

## Section 199A Final Regulations Truncated

The final regulations released by the Treasury Department and the IRS are over 240 pages. Given our attention to small business owners and reviewing our current clients' needs, we truncated this massive document into about 70 pages.

- ▲ Trade or Business Summary (includes rental property)
- ▲ Treatment of Other Deductions Summary
- ▲ Guaranteed Payments Summary
- ▲ Reasonable Compensation Summary
- ▲ Specified Service Trade or Business Summary (everyone's fav)
- ▲ Services or Property Provided to an SSTB Summary
- ▲ Specific Service Trade or Business Examples (a close second)
- ▲ Presumption of Employee Examples (yuck)

Proposed Section 199A Regs      [www.wcgroup.com/8321](http://www.wcgroup.com/8321) (full version)

Final Section 199A Regs      [www.wcgroup.com/8323](http://www.wcgroup.com/8323) (full version)

## **Trade or Business Summary**

### 3. Trade or Business

#### a. In General

The calculation of QBI and therefore, the benefits of section 199A, are limited to taxpayers with income from a trade or business. Section 199A and its legislative history, however, do not define the phrase “trade or business.” The proposed regulations define trade or business by reference to section 162. Section 162(a) permits a deduction for all the ordinary and necessary expenses paid or incurred in carrying on a trade or business. Multiple commenters agreed that section 162 is the most appropriate standard for what constitutes a trade or business for purposes of section 199A, but noted that there are significant uncertainties in the meaning of trade or business under section 162. However, because many taxpayers who will now benefit from the section 199A deduction are already familiar with the trade or business standard under section 162, using the section 162 standard appears to be the most practical for taxpayers and the IRS. Therefore, after considering all relevant comments, the final regulations retain and slightly reword the proposed regulation’s definition of trade or business. Specifically, for purposes of section 199A and the regulations thereunder, §1.199A-1(b)(14) defines trade or business as a trade or business under section 162 (section 162 trade or business) other than the trade or business of performing services as an employee.

The Treasury Department and the IRS received a number of comments requesting additional guidance with respect to determining whether an activity rises to the level of a section 162 trade or business, and therefore, will be considered to be a trade or business for purposes of determining the section 199A deduction.

Commenters suggested guidance in the form of a regulatory definition, a bright-line test, a factor-based test, or a safe harbor. Whether an activity rises to the level of a section 162 trade or business, however, is inherently a factual question and specific guidance under section 162 is beyond the scope of these regulations. Accordingly, the Treasury Department and the IRS have concluded that the factual setting of various trades or businesses varies so widely that a single rule or list of factors would be difficult to provide in a timely and manageable manner and would be difficult for taxpayers to apply.

In Higgins v. Commissioner, 312 U.S. 212 (1941), the Supreme Court noted that determining whether a trade or business exists is a factual determination. Specifically, the Court stated that the determination of “whether the activities of a taxpayer are ‘carrying on a business’ requires an examination of the facts in each case.” 312 U.S. at 217. Because there is no statutory or regulatory definition of a section 162 trade or business, courts have established elements to determine the existence of a trade or business. The courts have developed two definitional requirements. One, in relation to profit motive, is said to require the taxpayer to enter into and carry on the activity with a good faith intention to make a profit or with the belief that a profit can be made from the activity. The second is in relation to the scope of the activities and is said to require considerable, regular, and continuous activity. See generally Commissioner v. Groetzinger, 480 U.S. 23 (1987). In the seminal case of Groetzinger, the Supreme Court stated, “[w]e do not overrule or cut back on the Court’s holding in Higgins when we conclude that if one’s gambling activity is pursued full time, in good faith, and with

regularity, to the production of income for a livelihood, and is not a mere hobby, it is a trade or business within the statutes with which we are here concerned.” Id. at 35.

