



BDO Seidman, LLP
Accountants and Consultants

May 2004

Subject:
**Taxation of Advance
Payments**
(Rev. Proc. 2004-34)

Corporate Tax Alert

The Tax Practice at **BDO Seidman, LLP** is among the largest tax advisory practices in the U.S. With over 35 offices and 250 independent alliance firm locations in the U.S., BDO Seidman has the bench strength and coverage to serve you.

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FOR MORE INFORMATION

Please contact:

Jack Frame

330 Madison Ave

New York, NY 10017

Phone: 212-885-8125

Fax: 707-982-0633

Email: jframe@bdo.com

Date\Timing:

While the new rules are generally effective for taxable years ending on or after May 6, 2004, many taxpayers are eligible to file for an automatic change in accounting method under these rules for taxable years ending on or after December 31, 2003. This includes all extended 2003 calendar year returns due September 15, 2004. In addition, taxpayers that timely filed their 2003 returns can make an automatic accounting method change to apply the new rules by filing an amended 2003 tax return within 6 months of the original due date of the return.

Affecting:

These rules generally affect all accrual basis taxpayers that receive advance revenue classified as a liability for financial reporting purposes. The greatest opportunities exist for service companies that issue multi-year contracts, computer companies that sell, lease, or license computer software, non-life insurance companies that service multi-year insurance contracts, manufacturers that provide guaranty or warranty service contracts to its customers, sport franchises that have multi-year media contracts, taxpayers that receive payments for the use of intellectual property, and internet service companies. It also applies to any business that receives payment for the occupancy or use of property if the occupancy or use is ancillary to the provision of services.

Details:

The Internal Revenue Service recently issued new rules that expand the circumstances whereby accrual basis taxpayers may defer to the next succeeding taxable year income from payments received (advance payments) prior to the actual delivery of goods and/or the providing of services to their customers.

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Details ...(continued)

Prior to the new rules, accrual basis taxpayers were allowed to defer the inclusion in gross income of payments received in a taxable year for services to be performed and completed by the end of the succeeding taxable year. The prior rules also excluded advance payments for items that were not exclusively for services, leading to controversy about whether advance payments are for services.

The new rules, however, allow taxpayers to defer advance payments to the following taxable year even though the term of the agreement with customers may extend well beyond the end of the following taxable year or the advance payments are for the delivery of goods. **Proper implementation of these new rules may provide an immediate tax benefit to your company.**

Recommended Action:

We strongly recommend that you contact Jack Frame who will put you in touch with a BDO Seidman tax professional who can analyze the potential tax benefit these new rules can provide to your company. A BDO Seidman tax professional can then help your company take advantage of these new rules by preparing a formal request to change your tax accounting method for advance payments. Once again, this formal request should provide an immediate tax benefit for the 2003 calendar tax year and/or a reduction of required estimated tax payments for your fiscal year ended or ending in 2004.

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Email: jframe@bdo.com

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