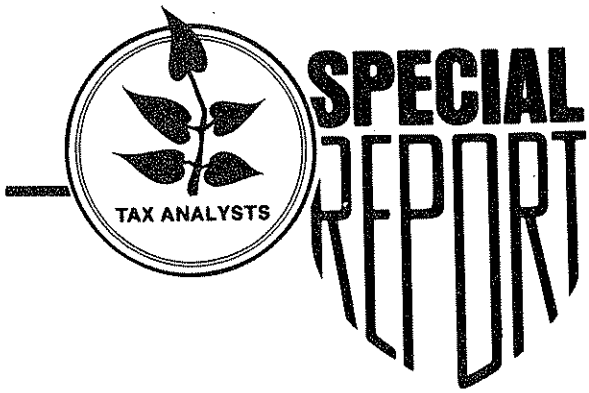

IN SEARCH OF A DEFINITION OF A PERSONAL SERVICE CORPORATION

by Richard B. Malamud

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In this report, he reviews the definition of a personal service corporation to provide guidance to tax professionals and taxpayers who, unfortunately, have been generally left to their own devices in trying to determine if a particular corporation's activities involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting.

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I. Overview

It is common for the sole shareholder-employee of a corporation[1] to ask his or her attorney or accountant if the corporation is a personal service corporation (PSC) for federal income tax purposes. Many tax professionals simply reply that the corporation is a PSC only if substantially all of the corporation's activities involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting.[2]

In trying to define a PSC, tax professionals usually find that the statutory list of eight activities is just about all the guidance available,[3] except for a few explanations and examples in the regulations and a handful of private letter rulings that generally offer only conclusions, not meaningful analysis.[4] This article reviews the existing authority in an attempt to help define those activities that cause a corporation to be classified as a PSC.

II. Effects of Being a PSC

It is important to determine whether a corporation is a PSC because there are both benefits and burdens to being classified as a PSC, including a higher tax rate, a required calendar year, a lower accumulated earnings

[1]Closely held corporations whose owners are also employees will also seek advice to determine if they own a personal service corporation.

[2]The list of types of services considered to be those that qualify as personal services is found in section 448(d)(2). As discussed below, all definitions in the Internal Revenue Code or regulations that use the term personal service corporation refer to this provision. All statutory references are to the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

[3]Even in articles, little more than the list of activities is presented. *See, e.g.* Richard D. Godshalk, "A Section 444 Election: Who, What, When, and Why," *Tax Notes*, Mar. 28, 1988, pp. 1537, 1551; Joseph A. Snoe, "The Entity Tax and Corporate Integration: An Agency Cost Analysis and a Call for a Deferred Distributions Tax," 48 *Miami L. Rev.* 1, 4 (1993); Cynthia Blum, "Should Professionals Accept 'Accrual' Fate?" 6 *Va. Tax Rev.* 593, 598 (1987).

[4]In addition, it does not appear that anyone has tried to put all of the regulations and rulings into one article.

credit, and the ability to use the cash method of accounting.

A. Flat 35 Percent Corporate Tax Rate

Unlike other C corporations which are subject to graduated income tax rates beginning at 15 percent on its first $50,000 of taxable income,[5] a PSC is taxed at a flat tax rate of 35 percent.[6] For this purpose, a PSC is defined by reference to section 448(d)(2) relating to the method of accounting of a taxable corporation.[7]

B. Calendar Year Required

Unlike other C corporations, which can adopt a fiscal tax year, a PSC is required to adopt a calendar year.[8] The regulations under this section also define personal services as those services referred to in section 448(d)(2).[9]

C. Accumulated Earning Credit

Unlike other C corporations, which receive an accumulated earnings credit of $250,000,[10] this amount is reduced to $150,000 for "... a corporation the principal function of which is the performance of services in the field of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting...."[11] Although not referenced in the code or regulations, these are the same activities listed in section 448(d)(2).

