

## Should Income be Reported on Schedule C or S Corporation

The sole issue in this case is whether the income earned during the year should be reported on the taxpayer's Schedule C as self-employment income or on his solely owned S corporation. The dates and agreements/contracts are important in this case. The amounts in this article are rounded to make it easier to read.

Mr. Fleischer is a financial consultant with series 6, 7, 24, 63, and 65 licenses. He is also a certified financial planner, a registered financial consultant, and a licensed seller of variable health and life insurance policies. On February 2, 2006, he entered into a representative agreement with Linsco/Private Ledger Financial Services (LPL). The agreement expressly states that Mr. Fleischer is an independent contractor. Mr. Fleischer signed the agreement in his personal capacity.

Five days later, on February 7, 2006, he created a corporation (FWP) and elected S status. On February 28, 2006, he entered into an employment agreement with FWP. He was paid an annual salary of about \$35,000 (35k) to manage client investment portfolios, expand FWP's client base, drafting and reviewing financial documents, and representing FWP "diligently and responsibly at all times." The agreement DOES NOT include a provision requiring petitioner to remit any commissions or fees from LPL or any other third party to FWP.

A little over two years later, on March 13, 2008, Mr. Fleischer entered into a broker contract with MassMutual Financial Group (MassMutual). This contract is between Mr. Fleischer and MassMutual. No mention of FWP exists.

There were no amendments to either of the LPL or MassMutual agreements requiring those entities to begin paying FWP instead of Mr. Fleischer nor to recognize FWP in any capacity.

On his 2009 Form 1040 Mr. Fleischer reported his wages and 12k of K-1 income from FWP on Schedule E. On its Form 1120S, FWP reported gross receipts of 147k and expenses of 135k, for a net of 12k.

On his 2010 Form 1040 Mr. Fleischer reported his wages and 147k of K-1 income from FWP. His Form 1040 included a Schedule C, page 2 only with an entry in Other Expenses of 284k of "Reported by...". Apparently this Schedule C entry was made to offset Form 1099 income reported in Mr. Fleischer's name and EIN.

On his 2011 Form 1040 Mr. Fleischer reported his wages and 115k of K-1 income from FWP, again with a Schedule C with the entry to offset the Form 1099 income.

Tax Court stated the income belongs to the taxpayer who earned the income. When it is a choice of whether the income is earned by a corporation or its service-provider employee, the question is one of "who controls the earning of the income." The Court gives two elements that must exist for the corporation to be the controller of the income: 1) the individual must be an employee of the corporation whom the corporation can direct and control in a meaningful sense, and 2) there must exist between the corporation and the person or entity using the services a

contract or similar indication recognizing the corporation's controlling position. In this case Tax Court determined Mr. Fleischer's employer-employee relationship with FWP began about three weeks after Mr. Fleischer entered into the agreement with LPL and that LPL was not aware that FWP controlled petitioner.

Mr. Fleisher also argued the reason FWP was not on the contracts is because it could not enter into representative agreements and broker contracts since it was not a registered entity under the securities laws and regulations. He further stated it would cost millions of dollars to get FWP registered and that was unreasonable to do. Tax Court took the position that the high cost of getting FWP registered was not a substantial authority that would PROHIBIT FWP from registering. Since FWP was not registered this prevents it from engaging in the sale of securities and therefore does NOT allow Mr. Fleischer to assigning the income he earned in his personal capacity to FWP.

Summary – Court determination = this income belongs on Mr. Fleischer's Schedule C as self-employment income.

Ryan M. Fleischer, TC Memo 2016-238. This case can be found by going to [www.ustaxcourt.gov](http://www.ustaxcourt.gov), clicking on Opinion Search, and entering Fleischer in the "Case Name Keyword" box.

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