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# The VOS Voice

*“Because Accounting Matters And We Know It”*

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## Inside This Issue




## 2018 Q4 Tax Calendar: Key Deadlines for Businesses and Other Employees

Here are some of the key tax-related deadlines affecting businesses and other employers during the fourth quarter of 2018. Keep in mind that this list isn’t all-inclusive, so there may be additional deadlines that apply to you. Contact us to ensure you’re meeting all applicable deadlines and to learn more about the filing requirements.

***October 15***

- If a calendar-year C corporation that filed an automatic six-month extension:
  - File a 2017 income tax return (Form 1120) and pay any tax, interest and penalties due.
  - Make contributions for 2017 to certain employer-sponsored retirement plans.

***October 31***

- Report income tax withholding and FICA taxes for third quarter 2018 (Form 941) and pay any tax due. (See exception below under “November 13.”)

***November 13***

- Report income tax withholding and FICA taxes for third quarter 2018 (Form 941), if you deposited on time and in full all of the associated taxes due.

***December 17***

- If a calendar-year C corporation, pay the fourth installment of 2018 estimated income taxes.

> *Action is the foundational KEY to all success.*
>
> *-- Pablo Picasso*


## Beware Of Unexpected Tax Liabilities Under the New Accounting & Tax Rules

The Tax Cuts and Jobs Act (TCJA) contains a provision that ties revenue recognition for book purposes to income reporting for tax purposes, for tax years starting in 2018. This narrow section of the law could have a major impact on certain industries, especially as companies implement the updated revenue recognition standard under U.S. Generally Accepted Accounting Principles (GAAP).

***Recognizing revenue under GAAP***

Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers, went into effect for public companies this year; it will go into effect for private companies next year. The updated standard requires businesses to all use a single model for calculating the top line in their income statements under GAAP, as opposed to following various industry-specific models.

The standard doesn’t change the underlying economics of a business’s revenue streams. But it may change the timing of when companies record revenue in their financial statements. The standard introduces the concept of “performance obligations” in contracts with customers and allows revenue to be recorded only when these obligations are satisfied. It could

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mean revenue is recorded right away or in increments over time, depending on the transaction.

The changes will be most apparent for complex, long-term contracts. For example, most software companies expect to record revenues in their financial statements earlier under ASU 2014-09 than under the old accounting rules.

### ***Matching book and tax records***

Starting in 2018, the TCJA modifies Section 451 of the Internal Revenue Code so that a business recognizes revenue for tax purposes no later than when it's recognized for financial reporting purposes. Under Sec. 451(b), taxpayers that use the accrual method of accounting will meet the "all events test" no later than the taxable year in which the item is taken into account as revenue in a taxpayer's "applicable financial statement."

The TCJA also added Sec. 451(c), referred to as the "rule for advance payments." At a high level, the rule can require businesses to recognize taxable income even earlier than when it's recognized for book purposes if the company receives a so-called "advance payment."

Some companies delivering complex products, such as an aerospace parts supplier making a custom component, can receive payments from customers years before they build and deliver the product. Under ASU 2014-09, a business can't recognize revenue until it's completed its performance obligations in the contract, even if an amount has been paid in advance. However, under Sec. 451(c), companies may be taxed before they recognize revenue on their financial statements from contracts that call for advance payments.

### ***Will the changes affect your business?***

Changes in the TCJA, combined with the new revenue recognition rules under GAAP, will cause some companies to recognize taxable income sooner than in the past. In some industries, this could mean significantly accelerated tax bills. However, others won't experience any noticeable differences. We can help you evaluate how the accounting rule and tax law changes will affect your company, based on its unique circumstances.

> *There is no elevator to success,*
> *You have to take the stairs.*
>
> *-- Zig Ziglar*


## ASSESSING THE S-CORP

The S corporation business structure offers many advantages, including limited liability for owners and no double taxation (at least at the federal level). But not all businesses are eligible - and, with the new 21% flat income tax rate that now applies to C corporations, S-Corps may not be quite as attractive as they once were.

### ***Tax comparison***

The primary reason for electing S status is the combination of the limited liability of a corporation and the ability to pass corporate income, losses, deductions and credits through to shareholders. In other words, S-Corps generally avoid double taxation of corporate income — once at the corporate level and again when distributed to the shareholder. Instead, S-Corp tax items pass through to the shareholders' personal returns and the shareholders pay tax at their individual income tax rates.

But now that the C-Corp rate is only 21% and the top rate on qualified dividends remains at 20%, while the top individual rate is 37%, double taxation might be less of a concern. On the other hand, S-Corp owners may be able to take advantage of the new qualified business income (QBI) deduction, which can be equal to as much as 20% of QBI.

You have to run the numbers with your tax advisor, factoring in state taxes, too, to determine which structure will be the most tax efficient for you and your business.

### ***S eligibility requirements***

If S-Corp status makes tax sense for your business, you need to make sure you qualify - and stay qualified. To be eligible to elect to be an S-Corp or to convert to S status, your business must:

- Be a domestic corporation and have only one class of stock,
- Have no more than 100 shareholders, and
- Have only "allowable" shareholders, including individuals, certain trusts and estates. Shareholders can't include partnerships, corporations and nonresident alien shareholders.

In addition, certain businesses are ineligible, such as insurance companies.

**Please see *Assessing the S-Corp* on page 3**

***Assessing the S-Corp*** **from page 2**

***Reasonable compensation***

Another important consideration when electing S status is shareholder compensation. The IRS is on the lookout for S-Corps that pay shareholder-employees an unreasonably low salary to avoid paying Social Security and Medicare taxes and then make distributions that aren't subject to payroll taxes.

