

TD 93/18 - Income tax: what factors does a taxpayer need to consider in deciding between the cash and accruals methods of accounting for income for taxation purposes?

 This cover sheet is provided for information only. It does not form part of *TD 93/18 - Income tax: what factors does a taxpayer need to consider in deciding between the cash and accruals methods of accounting for income for taxation purposes?*

 This document has changed over time. This is a consolidated version of the ruling which was published on *4 February 1993*

This Determination, to the extent that it is capable of being a 'public ruling' in terms of Part 4VAAA of the *Taxation Administration Act 1953*, is a public ruling for the purposes of that Part. Taxation Ruling TR 92/1 explains when a Determination is a public ruling and how it is binding on the Commissioner. Unless otherwise stated, this Determination applies to years commencing both before and after its date of issue. However, this Determination does not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Taxation Determination

Income tax: what factors does a taxpayer need to consider in deciding between the cash and accruals methods of accounting for income for taxation purposes?

1. Total assessable income under subsection 25(1) of the *Income Tax Assessment Act 1936* must be calculated using a method which brings to account and correctly reflects a taxpayer's true income (*C of T (SA) v. Executor Trustee and Agency Company of South Australia Ltd* (1938) 63 CLR 108; 5 ATD 98).
2. The cash method brings to account as assessable income all cash amounts received during the year of income. The accruals method brings to account as income amounts charged or chargeable, irrespective of whether these amounts have been collected in the income year. These methods refer to the calculation of assessable income. Whichever method is used, a taxpayer is only entitled to a deduction under subsection 51(1) for a loss or outgoing which has been incurred.
3. In determining which method is more appropriate the courts have considered:
 - (a) the size of the business;
 - (b) the type of business;
 - (c) method of accounting;
 - (d) current practice in the industry;
 - (e) overhead costs; and
 - (f) policy for recovery of outstanding debts.Of course, any other relevant factors must also be considered.
4. The relative importance of each of these factors will depend on the particular circumstances of each case. Generally the smaller the business the more likely the cash method should be used. It is important to note that there is no threshold relating to size etc which will determine the most appropriate method.
5. In *Henderson v. FC of T* (1970) 119 CLR 612; 70 ATC 4016; 1 ATR 596 the court held that the accruals method was the most appropriate. Mr Henderson was an accountant who was in partnership with 18 others and the business operated on a large scale. Almost three hundred people were employed, fees earned in the relevant years exceeded \$1 million and bad debts were virtually non-existent.

6. In *FC of T v. Firstenberg* (1976) 6 ATR 297; 76 ATC 4141 it was held that the cash method was the most appropriate. Mr Firstenberg practised as a solicitor on his own account and his only employee was his secretary-typist-telephonist.

7. The most recent case in this area is *Barratt v. FC of T* 23 ATR 339; 92 ATC 4275. In determining which method was more appropriate the court considered those factors listed in paragraph 3 which were relevant to the circumstances.

Commissioner of Taxation

04/03/92

FOI INDEX DETAIL: Reference No. I 1214002 Previously issued as Draft TD 92/30

Subject Ref: accounting method; accruals method, assessable income, cash method

Legislative Ref: ITAA 25

Case Ref: *C of T(SA) v. Executor Trustee and Agency Company of South Australia Ltd* (1938) 63 CLR 108, 5 ATD 98

Henderson v. FC of T (1970) 119 CLR 612; 70 ATC 4016; 1 ATR 596

FC of T v. Firstenberg (1976) 6 ATR 297, 76 ATC 4141

Barratt v. FC of T 23 ATR 339; 92 ATC 4275

ATO Ref: TD/92/0003/Par

ISSN 1038 - 8982