D. Passive Activity Losses Limited

Unlike many C corporations which can deduct passive losses against their active income,[12] a PSC cannot offset passive losses against its active income.[13] The regulations state that the definition of a PSC is the same as the definition under the accounting period regulations listed above, which themselves refer to section 448(d)(2).[14]

E. Reallocation of Income

The IRS is permitted to reallocate income, deductions, credits, and exclusions between a PSC and a related corporation, partnership, or other entity if it is formed or availed of to avoid or evade federal income taxes. Unfortunately, there is no definition of a PSC for this purpose.[15]

F. Cash Method of Accounting Permitted

Section 448, which is referred to directly or indirectly by all of the above-noted sections except the reallocation under section 269A, provides that a C corporation is generally prohibited from computing its taxable income under the cash receipts and disbursements method of accounting[16] unless it is in the farming business,[17] has average annual gross receipts for the three prior taxable years of $5,000,000 or less,[18] or it is a qualified PSC.[19] Thus, the one major benefit of being classified as a PSC is that a C corporation with over $5,000,000 of average gross receipts can continue to use the cash method of accounting.[20]

A corporation is treated as a PSC for this purpose only if it meets two tests, the ownership test and the functional activity test.[21]

1. Ownership test. The ownership test is met if "substantially all" of the corporation's stock is owned either directly or indirectly by current or retired employees or their estates if the employee-owners perform activities involving a field listed as part of the activities test.[22] For this purpose, substantially all is defined as 95 percent.[23] This article assumes that the ownership test has been met. This will usually be the case in closely held companies in which the shareholders comprise the entire workforce.[24]

2. Functional activity test. The functional activity test is met if substantially all of a corporation's activities involve the performance of services in one or more of the fields of "health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting...".[25] For this purpose, "substantially all" is defined as 95 percent of the corporation's activities.[26] Activities incidental to the performance of services

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[5]Section 11(b)(1).

[6]Section 11(b)(2).

[7]Section 11(b)(2) states in pertinent part:

(2) CERTAIN PERSONAL SERVICE CORPORATIONS NOT ELIGIBLE FOR GRADUATED RATES

Notwithstanding paragraph (1), the amount of the tax imposed by subsection (a) on the taxable income of a qualified personal service corporation (as defined in section 448(d)(2)) shall be equal to 35 percent of the taxable income.

[8]Section 441(i). Although not relevant to this discussion, there is an exception for a PSC that can demonstrate a business purpose for a fiscal year.

[9]Reg. section 1.441-4T(e)(1) and (2).

[10]Section 535(c)(2)(A).

[11]Section 535(c)(2)(B). *See also* S. Rep. No. 97-144, 97th Cong., 1st Sess. 90 (1981), 1981-2 C.B. 412, 445, and Rev. Rul. 84-101, 1984-2 C.B. 115.

[12]Section 469(a)(2)(B) prevents only closely held C corporations from offsetting passive losses against active income.

[13]Section 469(a)(2)(C). Closely held C corporations are also precluded from offsetting their passive losses against their active income. Section 469(a)(2)(B).

[14]Reg. section 1.469-1T(g)(2)(i) referring to section 1.441-4T(d).

[15]Section 269A. Because the temporary regulations do not incorporate the limited categories of services, such as law, accounting, engineering, etc. it is possible that the following discussion of those fields may not be applicable to situations involving section 269. *See* temp. reg. section 1.269A-1.

[16]Section 448(a).

[17]Section 448(b)(1)

[18]Section 448(b)(3).

[19]Section 448(b)(2).

[20]However, if inventory is a material income-producing factor, the corporation must use the accrual method of accounting.

[21]Section 448(d)(2).

[22]Section 448(d)(2)(B).

[23]Reg. section 1.448-1T(e)(5), flush language.

[24]In appropriate situations, such as where the owner does not work for the company, this may not be the case.

[25]Section 448(d)(2)(A).

[26]Reg. section 1.448-1T(e)(4)(i).

within a qualifying field are considered the performance of services within that field.[27] Thus, to determine whether a particular corporation is a PSC, one must compare the business activity of the corporation with the definitions of each field listed above.

