i) The nature of the changed conditions and the reasons why they require the requested modifications of the rule or order; or

(ii) The reasons why the public interest would be served by the modification.

(2) Each affidavit shall set forth facts that would be admissible in evidence and shall show that the affiant is competent to testify to the matters stated therein. All information and material that the requester wishes the Commission to consider shall be contained in the request at the time of filing.

* * * * *

By direction of the Commission.

Donald S. Clark,

Secretary.

[FR Doc. 00–21185 Filed 8–18–00; 8:45 am]

BILLING CODE 6750–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

18 CFR Parts 125 and 225

[Docket No. RM99–8–000; Order No. 617]

Preservation of Records of Public Utilities and Licensees, Natural Gas Companies, and Oil Pipeline Companies

Issued August 15, 2000.

AGENCY: Federal Energy Regulatory Commission

ACTION: Final rule; correction.

SUMMARY: The Federal Energy Regulatory Commission published in the **Federal Register** of August 7, 2000, a final rule amending its records retention regulations for public utilities and licensees, natural gas companies, and oil pipeline companies (''regulated companies''). The Commission inadvertently omitted a cross reference in the schedule of records and periods of retention in Parts 125 and 225. The Commission also did not revise a record retention period in § 225.3 that it had agreed to do in the final rule's preamble language. This document corrects these omissions.

EFFECTIVE DATE: These corrections are effective on August 21, 2000.

FOR FURTHER INFORMATION CONTACT: Mary C. Lauermann, Office of Finance, Accounting and Operations, 888 First Street, N.E., Washington, DC 20426, (202) 208–0087.

SUPPLEMENTARY INFORMATION: The Federal Energy Regulatory Commission published a final rule in the **Federal Register** of August 7, 2000 (65 FR 48148). The following corrections are made to the final rule.

§ 125.3 [Corrected]

1. On pages 48157–48159 in § 125.3, in the second column of the table, add the phrase ''See § 125.2(g).'' after the years shown for the following item numbers: Item No. 8(b)(1); Item No. 10; Item No. 11(a), (b) and (d); Item No. 12(b); Item No. 13.1(c)(1) and (c)(2); Item No.16(a) and (b); Item No. 25(a)(1) and (b); and Item No. 27.

§ 225.3 [Corrected]

2. On pages 48162–48165 in § 225.3, in the second column of the table, add the phrase ''See § 225.2(g).'' after the years shown for the following item numbers: Item No. 8(b)(1); Item No. 10; Item No. 11(a), (b) and (d); Item No. 12(b); Item No. 16(a) and (b); Item No. 25(a)(1) and (b); and Item No. 27.

3. On page 48165, also in § 225.3, in the second column for Item No. 31, remove the words ''7 months.'' and add in their place the words ''1 year.''

David P. Boergers,

Secretary.

[FR Doc. 00–21147 Filed 8–18–00; 8:45 am]

BILLING CODE 6717–01–U

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 8897]

RIN 1545–AQ91

Rules for Property Produced in a Farming Business

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the application of section 263A of the Internal Revenue Code to property produced in the trade or business of farming. These regulations also provide guidance regarding the election available to certain taxpayers to not have section 263A apply to any plant produced by the electing taxpayers in each taxpayer's farming trade or business. These regulations affect taxpayers engaged in the trade or business of farming.

DATES: *Effective Date:* These regulations are effective August 21, 2000.

Applicability Date: For dates of applicability, see § 1.263A–4(f) of these regulations.

FOR FURTHER INFORMATION CONTACT: Grant D. Anderson, (202) 622–4970 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

Background

On March 30, 1987, the IRS published in the **Federal Register** a notice of proposed rulemaking (REG–208151–91) (52 FR 10118) by cross reference to temporary regulations published the same day (TD 8131, 52 FR 10052). Amendments to the notice of proposed rulemaking and temporary regulations were published in the **Federal Register** on August 7, 1987, by a notice of proposed rulemaking (52 FR 29391) that cross referenced to temporary regulations published the same day (TD 8148, 52 FR 29375). Notice 88–24 (1988–1 C.B. 491), provided that forthcoming regulations would modify the proposed regulations and the regulations under § 1.471–6. Notice 88–86 (1988–2 C.B. 401), provided that forthcoming regulations would clarify the definition of *members of family* for purposes of the election out of section 263A. In addition, Notice 88–86 provided that forthcoming regulations would provide that certain taxpayers could elect to use the simplified production method for property used in the trade or business of farming. On August 5, 1994, the temporary regulations relating to property produced in a farming business were reissued and published in the **Federal Register** (TD 8559, 59 FR 39958). On August 22, 1997, proposed and revised temporary regulations were issued and published in the **Federal Register** (TD 8729, 62 FR 44542). A public hearing was held on November 19, 1997.

Written comments responding to the notice of proposed rulemaking were received. After consideration of all the public comments, the regulations are adopted as revised by this Treasury decision and the corresponding temporary regulations are withdrawn.

Explanation of Provisions and Summary of Comments

Section 263A provides uniform capitalization rules that govern the treatment of costs incurred in the production of property or the acquisition of property for resale. Section 263A generally requires

taxpayers to capitalize the direct costs and an allocable portion of indirect costs of producing property in a farming business (including both plants and animals). However, taxpayers that are neither required to use an accrual method by section 447 nor prohibited by section 448(a)(3) from using the cash receipts and disbursements method (qualified taxpayers) are eligible for two exceptions provided in section 263A(d). First, under section 263A(d)(1), section 263A does not apply to a qualified taxpayer's cost of producing plants with a preproductive period of two years or less or animals in a farming business. Second, pursuant to section 263A(d)(3), a qualified taxpayer may elect to have section 263A not apply to the cost of producing plants in a farming business.

Property Produced in a Farming Business

Consistent with sections 263A(d)(1)(A) and 263A(d)(3)(A), the proposed regulations provided that the special rules of section 263A(d) apply only to property produced by a taxpayer in a farming business. The term *farming business* means the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity. Examples include operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than 6 years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals.

The proposed regulations explained that taxpayers engaged in contract harvesting, reselling of plants or animals that are not produced by the taxpayer, and processing that is not incident to growing, raising, or harvesting of agricultural or horticultural commodities, are not producing property in a farming business. Several commentators requested that the final regulations permit some of these taxpayers to use the special rules of section 263A(d). However, sections 263A(d)(1)(A) and 263A(d)(3)(A) limit the special rules of section 263A(d) to property *produced* by the taxpayer in a farming business. As discussed below, the IRS and Treasury Department continue to believe that taxpayers that merely contract harvest, resell plants or animals that they do not raise or grow, or engage in processing agricultural or horticultural commodities that is not incident to growing, raising, or harvesting of these commodities, are not producing property in a farming business and therefore do not meet this requirement. Accordingly, the final regulations do not adopt these suggestions.

The proposed regulations provided that, for purposes of the definition of farming business, harvesting, does not include contract harvesting of an agricultural or horticultural commodity that is not grown or raised by the taxpayer. Some commentators were concerned that this language may be used to disqualify otherwise legitimate farmers who make arrangements with their neighbors to harvest each others crops. First, the IRS and Treasury Department believe that whether and to what extent a taxpayer is engaged in a farming business is to be determined based on all the facts and circumstances. No inference is intended that merely because a taxpayer engages in nonfarm activities, such as contract harvesting, in addition to farm activities, that such taxpayer is not engaged in a farming business. Further, the exception under section 263A(d) is relevant only to taxpayers whose costs are otherwise subject to capitalization under section 263A. Thus, for example, while taxpayers that grow plants are generally subject to section 263A with respect to that production activity, taxpayers that contract harvest horticultural commodities are not, because they are engaged in a service activity. A taxpayer that harvests crops grown by the taxpayer and contract harvests crops grown by another is subject to section 263A (and the exception contained in section 263A(d)), but only for the costs of harvesting its own crops. Accordingly, the final regulations do not adopt the commentators' suggestion to include contract harvesting in the special rules of section 263A(d).

Similarly, the proposed regulations provided that the special rules of section 263A(d) do not apply to a taxpayer that merely buys and resells plants or animals grown or raised by another taxpayer. The preamble to the proposed regulations indicated that in evaluating whether the taxpayer is engaged in the production, or merely the resale, of plants or animals, it is anticipated that consideration will be given to factors including: the length of time between the taxpayer's acquisition of a plant or animal and the time the plant or animal is made available for sale to the taxpayer's customers, and, in the case of plants, whether plants acquired by the taxpayer are planted in the ground or kept in temporary containers.

Many commentators expressed concern that the proposed regulations' concept of ''merely buying and reselling plants grown by another'' could be interpreted to mean that only taxpayers growing a plant from seed would be regarded as engaged in a farming business. For example, the commentators were concerned that a taxpayer that buys a partially grown plant, grows the plant to a larger size, and then sells the plant would not be engaged in a farming business. The final regulations clarify that a taxpayer is engaged in the production of property in a farming business, rather than the mere resale of plants or animals, if the plant or animal is held for further cultivation and development prior to sale. In addition, the final regulations include an example illustrating that a taxpayer that buys plants, grows them, and sells them, is producing property in a farming business; whereas a taxpayer that buys plants and, without further cultivation and development, resells them is not producing property in a farming business. The example also illustrates that a taxpayer engaged in both farming activities and resale activities is not required to capitalize costs under section 263A with respect to the resale activities if the taxpayer has average annual gross receipts of less than $10 million. See also, Ann. 97–120 (1997–50 I.R.B. 61 (Dec. 15, 1997)) (confirming that nursery growers using the farming exception may deduct the costs of young plants purchased for further development and cultivation prior to sale as well as the costs of growing the plants).

