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## **Internal Revenue Code Section 471**

### General rule for inventories

(a) General rule.

Whenever in the opinion of the Secretary the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer on such basis as the Secretary may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.

(b) Estimates of inventory shrinkage permitted.

A method of determining inventories shall not be treated as failing to clearly reflect income solely because it utilizes estimates of inventory shrinkage that are confirmed by a physical count only after the last day of the taxable year if-

- (1) the taxpayer normally does a physical count of inventories at each location on a regular and consistent basis, and
- (2) the taxpayer makes proper adjustments to such inventories and to its estimating methods to the extent such estimates are greater than or less than the actual shrinkage.

(c) Cross reference.

For rules relating to capitalization of direct and indirect costs of property, see section 263A .