**8504. What is a taxable year for individual income tax purposes?**

The basic period for computing income tax liability is one year, known as the *taxable year*. The taxable year may be either (a) the calendar year or (b) a fiscal year. A “calendar year” is a period of 12 months ending on December 31. A “fiscal year” is a period of 12 months ending on the last day of a month other than December.[[1]](#footnote-1)

Although most individuals report tax liability on a calendar year, it is possible to use a fiscal year. In any event, the year used for reporting tax liability must generally correspond to the taxpayer’s accounting period.[[2]](#footnote-2) Thus, if the taxpayer keeps books on a fiscal year basis the taxpayer cannot determine tax liability on a calendar year basis. If the taxpayer keeps no books, however, reporting on a calendar year basis is required.[[3]](#footnote-3) Once the taxpayer has chosen a tax year, it cannot be changed without the permission of the Internal Revenue Service.[[4]](#footnote-4) A principal partner cannot change to a taxable year other than that of the partnership unless the principal partner establishes, to the satisfaction of the IRS, a business purpose for doing so.[[5]](#footnote-5)

A personal service corporation is required to use the calendar year for computing tax liability unless it can establish a valid business purpose for using a different period. The code specifically provides that deferral of income to shareholders does not constitute a valid business purpose.[[6]](#footnote-6)

Under certain circumstances, partnerships and S corporations are required to use the calendar year for computing income tax liability.[[7]](#footnote-7)

A short period (one that is less than 12 months) return is required where (1) the taxpayer changes the taxpayer’s annual accounting period, and (2) a taxpayer has been in existence for only part of a taxable year.[[8]](#footnote-8) A short period is treated in the law as a “taxable year.”[[9]](#footnote-9)

 *Example:* On June 1, 2014, ASK, Inc., a C corporation reporting its tax liability based on a calendar year began doing business. Since ASK was not operating for the entire calendar year, a short period return (June 1 through December 31) is required.

If the short period return is made because of a change in accounting period, the income during the short period must be annualized, and deductions and exemptions prorated.[[10]](#footnote-10) But income for the short period is not required to be annualized if the taxpayer is not in existence for the entire taxable year.[[11]](#footnote-11) For a discussion of the considerations applicable in determining a taxpayer’s accounting period, see Q 8838-Q 8844.

For the final regulations affecting taxpayers who want to adopt an annual accounting period (under IRC Section 441), or who must receive approval to adopt, change, or retain their annual accounting periods (under IRC Section 442), see Treasury Regulation Sections 1.441-0, 1.441-1, 1.441-2, 1.441-3, 1.441-4.

For the general procedures for establishing a business purpose and obtaining approval to adopt, change, or retain an annual accounting period, see Revenue Procedure 2002-39.[[12]](#footnote-12)

In Revenue Procedure 2003-62, the IRS has set forth the procedure under which IRC Section 442 allows individuals (e.g., sole proprietors) filing tax returns on a fiscal year basis to obtain automatic approval to change their annual accounting period to a calendar year.[[13]](#footnote-13)

The exclusive procedures for (1) certain partnerships, (2) S corporations, (3) electing S corporations, (4) personal service corporations, and (5) trusts to obtain automatic approval to adopt, change, or retain their annual accounting period are set forth in Revenue Procedure 2006-46.[[14]](#footnote-14)

1. . IRC Secs. 441(a), 441(b), 441(d), 441(e). [↑](#footnote-ref-1)
2. . IRC Sec. 441(f)(1). [↑](#footnote-ref-2)
3. . IRC Sec. 441(g). [↑](#footnote-ref-3)
4. . IRC Sec. 442. [↑](#footnote-ref-4)
5. . IRC Sec. 706(b)(2). [↑](#footnote-ref-5)
6. . IRC Sec. 441(i). [↑](#footnote-ref-6)
7. . See IRC Secs. 706(b), 1378. [↑](#footnote-ref-7)
8. . IRC Sec. 443(a). [↑](#footnote-ref-8)
9. . IRC Sec. 441(b)(3). [↑](#footnote-ref-9)
10. . IRC Secs. 443(b), 443(c). [↑](#footnote-ref-10)
11. . Treas. Reg. §1.443-1(a)(2). [↑](#footnote-ref-11)
12. . 2002-1 CB 1046, *as modified by*, Notice 2002-72, 2002-2 CB 843, *and further modified by*, Rev. Proc. 2003-79, 2003-2 CB 1036. [↑](#footnote-ref-12)
13. . 2003-2 CB 299, *modifying, amplifying, and superseding*, Rev. Proc. 66-50, 1966-2 CB 1260, and *modifying and superseding*, Rev. Proc. 81-40, 1981-2 CB 604. See also Ann. 2003-49, 2003-2 CB 339. [↑](#footnote-ref-13)
14. . 2006-45 IRB 859. [↑](#footnote-ref-14)