Some commentators suggested that the final regulations disregard whether a plant is kept in its container out of concern that taxpayers who grow plants in containers would not be considered to be producing property in a farming business. The IRS and Treasury Department continue to believe that this is a factor to be considered in addition to all the other facts and circumstances. Accordingly, the final regulations retain this factor. However, the final regulations have been clarified to explain that a plant that is *grown* by a taxpayer in a container is regarded as a plant produced in a farming business.

One commentator requested that the value added to a plant or animal by a taxpayer also be a factor in determining whether a taxpayer is engaged in the production, or the mere resale, of plants or animals. The final regulations provide that a taxpayer's addition of value to plants or animals through agricultural or horticultural processes is a factor to be considered in evaluating whether a taxpayer is producing property in a farming business.

Some commentators requested that the list of factors contained in the preamble be included in the regulations.

In response to these comments, the final regulations contain a list of factors, modified as discussed above, to assist in the determination of whether a plant or animal is held for further cultivation and development prior to sale or merely held for resale.

One commentator expressed concern that under the proposed regulations a farming business only includes processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural commodities. This commentator also suggested that farmers are engaging in processing activities as the result of new technology and changes in the market for agricultural or horticultural products. The IRS and Treasury Department believe that processing activities that are not normally incident to the growing, raising, or harvesting of agricultural or horticultural products, such as the canning of an agricultural product or the combination of an agricultural product with other ingredients to produce a different edible item, are not farming activities. Accordingly, the final regulations, like the proposed regulations, include in the definition of farming business only those processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural products, such as the washing, inspecting, and packaging of those products.

Exceptions to Section 263A for Certain Property

Taxpayers generally must capitalize direct costs and an allocable portion of indirect costs of producing all plants (without regard to the length of the preproductive period) and animals. Qualified taxpayers, however, are eligible for an exception to this general rule. Under this exception, qualified taxpayers are not required to capitalize under section 263A the costs of producing plants that have a preproductive period of 2 years or less or with respect to animals. Thus, under this exception, qualified taxpayers are required to capitalize only those costs of producing plants that have a preproductive period in excess of 2 years.

A few commentators suggested that, for purposes of determining the application of section 263A, the preproductive period of a plant should be determined with reference to the length of time a particular taxpayer grows a plant rather than with reference to how long it takes the plant to reach a productive stage. The commentators suggested this method would, in essence, supplant the nationwide weighted average preproductive period used for plants grown in commercial quantities in the United States and the reasonable estimate of the preproductive period used for all other plants. For example, a qualified taxpayer grows bushes that have a preproductive period of 3 years and 3 months. If the taxpayer purchases and plants the bushes when they are 2 years old, the commentators suggest that the preproductive period of the bushes should be regarded as 2 years or less (and the taxpayer would, therefore, not be required to capitalize the costs associated with growing the bushes) because this taxpayer grows the bushes for only 15 months before the bushes become productive in marketable quantities. If, however, another qualified taxpayer purchased the same type of bushes when the bushes were 14 months old and grew them for 2 years and 1 month, the preproductive period of the bushes would be regarded as in excess of 2 years, and this taxpayer would be required to capitalize the costs of growing the bushes.

The final regulations do not adopt this recommendation. First, the statute requires that the preproductive period of a plant grown in commercial quantities in the United States be based on the nationwide weighted average preproductive period of the plant. *See Pelaez and Sons, Inc., et al.* v. *Commissioner*, 114 T.C. No. 28 (No. 18049–97 May 30, 2000). Further, the IRS and Treasury Department continue to believe that, for purposes of determining whether section 263A applies, the preproductive period of a plant not grown in commercial quantities in the United States also should be determined on a plant-by-plant basis rather than on a taxpayer-by-taxpayer basis.

In the case of a plant that is not produced in commercial quantities in the United States, the proposed regulations provided that, at or before the time the seed or plant is acquired or planted, the taxpayer is required to reasonably estimate whether the plant has a preproductive period in excess of 2 years. One commentator suggested that the regulations provide that if the United States Department of Agriculture (USDA) or a state department of agriculture certifies that a plant is not grown in commercial quantities in the United States, the plant will be deemed to have a preproductive period of 2 years or less. The effect of this suggestion would be to provide an exemption from section 263A for all qualified taxpayers growing plants that are not grown in commercial quantities in the United States. The IRS and Treasury Department believe that such a rule would be inconsistent with the statutory language of section 263A. Accordingly, the final regulations do not adopt this suggestion.

The proposed regulations provided that, for purposes of determining whether a plant has a preproductive period in excess of 2 years, in the case of a plant grown in commercial quantities in the United States, the nationwide weighted average preproductive period of such plant is used. One commentator requested that a list of plants with nationwide weighted average preproductive periods in excess of 2 years be published and kept current as needed. Notice 2000–45 (2000–36 I.R.B. (Sept. 5, 2000)) issued contemporaneously with the publication of these final regulations, provides a list of plants grown in commercial quantities in the United States that have a nationwide weighted average preproductive period in excess of 2 years. Notice 2000–45 will be modified and superseded as needed.

Tax shelters, within the meaning of section 448(a)(3), are not qualified taxpayers and are therefore not eligible for the special rules of section 263A(d). A tax shelter, for purposes of section 448(a)(3), means a farming business that is a farming syndicate as defined under section 464(c) or any partnership, entity, plan or arrangement that is a tax shelter within the meaning of section 6662(d)(2)(C)(iii) (that is, its principal purpose is to avoid or evade Federal income tax). See § 1.448–1T(b)(1)(iii). There is a presumption under section 448 that marketed arrangements, in which persons carry on farming activities using the services of a common managerial or administrative service, will fall within the meaning of a tax shelter if a substantial portion of farming expenses are prepaid with borrowed funds. See § 1.448–1T(b)(4). The proposed regulations repeated the text of § 1.448–1T(b)(1)(iii) and (4) to explain which farming businesses are tax shelters.

A commentator suggested that the marketed arrangement presumption set forth in § 1.448–1T(b)(4) and the proposed regulations is too broad in scope and should be modified. The commentator is concerned that this provision of the regulations will cause taxpayers participating in farming cooperatives to be treated as tax shelters and, therefore, require them to use an accrual method of accounting and to capitalize the direct costs and an allocable portion of indirect costs of producing all plants and animals. The commentator explained that such a result is unwarranted with respect to

individual farmers and farming businesses that join together to form farming cooperatives for non-tax reasons, such as to obtain supplies at lower prices and have a steady market for their farm products.

The IRS and Treasury Department believe that the marketed arrangement presumption is necessary to preclude taxpayers from investing in farming operations in order to generate losses, often without making economic outlays, that may be used to shelter income from other sources. However, the IRS and Treasury Department do not believe that the marketed arrangement presumption, as described in the temporary Income Tax Regulations under section 448 and the proposed section 263A regulations, would cause a taxpayer producing property in a farming business to be regarded as a tax shelter merely because the taxpayer joined a farming cooperative. Therefore, the marketed arrangement presumption is not modified in the final regulations.

Preparatory and Preproductive Period Costs

The IRS and Treasury Department believe that, in general, section 263A does not change the rules under section 263 regarding the need to capitalize preparatory costs (that is, costs incurred prior to raising agricultural or horticultural commodities or that otherwise enable a farmer to begin the farming process). Thus, the proposed regulations clarified that, as under prior law, taxpayers generally must capitalize preparatory expenditures (for example, the cost of seeds, seedlings, and animals; clearing, leveling and grading land; drilling and equipping wells; irrigation systems; budding trees, *etc.*). However, because section 263A requires the capitalization of certain additional costs, the amount of preparatory expenditures capitalized to property that is subject to section 263A may be greater than under prior law. By requiring the capitalization of all the direct costs and the allocable portion of indirect costs incurred during the preparatory period, section 263A ensures that the income from farming will be appropriately matched with all of the costs of producing property in a farming business.

Section 263A expanded the circumstances under which costs that were once termed *developmental expenditures* or *cultural practices expenditures* (that is, costs incurred by a taxpayer so that the growing process can continue in the desired manner) must be capitalized. The proposed regulations clarified that these costs are included in the category of preproductive period costs that are required to be capitalized under section 263A. Thus, the proposed regulations provided that all appropriate costs incurred during the preproductive period of property subject to section 263A must be capitalized, including the costs of certain soil and water conservation expenditures and fertilizing incurred during the preproductive period.