III. Definitions and Discussion

Although the code lists eight personal service activities, the regulations define only the fields of health, performing arts, and consulting. Additionally, the regulations provide one example of what constitutes accounting. The regulations do not provide any guidance in defining actuarial science, architecture, engineering, or law. Even when the regulations provide definitions, they are often very broad and not very useful when trying to determine whether a particular company is a PSC.

A. Health

The following definition of health services is provided by the regulations:

> [T]he performance of services in the field of health means the provision of *medical services* by *physicians, nurses, dentists, and other similar healthcare professionals*. The performance of services in the field of health does not include the provision of services not directly related to a medical field, even though the services may purportedly relate to the health of the service recipient. For example, the performance of services in the field of health does not include the operation of health clubs or health spas that provide physical exercise or conditioning to their customers.[28] (Emphasis added.)

The regulation requires that two tests be met. The services must be medical services and they must be provided by health care professionals. An example of a profession that meets both is a physical therapist. A private letter ruling states that because physical therapy is defined under section 213 as deductible medical care, it must also be medical services under section 448.[29] It further states that physical therapists are "similar" to physicians, nurses, and dentists.[30]

In addressing whether veterinarians are health care providers, the IRS did not break the definition into its two parts. It simply quoted the regulation's "and other similar healthcare professionals" language and concluded without analysis that veterinarians are "similar healthcare professionals" and, therefore, the corporation in question was a PSC.[31] If the ruling had been based on whether veterinarian expense is a deductible medical expense under section 213, as was done in the case of the physical therapist, it would have to have concluded that the veterinarian was not a PSC because veterinarian bills are not deductible, and section 213 is applicable only to medical care of a taxpayer, his or her spouse, and dependents.[32] Thus, if the section 213 analysis is not the test for medical expense, it would have been helpful if the IRS had at least analyzed the situation and stated that the PSC definition also applies to similar medical expenses even if they relate to the care of animals, rather than humans. That may have been intended by Congress, but is not expressly discussed in the regulations or the ruling.

The problem with the limited definition provided by the regulation and the veterinarian ruling is that it provides little guidance in determining whether other medical businesses such as weight loss clinics, therapeutic hypnotists, or yoga instructors are considered to be medical care and whether they are "similar healthcare professionals."

In ruling that an emergency medical ambulance service was a PSC, the IRS stated that the technicians were licensed and certified by the state and therefore are health care professionals. In addition, they provided medically related services, transporting patients to hospitals while in direct radio contact with the hospital emergency room physicians.[33] This would seem to be the proper result. However, it is interesting that the examining agent contended that the technicians did not "perform services in the field of health."[34] If the IRS agent improperly classified this company, it seems apparent that there is a lack of adequate guidance for both the IRS and taxpayers to determine if a corporation is a PSC.

B. Performing Arts

The regulations define the field of performing arts as:

> [S]ervices by actors, actresses, singers, musicians, entertainers, and similar artists in their capacity as such. The performance of services in the field of the performing arts does not include the provision of services by persons who themselves are not performing artists (e.g., persons who may manage or promote such artists, and other persons in a trade or business that relates to the performing arts). Similarly, the performance of services in the field of the performing arts does not include the provision of services by persons who broadcast or otherwise disseminate the performances of such artists to members of the public (e.g., employees of a radio station that broadcasts the performances of musicians and singers). Finally, the performance of services in the field of the performing arts does not include the provision of services by athletes.[35]

In equating the statutory term "performing arts" with the term "performing artist," the regulation has

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[27]Reg. section 1.448-1T(e)(4)(i).
[28]Reg. section 1.448-1T(e)(4)(ii).
[29]LTR 9222004, *92 TNT 113-29*.
[30]*Id.*
[31]Rev. Rul. 91-30, 1991-1 C.B. 61, *91 TNT 91-19*.
[32]Section 213(a).
[33]LTR 9309004, *93 TNT 53-12*.
[34]*Id.*
[35]Reg. section 1.448-1T(e)(4)(iii).

