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How Do the New Revenue Recognition Rules Impact Tax?

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Most companies are aware of the new Accounting Standards Update for revenue recognition related to when revenue from contracts with customers for goods and services is recognized for financial statement purposes under Generally Accepted Accounting Principles. The Financial Accounting Standards Board issued the new standards in May 2014, but delayed implementation for public entities until years beginning after December 15, 2017 and for nonpublic entities until years beginning after December 15, 2018 (with an option to adopt early).

While many companies have considered the impact and implementation of the new rules on financial statements, far fewer have given equal consideration to the implications these new standards will have on their tax returns. There is very little guidance available as to the impact these new rules will have on tax reporting. The IRS issued Notice 2017-17 requesting comments on procedures for accounting method changes and on conformity between the new Standards and the Internal Revenue Code.   These comments are due to be submitted to the IRS by July 24, 2017.

While we do not have concrete information at this time, we anticipate that the adoption of the new revenue recognition standards for financial reporting purposes will result in accounting method changes for tax. If a company’s tax method has been following financial accounting and the company changes its book method, it cannot just change its tax method to follow the new book method. Rather, the company must first determine if the new book method is in accordance with the tax rules, and if so, the company will be required to file a Form 3115 requesting permission to change its tax method of accounting. Based on the preliminary guidance available, it appears that a change that is made as a result of, or directly related to, the adoption of the new revenue recognition standards for financial reporting purposes for the same year (a qualifying same-year method change) will be considered an automatic method change. Automatic method changes require the filing of a Form 3115 to be attached to a timely filed federal income tax return (including extension) for the year of the change and a filing of a duplicate copy with the National office of the IRS. It does not require a user fee.

It is important to evaluate the tax implications of the new revenue recognition standards as the accounting department is adopting the new rules. There may be potential impacts for federal income tax purposes, including accounting method changes and additional book-tax differences if the new book method does not comply with the Internal Revenue Code.   More guidance from the IRS is expected in the near future to address these questions, so be on the lookout for additional Insights on this topic soon.

If you have questions about the tax implications of revenue recognition, contact us.

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