One commentator requested that expenditures for soil and water conservation, described in section 175, and fertilizer, described in section 180, be excepted from capitalization under section 263A. However, the legislative history of former section 447(b) indicates that Congress believed that soil and water conservation expenditures incurred during the preproductive period were required to be capitalized into the basis of the plants produced. See H.R. Rep. No. 658, 94th Cong., 1st Sess. 95 (1975), 1976–3 (Vol. 2) C.B. 787. See also, Staff of the Joint Committee on Taxation, General Explanation of the Tax Reform Act of 1976, H.R. Rep. No. 10612, 94th Cong., 2nd Sess. 55 (1976), 1976–3 (Vol. 2) C.B. 67. In addition, the legislative history to section 464 indicates that Congress believed that the costs of fertilizer incurred during the preproductive period was capitalized under former section 278. See Senate Report No. 938, 94th Cong., 2nd Sess. 62 (1976), 1976–3 (Vol. 3) C.B. 100. See also, Staff of the Joint Committee on Taxation, General Explanation of the Tax Reform Act of 1976, H.R. Rep. No. 10612, 94th Cong., 2nd Sess. 49 (1976), 1976–3 (Vol. 2) C.B. 61. Because section 263A was intended to continue the principles of sections 447 and 278, the IRS and Treasury Department believe that expenditures for soil and water conservation and fertilizer incurred during the preproductive period are costs of producing those plants. Further, the IRS and Treasury Department believe that providing a single rule regarding when expenditures for soil and water conservation and fertilizer incurred during the preproductive period must be capitalized is consistent with the intent of Congress to provide uniform capitalization rules. Accordingly, the final regulations retain the proposed regulations' provision that these costs incurred during the preproductive period are included in the category of costs that are required to be capitalized under section 263A. However, the IRS and Treasury Department do not believe that Congress intended to require capitalization of expenditures for soil and water conservation deductible under section 175 and fertilizer deductible under section 180 that are not incurred during the preproductive period. Accordingly, the final regulations clarify that these expenditures are not subject to capitalization under section 263A except to the extent they are required to be capitalized as a preproductive period cost.

Capitalization Period

Preproductive period costs (for example, irrigating, fertilizing, real estate taxes) are capitalized during the actual preproductive period of a plant or animal. A taxpayer that grows a plant that will have more than 1 crop or yield is engaged in the production of two types of property, the plant and the crop or yield of the plant (for example, the orange tree and the orange). The proposed regulations clarified the capitalization period for plants that will have more than 1 crop or yield, for crops or yields of plants that will have more than 1 crop or yield, and for other plants.

The proposed regulations provided that the preproductive period of a plant generally begins when a taxpayer first incurs costs with respect to the plant, for example, when the plant is acquired or the seed is planted. In the case of crops or yields of a plant that has more than 1 crop or yield, the preproductive period of the crop or yield begins when the plant has become productive in marketable quantities and the crop or yield first appears, whether in the form of a sprout, bloom, blossom, bud, *etc.*

One commentator suggested that the preproductive period for crops or yields that require several years of growth (for example, biennial crops) begins upon first appearance of the crop in the year the crop actually develops. For example, a biennial plant produces fruit buds in the first year, but the buds do not develop until the second year. In the second year, the plant produces blossoms, which subsequently grow into an edible food product that is harvested and sold in that year. However, if weather conditions are harsh, the buds produced in the first year may not blossom and develop in the second year. The commentator suggests that the preproductive period begin not when the buds first appear in the first year but when the blossoms appear in the second year as that is the first sign of actual development. The IRS and Treasury Department are concerned that the suggested rule would be difficult to apply because a taxpayer may not know in any case whether the appearance of a crop will actually develop.

Accordingly, the final regulations do not adopt this suggestion.

In the case of a plant that will have more than 1 crop or yield, the preproductive period of the plant ends when the plant becomes productive in marketable quantities. In the case of the crop or yield of a plant that has more than 1 crop or yield that has become productive in marketable quantities, the preproductive period of the crop or yield ends when the crop or yield is disposed of. Finally, in the case of other plants, the preproductive period ends when the plant is disposed of.

One commentator requested that the proper tax treatment of field costs (such as the costs of irrigating, fertilizing, *etc.*) that are incurred after a crop or yield is harvested but before the crop or yield is disposed of, which do not benefit and are unrelated to the crop or yield that has been harvested, be clarified. The commentator is concerned that the proposed regulations subject such field costs to capitalization under the general principles of section 263A. The IRS and Treasury Department agree with the commentator's concerns. Accordingly, the final regulations provide that field costs incurred after a crop or yield is harvested but before the crop or yield is disposed of do not have to be capitalized to the harvested crop or yield because such costs relate to the plant or a future crop or yield rather than to the harvested crop or yield.

One commentator requested that the definition of when a plant that will have more than 1 crop or yield becomes productive in marketable quantities be clarified. Under the proposed regulations such a plant becomes productive in marketable quantities when it is (or would be considered) placed in service for purposes of section 168 (without regard to the applicable convention). The commentator noted that some taxpayers regard a plant as being placed in service for purposes of depreciation at the time the preproductive period ends for purposes of section 263A. The commentator requested that the final regulations adopt a rule that provides more guidance with respect to the end of the preproductive period.

The IRS and Treasury Department agree with the commentator's concerns. Accordingly, the final regulations provide that a plant becomes productive in marketable quantities once a crop or yield is produced in sufficient quantities to be harvested and marketed in the ordinary course of the taxpayer's business. Factors that are relevant in determining whether the crop or yield is produced in sufficient quantities to be harvested and marketed in the ordinary course include: whether a crop or yield is harvested that is more than *de minimis*, although it may be less than expected at the maximum bearing stage, based on a comparison of the quantities per acre harvested in the year in question to the quantities per acre expected to be harvested when the plant reaches full maturity; and whether the sales proceeds exceed the costs of harvest and make a reasonable contribution to an allocable share of farm expenses.

Election Not To Capitalize Costs

Qualified taxpayers may elect not to capitalize under section 263A the costs of producing certain plants even though such plants have a preproductive period in excess of 2 years and would otherwise be subject to the capitalization requirements of section 263A. Taxpayers making this election may continue to deduct (subject to other limitations of the Internal Revenue Code) the costs that were deductible under the rules in effect before the enactment of section 263A.

A taxpayer may make this election automatically on its original federal income tax return for the first taxable year in which the taxpayer would otherwise be required to capitalize costs under section 263A. The final regulations provide that if a taxpayer does not make this election in this first taxable year, the taxpayer may make this election by filing Form 3115, ''Application for Change in Accounting Method,'' using the appropriate procedures that govern the filing of the Form 3115.

A taxpayer and any person related to the taxpayer (including a member of the taxpayer's family) electing to not capitalize costs under section 263A for certain plants are required to use the alternative depreciation system of section 168(g)(2) for any property used predominantly in a farming business that is placed in service in a taxable year for which the election is in effect. In Notice 88–86, the IRS noted that commentators had suggested that guidance be provided clarifying the definition of members of a family. This guidance was provided in the proposed regulations. One commentator suggested that this proposed guidance be modified so that elections made by some family members do not bind other family members. The statutory language provides that an election affects family members and defines family members for this purpose. Thus, the IRS and Treasury Department believe that Congress's intent was to bind all family members when one member makes an election not to capitalize costs under section 263A. Accordingly, the final regulations do not adopt the suggestion.

Casualty Loss Exception

Section 263A(d)(2) provides an exception from capitalization under section 263A for costs incurred with respect to plants that are replacing certain plants that were lost by reason of certain casualties. The proposed regulations clarified that this exception does not apply to preparatory expenditures or the costs of capital assets. In addition, the regulations clarified that the casualty loss exception applies whether the plants are replanted on the same parcel of land as the plants destroyed by casualty or a parcel of land of the same acreage in the United States. The regulations additionally clarified that the exception applies to all plants replanted on such acreage, even if the plants are replanted in greater density than the plants destroyed by the casualty.

One commentator requested that the casualty loss exception be expanded to allow a current deduction for the expenditures incurred for replacing capital assets. The final regulations do not adopt this recommendation. Prior to the enactment of section 263A, preparatory expenditures as well as acquisition costs incurred during the preparatory period were generally capitalized under section 263. Also, prior to the enactment of section 263A, certain preproductive period costs were capitalized under former sections 447(b) and 278. Former section 278(c) provided an exception to the capitalization of preproductive period costs where such costs were incurred to replant a grove, orchard, or vineyard which had been lost or destroyed by reason of a casualty. However, this exception only applied to preproductive period costs capitalized under former section 278 and did not apply to preparatory expenditures and acquisition costs capitalized under section 263. The special exception in section 263A(d)(2) was intended to be a continuation, as modified to include all plants bearing an edible crop for human consumption, of the exception found in former section 278(c). Nothing in the statute or legislative history of section 263A indicates an intention to expand the exception to include other costs, such as the costs of replacing capital assets, in addition to the preproductive period costs.

Unit Livestock Price Method

The unit livestock price method provides for the valuation of different classes of animals in inventory at a standard unit price for each animal within a class. A taxpayer who elects to

use the unit livestock price method must apply it to all livestock raised, whether for sale or for draft, breeding, or dairy purposes. In Notice 88–24, the IRS indicated that forthcoming regulations would modify the rule contained in § 1.471–6 and require that taxpayers adjust the unit prices upward, from time to time as specified by those regulations, to reflect increases in costs taxpayers experience in raising livestock. Contemporaneous with the section 263A proposed regulations published August 22, 1997, § 1.471–6 was modified to require a taxpayer to annually reevaluate the unit livestock prices and adjust the prices upward to reflect increases in the costs of raising livestock. Under this regulation, the consent of the Commissioner is not required to make such upward adjustments; however, consent is required to make any other change in animal classification or unit prices.

One commentator expressed concern that if taxpayers are required to annually reevaluate their unit prices, they should be able to both increase and decrease the unit price to reflect all changes in the cost of raising livestock. In addition, this commentator suggested that the unit livestock price method should be modified to allow a taxpayer to remove from inventory animals that have been raised for use in the taxpayer's trade or business (such as a breeding cow) and depreciate the inventory value of the animal.

