

Financial Policies and Procedures

What is the "basis of accounting"?

The basis of accounting describes the method used to determine when and how income and expenses are recorded and reported. Good accounting practices include using a consistent accounting method; however, no entity is required to use one method over another. It is important to use the method that clearly reflects your income and expenses. Small business accounting needs can usually be met through cash accounting. If an entity has an inventory that produces, purchases, or sells merchandise, the accrual method of accounting is typically used.

What are the methods of accounting?

- Cash method: Income is recorded when it is received, and expenses are recorded when they are paid.
- Accrual method: Income is recorded when it is earned, and expenses are recorded when they are incurred.
- ◆ Modified accrual method: Income is recorded both when it is earned and when it is received, and expenses are recorded when they are incurred.

Can an entity change its method of accounting?

An entity can change its method of accounting. If the entity is required to file a tax return with the Internal Revenue Service (IRS), it must have IRS approval.

Which accounting method is appropriate for your entity?

It is best to consult with a tax professional or Certified Public Accountant (CPA) on the most appropriate accounting method for your entity. Consider the following:

- ◆ The cash method is the easiest to use; however, because it does not record payables and receivables, it does not provide an accurate financial picture.
- ◆ The accrual method provides an accurate report on how much money is earned and how much is spent. It also adheres to the Generally Accepted Accounting Principles (also known as GAAP, as defined by the American Institute of Certified Public Accountants). It requires a more complex accounting system than the cash method.
- The modified accrual method works well when inventory is accounted for using the accrual method and the cash method is used for recording income and expenses.

Resources

- ◆ Internal Revenue Service, Publication 538, Accounting Periods and Methods
- American Institute of CPAs (AICPA)



The OVC Tribal Financial Management Center (OVC TFMC) provides training, technical assistance, and resources to support American Indian and Alaska Native communities as they successfully manage the financial aspects of their federal awards. OVC TFMC also offers support via our Virtual Support Center (VSC) to Office for Victims of Crime (OVC) grantees and those seeking federal funding from OVC for the first time. Email questions or requests for grant financial management technical assistance to TFMC@OVCTFMC.org or call 703.462.6900. Visit OVCTFMC.org for additional resources and information.

Feedback Requested

OVC TFMC will continually work to provide resources to support grantees as they successfully manage their OVC financial awards. Your feedback assists us in creating these resources to meet your needs. To help us provide the most useful resources, we would appreciate your feedback on this guide sheet. Please send any comments or suggestions to Evaluation@OVCTFMC.org.

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