BROTEMARKLE, DAVIS & CO. LLP
Putting People First

Think you're only keeping one set of books?

We've got news for you. You've actually got at least three sets of books and they're all legal. In fact, they're required.

You see, for financial statement reporting purposes, you are required to compute your business results according to a set of rules known as GAAP or Generally Accepted Accounting Principles. (Among other things, these rules dictate how loan payments are to be treated and when revenue can be recognized.) For federal income tax purposes, you are required (or in some cases allowed) to calculate results in conformity with rules and regulations passed by Congress and interpreted by the IRS and the court system. (Hence the recent LIFO inventory controversy of wineries versus the IRS.) And finally, the states didn't want to be left out, so they each have a different set of rules. ((California doesn't allow the accelerated write-offs for equipment purchases that are allowed under the Federal Stimulus Packages.)

So far, we're up to three sets of books and we haven't even talked about managerial reporting. When you go to present a financial statement to a bank or other interested party, you need to be clear about which set of books you are providing.

If an accountant is involved in the preparation of your financial statements, he is required to add a report that includes an explanation of how the statements have been prepared - are they in accordance with GAAP (Generally Accepted Accounting Principles)? or are they based on some other method commonly known as OCBOA (Other Comprehensive Basis of Accounting like federal income tax basis or cash basis)? You will see these reports issued as part of a compilation, review or audit engagement and they should always remain with your financial statements.

When you are creating a tax basis set of financial statements, your goal is to maximize deductions and minimize taxable income by taking advantage of every available tax-saving opportunity. That means your net income is likely to be lower when compared to other accounting methods. GAAP basis financial statements are designed to be a more accurate reflection of your results of operation, as such, they will likely reflect a very different net income figure. Information you generate from your own accounting system is probably created with an entirely different objective and may show an entirely different result than either an independently prepared financial statement or your tax return.

It is fine to have different results for different purposes, but make sure you provide financial statements that accurately reflect your business results the next time you meet with your banker. Different books could lead to different lending decisions.

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