

## Accrual to Cash Consulting

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### **Definition:**

To assess a taxpayer's potential tax savings in changing its accounting method from accrual to cash. To be completed by a professional from the tax department.

### **Benefits:**

A major advantage of the cash basis method of accounting over other accounting methods is allowing taxpayers to defer income until payments are actually or constructively received, instead of having to recognize income as receivables are created. It also applies to deductions for expenses as well, allowing expenses to be deducted at the later date of payment or use.

### **Process:**

- Determine the classification of the taxpayer's principle business and whether the cash method of accounting is permissible
- Determine any inventory accounting requirements
- Determine the taxpayer's type of entity and whether the accrual method of accounting is a requirement
- Consider converting the entity type if changing to the cash method of accounting would result in significant tax savings
- Gather financial information and analyze for any further restrictions
- Compute taxable income, income tax and tax savings from changing accounting methods
- Complete and file required tax forms and returns

### **Case Example:**

A construction client, filing as an S Corporation, was considered to be a candidate to benefit in tax savings in converting from the accrual method to the cash method of accounting. The conversion process resulted in a built in change of \$128,820 of prior years' income, which was spread over a four-year period. The current year expense adjustment was \$204,287. If we assume the taxpayer's marginal tax bracket to be 35%, the taxpayer would have reduced income by \$172,082 during the first year, which equates to approximately \$60,000 of tax savings.