July 24, 2017

Via Electronic Mail
Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2017-17)
P.O. Box 7602
Ben Franklin Station
Washington, D.C. 20044

RE: Notice 2017-17 - Proposed Revenue Procedure Guidance for Requesting Accounting Method Changes Resulting or Related to the Adoption of New Financial Accounting Standards for the Recognition of Revenue

The Pennsylvania Institute of Certified Public Accountants (PICPA), respectfully submits the following comments on Notice 2017-17. Founded in 1897, the Pennsylvania Institute of Certified Public Accountants (PICPA) is a nonprofit, voluntary professional organization representing more than 22,000 members. Expressed goals of the PICPA are to speak on behalf of CPAs in Pennsylvania, as well as on behalf of the public interest. Thank you for the opportunity to review and comment.

Comments on Issues of Conformity Between the New Standards and the Code and Regulations

Question 1: To what extent would using the new standards for federal income tax purposes result in acceleration or deferral of income under Section 451 or other income provisions of the Internal Revenue Code?

It is very difficult to determine with accuracy the impact of the new revenue recognition accounting standards relative to acceleration or deferral of income under Internal Revenue Code Section 451 (and/or other sections such as Section 460) and the related regulations. Taxpayers need to determine on a contract-by-contract basis what the impact of these new accounting standards will be based on the specific terms of the contracts. We believe these new standards will impact when the "all events test" occurs, as referenced under Regulation Section 1.451-1.

It appears in some cases that the new accounting guidance has changed the definition used to determine when all events have occurred to enable the taxpayer to consider the revenue earned, and therefore release any future restrictions. Depending on the industry of the taxpayer, this could be a substantial change to the current method of accounting (i.e., percentage of completion), as the previously existing standards have now been redefined. Taxpayers may undertake preliminary procedures to review their contracts and determine the extent of the impact to their financial statements based on their existing method of accounting, but in most cases the true extent of this impact will not be known until books and records have been closed for the tax year. In some cases, this could either accelerate or decelerate the deferral of income. In either case, it is a timing difference that will have zero net impact over the life of the contract.

This IRS expectation of taxpayers requesting a change of accounting method accompanying the adoption of the new revenue recognition standards may anticipates a desire of some U.S. business taxpayers to seek more book-to-tax conformity regarding their revenue reporting system. Empirical evidence from one study suggests that with stronger book-to-tax earnings conformity, and the closer these two income sets become aligned, public firms have reported lower financial accounting earnings in order to defer taxes (Hanlon, Maydew, Shevlin 2005). Such possible conformity, and the possibility of greater deferral of tax, will be affected by innumerable factors, not limited to: challenges to obtaining consent for changes to the entities accounting methods, specific industry concerns, the expectation of future long-term tax rates, and the cost/complexity.
Question 2: What industry and/or transaction specific issues might arise as a result of the new standards that may need to be addressed by future guidance?

It appears industries that incorporate longer-term contracts will be those most affected as a result of the new accounting standards. Industries such as construction, service providers of repair or warranty services, technology companies that work on a contract basis with their customers, and other business segments that use contracts that last more than one year or span across year-ends will be those most impacted by the new accounting standards. The administrative burden placed on taxpayers in these specific industries will be enormous as they track the differences between book (Generally Accepted Accounting Provisions - GAAP) and tax revenue on a contract-by-contract basis. It will provide an unnecessary burden that, in most cases, we believe will not have a material impact on the taxpayers’ overall income tax returns. Often, the taxpayers will be accelerating income in comparison to the existing rules by estimating a portion of income that should be recognized over the life of a contract, even if under the current standards the “all events test” had not been fully met based on required estimates.

It is our recommendation that the rules be structured to allow taxpayers to change their current method for revenue recognition to match the GAAP method and standards if they choose. While we acknowledge the concern of the IRS that taxpayers may use more estimates in determining the revenue to be recognized under the new standards, we believe that GAAP-tax conformity is the most reasonable method to provide consistency of reporting from both the taxpayer perspective as well as the IRS perspective with respect to required examination procedures and approach.

Question 3: To what extent do the new standards deviate from the requirements of Section 451? In what situations should the IRS allow taxpayers who adopt the new standards to follow their book method of accounting for tax purposes (for example, where income is always accelerated)?

The general rule of Section 451 is that when a taxpayer has taxable income that is computed under an accrual method of accounting, any income attributable to the sale or furnishing of utility services to customers shall be included in gross income no later than the taxable year in which such services are provided to such customers.

Furthermore, the amount of any item of gross income shall be included in the gross income (cash basis) for the taxable year in which received by the taxpayer, unless, under the method of accounting used in computing taxable income, such amount is to be properly accounted for as of a different period. Section 451 goes on to provide a significant number of statutory exceptions, or so-called “special rules.”

The new accounting standards state that when transfer of control (or use of the benefit of the goods or services provided is transferred), you must then recognize revenue. Therefore, the new standards, if applied to a tax basis of revenue recognition, (making the tax and book records similar) - would then appear to be not a deviation, per se, but more of a clarification of the specific revenue recognition timing.