Compensation paid to a shareholder should be reasonable considering what a non-owner would be paid for a comparable position. If a shareholder's compensation doesn't reflect the fair market value of the services he or she provides, the IRS may reclassify a portion of distributions as unpaid wages. The company will then owe payroll taxes, interest and penalties on the reclassified wages.

***Pros and cons***

S-Corp status isn't the best option for every business. To ensure that you've considered all the pros and cons, contact us. Assessing the tax differences can be tricky — especially with the tax law changes going into effect this year.


## CASH VS. ACCRUAL REPORTING: WHICH IS RIGHT FOR YOUR BUSINESS?

Small businesses often use the cash-basis method of accounting. As businesses grow, they usually convert to accrual-basis reporting for federal tax purposes and to conform with U.S. Generally Accepted Accounting Principles (GAAP).

Starting this tax year, the Tax Cuts and Jobs Act (TCJA) has increased the threshold for businesses that qualify for the simpler cash method for federal tax purposes. Here's how these accounting methods compare and how the TCJA could affect your financial and tax reporting decisions.

***Cash method***

Companies that use the cash-basis method of accounting recognize revenue as customers pay invoices and expenses as they pay bills. So, cash-basis entities often report large fluctuations in profits from period to period, especially if they're engaged in long-term projects. This can make it hard to benchmark a company's performance from year to year — or against other entities that use the accrual method.

Cash-basis entities also tend to postpone revenue recognition and accelerate expense payments at year end. This strategy can temporarily defer the company's tax liability. But the flipside is that it can make a company appear less profitable to lenders and investors.

***Accrual method***

The more complex accrual-basis accounting method conforms to the matching principle under GAAP. That is, revenue (and expenses) are "matched" to the periods in which they're earned (or incurred).

Accrual-basis entities report several asset and liability accounts that are generally absent on a cash-basis balance sheet. Examples include prepaid expenses, accounts receivable, accounts payable, work in progress, accrued expenses and deferred taxes.

***TCJA considerations***

Under the TCJA, for tax years beginning after 2017, businesses with average annual gross receipts of $25 million or less for the previous three tax years are eligible for the cash method of accounting for federal income tax purposes. Under prior law, the gross-receipts threshold for the cash method was only $5 million.

In addition, for tax years beginning after 2017, the TCJA modifies Section 451 of the Internal Revenue Code so that a business recognizes revenue for tax purposes no later than when it's recognized for financial reporting purposes. So, if you use the accrual method for financial reporting purposes, you must also use it for federal income tax purposes.

These changes could prompt more companies to opt for the simpler, tax-deferred cash method for both financial reporting and tax purposes. But it's not right for everyone.

***Look before you leap***

As your small business grows, you might be tempted to switch to the accrual method of accounting to reduce variability in financial reporting from year to year — and to attract more sophisticated lenders and investors who prefer GAAP financials. But doing so could accelerate your tax obligations. On the other hand, if you're newly eligible for the cash method for tax purposes, you may want to switch to that method for the simplicity and tax deferral it offers.

If you're in either situation, contact us to discuss the pros and cons of these two options to ensure you're using the optimal method based on your circumstances.

***"Because Accounting Matters"***

## ~ *I R S Corner*

**IRS TAX TIP 2018-165:TIPS FOR TAXPAYERS WHO NEED TO RECONSTRUCT RECORDS AFTER DISASTER STRIKES**

After a disaster, taxpayers might need to reconstruct records. This could help them prove their losses, which may be essential for tax purposes, getting federal assistance or insurance reimbursement.

Here are several things taxpayers can do to help reconstruct or get copies of specific types of records after a disaster:

***Tax Return Transcripts***

- Taxpayers can get free tax return transcripts by using the Get Transcript tool on IRS.gov. They can also call 800-908-9946 to order them by phone.

***Proof of loss***

- To establish the extent of the damage, taxpayers should take photographs or videos of affected property as soon as possible after the disaster.
- Taxpayers can look on their mobile phone for pictures that show the property before the disaster damaged it.
- If a taxpayer doesn't have photographs or videos of their property, a simple method to help them remember what items they lost is to sketch pictures of each room that was affected.
- Taxpayers can support the valuation of property with photographs, videos, canceled checks, receipts, or other evidence.
- If they bought items using a credit card or debit card, they should gather past statements from their credit card company or bank. If the taxpayer didn't keep these records or they were destroyed, statements may be available online or they can contact their financial institution.

***Records about property***

- Taxpayers can contact the title company, escrow company, or bank that handled the purchase of their home to get copies of appropriate documents.
- Taxpayers who made improvements to their home should contact the contractors who did the work to see if records are available. If possible, the home owner should get statements from the contractors to verify the work and cost. They can also get written accounts from friends and relatives who saw the house before and after any improvements.
- For inherited property, taxpayers can check court records for probate values. If a trust or estate existed, the taxpayer can contact the attorney who handled the trust.
- When no other records are available, taxpayers can check the county assessor's office for old records that might address the value of the property.
- There are several resources that can help someone determine the current fair-market value of most cars on the road. These resources are all available online and at most libraries. They include Kelley's Blue Book, the National Automobile Dealers Association, and Edmunds.

More Information:
Publication 547, Casualties, Disasters, and Thefts
Publication 584, Casualty, Disaster, and Theft Loss Workbook
Publication 584-B, Business Casualty, Disaster, and Theft Loss Workbook
Publication 2194, Disaster Resource Guide for Individuals and Businesses
Small Business Administration
DisasterAssistance.gov