A few commenters suggested adopting the definitions or rules regarding a trade or business found in other provisions of the Code, including sections 469 and 1411. Section 469(c)(6) and §1.469-4(b)(1) broadly define trade or business activities other than rental activities to include any activity performed: (i) in connection with a trade or business within the meaning of section 162, (ii) with respect to which expenses are allowable as a deduction under section 212, (iii) conducted in anticipation of the commencement of a trade or business, or (iv) that involves research and experimentation expenditures (within the meaning of section 174). Section 1.469-4(b)(2) defines a rental activity as an activity that constitutes a rental activity within the meaning of §1.469-1T(e)(3). Passive activities for purposes of section 469 are defined as any activity that involves the conduct of a trade or business in which the taxpayer does not materially participate and includes all rental activity. The definition of trade or business for section 469 purposes is significantly broader than the definition for purposes of section 162 as it is intended to capture a larger universe of activities, including passive activities. Section 469 was enacted to limit the deduction of certain passive losses and therefore, serves a very different purpose than the allowance of a deduction under section 199A. Further, section 199A does not require that a taxpayer materially participate in a trade or business in order to qualify for the section 199A deduction. Consequently, the Treasury Department and the IRS decline to adopt the recommendation to define trade or business for purposes of section 199A by reference to section 469. The Treasury Department and the IRS also decline to define trade or

business by reference to section 1411 as §1.1411-1(d)(12) defines trade or business by reference to section 162 in a manner similar to §1.199A-1(b)(14).

Commenters also suggested that the section 199A regulations incorporate the real estate professional provisions in section 469(c)(7) in a manner similar to the cross references in section 163(j) and §1.1411-4(g)(7). Under section 469, a real estate professional may treat rental real estate activities described in section 469(c)(7)(C) as nonpassive if the taxpayer materially participates in such activities. Section 1.469-5T(a) provides seven tests to establish material participation, but as noted above, these tests only determine whether an individual materially participates in a rental real estate activity. They cannot be used to determine whether the activity itself is a trade or business. Unlike section 469, whether a taxpayer is entitled to a section 199A deduction is not determined based on the taxpayer's level of participation in a trade or business, nor does it require that an individual materially participate in the trade or business. Instead, section 199A is dependent on whether the individual has QBI from a trade or business. Consequently, the Treasury Department and the IRS decline to adopt these comments because the §1.469-5T material participation tests are not a proxy to establish regular, continuous, and considerable activity that rises to the level of a trade or business for purposes of section 199A.

b. Rental Real Estate Activities as a Trade or Business.

A majority of the comments received on the meaning of a trade or business focus on the treatment of rental real estate activities. Commenters noted inconsistency in the case law in determining whether a taxpayer renting real estate is engaged in a trade or business. Some commenters suggested including safe harbors, tests, or a variety of

factors, which if satisfied, would qualify a rental real estate activity as a trade or business. A number of commenters suggested that all rental real estate activity should qualify as a trade or business. Further, one commenter suggested that rental income from real property held for the production of rents within the meaning of section 62(a)(4) should be considered a trade or business for purposes of section 199A. Another commenter suggested that final regulations provide that an individual whose taxable income does not exceed the threshold amount will be considered to be conducting a trade or business with respect to any real estate rental of which the individual owns at least ten percent and in which the individual actively participates within the meaning of section 469(i).

In determining whether a rental real estate activity is a section 162 trade or business, relevant factors might include, but are not limited to (i) the type of rented property (commercial real property versus residential property), (ii) the number of properties rented, (iii) the owner's or the owner's agents day-to-day involvement, (iv) the types and significance of any ancillary services provided under the lease, and (v) the terms of the lease (for example, a net lease versus a traditional lease and a short-term lease versus a long-term lease).

Providing bright line rules on whether a rental real estate activity is a section 162 trade or business for purposes of section 199A is beyond the scope of these regulations. Additionally, the Treasury Department and the IRS decline to adopt a position deeming all rental real estate activity to be a trade or business for purposes of section 199A. However, the Treasury Department and IRS recognize the difficulties taxpayers and practitioners may have in determining whether a taxpayer's rental real

estate activity is sufficiently regular, continuous, and considerable for the activity to constitute a section 162 trade or business. Accordingly, **Notice 2019-07**, 2019-XXX IRB **XXX** released concurrently with these final regulations, provides notice of a proposed revenue procedure detailing a proposed safe harbor under which a rental real estate enterprise may be treated as a trade or business solely for purposes of section 199A.

