Qualified Personal Service Corporations That Used Incorrect Tax Rates Should Promptly File Amended Returns

Announcement 97–88

The Internal Revenue Service has found that many qualified personal service corporations had filed using the incorrect tax rate. Instead of computing tax using the flat Qualified Personal Service Corporation rate, the graduated corporate rate was used which understated the corporations' tax liabilities. Some practitioners have attributed the problem to difficulties with using certain computer tax software programs, while others acknowledged the mistakes as unintentional oversights.

A qualified personal service corporation is taxed at a flat rate of 35% on its taxable income. A corporation is a qualified personal service corporation if it meets both of the following tests:

- 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, and
- At least 95% of the corporation's stock, by value, is owned, directly or indirectly, by (1) employees performing the services, (2) retired employees who had performed the services listed

above, (3) any estate of the employee or retiree described above, or (4) any person who acquired the stock of the corporation as a result of the death of an employee or retiree (but only for the 2-year period beginning on the date of the employee's or retiree's death). See Temporary Regulations section 1.448-1T(e) for details.

The Service has been looking closely into this matter, and will continue to pursue compliance activities to identify taxpayers with the issue and bring them into compliance. In our ongoing efforts to foster taxpayer education and voluntary compliance, we would like to alert taxpayers and practitioners about the problem, and ask any qualified personal service corporations that did not file using the qualified personal service corporation rate to promptly file amended returns with their respective IRS service center to correct the error. Prompt filing will minimize interest assessments.