

IRC Section 448(d)(4)(C)

Election by Common Parent of Affiliated Personal Service Corporations With Regard to the Cash Method

Overview

Under the general rule of IRC Section 448, C corporations are generally prohibited from using the cash receipts and disbursements method ("cash method") of accounting in computing taxable income. Except in the case of a tax shelter, however, this prohibition does not apply to qualified personal service corporations. A C corporation is considered a qualified personal service corporation if it passes two tests, a "function test" and an "ownership test."

The "function test" requires that 95% or more 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. The "ownership test" requires that, at all times during the year, 95% or more of the value of the corporation's stock be owned directly (or indirectly through certain partnerships, S corporations, or qualified personal service corporations) by:

- active employees performing services in one of the qualified fields for the corporation,
- retired employees who had performed services in one of the qualified fields for the corporation,
- the estate of any of the above individuals,
- any other person who acquired the corporation's stock by reason of the death of any of the above individuals, but only for the two year period beginning on the date of the death of the individual, or
- indirect holdings through a trust as prescribed by the Secretary in regulations.

For purposes of determining whether the "ownership test" has been met an affiliated group may, at the election of the common parent, be treated as one taxpayer if 90% or more of the group's activities involve the performance of services in the same qualified field (§448(d)(4)(C)).

Once made, the election is revocable only with the consent of the Commissioner.

When to File

The election is made by attaching a statement to the corporation's income tax return for the taxable year for which the election is to be effective. The election must be made no later than the due date, including extensions, of the corporation's return for such year.

Where to File

The election statement is attached to the corporation's timely-filed return, which is mailed to the designated Internal Revenue Service Center.

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1. Code Section: 448
2. Topic: Accounting Periods and Methods, Consolidated Returns
3. Return Type: 1120

Authorities

IRC §448(d)(4)(C); Reg. §1.448-1T(e)(5)(vi)