apparently adopted a very narrow definition consistent with *Webster's New World Dictionary, Second College Edition* which defines performing arts to include "arts such as drama, dance, and music that involve performance before an audience."[36] The regulation appears to cover only activities "in front of the camera" and excludes those behind it, such as producers, directors,[37] athletes,[38] etc.[39]

In excluding from coverage persons who broadcast or otherwise disseminate the performances of other artists to members of the public, the regulation appears to exclude disc jockeys and newscasters. But what about newscasters who also arguably perform or are themselves personalities such as Paul Harvey, Dan Rather, or Barbara Walters? Does it make a difference if they are on a straight news broadcast vs. being on a news magazine such as "60 Minutes" or "20/20"?[40] Some guidance is arguably found in a private ruling that states that the term "entertainer" is not so broadly interpreted to include anyone whose mere presence the public finds entertaining if they are not performing artists.[41] Unfortunately, this seems to be more of a conclusion than a test, and it really doesn't help in characterizing news reporters.[42] It is clear, however, that the IRS has determined to define the fields narrowly, since broadening the definition would allow otherwise ineligible corporations to use the cash method of accounting.[43] This does not appear to be based on congressional intent as the committee reports do not provide guidance on the intended breadth of the qualifying fields or the interaction between sections 448 and 441(i).[44]

C. Consultants

The definition of consultants is critical to an understanding of PSCs because it is the "catch-all" for service companies that are not in the businesses of health, law, engineering, architecture, accounting, actuarial science, or performing arts. The regulations define a consultant as:

> [T]he performance of services in the field of consulting means the provision of *advice and counsel.* The performance of services in the field of consulting does not include the performance of services other than *advice and counsel,* such as sales or brokerage services, or economically similar services. . . . For purposes of the preceding sentence, the determination of whether a person's services are sales or brokerage services, or economically similar services, shall be based on all the facts and circumstances of that person's business. Such facts and circumstances include, for example, the manner in which the taxpayer is compensated for the services provided (e.g., whether the compensation for the services is contingent upon the consummation of the transaction that the services were intended to effect).[45] (Emphasis added.)

In an early private ruling, the IRS emphasizes the importance of the term "advice and counsel." It states that " . . . consulting means the provision of advice and counsel. It does not include the performance of services other than advice and counsel."[46] Examples provided in the regulations provide some guidance in defining a consulting business.

The first example states that a taxpayer who provides economic analyses and forecasts for a particular industry and who makes recommendations to a client on the prospects of entering the industry is considered to be engaged in consulting.[47]

In the second example, a taxpayer who determines a client's electronic data processing needs and makes recommendations regarding the design and implementation of data processing systems needs of the client is also considered to be engaged in the performance of services in the field of consulting.[48]

In another example, a taxpayer who determines a client's management and business structure needs, such as organizational structure and personnel matters, and who advises the client on changes in the client's management and business structure is also considered to be engaged in services in the field of consulting.[49]

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[36]LTR 9416006, *94 TNT 79-33.*

[37]*Id.*

[38]It is interesting that in defining those professions that are not entitled to a 50 percent capital gains tax exclusion from the sale of small-business stock, Congress excluded most PSC activities as well as "athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of 1 or more of its employees." Section 1202(e)(3)(A).

[39]For a fairly detailed discussion of PSC coverage of entertainment loan-out corporations, see Mary LaFrance, "The Separate Tax Status of Loan-Out Corporations," 48 *Vand. L. Rev.* 879 (1995).

[40]Even if they are not PSCs, most corporations that loan out the services of their sole shareholder to radio or television will be a personal holding company under section 542, because they have gross receipts consisting exclusively of personal service contracts under section 543(a)(7). As personal holding companies, they face additional taxes, such as the tax under section 541 if they fail to distribute their net after-tax income.

[41]LTR 9529002, *95 TNT 143-14.*

[42]In fact, it is difficult to think of a corporation (or its sole employee) whose mere presence the public finds entertaining who is not a performing artist, unless the ruling is contemplating public speakers, such as ex-presidents who simply give speeches, rather than "performances."

