***Roubik v. Commissioner, 53 T. C. 365 (1969)***

For a professional service corporation to be recognized as a separate tax entity, it must operate independently and actually earn the income, not merely serve as a conduit for individual earnings.

**Summary**

In Roubik v. Commissioner, the Tax Court held that income generated by radiologists was taxable to them individually, not to their professional service corporation, because the corporation lacked independent operation and control over the income. The physicians formed a corporation but continued their separate practices, using the corporation mainly for bookkeeping. The court emphasized that the corporation did not enter contracts, own equipment, or direct the physicians' work, thus failing to earn the income. This case underscores that a professional service corporation must have substantive operations to be recognized as a separate tax entity.

**Facts**

In 1961, four radiologists formed a professional service corporation named Pfeffer Associates, which was validly incorporated under Wisconsin law. Each radiologist entered into an employment agreement with the corporation, but they continued their individual practices. During the taxable year 1965, the corporation was an electing small business corporation under IRC section 1371(b). The income from the radiologists' services was deposited into corporate accounts, and expenses were paid from these accounts. However, the corporation did not enter into service contracts, own equipment, or direct the radiologists' work. The radiologists reported their compensation and the corporation's undistributed taxable income on their individual tax returns.

**Procedural History**

The Commissioner of Internal Revenue determined deficiencies in the radiologists' income taxes for 1965, asserting that they were engaged in business as partners, not as employees of the corporation. The Tax Court consolidated the cases and held that the income was taxable to the radiologists individually, as the corporation did not earn the income.

**Issue(s)**

1. Whether the income generated from the radiologists' professional services was earned by and taxable to the professional service corporation, Pfeffer Associates, or to the individual radiologists.

**Holding**

 

1. No, because the corporation did not actually earn the income. The radiologists continued their separate practices, and the corporation served merely as a conduit for their earnings.

**Court's Reasoning**

The Tax Court found that Pfeffer Associates did not operate as a true corporation. It did not enter into service contracts, own equipment, or direct the radiologists' work. The corporation's activities were limited to maintaining bookkeeping entries and bank accounts. The court noted that the radiologists' employment agreements with the corporation were drafted to create an appearance of control, but in practice, they retained control over their practices. The court distinguished this case from United States v. Empey, where the corporation was found to have operated independently. Judge Tannenwald's concurring opinion emphasized that the corporation must have substantive operations to be recognized as a separate tax entity.

**Practical Implications**

This decision has significant implications for professionals considering incorporation under state professional service corporation acts. It underscores that the corporation must have independent operations and control over income to be recognized as a separate tax entity. Professionals must ensure that the corporation enters contracts, owns assets, and directs the work of its employees to avoid having income taxed to them individually. This case has been cited in later decisions to support the principle that a corporation must have substance to be recognized for tax purposes. Professionals should consult with tax advisors to structure their practices to meet these requirements, as failure to do so could result in individual tax liability for corporate income.

 