Many businesses are still identifying the financial accounting impact of the new rules, let alone the extent of the deviation from Section 451 and other tax rules related to the timing and amount of revenue recognition changes. Therefore, the IRS should be accommodating to taxpayers by adopting rules that will allow tax income to follow book financial income, particularly in instances where the difference would be immaterial or the cost of compliance of identifying and annually calculating the book/tax difference would far outweigh the tax costs (or benefits) to the Treasury. One example of this position, as identified in the notice, would be where income is always accelerated under the new rules compared to existing rules (even though income is rarely “always accelerated” given business and economic cycles).

Question 4: To what extent do the rules regarding allocation of standalone sales price and transaction price in the new standards affect the taxpayers’ ability to satisfy their tax obligations?

We believe the requirements relative to the allocation of sales price may potentially require contracts to be broken into smaller pieces. In these cases, the amount of time and effort to track contracts for GAAP vs. tax purposes would be enormous because the number of allocations could be substantial. It is too early to tell, but we believe the analysis related to the allocation of standalone sales price could conflict with IRC Section 451 and the related Regulations, including interaction with other sections of the Internal Revenue Code. The ability of taxpayers to change their accounting method
to conform to GAAP in this area would alleviate the possibility of errors in tax reporting that may occur as a result of the volume of information to be analyzed. We believe additional time will allow for a better evaluation of the effect of this provision of the new accounting standards.

**Comments on Procedures for Method Changes**

**Question 1:** Is the exception for small businesses in paragraph 5.02(2) of the proposed revenue procedure appropriate?

The exception for small businesses in paragraph 5.02(2) is insufficient. The IRS should allow maximum flexibility in the application of the rules to allow smaller taxpayers, at a minimum, the same outcome as larger taxpayers. Therefore, smaller taxpayers should be allowed to use a Section 481(a) adjustment in addition to a cut-off method to determine the immediate taxable income impact resulting from the new revenue recognition rules rather than just requiring the cut-off method for those smaller taxpayers. To allow otherwise appears to assume that accounting method changes resulting from the new revenue recognition rules would always be favorable to small business, and that the need for Section 481(a) adjustments spreading the impact over a period of years for these taxpayers is unnecessary.

Additionally, the ceiling that defines a small taxpayer should be raised. For example, the Small Business Administration defines many different business segments in terms of revenue greatly exceeding $10 million. Due to the magnitude of taxpayers affected by the revenue recognition changes, it is recommended that a larger proportion of taxpayers be classified as small taxpayers by raising the revenue recognition threshold to at least $25 million.

**Question 2:** What types of changes in methods of accounting do taxpayers anticipate requesting?

Additional time is needed to fully and properly address this issue.

**Question 3:** Do taxpayers anticipate requesting changes in methods of accounting prior to the effective date of the new standards?

Due to the complexity of the new rules, the ongoing effort by businesses to understand and quantify the impact of the new rules for both financial reporting and tax reporting purposes, the potential negative impact of accelerating income in situations where changes in methods are required, and the uncertainty of the status surrounding potential tax reform, we anticipate few taxpayers will be requesting changes in methods of accounting prior to the effective dates of the new standards.

**Question 4:** Which procedures should taxpayers be required to use to request permission for a qualifying same-year method change: the automatic method change procedures or the advance consent procedures?

Requiring permission under advance consent procedures for qualifying same-year method changes places an administrative burden on taxpayers as well as appearing to place additional administrative burden on the IRS that, arguably, already appears to be underfunded and understaffed. Therefore, all method of accounting changes resulting from the new standards should be automatic.

**Question 5:** What changes, other than those described in Section 5 of the proposed revenue procedure, do taxpayers expect will be requested in the year the taxpayer adopts the new financial standards, and should they be allowed as automatic changes?

It is difficult to determine the other additional accounting method changes that will be required because of the new revenue recognition standards. We believe additional time is required to fully understand the impact these new accounting standards will have on other related segments of a taxpayer’s business, which would involve other accounting methods.
Question 6: What related accounting method changes do taxpayers anticipate requesting that may appropriately be made on a single Form 3115?

Similar to our response in Question 5, it is difficult to determine at this time what other accounting method areas will be affected by these new accounting standards.

Question 7: If multiple changes are requested on a single Form 3115, should the taxpayer report a separate Section 481 adjustment for each change, and should those adjustments be netted and a single spread period applied?

It would be overkill to report separate Section 481 adjustments for each individual change resulting from an overall change as the result of the new revenue recognition standard. The aggregate of the Section 481(a) changes related to the implementation of these accounting standards could be reported in one consolidated Form 3115, similar to the repair and maintenance regulations.

Question 8: What alternatives to filing a Form 3115 would reduce the burden of compliance?

It is clear that the new revenue recognition standards will impact many taxpayers, and changes in method of accounting for tax purposes will result. Therefore, consideration should be given whether a Form 3115 is even necessary for this particular item in this instance. Rather, consider whether statements attached to the return explaining that the revenue recognition standard was adopted for books, a summary calculation of the overall impact on the difference between book and tax calculations, and one Section 481 adjustments amount would suffice. Taxpayers would be required to have detailed calculations available upon examination.

Question 9: What transition procedures may be helpful?

No specific comments other than those incorporated into other questions.

Question 10: What additional procedural changes would be appropriate and helpful?

No specific comments other than those incorporated into other questions.

Again, thank you for the opportunity to review and comment on Notice 2017-17. If you would like to discuss our comments or recommendations do not hesitate to contact the PICPA’s Government Affairs office at (717) 232-1821.

Sincerely,

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