[43]*Id.* However, what the ruling does not address is that what is good for the fisc under section 448 (preventing the use of the cash method of accounting) could easily backfire because the failure to be a PSC under that section may result in the allowance of a fiscal year under section 441 (thus allowing fiscal year deferrals of salary to the owner-employee).

[44]H.R. Rep. No 426, 99th Cong., 1st Sess. 605 (1985).

[45]Reg. section 1.448-1T(e)(4)(iv).

[46]LTR 8913012, *89 TNT 74-42.*

[47]Reg. section 1.448-1T(e)(4)(iv)(B), Example (1).

[48]Reg. section 1.448-1T(e)(4)(iv)(B), Example (2).

[49]Reg. section 1.448-1T(e)(4)(iv)(B), Example (3).

Finally, a taxpayer who provides financial planning services and who assists clients in making decisions and plans regarding the client's financial activities, including designing personal budgets and the adoption of investment strategies tailored to the client's needs and other similar services, is considered to be engaged in the performance of services in the field of consulting.[50]

The regulations also provide examples of businesses that are not engaged in the performance of services in the field of consulting. One example states that a taxpayer who executes transactions for customers involving various types of securities or commodities generally traded through organized exchanges, provides economic analyses, and forecasts and makes recommendations regarding transactions in securities and commodities, and whose compensation for its services is typically based on the trade orders is not considered to be engaged in the performance of services in the field of consulting since the taxpayer is engaged in brokerage rather than consulting services.[51]

Although consistent with the regulations, this example appears to reduce or eliminate any analysis of the type of services performed by the business. Instead, it looks solely to the form of compensation to classify the company as either a consulting firm or a sales firm. It therefore seems to imply that of two identical businesses, one that is paid by the hour or the job and one that is paid by way of a commission on the sale of a product, the first is a consultant and the second is in the business of sales.

The apparent intent of the regulations to use the form of compensation over the substance of the service provided is illustrated in another example in which a taxpayers's data processing is identical to the above example except that the taxpayer is compensated based on a commission or a markup on the sale of equipment. In that example, the regulation concludes that this identical business, the only difference being the form of compensation, is not considered to be engaged in the performance of services in the field of consulting.

"The taxpayer is engaged in the performance of sales services. Relevant to this determination is the fact that the compensation of the taxpayer for its services it contingent upon the consummation of the transaction the services were intended to effect (i.e., the execution of equipment orders for its clients)."[52]

Assuming that the IRS is correct in treating these two businesses differently based soley on the form of compensation, it would have been helpful if the regulation explained why the method of compensation is the sole determining factor, especially when the regulation's own terms state that this is "sales services" and not the sale of a product.[53] Similarly, an employment agency, whether compensated by the employer or by the employee, is not performing consulting services because the "taxpayer is involved in the performance of services economically similar to brokerage services."[54] However, a corporation that provided interior design, graphic design, lighting design, marketing consulting, and merchandising services (designing the presentation of merchandise) for a lump sum or hourly fee was determined to be engaged in the consulting services.[55]

Several other examples continue this distinction. One concludes that an advertising agency that is compensated based on orders placed for advertisements is not a consultant.[56] Similarly, a taxpayer in the business of selling life and casualty insurance, annuities, and other similar products that is compensated for its services based on the purchases made by the clients is engaged in the performance of brokerage or sales services and is therefore not a consultant because the compensation is contingent upon the consummation of the transaction.[57]

Even companies that perform services rather than sales activities may still avoid PSC status as consultants if they do not provide advice and counsel. Thus, a company that provided lobbying efforts to influence legislation (services for a fee) was not considered to be a consultant because it did not examine its clients' businesses or make recommendations. It simply provided lobbying services as requested by the company.[58] In deciding if a commercial photographer was engaged in one of the enumerated PSC fields, a private letter ruling simply listed all of the PSC activities and concluded, without analysis, that commercial photography does not fall within any of them.[59]

It is also interesting that although the regulations provide that a company is a PSC if it performs substantially all of its services in "one or more" of the listed

[50]Reg. section 1.448-1T(e)(4)(iv)(B), Example (4).