Although these comments are outside the scope of this regulation, the IRS and Treasury Department understand the commentator's concerns. In addition, the IRS and Treasury Department recognize a broader concern that the requirement to annually reevaluate unit prices may have eliminated much of the simplicity of the unit livestock price method, especially for farmers neither required to use an accrual method by section 447 nor prohibited from using the cash method by section 448(a)(3). Accordingly, the IRS and Treasury Department intend to study the unit livestock price method to determine whether the method may be made simpler to apply and will take into account the commentator's suggestions as part of this study.

Record Keeping Requirements

Pursuant to 26 U.S.C. 7805(f)(1), copies of the 1997 notice of proposed rulemaking and temporary rule were provided to the Chief Counsel for Advocacy of the Small Business Administration for comment. The Chief Counsel for Advocacy submitted comments requesting that the IRS conduct a regulatory flexibility analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) (RFA) on how the notice of proposed rulemaking would affect recordkeeping burdens imposed on small business taxpayers engaged in a farming business.

Under the RFA, the IRS is required to prepare a regulatory flexibility analysis if the proposed rule imposes a collection of information requirement (including a recordkeeping requirement) on small entities and that requirement is likely to have a significant economic impact on a substantial number of small entities (5 U.S.C 603(a)). The RFA defines a *recordkeeping requirement* as a ''requirement imposed by an agency on persons to maintain specified records'' (5 U.S.C. 601(7) and (8)). Since neither the proposed nor final regulation contain a collection of information requirement (including a requirement that persons maintain specified records), an analysis is not required by the RFA.

Effective Date and Method Changes

The final regulations provide that, in the case of property that is not inventory in the hands of the taxpayer, the regulations are applicable to costs incurred after August 21, 2000 in taxable years ending after such date. In the case of inventory property, the final regulations are applicable to taxable years beginning after August 21, 2000.

For property that is not inventory, a taxpayer is granted the consent of the Commissioner to change its method of accounting to comply with the provisions of these final regulations for costs incurred after August 21, 2000, provided the change is made for the first taxable year ending after August 21, 2000. For inventory property, a taxpayer is granted the consent of the Commissioner to change its method of accounting to comply with the provisions of these final regulations for the first taxable year beginning after August 21, 2000. To make such a change, a taxpayer must follow the automatic consent procedures in Rev. Proc. 99–49 (1999–2 I.R.B. 725) (see § 601.601(d)(2) of this chapter), as modified by these regulations.

Effect on Other Documents

The following publications are obsolete as of August 22, 2000: Notice 87–76 (1987–2 C.B. 384); Notice 88–24 (1988–1 C.B. 491); and section V of Notice 88–86 (1988–2 C.B. 401).

Special Analyses

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

Drafting Information

The principal authors of these final regulations are Jan Skelton and Richard C. Farley, Jr. previously of the Office of the Associate Chief Counsel (Income Tax and Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

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

Par. 2. Section 1.162–12 is amended by revising the ninth sentence of paragraph (a) to read as follows:

§ 1.162–12 Expenses for farmers.

(a) * * * For rules regarding the capitalization of expenses of producing property in the trade or business of farming, see section 263A of the Internal Revenue Code and § 1.263A–4. * * *

* * * * *

Par. 3. Section 1.263A–0 is amended by revising the introductory text and adding entries for § 1.263A–4 to read as follows:

§ 1.263A–0 Outline of regulations under section 263A.

This section lists the paragraphs in §§ 1.263A–1 through 1.263A–4 and §§ 1.263A–7 through 1.263A–15 as follows:

* * * * *

§ 1.263A–4 Rules for property produced in a farming business.

(a) Introduction.

(1) In general.
(2) Exception.
(i) In general.
(ii) Tax shelter.
(A) In general.
(B) Presumption.
(iii) Examples.
(3) Costs required to be capitalized or inventoried under another provision.
(4) Farming business.
(i) In general.
(A) Plant.
(B) Animal.
(ii) Incidental activities.
(A) In general.
(B) Activities that are not incidental.
(iii) Examples.
(b) Application of section 263A to property produced in a farming business.
(1) In general.
(i) Plants.
(ii) Animals.
(2) Preproductive period.
(i) Plant.
(A) In general.
(B) Applicability of section 263A.
(C) Actual preproductive period.
(*1*) Beginning of the preproductive period.
(*2*) End of the preproductive period.
(*i*) In general.
(*ii*) Marketable quantities.
(D) Examples.
(ii) Animal.
(A) Beginning of the preproductive period.
(B) End of the preproductive period.
(C) Allocation of costs between animal and first yield.
(c) Inventory methods.
(1) In general.
(2) Available for property used in a trade or business.
(3) Exclusion of property to which section 263A does not apply.
(d) Election not to have section 263A apply.
(1) Introduction.
(2) Availability of the election.
(3) Time and manner of making the election.
(i) Automatic election.
(ii) Nonautomatic election.
(4) Special rules.
(i) Section 1245 treatment.
(ii) Required use of alternative depreciation system.
(iii) Related person.
(A) In general.
(B) Members of family.
(5) Examples.
(e) Exception for certain costs resulting from casualty losses.
(1) In general.
(2) Ownership.
(3) Examples.
(4) Special rule for citrus and almond groves.
(i) In general.
(ii) Example.
(f) Effective date and change in method of accounting.
(1) Effective date.
(2) Change in method of accounting.

* * * * *

§ 1.263A–0T [Removed]

Par. 4. Section 1.263A–0T is removed.

Par. 5. Section 1.263A–1 is amended as follows:

1. The last sentence of paragraph (b)(3) is revised.

2. The last sentence of paragraph (b)(4) is revised.

The revisions read as follows:

§ 1.263A–1 Uniform capitalization of costs.

* * * * *

(b) * * *

(3) * * * See § 1.263A–4 for specific rules relating to taxpayers engaged in the trade or business of farming.

(4) * * * See § 1.263A–4, however, for rules relating to taxpayers producing certain trees to which section 263A applies.

* * * * *

Par. 6. Section 1.263A–4 is revised to read as follows:

§ 1.263A–4 Rules for property produced in a farming business.

(a) *Introduction*—(1) *In general.* This section provides guidance with respect to the application of section 263A to property produced in a farming business as defined in paragraph (a)(4) of this section. Except as otherwise provided by the rules of this section, the general rules of §§ 1.263A–1 through 1.263A–3 and §§ 1.263A–7 through 1.263A–15 apply to property produced in a farming business. A taxpayer that engages in the raising or growing of any agricultural or horticultural commodity, including both plants and animals, is engaged in the production of property. Section 263A generally requires the capitalization of the direct costs and an allocable portion of the indirect costs that directly benefit or are incurred by reason of the production of this property. The direct and indirect costs of producing plants or animals generally include preparatory costs allocable to the plant or animal and preproductive period costs of the plant or animal. Except as provided in paragraphs (a)(2) and (e) of this section, taxpayers must capitalize the costs of producing all plants and animals unless the election described in paragraph (d) of this section is made.

(2) *Exception*—(i) *In general.* Section 263A does not apply to the costs of producing plants with a preproductive period of 2 years or less or the costs of producing animals in a farming business, if the taxpayer is not—

(A) A corporation or partnership required to use an accrual method of accounting (accrual method) under section 447 in computing its taxable income from farming; or

(B) A tax shelter prohibited from using the cash receipts and disbursements method under section 448(a)(3).

(ii) *Tax shelter*—(A) *In general.* A farming business is considered a tax shelter, and thus a taxpayer prohibited from using the cash method under section 448(a)(3), if the farming business is—

(*1*) A farming syndicate as defined in section 464(c); or

(*2*) A tax shelter, within the meaning of section 6662(d)(2)(C)(iii).

(B) *Presumption.* Marketed arrangements in which persons carry on farming activities using the services of a common managerial or administrative service will be presumed to have the principal purpose of tax avoidance, within the meaning of section 6662(d)(2)(C)(iii), if such persons prepay a substantial portion of their farming expenses with borrowed funds.

(iii) *Examples.* The following examples illustrate the provisions of this paragraph (a)(2):

Example 1. Farmer A grows trees that have a preproductive period in excess of 2 years, and that produce an annual crop. Farmer A is not required by section 447 to use an accrual method or prohibited by section 448(a)(3) from using the cash method. Accordingly, Farmer A qualifies for the exception described in this paragraph (a)(2). Since the trees have a preproductive period in excess of 2 years, Farmer A must capitalize the direct costs and an allocable portion of the indirect costs that directly benefit or are incurred by reason of the production of the trees. Since the annual crop has a preproductive period of 2 years or less, Farmer A is not required to capitalize the costs of producing the crops.

Example 2. Assume the same facts as *Example 1*, except that Farmer A is required by section 447 to use an accrual method or prohibited by 448(a)(3) from using the cash method. Farmer A does not qualify for the exception described in this paragraph (a)(2). Farmer A is required to capitalize the direct costs and an allocable portion of the indirect costs that directly benefit or are incurred by reason of the production of the trees and crops.

(3) *Costs required to be capitalized or inventoried under another provision.* The exceptions from capitalization provided in paragraphs (a)(2), (d) and (e) of this section do not apply to any cost that is required to be capitalized or inventoried under another Internal Revenue Code or regulatory provision, such as section 263 or 471.

