

108TH CONGRESS  
2D SESSION

# S. 2961

To amend the Internal Revenue Code of 1986 to clarify that qualified personal service corporations may continue to use the cash method of accounting, and for other purposes.

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IN THE SENATE OF THE UNITED STATES

OCTOBER 8, 2004

Mr. BROWNBACK (for himself and Mrs. DOLE) introduced the following bill;  
which was read twice and referred to the Committee on Finance

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## A BILL

To amend the Internal Revenue Code of 1986 to clarify that qualified personal service corporations may continue to use the cash method of accounting, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*  
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Qualified Personal  
5 Service Corporations Clarification Act of 2004”.

1 **SEC. 2. MODIFICATIONS TO DETERMINATION OF WHETHER**  
 2 **CORPORATION IS A QUALIFIED PERSONAL**  
 3 **SERVICE CORPORATION.**

4 (a) STOCK HELD BY CERTAIN FORMER EMPLOYEES  
 5 TAKEN INTO ACCOUNT.—Subparagraph (B) of section  
 6 448(d)(2) of the Internal Revenue Code of 1986 (defining  
 7 qualified personal service corporation) is amended by  
 8 striking “or” at the end of clause (iii), by striking the pe-  
 9 riod at the end of clause (iv) and inserting a comma, and  
 10 by inserting after clause (iv) the following new clauses:

11 “(v) former employees of such cor-  
 12 poration who performed the services re-  
 13 ferred to in subparagraph (A) and who are  
 14 holding such stock by reason of their  
 15 former employment with such corporation,  
 16 or

17 “(vi) former employees of such cor-  
 18 poration who performed the services re-  
 19 ferred to in subparagraph (A) and who are  
 20 holding such stock by reason of their cur-  
 21 rent or former employment with any con-  
 22 trolled entity (as defined in paragraph  
 23 (4)(B)).”.

24 (b) OTHER MODIFICATIONS.—Paragraph (4) of sec-  
 25 tion 448(d) of such Code is amended to read as follows:

26 “(4) SPECIAL RULES FOR PARAGRAPH (2).—

1           “(A) IN GENERAL.—For purposes of para-  
2 graph (2)—

3           “(i) community property laws shall be  
4 disregarded,

5           “(ii) stock held by a plan described in  
6 section 401(a) which is exempt from tax  
7 under section 501(a) shall be treated as  
8 held by an employee described in para-  
9 graph (2)(B)(i), and

10           “(iii) at the election of the common  
11 parent of an affiliated group (within the  
12 meaning of section 1504(a)), all members  
13 of such group may be treated as 1 tax-  
14 payer for purposes of paragraph (2)(B) if  
15 80 percent or more of the activities of such  
16 group involve the performance of services  
17 in the fields described in paragraph (2)(A).

18           “(B) CONTROLLED ENTITY.—For purposes  
19 of paragraph (2)(B)(vi), the term ‘controlled  
20 entity’ means, with respect to a corporation—

21           “(i) any corporation at least 50 per-  
22 cent (by value) of the outstanding stock of  
23 which is owned (directly or indirectly as  
24 determined under section 318) by such  
25 corporation, and

1           “(ii) any partnership at least 50 per-  
2           cent of the capital interest or profits inter-  
3           est in which is owned (directly or indirectly  
4           as determined under section 318) by such  
5           corporation.

6           “(C) NEW CORPORATIONS.—A corporation  
7           shall be treated as a qualified personal service  
8           corporation for each taxable year preceding the  
9           first taxable year for which the corporation has  
10          gross receipts if the corporation is a qualified  
11          personal service corporation for such first tax-  
12          able year.

13          “(D) CERTAIN STOCK NOT TAKEN INTO  
14          ACCOUNT.—

15                 “(i) IN GENERAL.—The determination  
16                 of whether an employee-owned corporation  
17                 is a qualified personal service corporation  
18                 shall be made without regard to stock in  
19                 such corporation which is held by employ-  
20                 ees of unaffiliated controlled entities. The  
21                 preceding sentence shall not apply to em-  
22                 ployees described in clause (v) or (vi) of  
23                 paragraph (2)(B).

24                 “(ii) EMPLOYEE-OWNED CORPORA-  
25                 TION.—For purposes of clause (i), the

1 term ‘employee-owned corporation’ means  
2 any corporation at least 50 percent of the  
3 value of the outstanding stock of which is  
4 owned (directly or indirectly) by employees  
5 described in paragraph (2)(B) (without re-  
6 gard to this subparagraph) of such cor-  
7 poration.

8 “(iii) UNAFFILIATED CONTROLLED  
9 ENTITY.—For purposes of clause (i), the  
10 term ‘unaffiliated controlled entity’ means,  
11 with respect to an employee-owned cor-  
12 poration—

13 “(I) any corporation at least 50  
14 percent (by value) of the outstanding  
15 stock of which is owned (directly or  
16 indirectly as determined under section  
17 318) by members of an affiliated  
18 group (within the meaning of section  
19 1504(a)) which includes such em-  
20 ployee-owned corporation, and

21 “(II) any partnership at least 50  
22 percent of the capital interest or prof-  
23 its interest in which is owned (directly  
24 or indirectly as determined under sec-

1                   tion 318) by members of such affili-  
2                   ated group.

3                   Such term shall not include any corpora-  
4                   tion which is permitted to file a consoli-  
5                   dated return with such affiliated group.

6                   “(E) CERTAIN SERVICES DEFINED.—For  
7                   purposes of paragraph (2), the terms ‘engineer-  
8                   ing’ and ‘architecture’ include—

9                   “(i) the performance of professional  
10                  services described in section 1102(2) of  
11                  title 40, United States Code, and

12                  “(ii) design-build and its various op-  
13                  tions, including financing, owning, and op-  
14                  eration.”.

15                  (c) EFFECTIVE DATE.—The amendments made by  
16                  this section shall apply to taxable years ending after the  
17                  date of the enactment of this Act.

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