

CONSTRUCTION
INDUSTRY

CASE STUDY:

Top-ranked Contractor Saves \$4 Million through Change of Accounting Method

ABOUT THE CLIENT

One of the largest contractors in its region, our client is also a top-ranked contractor in the U.S. The business has decades of experience in a full range of contracting services and is noted for innovative high-profile projects.

THE CHALLENGE

The company had historically reported revenue from construction projects for income tax purposes the same way it reported for financial statements. The company was not aware that tax accounting methods for construction contractors could differ from GAAP. The client's present method of accounting for long-term contracts did not properly allocate costs to construction contracts for income tax purposes. The utilization of other available tax accounting methods would result in significant income tax savings and profit deferrals, and retain much-needed working capital.

THE GOAL

Tax leaders from Marcum's construction group met with key financial personnel from the company to discuss tax planning opportunities inherent in other acceptable income tax methods of accounting for contractors. The goal was to implement a construction industry-specific tax strategy that would properly allocate general and administrative costs to contracts in progress, thereby reducing the overall gross profit on construction contracts.

THE PROCESS

Marcum's construction tax professionals reviewed several years of the company's financial data and construction contracts, both completed and in process. We then developed a methodology for apportioning general and administrative (G&A) expenses that the company could utilize to properly allocate identified indirect costs to contracts. The client would be requesting a change in accounting methods that was not automatic and subject to IRS approval. The company would apply to the IRS by timely filing Form 3115, "Application for Change in Accounting Method," together with a user fee, prior to the end of the fiscal year in which it would effectuate the change. Significant detail and narrative would be required with the application for change. Marcum collaborated with company executives to properly document and clearly describe the new way the company proposed to allocate G&A costs prospectively.

THE SOLUTION

The IRS granted the application for change in accounting method for allocating costs to long-term construction contracts. The taxpayer was able to generate a \$4 million deduction and deferral of profit on open jobs in the first year of adopting the change in accounting method.