Under the proposed safe harbor, a rental real estate enterprise may be treated as a trade or business for purposes of section 199A if at least 250 hours of services are performed each taxable year with respect to the enterprise. This includes services performed by owners, employees, and independent contractors and time spent on maintenance, repairs, collection of rent, payment of expenses, provision of services to tenants, and efforts to rent the property. Hours spent by any person with respect to the owner's capacity as an investor, such as arranging financing, procuring property, reviewing financial statements or reports on operations, planning, managing, or constructing long-term capital improvements, and traveling to and from the real estate are not considered to be hours of service with respect to the enterprise. The proposed safe harbor also would require that separate books and records and separate bank accounts be maintained for the rental real estate enterprise. Property leased under a triple net lease or used by the taxpayer (including an owner or beneficiary of an RPE) as a residence for any part of the year under section 280A would not be eligible under the proposed safe harbor. A rental real estate enterprise that satisfies the proposed safe harbor may be treated as a trade or business solely for purposes of section 199A and such satisfaction does not necessarily determine whether the rental real estate activity

is a section 162 trade or business. Likewise, failure to meet the proposed safe harbor would not necessarily preclude rental real estate activities from being a section 162 trade or business.

Examples 1 and 2 of proposed §1.199A-1(d)(4) describe a taxpayer who owns several parcels of land that the taxpayer manages and leases to airports for parking lots. The Treasury Department and the IRS are aware that some practitioners and taxpayers questioned whether the use of the lease of unimproved land in these examples was intended to imply that the lease of unimproved land is a trade or business for purposes of section 199A. Proposed §1.199A-1(d)(4) provides that for purposes of the examples all businesses described in the examples are trades or business for purposes of section 199A. Example 1 was intended to provide a simple illustration of how the calculation would work if a taxpayer lacked sufficient W-2 wages or UBIA of qualified property to claim the deduction. Example 2 built on the fact pattern by adding UBIA of qualified property to the facts. The examples in the proposed regulations were not intended to imply that the lease of the land is, or is not, a trade or business for purposes of section 199A beyond the assumption in the examples. In order to avoid any confusion, the final regulations remove the references to land in both examples.

c. Special Rule for Renting Property to a Related Person.

In one instance, the proposed regulations and the final regulations extend the definition of trade or business for purposes of section 199A beyond section 162. Solely for purposes of section 199A, the rental or licensing of tangible or intangible property to a related trade or business is treated as a trade or business if the rental or licensing

activity and the other trade or business are commonly controlled under proposed §1.199A-4(b)(1)(i). This rule also allows taxpayers to aggregate their trades or businesses with the leasing or licensing of the associated rental or intangible property if all of the requirements of proposed §1.199A-4 are met.

One commenter asked for clarification regarding whether this rule applies to situations in which the rental or licensing is to a commonly controlled C corporation. Another commenter suggested that the rule in the proposed regulations could allow passive leasing and licensing-type activities to benefit from section 199A even if the counterparty is not an individual or an RPE. The commenter recommended that the exception be limited to scenarios in which the related party is an individual or an RPE and that the term related party be defined with reference to existing attribution rules under sections 267, 707, or 414. The final regulations clarify these rules by adopting these recommendations and limiting this special rule to situations in which the related party is an individual or an RPE. Further, as discussed in part V.B. of this Summary of Comments and Explanation of Revisions, the final regulations provide that the related party rules under sections 267(b) or 707(b) will be used to determine relatedness for purposes of §1.199A-4 and this special rule.

d. Multiple Trades or Businesses Within an Entity

Several commenters suggested that there should be safe harbors or factors to determine how to delineate separate section 162 trades or businesses within an entity and when an entity's combined activities should be considered a single section 162 trade or business. Some of the factors suggested include whether the activities: have separate books and records, facilities, locations, employees, and bank accounts;

## **Treatment of Other Deductions Summary**

## **Guaranteed Payments Summary**

or business in the tax year concerned and the recapture rules in section 904(f) apply only for purposes of subchapter N, Part III, Subpart A of the Code. In addition, it would not be appropriate to expand the scope of QBI for recaptured foreign losses when no similar relief is available if non-qualifying domestic losses are subsequently offset by non-qualifying domestic income.

