

June 20, 2014

The Honorable Ron Wyden
Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

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

Dear Chairman Wyden and Ranking Member Hatch:

We write to express our support for appropriate reform of the federal tax code. As it currently stands, the federal tax code is overly complex, inefficient, and a significant hurdle to economic growth. Tax reform is needed to make the tax code simpler, fairer, easier to administer, and easier to comply. Further, the tax code should provide for economic growth for small businesses and benefit workers and consumers.

While we applaud your committee's efforts to reform the tax code, we are concerned about a provision contained in the Cost Recovery and Accounting Discussion Draft released late last year by former Chairman Baucus that would require many businesses to change the method of accounting used for tax purposes from the traditional cash basis method to the accrual method. As the Finance Committee develops its comprehensive tax reform package, we ask that you consider the negative impact that this proposal would have on the professional services sector as well as farming and ranching businesses. We believe that such a change has not been fully vetted and many of the concerns raised by these businesses have not been addressed.

Currently, the cash method is generally available for C corporations with no more than \$5 million in average annual gross receipts, and for individuals, partnerships, S corporations, professional service corporations and most farming and ranching businesses regardless of their annual revenue, unless they have inventory. The Cost Recovery and Accounting tax reform draft would require all of these businesses and individuals who exceed \$10 million in annual gross receipts to use the accrual method of accounting. While the draft is encouraging in that it raises the gross receipts test for C corporations from \$5 to \$10 million and therefore allows those affected businesses to use the traditional cash basis method, the adverse impact on previously exempt businesses having to convert to the accrual basis would be substantial.

While some may believe that subjecting all taxpayers with more than \$10 million in annual gross receipts to the same threshold is simpler, we disagree. Requiring more businesses to use the accrual method of accounting would create unnecessary complexity in the tax law and substantially increase compliance costs. In addition, the proposal would create a significant barrier to economic growth by discouraging many small businesses from expanding. Furthermore, requiring these businesses to switch from cash to accrual accounting would create significant long-term financial hardships, not just a one-time cost. In addition to the substantial cost of changing accounting systems, these businesses would also be burdened by having to pay tax on income before it is actually received.

For example, for professional services firms where the primary costs to operate include labor and office expenses—including many medical, dental, accounting, law, architectural, engineering, and consulting firms—the businesses must pay their employees and fixed operating expenses, regardless of when their patients or clients pay them. With farming and ranching businesses, an additional complication exists because growing crops and raising livestock are considered production activities under accrual accounting that would have to be accumulated as inventory and deducted when the commodity is sold. In each of these cases, the acceleration of the business' tax liability combined with the inability to match revenues with expenses would force businesses to borrow money to meet their tax liability. The basic tenant of taxation is "ability to pay." Forcing businesses to recognize income before they receive payment violates this basic tenant.

We believe that tax reform is very important and should be pursued with rigorous and thoughtful consideration by all Members of Congress. However, the proposal to limit the use of the cash basis of accounting for businesses in the professional services sector, as well as farms and ranches, would cause numerous adverse unintended consequences and as a result is opposed by many members of both parties. Therefore, we strongly encourage you to maintain the current ability of pass-through entities, personal services corporations, and farming and ranching businesses to use the cash basis for tax purposes irrespective of annual gross receipts.

Sincerely,