(4) *Farming business*—(i) *In general.* A farming business means a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity. Examples include the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than 6 years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals. For purposes of this section, the term harvesting does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another. Similarly, merely buying and reselling plants or animals grown or raised entirely by another is not raising an agricultural or horticultural commodity. A taxpayer is engaged in raising a plant or animal, rather than the mere resale of a plant or animal, if the plant or animal is held for further cultivation and development prior to sale. In determining whether a plant or animal is held for further cultivation and development prior to sale, consideration will be given to all of the facts and circumstances, including: the value added by the taxpayer to the plant or animal through agricultural or horticultural processes; the length of time between the taxpayer's acquisition of the plant or animal and the time that the taxpayer makes the plant or animal available for sale; and in the case of a plant, whether the plant is kept in the container in which purchased, replanted in the ground, or replanted in a series of larger containers as it is grown to a larger size.

(A) *Plant.* A plant produced in a farming business includes, but is not limited to, a fruit, nut, or other crop bearing tree, an ornamental tree, a vine, a bush, sod, and the crop or yield of a plant that will have more than one crop or yield raised by the taxpayer. Sea plants are produced in a farming business if they are tended and cultivated as opposed to merely harvested.

(B) *Animal.* An animal produced in a farming business includes, but is not limited to, any stock, poultry or other bird, and fish or other sea life raised by the taxpayer. Thus, for example, the term animal may include a cow, chicken, emu, or salmon raised by the taxpayer. Fish and other sea life are produced in a farming business if they are raised on a fish farm. A fish farm is an area where fish or other sea life are grown or raised as opposed to merely caught or harvested.

(ii) *Incidental activities*—(A) *In general.* A farming business includes processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural products. For example, a taxpayer in the trade or business of growing fruits and vegetables may harvest, wash, inspect, and package the fruits and vegetables for sale. Such activities are normally incident to the raising of these crops by farmers. The taxpayer will be considered to be in the trade or business of farming with respect to the growing of fruits and vegetables and the processing activities incident to their harvest.

(B) *Activities that are not incidental.* Farming business does not include the processing of commodities or products beyond those activities that are normally incident to the growing, raising, or harvesting of such products.

(iii) *Examples.* The following examples illustrate the provisions of this paragraph (a)(4):

Example 1. Individual A operates a retail nursery. Individual A has three categories of plants. The first category is comprised of plants that Individual A grows from seeds or cuttings. The second category is comprised of plants that Individual A purchases in containers and grows for a period of from several months to several years. Individual A replants some of these plants in the ground. The others are replanted in a series of larger containers as they grow. The third category is comprised of plants that are purchased by Individual A in containers. Individual A does not grow these plants to a larger size before making them available for resale. Instead, Individual A makes these plants available for resale, in the container in which purchased, shortly after receiving them. Thus, no value is added to these plants by Individual A through horticultural processes. Individual A also sells soil, mulch, chemicals, and yard tools. Individual A is producing property in the farming business with respect to the first two categories of plants because these plants are held for further cultivation and development prior to sale. The plants in the third category are not held for further cultivation and development prior to sale and, therefore, are not regarded as property produced in a farming business for purposes of section 263A. Accordingly, Individual A must account for the third category of plants, along with the soil, mulch, chemicals, and yard tools, as property acquired for resale. If Individual A's average annual gross receipts are less than $10 million, Individual A will not be required to capitalize costs with respect to its resale activities under section 263A.

Example 2. Individual B is in the business of growing and harvesting wheat and other grains. Individual B also processes grain that Individual B has harvested in order to produce breads, cereals, and other similar food products, which Individual B then sells to customers in the course of its business. Although Individual B is in the farming business with respect to the growing and harvesting of grain, Individual B is not in the farming business with respect to the processing of such grain to produce the food products.

Example 3. Individual C is in the business of raising poultry and other livestock. Individual C also operates a meat processing operation in which the poultry and other livestock are slaughtered, processed, and packaged or canned. The packaged or canned meat is sold to Individual C's customers. Although Individual C is in the farming business with respect to the raising of poultry and other livestock, Individual C is not in the farming business with respect to the slaughtering, processing, packaging, and canning of such animals to produce the food products.

(b) *Application of section 263A to property produced in a farming business*—(1) *In general.* Unless otherwise provided in this section, section 263A requires the capitalization of the direct costs and an allocable portion of the indirect costs that directly benefit or are incurred by reason of the production of any property in a farming business (including animals and plants without regard to the length of their preproductive period). Section 1.263A–1(e) describes the types of direct and indirect costs that generally must be capitalized by taxpayers under section 263A and paragraphs (b)(1)(i) and (ii) of this section provide specific examples of the types of costs typically incurred in the trade or business of farming. For purposes of this section, soil and water conservation expenditures that a taxpayer has elected to deduct under section 175 and fertilizer that a taxpayer has elected to deduct under section 180 are not subject to capitalization under section 263A, except to the extent these costs are required to be capitalized as a preproductive period cost of a plant or animal.

(i) *Plants.* The costs of producing a plant typically required to be capitalized under section 263A include the costs incurred so that the plant's growing process may begin (preparatory costs), such as the acquisition costs of the seed, seedling, or plant, and the costs of planting, cultivating, maintaining, or developing the plant during the preproductive period (preproductive period costs). Preproductive period costs include, but are not limited to, management, irrigation, pruning, soil and water conservation (including costs that the taxpayer has elected to deduct under section 175), fertilizing (including costs that the taxpayer has elected to deduct under section 180), frost protection, spraying, harvesting, storage and handling, upkeep, electricity, tax depreciation and repairs on buildings

and equipment used in raising the plants, farm overhead, taxes (except state and Federal income taxes), and interest required to be capitalized under section 263A(f).

(ii) *Animals.* The costs of producing an animal typically required to be capitalized under section 263A include the costs incurred so that the animal's raising process may begin (preparatory costs), such as the acquisition costs of the animal, and the costs of raising or caring for such animal during the preproductive period (preproductive period costs). Preproductive period costs include, but are not limited to, management, feed (such as grain, silage, concentrates, supplements, haylage, hay, pasture and other forages), maintaining pasture or pen areas (including costs that the taxpayer has elected to deduct under sections 175 or 180), breeding, artificial insemination, veterinary services and medicine, livestock hauling, bedding, fuel, electricity, hired labor, tax depreciation and repairs on buildings and equipment used in raising the animals (for example, barns, trucks, and trailers), farm overhead, taxes (except state and Federal income taxes), and interest required to be capitalized under section 263A(f).

(2) *Preproductive period*—(i) *Plant*—(A) *In general.* The preproductive period of property produced in a farming business means—

(*1*) In the case of a plant that will have more than one crop or yield (for example, an orange tree), the period before the first marketable crop or yield from such plant;

(*2*) In the case of the crop or yield of a plant that will have more than one crop or yield (for example, the orange), the period before such crop or yield is disposed of; or

(*3*) In the case of any other plant, the period before such plant is disposed of.

(B) *Applicability of section 263A.* For purposes of determining whether a plant has a preproductive period in excess of 2 years, the preproductive period of plants grown in commercial quantities in the United States is based on the nationwide weighted average preproductive period for such plant. The Commissioner will publish a noninclusive list of plants with a nationwide weighted average preproductive period in excess of 2 years. In the case of other plants grown in commercial quantities in the United States, the nationwide weighted average preproductive period must be determined based on available statistical data. For all other plants, the taxpayer is required, at or before the time the seed or plant is acquired or planted, to reasonably estimate the preproductive period of the plant. If the taxpayer estimates a preproductive period in excess of 2 years, the taxpayer must capitalize the costs of producing the plant. If the estimate is reasonable, based on the facts in existence at the time it is made, the determination of whether section 263A applies is not modified at a later time even if the actual length of the preproductive period differs from the estimate. The actual length of the preproductive period will, however, be considered in evaluating the reasonableness of the taxpayer's future estimates. The nationwide weighted average preproductive period or the estimated preproductive period is only used for purposes of determining whether the preproductive period of a plant is greater than 2 years.

(C) *Actual preproductive period.* The plant's actual preproductive period is used for purposes of determining the period during which a taxpayer must capitalize preproductive period costs with respect to a particular plant.

(*1*) *Beginning of the preproductive period.* The actual preproductive period of a plant begins when the taxpayer first incurs costs that directly benefit or are incurred by reason of the plant. Generally, this occurs when the taxpayer plants the seed or plant. In the case of a taxpayer that acquires plants that have already been permanently planted, or plants that are tended by the taxpayer or another prior to permanent planting, the actual preproductive period of the plant begins upon acquisition of the plant by the taxpayer. In the case of the crop or yield of a plant that will have more than one crop or yield, the actual preproductive period begins when the plant has become productive in marketable quantities and the crop or yield first appears, for example, in the form of a sprout, bloom, blossom, or bud.

(*2*) *End of the preproductive period*—(i) *In general.* In the case of a plant that will have more than one crop or yield, the actual preproductive period ends when the plant first becomes productive in marketable quantities. In the case of any other plant (including the crop or yield of a plant that will have more than one crop or yield), the actual preproductive period ends when the plant, crop, or yield is sold or otherwise disposed of. Field costs, such as irrigating, fertilizing, spraying and pruning, that are incurred after the harvest of a crop or yield but before the crop or yield is sold or otherwise disposed of are not required to be included in the preproductive period costs of the harvested crop or yield because they do not benefit and are unrelated to the harvested crop or yield.