#### 5. Treatment of Other Deductions

Section 199A(c)(1) provides that QBI includes the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer. Commenters requested additional guidance on whether certain items constitute qualified items under this provision. Several commenters suggested that deductions for self-employment tax, self-employed health insurance, and certain other retirement plan contribution deductions should not reduce QBI. One commenter reasoned that qualified retirement plan contributions should not reduce QBI because they should not be treated as being associated with a trade or business, consistent with the treatment when calculating net operating losses under section 172(d)(4)(D). The commenter also suggested that while self-employed health insurance is treated as associated with a trade or business, such expense should likewise not reduce QBI for purposes of simplification in administering the rule. Another commenter suggested that QBI should not be reduced by these expenses because they are personal adjustments. One commenter also requested guidance on whether unreimbursed partnership expenses, the interest expense to acquire partnership and S corporation interests, and state and local taxes reduce QBI.

The Treasury Department and the IRS have not adopted these recommendations because they are inconsistent with the statutory language of section 199A(c). Whether a deduction is attributable to a trade or business must be determined under the section of the Code governing the deduction. All deductions attributable to a trade or business should be taken into account for purposes of computing QBI except to the extent provided by section 199A and these regulations. Accordingly, §1.199A-3(b)(1)(vi) provides that, in general, deductions attributable to a trade or business are taken into account for purposes of computing QBI to the extent that the requirements of section 199A and §1.199A-3 are otherwise satisfied. Thus, for purposes of section 199A, deductions such as the deductible portion of the tax on self-employment income under section 164(f), the self-employed health insurance deduction under section 162(l), and the deduction for contributions to qualified retirement plans under section 404 are considered attributable to a trade or business to the extent that the individual's gross income from the trade or business is taken into account in calculating the allowable deduction, on a proportionate basis. The Treasury Department and the IRS decline to address whether deductions for unreimbursed partnership expenses, the interest expense to acquire partnership and S corporation interests, and state and local taxes are attributable to a trade or business as such guidance is beyond the scope of these regulations.

#### 6. Guaranteed Payments for the Use of Capital

A few commenters suggested that the rule in the proposed regulations which excludes guaranteed payments for the use of capital under section 707(c) should be removed. Commenters argued that while section 199A(c)(4) excludes guaranteed

payments paid to a partner for services rendered with respect to a trade or business under section 707(a), the statutory language does not likewise exclude guaranteed payments for the use of capital under section 707(c). The commenters argued that Congress drew a line between payments for services and payments for the use of capital when it drafted section 199A(c) and that even though payments for the use of capital are determined without regard to the partnership's income, that does not mean that they are not attributable to a trade or business. Several commenters stated that contrary to the reasoning in the preamble to the proposed regulations, there is risk involved when making guaranteed payments for the use of capital because the payments do rely to some degree on the partnership's success. Commenters noted that guaranteed payments for the use of capital are generally accepted as part of the partner's distributive share from the partnership and taxed as such, and should be included in calculating QBI. Similarly, another commenter generally requested additional guidance for how to determine when a payment to a partner is considered for the use of capital and excluded from the calculation of QBI. Another commenter suggested that if guaranteed payments for the use of capital under section 707(c) are excluded from the calculation of QBI, a partnership's expense related to guaranteed payments for the use of capital also should be excluded from the calculation of QBI. One commenter suggested that to the extent a guaranteed payment for the use of capital is considered akin to interest income on indebtedness, it is generally appropriate to exclude the payment from QBI but noted the significant uncertainty in determining whether an arrangement is a guaranteed payment for the use of capital, a gross income

allocation, or something else. The commenter also noted that guaranteed payments for the use of capital are not necessarily akin to interest income.

