Where Can I Go For Help?

Telephone: Order free copies of all IRS forms and publications by calling 1-800-829-3676 (1-800-Tax-Form).

Excellent Publications for Small Businesses:
- At A Glance, Publication 3698

If you have questions, contact your tax preparer or the IRS 24 hours a day, seven days a week at 1-800-829-1040 (1-800-Tax-1040).

On the Internet: Access the IRS Web Site for federal tax forms, publications, tax law changes, and other tax information for individuals and businesses on the Internet at www.irs.gov.

For more information specific to the construction industry, go to: www.irs.gov/smallbiz, Under "Contents" click on "Industries/Professions." Click on, "Construction."

The construction industry can benefit by using the IRS e-file program. Returns are processed more quickly, accurately and an electronic acknowledgement is sent with each return received. Forms 940/941, 1065, and information returns (Forms 1042-S, 1098, 1099, 5498, 8027, W-2G and QWF (Questionable Forms W-4) can be electronically filed. Beginning in 2004, Forms 1120/1120S will be available. Visit www.irs.gov/efile for a list of approved IRS e-file Providers.

Pay all of your Federal Business and individual taxes through the Electronic Federal Payment Systems (EFTPS). It is a free service and you can make your payments 24 hours a day 7 days a week by phone or through the internet. For more information call EFTPS Customer Service at 1-800-555-4477 or 1-800-945-8400 or visit our website at www.eftps.gov.
year the merchandise is sold or paid for, whichever is later. Generally the percentage of completion method is required for long-term contracts. A long-term contract is one that is still in process at the end of your taxable year. For example, if work on a contract to construct a building begins in November 2000, and ends in January 2001, and the contractor used the calendar tax year, the contract is a long-term contract.

Home construction contracts are not subject to the percentage-of-completion method. In addition, general construction contracts are not subject to the percentage of completion method if certain completion time and gross receipts tests are satisfied. For all these exempt construction contracts, a taxpayer may use an “exempt contract” method, which includes the percentage of completion method, the exempt-contract percentage-of-completion method, the completed contract method, or any other permissible method.

Whether a method is permissible depends on a number of factors, such as the type of business entity, business activity, level of gross receipts, and existence or absence of merchandise as an income-producing factor in the business.

Indirect Cost Issues

Contractors are required to allocate indirect job costs to their long-term contracts annually unless the Code or regulations provide otherwise. Whether contractors are required to capitalize these allocable job costs, or are permitted to deduct these allocable job costs, depends on the contractor’s method of accounting for long-term contracts.

Allocable job costs include costs that are incurred because of the contractor’s construction projects, such as repairs, equipment maintenance and rentals, utilities at the job site, depreciation on construction equipment, officer’s compensation, and workers’ compensation insurance.

Non-allocable job costs included expenses for unsuccessful bids and proposals and for marketing, selling, and advertising expenses. These costs are exempted from the cost allocation requirement.

In general, contractors using the percentage of completion method are required to allocate indirect job costs to their long-term contracts. Contractors using the completed contract method of accounting are required to capitalize indirect job costs allocated to long-term contracts until the contract is completed.

Why is the Capitalization of Indirect Costs an Important Issue?

Many contractors utilizing the completed contract method of accounting overstate their deductions because they are not properly allocating costs to long-term contracts. Under the completed contract method, income or loss is reported in the year in which the contract is completed. In addition to direct materials and labor costs, all indirect costs incurred for reason of a long-term contract or that directly benefit the long-term contract, must be allocated, or capitalized to that contract. As long as that contract has not been completed and accepted these costs must not be deducted as current period costs.

Some indirect costs may benefit both the long-term contract and other business activities. These costs will require a reasonable allocation between the other business activities and the long-term contract. Suggested methods are specific identification method or the use of ratios based on direct costs, hours, or other units of measure.

Further information is contained in Treasury Regulation 1.460 and IRC section 263A for certain contractors such as large home construction contractors. Contractors required to use the percentage of completion method for long-term contracts should refer to IRC Section 460.