(ii) *Marketable quantities.* A plant that will have more than one crop or yield becomes productive in marketable quantities once a crop or yield is produced in sufficient quantities to be harvested and marketed in the ordinary course of the taxpayer's business. Factors that are relevant to determining whether a crop or yield is produced in sufficient quantities to be harvested and marketed in the ordinary course include: whether the crop or yield is harvested that is more than *de minimis*, although it may be less than expected at the maximum bearing stage, based on a comparison of the quantities per acre harvested in the year in question to the quantities per acre expected to be harvested when the plant reaches full maturity; and whether the sales proceeds exceed the costs of harvest and make a reasonable contribution to an allocable share of farm expenses.

(D) *Examples.* The following examples illustrate the provisions of this paragraph (b)(2):

Example 1. (i) Farmer A, a taxpayer that qualifies for the exception in paragraph (a)(2) of this section, grows plants that will have more than one crop or yield. The plants are grown in commercial quantities in the United States. Farmer A acquires 1 year-old plants by purchasing them from an unrelated party, Corporation B, and plants them immediately. The nationwide weighted average preproductive period of the plant is 4 years. The particular plants grown by Farmer A do not begin to produce in marketable quantities until 3 years and 6 months after they are planted by Farmer A.

(ii) Since the plants are deemed to have a preproductive period in excess of 2 years, Farmer A is required to capitalize the costs of producing the plants. See paragraphs (a)(2) and (b)(2)(i)(B) of this section. In accordance with paragraph (b)(2)(i)(C)(*1*) of this section, Farmer A must begin to capitalize the preproductive period costs when the plants are planted. In accordance with paragraph (b)(2)(i)(C)(*2*) of this section, Farmer A must continue to capitalize preproductive period costs to the plants until the plants begin to produce in marketable quantities. Thus, Farmer A must capitalize the preproductive period costs for a period of 3 years and 6 months (that is, until the plants are 4 years and 6 months old), notwithstanding the fact that the plants, in general, have a nationwide weighted average preproductive period of 4 years.

Example 2. (i) Farmer B, a taxpayer that qualifies for the exception in paragraph (a)(2) of this section, grows plants that will have more than one crop or yield. The plants are grown in commercial quantities in the United States. The nationwide weighted average preproductive period of the plant is 2 years and 5 months. Farmer B acquires 1 month-old plants by purchasing them from an unrelated party, Corporation B. Farmer B enters into a contract with Corporation B

under which Corporation B will retain and tend the plants for 7 months following the sale. At the end of 7 months, Farmer B takes possession of the plants and plants them in the permanent orchard. The plants become productive in marketable quantities 1 year and 11 months after they are planted by Farmer B.

(ii) Since the plants are deemed to have a preproductive period in excess of 2 years, Farmer B is required to capitalize the costs of producing the plants. See paragraphs (a)(2) and (b)(2)(i)(B) of this section. In accordance with paragraph (b)(2)(i)(C)(*1*) of this section, Farmer B must begin to capitalize the preproductive period costs when the purchase occurs. In accordance with paragraph (b)(2)(i)(C)(*2*) of this section, Farmer B must continue to capitalize the preproductive period costs to the plants until the plants begin to produce in marketable quantities. Thus, Farmer B must capitalize the preproductive period costs of the plants for a period of 2 years and 6 months (the 7 months the plants are tended by Corporation B and the 1 year and 11 months after the plants are planted by Farmer B), that is, until the plants are 2 years and 7 months old, notwithstanding the fact that the plants, in general, have a nationwide weighted average preproductive period of 2 years and 5 months.

Example 3. (i) Assume the same facts as in *Example 2*, except that Farmer B acquires the plants by purchasing them from Corporation B when the plants are 8 months old and that the plants are planted by Farmer B upon acquisition.

(ii) Since the plants are deemed to have a preproductive period in excess of 2 years, Farmer B is required to capitalize the costs of producing the plants. See paragraphs (a)(2) and (b)(2)(i)(B) of this section. In accordance with paragraph (b)(2)(i)(C)(*1*) of this section, Farmer B must begin to capitalize the preproductive period costs when the plants are planted. In accordance with paragraph (b)(2)(i)(C)(*2*) of this section, Farmer B must continue to capitalize the preproductive period costs to the plants until the plants begin to produce in marketable quantities. Thus, Farmer B must capitalize the preproductive period costs of the plants for a period of 1 year and 11 months.

Example 4. (i) Farmer C, a taxpayer that qualifies for the exception in paragraph (a)(2) of this section, grows plants that will have more than one crop or yield. The plants are grown in commercial quantities in the United States. Farmer C acquires 1 month-old plants from an unrelated party and plants them immediately. The nationwide weighted average preproductive period of the plant is 2 years and 3 months. The particular plants grown by Farmer C begin to produce in marketable quantities 1 year and 10 months after they are planted by Farmer C.

(ii) Since the plants are deemed to have a nationwide weighted average preproductive period in excess of 2 years, Farmer C is required to capitalize the costs of producing the plants, notwithstanding the fact that the particular plants grown by Farmer C become productive in less than 2 years. See paragraph (b)(2)(i)(B) of this section. In accordance with paragraph (b)(2)(i)(C)(*1*) of this section, Farmer C must begin to capitalize the preproductive period costs when it plants the plants. In accordance with paragraph (b)(2)(i)(C)(*2*) of this section, Farmer C properly ceases capitalization of preproductive period costs when the plants become productive in marketable quantities (that is, 1 year and 10 months after they are planted, which is when they are 1 year and 11 months old).

Example 5. (i) Farmer D, a taxpayer that qualifies for the exception in paragraph (a)(2) of this section, grows plants that will have more than one crop or yield. The plants are not grown in commercial quantities in the United States. Farmer D acquires and plants the plants when they are 1 year old and estimates that they will become productive in marketable quantities 3 years after planting. Thus, at the time the plants are acquired and planted Farmer D reasonably estimates that the plants will have a preproductive period of 4 years. The actual plants grown by Farmer D do not begin to produce in marketable quantities until 3 years and 6 months after they are planted by Farmer D.

(ii) Since the plants have an estimated preproductive period in excess of 2 years, Farmer D is required to capitalize the costs of producing the plants. See paragraph (b)(2)(i)(B) of this section. In accordance with paragraph (b)(2)(i)(C)(*1*) of this section, Farmer D must begin to capitalize the preproductive period costs when it acquires and plants the plants. In accordance with paragraph (b)(2)(i)(C)(*2*) of this section, Farmer D must continue to capitalize the preproductive period costs until the plants begin to produce in marketable quantities. Thus, Farmer D must capitalize the preproductive period costs of the plants for a period of 3 years and 6 months (that is, until the plants are 4 years and 6 months old), notwithstanding the fact that Farmer D estimated that the plants would become productive after 4 years.

Example 6. (i) Farmer E, a taxpayer that qualifies for the exception in paragraph (a)(2) of this section grows plants from seed. The plants are not grown in commercial quantities in the United States. The plants do not have more than 1 crop or yield. At the time the seeds are planted Farmer E reasonably estimates that the plants will have a preproductive period of 1 year and 10 months. The actual plants grown by Farmer E are not ready for harvesting and disposal until 2 years and 2 months after the seeds are planted by Farmer E.

(ii) Because Farmer E's estimate of the preproductive period (which was 2 years or less) was reasonable at the time made based on the facts, Farmer E will not be required to capitalize the costs of producing the plants under section 263A, notwithstanding the fact that the actual preproductive period of the plants exceeded 2 years. See paragraph (b)(2)(i)(B) of this section. However, Farmer E must take the actual preproductive period of the plants into consideration when making future estimates of the preproductive period of such plants.

Example 7. (i) Farmer F, a calendar year taxpayer that does not qualify for the exception in paragraph (a)(2) of this section, grows trees that will have more than one crop. Farmer F acquires and plants the trees in April, Year 1. On October 1, Year 6, the trees become productive in marketable quantities.

(ii) The costs of producing the plant, including the preproductive period costs incurred by Farmer F on or before October 1, Year 6, are capitalized to the trees. Preproductive period costs incurred after October 1, Year 6, are capitalized to a crop when incurred during the preproductive period of the crop and deducted as a cost of maintaining the tree when incurred between the disposal of one crop and the appearance of the next crop. See paragraphs (b)(2)(i)(A), (b)(2)(i)(C)(*1*) and (b)(2)(i)(C)(*2*) of this section.

Example 8. (i) Farmer G, a taxpayer that qualifies for the exception in paragraph (a)(2) of this section, produces fig trees on 10 acres of land. The fig trees are grown in commercial quantities in the United States and have a nationwide weighted average preproductive period in excess of 2 years. Farmer G acquires and plants the fig trees in their permanent grove during Year 1. When the fig trees are mature, Farmer G expects to harvest 10x tons of figs per acre. At the end of Year 4, Farmer G harvests .5x tons of figs per acre that it sells for $100x. During Year 4, Farmer G incurs expenses related to the fig operation of: $50x to harvest the figs and transport them to market and other direct and indirect costs related to the fig operation in the amount of $1000x.

(ii) Since the fig trees have a preproductive period in excess of 2 years, Farmer G is required to capitalize the costs of producing the fig trees. See paragraphs (a)(2) and (b)(2)(i)(B) of this section. In accordance with paragraph (b)(2)(i)(C)(*2*) of this section, Farmer G must continue to capitalize preproductive period costs to the trees until they become productive in marketable quantities. The following factors weigh in favor of a determination that the fig trees did not become productive in Year 4: the quantity of harvested figs is *de minimis* based on the fact that the yield is only 5 percent of the expected yield at maturity and the proceeds from the sale of the figs are sufficient, after covering the costs of harvesting and transporting the figs, to cover only a negligible portion of the allocable farm expenses. Based on these facts and circumstances, the fig trees did not become productive in marketable quantities in Year 4.