[51]Reg. section 1.448-1T(e)(4)(iv)(B), Example (5).

[52]Reg. section 1.448-1T(e)(4)Ex. (6).

[53]It is interesting that in determining whether a company should use the accrual method of accounting, the IRS indicates that there are entities that are "mixed service-sales businesses." *See* Industry Specialization Program (ISP) Healthcare Industry, Oct. 31, 1991, Coordinated Issue Paper.

[54]Reg. section 1.448-1T(e)(4) Example (7) and (8). Would a different conclusion be reached (as in the following example) if the agency is hired to perform searches for a flat fee, payable regardless of success in finding an employee?

[55]LTR 9602013, *Doc 96-1520 (4 pages)*.

[56]Reg. section 1.448-1T(e)(4)(iv)(B), Example (9).

[57]Reg. section 1.448-1T(e)(4)(iv)(B), Example (10). *See also* Rev. Rul. 84-101, 1984-2 C.B. 115 in which, without specifically mentioning consulting, the IRS determined that an independent insurance broker did not perform services under one of the enumerated fields, and it was therefore not a PSC.

[58]LTR 8902005, *89 TNT 14-33*. Does this imply that if the company had analyzed the clients needs and advised it on what type of lobbying efforts would be of benefit, then the company might have been a consultant?

[59]LTR 9009017, *90 TNT 50-53*.

activities,[60] nowhere does the IRS state why a movie or theater director, who is not a performing artist, isn't a consultant. A director appears to meet the definition of a consultant because a director performs personal services for a fee and the director's sole job is to provide advice and counsel to the actors and actresses. Thus, it is very hard to figure out why a director isn't a consultant. The same analysis would seem to apply in the case of a commercial photographer, unless the IRS is focusing on the end product rather than the personal services provided by the photographer.

The failure to provide any analysis as to why the commercial photographer or a director is not a consultant makes it almost impossible to state with any certainty whether other professions are consultants. Practitioners and the IRS itself are probably frustrated by the lack of meaningful guidance. As one ruling states, "(t)he examples (in the regulations) do not address all types of services that may or may not qualify as consulting."[61] What are taxpayers to do in the absence of adequate guidance?

D. Accounting

Although the regulations do not define accounting, they do provide an example that states that the preparation of audit and financial statements and tax returns is the practice of accounting.[62] Additional guidance is provided in a private letter ruling that states that when a taxpayer does not perform bookkeeping services, except as a sideline to processing computerized billings and maintaining accounts receivable balances in a computer program, that company is not engaged in the field of accounting.[63] That seems to imply that a company that does perform bookkeeping services is engaged in the field of accounting, even though bookkeepers are not certified. This is only partially consistent with the definition of accounting, which involves the "practice of systematically recording, presenting, and interpreting financial accounts."[64] The problem is that the regulation and ruling do not clearly state that a bookkeeper is engaged in the field of accounting. Given the definition of accounting, must a bookkeeper prepare financial statements and analysis to be considered to be in the field of accounting? A more difficult question is whether a payroll company is engaged in accounting. Given the lack of guidance the answer to that question will probably depend on who is answering the question.

E. Law

There is no definition of law in the code or regulations and there are no rulings that define the term law. The dictionary defines law as the profession of lawyers, judges, etc.[65] Although this definition probably does not include a private company that provides bailiffs to a court or a home security service that provides private law enforcement services, what about a company that provides court reporters or a company that manages a law library or a legal referral service?

Although not surprising in result, it is interesting that guidance was sought to determine whether corporate general partners of a law partnership that practiced law in three cities would themselves be considered to be engaged in the practice of law. The ruling concluded that the corporate general partners are engaged in the practice of law and met the requisite ownership test, so they are PSCs and are permitted to use the cash method of accounting.[66]

F. Engineering

There is no definition of engineering in the code or regulations. The dictionary is helpful. It defines engineering as "a) the science concerned with putting scientific knowledge to practical uses, divided into different branches, as civil, electrical, mechanical, and chemical engineering b) the planning, designing, construction, or management of machinery, roads, bridges, buildings, etc."[67] It is apparent from this definition that most companies that hold themselves out as engineers will be treated as engineers for purposes of PSC classification.

