



THE AMERICAN  
INSTITUTE  
OF ARCHITECTS



January 17, 2014

The Honorable Max Baucus, Chairman  
Senate Committee on Finance  
Washington, D.C. 20510

The Honorable Orrin Hatch, Ranking Member  
Senate Committee on Finance  
Washington, D.C. 20510

RE: Cash Basis Method Should be Retained for All Professional Firms and Farms

Dear Chairman Baucus and Ranking Member Hatch:

We, the undersigned associations, represent businesses from across the entire American economy, including literally thousands of providers of essential services nationwide. We are writing to oppose a proposed change in the taxation of our businesses included in the Cost Recovery and Accounting Discussion Draft dated November 21, 2013 (Discussion Draft). This proposal would require many of our members to change the method of accounting used for tax purposes from the cash basis method to the accrual method.

Many of our members' businesses include pass-through entities and personal service corporations that, essentially, are comprised of groups of individuals who have banded together to share resources, such as office space and staff. These businesses do not carry inventory or have other expenses that can reasonably be deferred. Generally, each owner in a firm is responsible for the business's operations and the form of organization, whether a partnership, limited liability company, or personal services corporation, is chosen to facilitate efficient businesses practices.

Most significantly, a change from the cash basis method for tax purposes would result in those who own and operate these businesses to pay tax before cash is received. They would be required to recognize revenue in advance of actually getting paid. Because the expenses of such organizations would essentially remain the same, this requirement would result in higher net taxable income for Federal tax purposes. In addition, switching from the cash method to the accrual method of accounting will lead to significant cash-flow problems. For example, among professional services firms, the primary cost is labor, and businesses must regularly pay their employees even if they are not paid by their clients for several months. The use of cash accounting helps to mitigate this challenge by allowing the business's owners to make tax payments after receiving payment for their services.

Farm and ranch businesses have an additional complication because the growing of crops and raising of livestock is a production activity under accrual accounting. As a result, production costs could not be expensed but instead would be accumulated as inventory and deducted when the commodity is sold. The inability to match revenue with expenses to target an optimum level of income for tax purposes will result in higher effective tax rates. This problem is exacerbated by the volatility of commodity prices caused by uncontrollable weather and unpredictable markets.

The Discussion Draft calls for increasing the gross receipts test from \$5 million to \$10 million for all businesses in order to continue to utilize the cash basis method. This is a welcome change. Farms and businesses operating in the personal service sector, which include accounting firms, law firms, medical and dental practices, architecture firms, engineering firms and others, should be allowed to continue to use the cash basis method for paying Federal taxes. We strongly oppose requiring these personal service entities to use the accrual method and lowering the current \$25 million threshold for farms.

We believe that tax reform is a laudable goal and that simplification of the tax code is very important. However, converting from the cash method to accrual basis would not be simpler and may actually create a significant burden on these professional services sector businesses and farms.

Thank you for consideration of our views.

Sincerely,

American Council of Engineering Companies

American Dental Association

American Farm Bureau Federation

American Institute of Architects

American Institute of CPAs

S Corporation Association