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April 2, 2014

The Honorable Elizabeth Warren
United States Senate
317 Hart Senate Office Building
Washington, D.C. 20515

Re: **Opposition to Draft Legislation Requiring Many Law Firms and Other Personal Service Businesses to Pay Taxes Using the Accrual Method of Accounting**

Dear Senator Warren:

On behalf of the Boston Bar Association and its more than 11,000 members, I write to express our concerns regarding the proposal included in a tax reform discussion draft released by then-Chairman Baucus of the Senate Finance Committee and most recently included as Section 3301 of the discussion draft of the "Tax Reform Act of 2014" prepared by House Ways and Means Committee Chairman Dave Camp. If enacted, this provision would require all law firms, accounting firms, medical practices, and other professional service firms operated as partnerships or S corporations with gross receipts over $10 million to use the accrual method of accounting. We are concerned that this change would cause substantial hardship to many personal service businesses, but in particular, we address here the severe impact such a change would have on the legal profession and the practice of law.

Under current law, individuals and most partnerships and other pass-through entities are permitted to use the simple cash method of accounting, in which income is not recognized until cash or other payment is actually received and deductions are not allowed until payment is actually made. In addition, all law firms and various other types of personal service businesses are allowed to use the cash method of accounting regardless of their annual revenue if they do not maintain an inventory.

We commend Former-Chairman Baucus' and Chairman Camp's efforts to simplify the tax laws and raise additional revenue, but we believe that Section 3301 of the draft bill would have material, unintended consequences for the practice of law and the legal profession. Under the accrual method, any firm with large accounts receivable as of the effective date of the provision would be forced to recognize hundreds of thousands to tens of millions of dollars in income on an accelerated basis, even though the revenue associated with those

accounts receivable had not yet been received and may never be received. This would be particularly burdensome on pass-through entities like law firms, since each equity owner would have imputed income on which he or she would be required to pay taxes, even though the revenue for which those taxes would be due was not received. A firm's income thereafter would be based upon invoices issued for services rather than revenue received for those services, again with no certainty that the taxed amount would ever be received.

One can easily imagine the disruptions in financial planning both of these consequences would cause the firm and its partners, including forcing them to incur increased debt to meet their tax liabilities, which in turn could affect important family decisions, such as home purchases, college tuitions, and retirement.

There are professional consequences to be considered as well. For instance, the increased complexity associated with the accrual method of accounting will raise compliance costs for businesses while greatly increasing the risk of noncompliance with the Tax Code. In addition, the provisions would impose new financial burdens on many law firms and other personal service businesses by requiring them to pay taxes on income they have not yet received and may never receive.

The traditional cash method of accounting produces a sound and fair result because it properly recognizes that the cash a business actually receives in return for the services it provides—not the business' accounts receivable—is the proper reflection of its true income and ability to pay taxes on that income. Requiring law firms and other personal service businesses to pay taxes on income long before it is actually received—and to either use their scarce capital or borrow money to do so—would impose a serious financial burden and hardship on many of these firms. In the worst case scenario, such a proposal may not only stifle the growth of small to medium size firms, but could place them out of business altogether.

Section 3301 also could result in stifling the growth of firms as they attempt to avoid the implications of reaching the $10 million revenue threshold. For those already over that threshold, the added burden of monitoring write offs of aged receivables, and the pressure to make possibly arbitrary decisions at year end with respect to those write offs, would create significant administrative complexity and cost.

Those of us who earn our livelihood in the law profession are concerned that other complexities and inequities also have been overlooked by the proponents of Section 3301, such as the fact that, due to turnover from retirements and new admissions, the partners of a firm who paid tax on the income deemed received upon the issuance of an invoice for services performed may not be the same partners as those who later enjoy the revenue ultimately received. The potential inequities of such a result are obvious.

We respectfully request your help in opposing the accrual accounting requirement contained in Section 3301 of the draft bill by conveying your opposition to House Ways and Means Committee Chairman Camp and to the Committee's Ranking Member Sander Levin.

Thank you for your consideration of this issue, which is of great importance to lawyers, law firms, and many other types of personal service businesses throughout Massachusetts and around the country.

Very truly yours,

Paul T. Dacier
President