

USE OF CASH METHOD OF ACCOUNTING BY TAXPAYERS THAT PROVIDE GOODS AND SERVICES

- Recent court decisions have upheld the use of the cash method of accounting by certain taxpayers who provide both goods and services. (Galedrige, Osteopathic, Turin, RACMP, and Smith) The cases involved emulsified asphalt, concrete, and flooring contractors, and health care providers that administered chemotherapy drugs. The IRS had argued that the taxpayers were in the business of providing merchandise and, therefore, required to use inventory accounts and an accrual method of accounting.
- In response to these cases, and to reduce the burden on affected taxpayers, four significant pieces of guidance have been provided.
- First, on April 28th, 2000, the IRS issued an action on decision in response to the Osteopathic case (AOD 2000-05). The AOD says that the IRS agrees that prescription drugs or similar items administered by a health care provider are not merchandise that could prevent the provider from using the cash method..
- Second, on January 8th, 2001, Rev. Proc. 2001-10 was published. The revenue procedure permits taxpayers, including those that provide merchandise, that have average annual gross receipts of \$1 million or less to use the cash method.
- Third, a Chief Counsel notice was issued on February 9th, 2001 (CC-2001-010). The notice announces a change in the IRS's litigating position. The notice states that, pending further guidance, the IRS will not assert that taxpayers in businesses such as paving, painting, roofing, drywall, or landscaping are providing merchandise and, therefore, must use inventory accounts and an accrual method.
- Fourth, the Deputy Commissioner has written a memorandum to the Commissioners for SB/SE, W&I, and LMSB (February 14, 2001). Similar to the Chief Counsel notice, the memorandum states that, pending further guidance, an examiner will not propose that a taxpayer must use inventory accounts and an accrual method in businesses such as paving, painting, roofing, drywall, or landscaping on the basis that the taxpayer is providing merchandise.
- Finally, it has been recommended that a project aimed at finally resolving this issue be placed on the 2001 Priority Guidance Plan for publication this year.