(ii) *Animal.* An animal's actual preproductive period is used to determine the period that the taxpayer must capitalize preproductive period costs with respect to a particular animal.

(A) *Beginning of the preproductive period.* The preproductive period of an animal begins at the time of acquisition, breeding, or embryo implantation.

(B) *End of the preproductive period.* In the case of an animal that will be used in the trade or business of farming (for example, a dairy cow), the preproductive period generally ends when the animal is (or would be considered) placed in service for

purposes of section 168 (without regard to the applicable convention). However, in the case of an animal that will have more than one yield (for example, a breeding cow), the preproductive period ends when the animal produces (for example, gives birth to) its first yield. In the case of any other animal, the preproductive period ends when the animal is sold or otherwise disposed of.

(C) *Allocation of costs between animal and yields.* In the case of an animal that will have more than one yield, the costs incurred after the beginning of the preproductive period of the first yield but before the end of the preproductive period of the animal must be allocated between the animal and the yield using any reasonable method. Any depreciation allowance on the animal may be allocated entirely to the yield. Costs incurred after the beginning of the preproductive period of the second yield, but before the first yield is weaned from the animal must be allocated between the first and second yield using any reasonable method. However, a taxpayer may elect to allocate these costs entirely to the second yield. An allocation method used by a taxpayer is a method of accounting that must be used consistently and is subject to the rules of section 446 and the regulations thereunder.

(c) *Inventory methods*—(1) *In general.* Except as otherwise provided, the costs required to be allocated to any plant or animal under this section may be determined using reasonable inventory valuation methods such as the farm-price method or the unit-livestock-price method. See § 1.471–6. Under the unit-livestock-price method, unit prices must include all costs required to be capitalized under section 263A. A taxpayer using the unit-livestock-price method may elect to use the cost allocation methods in § 1.263A–1(f) or 1.263A–2(b) to allocate its direct and indirect costs to the property produced in the business of farming. In such a situation, section 471 costs are the costs taken into account by the taxpayer under the unit-livestock-price method using the taxpayer's standard unit price as modified by this paragraph (c)(1). Tax shelters, as defined in paragraph (a)(2)(ii) of this section, that use the unit-livestock-price method for inventories must include in inventory the annual standard unit price for all animals that are acquired during the taxable year, regardless of whether the purchases are made during the last 6 months of the taxable year. Taxpayers required by section 447 to use an accrual method or prohibited by section 448(a)(3) from using the cash method that use the unit-livestock-price method must modify the annual standard price in order to reasonably reflect the particular period in the taxable year in which purchases of livestock are made, if such modification is necessary in order to avoid significant distortions in income that would otherwise occur through operation of the unit-livestock-price method.

(2) *Available for property used in a trade or business.* The farm-price method or the unit-livestock-price method may be used by any taxpayer to allocate costs to any plant or animal under this section, regardless of whether the plant or animal is held or treated as inventory property by the taxpayer. Thus, for example, a taxpayer may use the unit-livestock-price method to account for the costs of raising livestock that will be used in the trade or business of farming (for example, a breeding animal or a dairy cow) even though the property in question is not inventory property.

(3) *Exclusion of property to which section 263A does not apply.* Notwithstanding a taxpayer's use of the farm-price method with respect to farm property to which the provisions of section 263A apply, that taxpayer is not required, solely by such use, to use the farm-price method with respect to farm property to which the provisions of section 263A do not apply. Thus, for example, assume Farmer A raises fruit trees that have a preproductive period in excess of 2 years and to which the provisions of section 263A, therefore, apply. Assume also that Farmer A raises cattle and is not required to use an accrual method by section 447 or prohibited from using the cash method by section 448(a)(3). Because Farmer A qualifies for the exception in paragraph (a)(2) of this section, Farmer A is not required to capitalize the costs of raising the cattle. Although Farmer A may use the farm-price method with respect to the fruit trees, Farmer A is not required to use the farm-price method with respect to the cattle. Instead, Farmer A's accounting for the cattle is determined under other provisions of the Code and regulations.

(d) *Election not to have section 263A apply*—(1) *Introduction.* This paragraph (d) permits certain taxpayers to make an election not to have the rules of this section apply to any plant produced in a farming business conducted by the electing taxpayer. The election is a method of accounting under section 446, and once an election is made, it is revocable only with the consent of the Commissioner.

(2) *Availability of the election.* The election described in this paragraph (d) is available to any taxpayer that produces plants in a farming business, except that no election may be made by a corporation, partnership, or tax shelter required to use the accrual method under section 447 or prohibited from using the cash method by section 448(a)(3). Moreover, the election does not apply to the costs of planting, cultivation, maintenance, or development of a citrus or almond grove (or any part thereof) incurred prior to the close of the fourth taxable year beginning with the taxable year in which the trees were planted in the permanent grove (including costs incurred prior to the permanent planting). If a citrus or almond grove is planted in more than one taxable year, the portion of the grove planted in any one taxable year is treated as a separate grove for purposes of determining the year of planting.

(3) *Time and manner of making the election*—(i) *Automatic election.* A taxpayer makes the election under this paragraph (d) by not applying the rules of section 263A to determine the capitalized costs of plants produced in a farming business and by applying the special rules in paragraph (d)(4) of this section on its original return for the first taxable year in which the taxpayer is otherwise required to capitalize section 263A costs. Thus, in order to be treated as having made the election under this paragraph (d), it is necessary to report both income and expenses in accordance with the rules of this paragraph (d) (for example, it is necessary to use the alternative depreciation system as provided in paragraph (d)(4)(ii) of this section). For example, a farmer who deducts costs that are otherwise required to be capitalized under section 263A but fails to use the alternative depreciation system under section 168(g)(2) for applicable property placed in service has not made an election under this paragraph (d) and is not in compliance with the provisions of section 263A. In the case of a partnership or S corporation, the election must be made by the partner, shareholder, or member.

(ii) *Nonautomatic election.* A taxpayer that does not make the election under this paragraph (d) as provided in paragraph (d)(3)(i) must obtain the consent of the Commissioner to make the election by filing a Form 3115, Application for Change in Method of Accounting, in accordance with § 1.446–1(e)(3).

(4) *Special rules.* If the election under this paragraph (d) is made, the taxpayer is subject to the special rules in this paragraph (d)(4).

(i) *Section 1245 treatment.* The plant produced by the taxpayer is treated as section 1245 property and any gain resulting from any disposition of the plant is recaptured (that is, treated as ordinary income) to the extent of the total amount of the deductions that, but for the election, would have been required to be capitalized with respect to the plant. In calculating the amount of gain that is recaptured under this paragraph (d)(4)(i), a taxpayer may use the farm-price method or another simplified method permitted under these regulations in determining the deductions that otherwise would have been capitalized with respect to the plant.

(ii) *Required use of alternative depreciation system.* If the taxpayer or a related person makes an election under this paragraph (d), the alternative depreciation system (as defined in section 168(g)(2)) must be applied to all property used predominantly in any farming business of the taxpayer or related person and placed in service in any taxable year during which the election is in effect. The requirement to use the alternative depreciation system by reason of an election under this paragraph (d) will not prevent a taxpayer from making an election under section 179 to deduct certain depreciable business assets.

(iii) *Related person*—(A) *In general.* For purposes of this paragraph (d)(4), related person means—

(*1*) The taxpayer and members of the taxpayer's family;

(*2*) Any corporation (including an S corporation) if 50 percent or more of the stock (in value) is owned directly or indirectly (through the application of section 318) by the taxpayer or members of the taxpayer's family;

(*3*) A corporation and any other corporation that is a member of the same controlled group (within the meaning of section 1563(a)(1)); and

(*4*) Any partnership if 50 percent or more (in value) of the interests in such partnership is owned directly or indirectly by the taxpayer or members of the taxpayer's family.

(B) *Members of family.* For purposes of this paragraph (d)(4)(iii), the terms ''members of the taxpayer's family'', and ''members of family'' (for purposes of applying section 318(a)(1)), means the spouse of the taxpayer (other than a spouse who is legally separated from the individual under a decree of divorce or separate maintenance) and any of the taxpayer's children (including legally adopted children) who have not reached the age of 18 as of the last day of the taxable year in question.

(5) *Examples.* The following examples illustrate the provisions of this paragraph (d):

Example 1. (i) Farmer A, an individual, is engaged in the trade or business of farming. Farmer A grows apple trees that have a preproductive period greater than 2 years. In addition, Farmer A grows and harvests wheat and other grains. Farmer A elects under this paragraph (d) not to have the rules of section 263A apply to the costs of growing the apple trees.

(ii) In accordance with paragraph (d)(4) of this section, Farmer A is required to use the alternative depreciation system described in section 168(g)(2) with respect to all property used predominantly in any farming business in which Farmer A engages (including the growing and harvesting of wheat) if such property is placed in service during a year for which the election is in effect. Thus, for example, all assets and equipment (including trees and any equipment used to grow and harvest wheat) placed in service during a year for which the election is in effect must be depreciated as provided in section 168(g)(2).

