

# Confused about S Corporations?

We get it! Like many types of income, S Corps are not just black and white. Participants involved in an S Corporation can potentially receive both earned and unearned income so let's break it down.

FAA4.H01B.63 S Corporation Profits

## What is an S Corporation?

S corporations are corporations that elect to pass corporate income, losses, deductions, and credits through to their shareholders for federal tax purposes.



**It's all in the paperwork...**

Tax forms required to be filed by S corporations are the **IRS form 2553**, **IRS form 1120S**, and **IRS Schedule K forms**. Check out the chart to see the information these forms provide.

2553	1120S	Schedule K
Form used to elect S corporation status	Filed to report income, gains, losses, deductions and credits for any tax year when they have elected to be classified as an S corporation.	Filed to report information regarding income, deductions, credits, and other items that pass through to the corporation's shareholders.

\*The IRS Schedule K-1 form provides information about the shareholder's shares of income from the corporation.



# Earned or Unearned

That is the question...

Profits from shares in an S Corporation are countable as **unearned income**

Any other income received from an S Corporation is countable and considered **earned income**

**The type is in the detail!**

The type is in the detail! Review all the relevant documents to make sure all income is present and accounted for. The 1120S will give you a picture of the total sum of income. Be sure to look at :

- Gross Receipt or Sales,
- Ordinary Business Income, and
- Compensation of Officers.

Check if corporation:  (1)  Aggregated activities for sec  
 on: Include **only** trade or business income and expense  
 1a Gross receipts or sales  b Le  
 2 Cost of goods sold (attach Form 1125-A) . . .

20 Other deductions (attach statement) . . . . .  
 21 **Total deductions.** Add lines 7 through 20 . . . . .  
 22 **Ordinary business income (loss).** Subtract line 21 from line 6 . . . . .  
 23a Excess net passive income or LIFO recapture tax (see instructions) . . . . . 23a

6 **Total income (loss).** Add lines 3 through 5 . . . . . 6   
 7 Compensation of officers (see instructions—attach Form 1125-E) . . . . . 7   
 8 Salaries and wages (less employment credits) . . . . . 8   
 a Repairs and maintenance . . . . . a

These areas will clue you in to whether you need to follow up on earned income or unearned income. When tax forms show income paid to shareholders, interest, royalties ,or dividends use policy to determine what additional documents you may need to request and what budgeting procedures you must follow.



**S corporation income is complicated so ask for everything you need!**