The Treasury Department and the IRS decline to adopt the comments suggesting that guaranteed payments for the use of capital are generally attributable to a trade or business. Although section 199A is silent with respect to guaranteed payments for the use of capital, section 199A does limit the deduction under section 199A to income from qualified trades or businesses. The Treasury Department and the IRS believe that guaranteed payments for the use of capital are not attributable to the trade or business of the partnership because they are determined without regard to the partnership's income. Consequently, such payments should not generally be considered part of the recipient's QBI. Rather, for purposes of section 199A, guaranteed payments for the use of capital should be treated in a manner similar to interest income. Interest income other than interest income which is properly allocated to trade or business is specifically excluded from qualified items of income, gain, deduction or loss under section 199A(c)(3)(B)(iii). One commenter noted that if guaranteed payments are treated like interest income for purposes of section 199A, and if such payments are properly allocated to a qualified trade or business of the recipient, they should constitute QBI to that recipient in respect of such qualified trade or business. Although, this is an unlikely fact pattern to occur, the Treasury Department and the IRS agree with this comment and the final regulations adopt this comment. Further, guidance under sections 707(a) and 707(c) is beyond the scope of these regulations.

#### 7. Section 707(a) Payments for Services

## Reasonable Compensation Summary

subtitle A of the Code is generally a function of section 864(c)(8). On **[INSERT DATE REG-113604-18 PUBLISHED IN THE FEDERAL REGISTER]**, the **Federal Register** published a notice of proposed rulemaking (REG-113604-18) at XX FR XXX under section 864(c)(8) (proposed section 864(c)(8) regulations). The proposed section 864(c)(8) regulations provide rules for determining the amount of gain or loss treated as effectively connected with the conduct of a trade or business within the United States (“effectively connected gain” or “effectively connected loss”) described in section 864(c)(8), including rules coordinating section 864(c)(8) with sections 741 and 751 (relating to the character of gain or loss realized in connection with the sale or exchange of an interest in a partnership). Because the proposed section 864(c)(8) regulations apply the deemed sale construct of section 751(a) to determine whether gain or loss on the sale of a partnership interest is subject to tax under section 864(c)(8), the issue raised in this comment does not arise, and thus this comment is not adopted. The Treasury Department and the IRS request further comments on the interaction of section 199A and the proposed regulations under section 864(c)(8) after the publication of those proposed regulations.

#### 9. Reasonable Compensation

Several commenters were concerned that an overlap of the QBI, W-2 wage limitation, and reasonable compensation rules for S corporations would cause disparities between taxpayers operating businesses in different entity structures. These commenters stated that the rules might have the unintended consequence of encouraging taxpayers to select or avoid certain business entities. For example, one commenter noted that the reasonable compensation requirement for S corporations

favors S corporations for purposes of the W-2 wage limitation when calculating the section 199A deduction, compared to sole proprietorships and partnerships which may not pay any wages. That commenter suggested the final regulations include an election for partners or sole proprietors to treat an amount of reasonable compensation paid as wages for purposes of the W-2 wage limitation. Other commenters similarly noted the entity choice issue, but from the perspective that S corporations can be less advantageous. The commenters argued that QBI is reduced for S corporation shareholders because reasonable compensation is not included in QBI and noted there could be further impacts depending on whether the taxpayer is above or below the income thresholds. These commenters suggested that the final regulations should strive for equity between taxpayers operating businesses in different entity structures. Finally, one commenter suggested the need for additional guidance regarding whether and how reasonable compensation paid to an S corporation shareholder is considered wages for purposes of the W-2 wage limitation.

One commenter maintained that to avoid incentivizing minimization of compensation and Federal Insurance Contributions Act tax, the final regulations should provide that deductions with respect to reasonable compensation should not reduce QBI. The commenter stated that reasonable compensation must be added back in calculating QBI.

