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**► IRS is attacking Personal Service Corporations!****IRS is attacking Personal Service Corporations!**

Look out... there are NEW IRS legal challenges: The latest IRS taxing initiatives include taking to court owners of Personal Service Corporations, PSC, that are used by professionals such as lawyers, accountants, doctors, engineers, and similar professionals, incorporated as C Corporations for their professional practices. As a reminder, PSC's income is taxed at flat rate of 35%... wow!

For many years the IRS has been examining C Corporations for reasonable compensation to determine whether C Corporation owners are excessively compensating themselves to reduce or eliminate the taxable income of the corporation which is many times higher rate than the owner's individual tax rate.

The IRS has taken to Tax Court and to other courts to argue the excessive compensation of PSC owners. Courts regularly have been applying an "independent investor" test to consider growth in equity from the retained earnings of the corporation to decide whether the owners are taking the appropriate income for the year. In these precedent setting cases, courts have presumed an independent investor would require a combination of dividend and equity growth in the range of 10% to 20% as shown in *L & B Pipe & Supply Co vs. Commissioner, Tax Court 1944-187*, and court case *Thousand Oaks Residential Care Home I, Inc. v. Commissioner, Tax Court 2013-10*.

In the tax court case of *Gilson & Lione v. Commissioner*, the court found that the corporation, a law firm of 150 attorneys, had a plan to zero out income at year end and left no return for shareholders' investments. It failed the independent investor test. The court upheld the IRS's request to assess accuracy-related penalties.

A permanent planning solution would be to convert to an S Corporation. S Corporations pass through their taxable income to the owners who then pay according to their individual rates which may be less than the PSC tax of 35%. Owners need to be aware of reasonable compensation as S Corporation owners. S Corporations are being audited by the IRS for reasonable compensation too.

Another possible solution is to consider use of merit or a point system to provide bonuses to all employees, not just shareholders.

## Regular Piece

### How To Make The Most Of Your Newsletter

Be sure to read the article with the mindset 'How could this apply to our business.' Thinking of it that way will guarantee that you get value. Better yet, take notes as you read and commit to having the ideas implemented by the time the next edition arrives. Also, make copies for each team member. To really make sure something positive happens, work with your business development specialist to talk your team through the ideas and how to set a schedule for getting them implemented. We're here to help you get started.

### An Important Message

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