

Is It Time to Check Your Tax Accounting Method?

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Are you currently an accrual-basis taxpayer who is eligible to use the cash method? Are you currently a cash-basis taxpayer who may be required to change to the accrual method? As the tax year for calendar year-end businesses has only a couple of months remaining, answering questions such as these is important for assessing a company's tax situation for 2009.

Each year, American businesses file their federal tax returns with the Internal Revenue Service, reporting an amount of taxable income or loss. These returns are generally characterized by multiple pages containing various schedules, all leading to the derivation of this number. The disciplinarian that guides the reporting and the calculations is the tax accounting method that is used.

Federal tax rules acknowledge certain permissible accounting methods, including the cash and accrual methods, and present options and eligibility requirements with respect to these methods. Determining factors in this regard are items such as business type (e.g., C corporation, S corporation, partnership), business activities (services, inventory sales), and business volume (e.g., annual gross receipts). Notably, there are rules providing special exceptions for use of the cash method by businesses that average \$1M in receipts and certain ones that average \$10M in receipts.

Many changes in accounting methods are automatic, and these can be acknowledged with the IRS by filing a special form by the due date of the company's tax return. Other changes require consent from the IRS, and they must be requested before the end of the tax year.

For most businesses, the tax accounting method used is well-established and unchangeable. For some, though, an assessment of the company's tax accounting method could lead to a discovery that the company is eligible to use the cash method or to a recognition that it is required to switch to the accrual method. By making this determination before the year ends, a company can avert unanticipated tax consequences.