Example 2. Assume the same facts as in *Example 1*, except that Farmer A and members of Farmer A's family (as defined in paragraph (d)(4)(iii)(B) of this section) also own 51 percent (in value) of the interests in Partnership P, which is engaged in the trade or business of growing and harvesting corn. Partnership P is a related person to Farmer A under the provisions of paragraph (d)(4)(iii) of this section. Thus, the requirements to use the alternative depreciation system under section 168(g)(2) also apply to any property used predominantly in a trade or business of farming which Partnership P places in service during a year for which an election made by Farmer A is in effect.

(e) *Exception for certain costs resulting from casualty losses*—(1) *In general.* Section 263A does not require the capitalization of costs that are attributable to the replanting, cultivating, maintaining, and developing of any plants bearing an edible crop for human consumption (including, but not limited to, plants that constitute a grove, orchard, or vineyard) that were lost or damaged while owned by the taxpayer by reason of freezing temperatures, disease, drought, pests, or other casualty (replanting costs). Such replanting costs may be incurred with respect to property other than the property on which the damage or loss occurred to the extent the acreage of the property with respect to which the replanting costs are incurred is not in excess of the acreage of the property on which the damage or loss occurred. This paragraph (e) applies only to the replanting of plants of the same type as those lost or damaged. This paragraph (e) applies to plants replanted on the property on which the damage or loss occurred or property of the same or lesser acreage in the United States irrespective of differences in density between the lost or damaged and replanted plants. Plants bearing crops for human consumption are those crops normally eaten or drunk by humans. Thus, for example, costs incurred with respect to replanting plants bearing jojoba beans do not qualify for the exception provided in this paragraph (e) because that crop is not normally eaten or drunk by humans.

(2) *Ownership.* Replanting costs described in paragraph (e)(1) of this section generally must be incurred by the taxpayer that owned the property at the time the plants were lost or damaged. Paragraph (e)(1) of this section will apply, however, to costs incurred by a person other than the taxpayer that owned the plants at the time of damage or loss if—

(i) The taxpayer that owned the plants at the time the damage or loss occurred owns an equity interest of more than 50 percent in such plants at all times during the taxable year in which the replanting costs are paid or incurred; and

(ii) Such other person owns any portion of the remaining equity interest and materially participates in the replanting, cultivating, maintaining, or developing of such plants during the taxable year in which the replanting costs are paid or incurred. A person will be treated as materially participating for purposes of this provision if such person would otherwise meet the requirements with respect to material participation within the meaning of section 2032A(e)(6).

(3) *Examples.* The following examples illustrate the provisions of this paragraph (e):

Example 1. (i) Farmer A grows cherry trees that have a preproductive period in excess of 2 years and produce an annual crop. These cherries are normally eaten by humans. Farmer A grows the trees on a 100 acre parcel of land (parcel 1) and the groves of trees cover the entire acreage of parcel 1. Farmer A also owns a 150 acre parcel of land (parcel 2) that Farmer A holds for future use. Both parcels are in the United States. In 2000, the trees and the irrigation and drainage systems that service the trees are destroyed in a casualty (within the meaning of paragraph (e)(1) of this section). Farmer A installs new irrigation and drainage systems on parcel 1, purchases young trees (seedlings), and plants the seedlings on parcel 1.

(ii) The costs of the irrigation and drainage systems and the seedlings must be capitalized. In accordance with paragraph (e)(1) of this section, the costs of planting, cultivating, developing, and maintaining the seedlings during their preproductive period are not required to be capitalized by section 263A.

Example 2. (i) Assume the same facts as in *Example 1* except that Farmer A decides to

replant the seedlings on parcel 2 rather than on parcel 1. Accordingly, Farmer A installs the new irrigation and drainage systems on 100 acres of parcel 2 and plants seedlings on those 100 acres.

(ii) The costs of the irrigation and drainage systems and the seedlings must be capitalized. Because the acreage of the related portion of parcel 2 does not exceed the acreage of the destroyed orchard on parcel 1, the costs of planting, cultivating, developing, and maintaining the seedlings during their preproductive period are not required to be capitalized by section 263A. See paragraph (e)(1) of this section.

Example 3. (i) Assume the same facts as in *Example 1* except that Farmer A replants the seedlings on parcel 2 rather than on parcel 1, and Farmer A additionally decides to expand its operations by growing 125 rather than 100 acres of trees. Accordingly, Farmer A installs new irrigation and drainage systems on 125 acres of parcel 2 and plants seedlings on those 125 acres.

(ii) The costs of the irrigation and drainage systems and the seedlings must be capitalized. The costs of planting, cultivating, developing, and maintaining 100 acres of the trees during their preproductive period are not required to be capitalized by section 263A. The costs of planting, cultivating, maintaining, and developing the additional 25 acres are, however, subject to capitalization under section 263A. See paragraph (e)(1) of this section.

(4) *Special rule for citrus and almond groves*—(i) *In general.* The exception in this paragraph (e) is available with respect to replanting costs of a citrus or almond grove incurred prior to the close of the fourth taxable year after replanting, notwithstanding the taxpayer's election to have section 263A not apply (described in paragraph (d) of this section).

(ii) *Example.* The following example illustrates the provisions of this paragraph (e)(4):

Example. (i) Farmer A, an individual, is engaged in the trade or business of farming. Farmer A grows citrus trees that have a preproductive period of 5 years. Farmer A elects, under paragraph (d) of this section, not to have section 263A apply. This election, however, is unavailable with respect to the costs of producing a citrus grove incurred within the first 4 years beginning with the year the trees were planted. See paragraph (d)(2) of this section. In year 10, after the citrus grove has become productive in marketable quantities, the citrus grove is destroyed by a casualty within the meaning of paragraph (e)(1) of this section. In year 10, Farmer A acquires and plants young citrus trees in the same grove to replace those destroyed by the casualty.

(ii) Farmer A must capitalize the costs of producing the citrus grove incurred before the close of the fourth taxable year beginning with the year in which the trees were permanently planted. As a result of the election not to have section 263A apply, Farmer A may deduct the preproductive period costs incurred in the fifth year. In year 10, Farmer A must capitalize the acquisition cost of the young trees. However, the costs of planting, cultivating, developing, and maintaining the young trees that replace those destroyed by the casualty are exempted from capitalization under this paragraph (e).

(f) *Effective date and change in method of accounting*—(1) *Effective date.* In the case of property that is not inventory in the hands of the taxpayer, this section is applicable to costs incurred after August 21, 2000 in taxable years ending after August 21, 2000. In the case of inventory property, this section is applicable to taxable years beginning after August 21, 2000.

(2) *Change in method of accounting.* Any change in a taxpayer's method of accounting necessary to comply with this section is a change in method of accounting to which the provisions of sections 446 and 481 and the regulations thereunder apply. For property that is not inventory in the hands of the taxpayer, a taxpayer is granted the consent of the Commissioner to change its method of accounting to comply with the provisions of this section for costs incurred after August 21, 2000, provided the change is made for the first taxable year ending after August 21, 2000. For inventory property, a taxpayer is granted the consent of the Commissioner to change its method of accounting to comply with the provisions of this section for the first taxable year beginning after August 21, 2000. A taxpayer changing its method of accounting under this paragraph (f)(2) must file a Form 3115, ''Application for Change in Accounting Method,'' in accordance with the automatic consent procedures in Rev. Proc. 99–49 (1999–2 I.R.B. 725) (see § 601.601(d)(2) of this chapter). However, the scope limitations in section 4.02 of Rev. Proc. 99–49 do not apply, provided the taxpayer's method of accounting for property produced in a farming business is not an issue under consideration within the meaning of section 3.09 of Rev. Proc. 99–49. If the taxpayer is under examination, before an appeals office, or before a federal court at the time that a copy of the Form 3115 is filed with the national office, the taxpayer must provide a duplicate copy of the Form 3115 to the examining agent, appeals officer, or counsel for the government, as appropriate, at the time the copy of the Form 3115 is filed. The Form 3115 must contain the name(s) and telephone number(s) of the examining agent, appeals officer, or counsel for the government, as appropriate. Further, in the case of property that is not inventory in the hands of the taxpayer, a change under this paragraph (f)(2) is made on a cutoff basis as described in section 2.06 of Rev. Proc. 99–49 and without the audit protection provided in section 7 of Rev. Proc. 99–49. However, a taxpayer may receive such audit protection for non-inventory property by taking into account any section 481(a) adjustment that results from the change in method of accounting to comply with this section. A taxpayer that opts to determine a section 481(a) adjustment (and, thus, obtain audit protection) for non-inventory property must take into account only additional section 263A costs incurred after December 31, 1986, in taxable years ending after December 31, 1986. Any change in method of accounting that is not made for the taxpayer's first taxable year ending or beginning after August 21, 2000, whichever is applicable, must be made in accord with the procedures in Rev. Proc. 97–27 (1997–1 C.B. 680) (see § 601.601(d)(2) of this chapter).

§ 1.263A–4T [Removed]

Par. 7. Section 1.263A–4T is removed.

Par. 8. Section 1.471–6 is amended as follows:

1. The third sentence of paragraph (d) is revised.

2. The last sentence of paragraph (f) is revised. The revisions read as follows:

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

* * * * *

(d) * * * However, see § 1.263A–4(c)(3) for an exception to this rule. * * *

* * * * * *

(f) * * * See § 1.263A–4 for rules regarding the computation of costs for purposes of the unit-livestock-price-method.

* * * * * *

Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: August 10, 2000.

Jonathan Talisman,

Acting Assistant Secretary of the Treasury (Tax Policy).

[FR Doc. 00–21103 Filed 8–18–00; 8:45 am]

BILLING CODE 4830–01–P