Is a claim staker who occasionally surveys land but who primarily places monuments on property based on a third-party survey to secure mineral rights but does not perform engineering services an engineer? In contrasting engineering to claim staking, a private ruling points out that claim stakers need not be licensed, but engineers and surveyors must be licensed.

> The very nature of engineering services is the application of mathematical, physical, and engineering sciences to services or creative work, such as surveying, consultation, investigation, evaluation, planning, design, and review of construction, public or private utilities, structures, buildings, machines, equipment, or projects.

The ruling concluded that claim staking was not engineering because the claim staking simply involved placing monuments on predetermined locations.[68]

G. Architecture

There is no definition of the term architecture in the code or regulations. The dictionary defines architecture as "the science, art, or profession of designing and

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[60]Reg. section 1.448-1T(e)(4)(i).

[61]LTR 8913012, *89 TNT 74-42*.

[62]Reg. section 1.448-1T(e)(5)(vii), Example (1).

[63]LTR 8927006, *89 TNT 141-20*.

[64]*Webster's New World Dictionary on Power CD, Third Edition.*

[65]*Webster's New World Dictionary on Power CD, Third Edition.*

[66]LTR 9431006, *94 TNT 154-68*.

[67]*Webster's New World Dictionary on Power CD, Third Edition.*

[68]LTR 9232009, *92 TNT 162-14*. Could the other reason be that claim stakers are not licensed? If so, what is the effect on unlicensed engineers? Is the license the only determining factor?

constructing buildings, bridges, etc."[69] Clearly, architectural firms would be considered to be engaging in the field of architecture. Interior decorators and landscape consultants probably wouldn't be covered by this definition, although they might be considered consultants or possibly engineers.

In the absence of better guidelines, many corporations will be faced with the certainty of knowing that there is no certainty in determining their status as a PSC.

H. Actuary

There is no definition of the term actuary in the code or regulations. The dictionary defines actuary as "a person whose work is to calculate statistically risks, premiums, life expectancies, etc. for insurance."[70] In the field of actuary this definition may be too narrow since many actuaries are hired to provide calculations for purposes of properly funding and reporting on qualified pension plans. Even though their work does not involve insurance, they probably should be considered actuaries for purposes of defining a PSC.

[69]*Webster's New World Dictionary on Power CD, Third Edition.*

[70]*Webster's New World Dictionary on Power CD, Third Edition.*

IV. PSC Conclusion and Checklist

Given the lack of clear definitions, examples, or listings of qualifying and nonqualifying PSC businesses, it is often difficult to give a definitive answer to a client who asks if a particular corporation is a PSC. In the absence of clear guidelines the following questions should be asked.

1. Is the company clearly engaged in any of the following fields: health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting?
2. If the company is engaged in what might be considered to be consulting, does it charge by the hour or by the job rather than sell a product?
3. If the company is engaged in what might be considered to be consulting, does it provide advice and counsel to its customers?
4. Are substantially all of the services provided either directly related or incidental to the performance of service in the fields listed above?
5. Does the company meet the ownership test?

If the answer to any of these questions is no, the company is probably not a PSC. In the absence of better guidelines, many corporations will be faced with the certainty of knowing that there is no certainty in determining their status as a PSC. The ability to select a fiscal year and the lower tax rate applicable to corporations that are not PSCs will probably cause corporations to err on the side of non-PSC status. If in doubt and if conservative, several actions can be taken that can reduce or eliminate some of the negative effects of an IRS classification of the corporation as a PSC. They include electing a calendar year and using the cash method of accounting only until average gross receipts exceed $5 million. Giving up the cash method of accounting, however, is probably more than most companies are willing to do.