

What methods of accounting are available to a small business and to a large business? If the business decides to make an accounting methods change, how is this accomplished?

Three accounting methods available: accrual, cash or hybrid methods

Accrual method reports income and expenses in the period in which they earned the income or incurred the expense.

Cash method reports income and expenses in the period when they actually receive the income or pay the expense.

Hybrid method is a blend of accrual and cash methods. The sales, cost of goods sold, inventories, account receivable and accounts payable are all accounted for using the accrual method. But all other income and expenses use the cash method.

Corporation must use the accrual method unless it meets one of the following:

- Family farm
- Personal service corporation
- Gross receipts did not exceed \$5 million in the prior tax years.
- Has elected S Corporation election

Small business can use the cash method unless they have one of the following, then they must use the accrual method.

- They have a corporation as a shareholder
- If you produce, purchase or sell merchandise – unless the average annual gross receipts for each prior year is under \$1 million

To change the accounting method, the business must complete form 3115- Application for Change in Accounting Method

Response 2

Two basic accounting methods available are accrual and cash methods.

Accrual method recognizes transactions when they occur, not necessarily when cash is received or paid. Cash method record expenses in financial accounts when cash is actually laid out, and book revenue when actual cash in hand. Another accounting method that is also available is the hybrid method. Hybrid method is the combination of using two or more than one of the accounting methods mentioned. Businesses that decide to change accounting methods requires a formal approval of the IRS and file Form 3115 in duplicate and pay a fee.

A copy should be attached of taxpayer's income tax return and the other copy to be sent to the IRS commissioners.

Third Response

There are three types of accounting methods: accrual, cash and hybrid. The accrual method is used for businesses that do more than \$5 million dollars in gross receipts. Therefore, this method of accounting would be good for a large business. There are additional criteria items if the company meets those items then they are also eligible to use cash and hybrid accounting methods as well. The cash-based accounting method fits well with a small business. Depending on collection rates it may work well for the company to delay recognizing income until it is received. There are some exceptions to using this method such as material income-producing factor. The hybrid method uses the accrual method of accounting for sales, cost of goods sold, inventories, accounts receivable, and accounts payable. The cash basis of accounting is used for all other income and expense accounts. This method is common with small businesses. If the business decides to make an accounting change has to be approved by the Internal Revenue Service. The accounting method corresponds with the accounting method used to calculate taxes.

Fourth Response

The cash basis and accrual basis are the two main accounting methods used. It is a requirement by law to have some form of record-keeping for tax purpose. Informational results may be helpful to managers when the correct decisions are made upon which type of method to use. Changing accounting methods later is possible, but it is a complicated process. Thus, for small business owners, its very important to make a decision up front on the type of method that would be most suitable for their particular business to use. There are several advantages that come with the cash method. The cash method is more simple compared to an accrual method. Until it shows a more accurate picture of the cash flow and the money is received, its income will not be subject to taxation.

Whereas, the accrual basis recognizes income and expenses on a greater effort and allows revenue to be recorded when it's earned instead of when payment is received, and expenses are recorded when they are incurred instead of when a payment is made. An accrual method's advantage gives a more clear picture on the performance of a business over the long-term compared to the cash method. A disadvantage of it is that it is more complex than the cash basis, and income taxes may be owed on revenue before payment is received.

When a business wants to change an accounting method, the IRS requires formal approval. A business that wants to make a change must pay a fee and file Form 3115 in duplicate. The tax payer's income tax return must have a copy attached as well as have the other copy sent to the IRS Commissioners.

Accounting method changes usually result in adjustments to either positive or negative taxable income. Also, when changing accounting methods it does not permanently change the business's long-term taxable income, except for the way that income is recognized over time.