The Treasury Department and the IRS decline to adopt these suggestions. Section 199A(c)(4) clearly excludes reasonable compensation paid to a taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business from QBI. These amounts are attributable to a trade or business and

are thus qualified items of deduction as described in section 199A(c)(3) to the extent they are effectively connected with the conduct of a trade or business within the United States and included or allowed in determining taxable income for the taxable year. In addition, reasonable compensation paid to a shareholder-employee is included as W-2 wages for purposes of the W-2 wage limitation to the extent that the requirements of §1.199A-2 are otherwise satisfied. Further, guaranteed payments and payments to independent contractors are not W-2 wages and therefore, cannot be counted for purposes of the W-2 wage limitation.

A few commenters were concerned about whether tax return preparers would have the responsibility to closely examine whether compensation paid to a shareholder of an S corporation is reasonable before calculating the section 199A deduction, and whether tax return preparers could be subject to penalties. One commenter suggested a small business safe harbor approach where certain cash method S corporations that treat at least 70 percent of dividend distributions to shareholder-employees as wages are deemed to satisfy the reasonable compensation requirement of Rev. Rul. 74-44, 1974-1 C.B. 287. Providing additional guidance with respect to what constitutes reasonable compensation for a shareholder-employee of an S corporation or the application or non-application of assessable penalties applicable to tax return preparers is beyond the scope of these final regulations.

#### 10. Items Treated as Capital Gain or Loss

The proposed regulations provide that any item of short-term capital gain, short-term capital loss, long-term capital gain, or long-term capital loss, including any item treated as one of such items, such as gains or losses under section 1231, that are

## **Specific Service Trade or Business Summary**

## E. Examples

The proposed regulations provide several examples of the aggregation rules. One commenter noted that proposed §1.199A-4(b)(1)(i) refers to the capital or profits of a partnership while the examples refer to the capital and profits of a partnership. The language in the examples was intended to demonstrate that the taxpayers were sharing proportionately in all items. For clarification, the final regulations retain the reference to capital or profits in §1.199A-4(b)(1)(i) and update the examples to remove the references to capital and profits.

## VI. Specified Service Trades or Businesses and the Trade or Business of Being an Employee.

### A. Definition of Specified Service Trade or Business

#### 1. In General

The proposed regulations provide definitional guidance on the meaning of a trade or business involving the performance of services in each of the fields listed in section 199A(d)(2). Multiple commenters requested guidance on whether specific trades or businesses would constitute SSTBs. In many cases, the determination of whether a specific trade or business is an SSTB depends on whether the facts and circumstances demonstrate that the trade or business is in one of the listed fields. Although the Treasury Department and the IRS understand the desire for certainty, because the determination of whether a particular trade or business is an SSTB is factually dependent, this analysis is beyond the scope of these regulations.

Several commenters argued that the meaning of performance of services in the various fields should be limited to the definitions provided in §1.448-1(T)(e)(4). A few

commenters noted that any expansion beyond these definitions is contrary to legislative intent as expressed in “Tax Cuts and Jobs Act,” Statement of Managers to the Conference Report to Accompany H.R. 1, H.R. Rept. 115-466 (Dec. 15, 2017), p. 216-222. These commenters argue that the Statement of Managers notes that the committee adopted the Senate Amendment and described the section 448 regulations as an indicator of the meaning of services in the health, performing arts, and consulting fields referenced in section 1202(e)(3)(A) as incorporated by section 199A. The Treasury Department and the IRS decline to adopt these comments. While the Statement of Managers does reference §1.448-1T(e)(4), nothing in the language of the report limits the definitions for purposes of section 199A to those provided in §1.448-1T(e)(4). Section 199A does not reference section 448; instead, section 199A incorporates section 1202(e)(3)(A) with modifications. The Treasury Department and the IRS believe it is appropriate to look to the definitions provided for in the regulations under section 448 because guidance under section 1202 is limited. However, as stated in the preamble to the proposed regulations, the existing guidance under section 448 is not a substitute for guidance under section 199A.

The intent of section 448 and the intent of section 199A are different. Section 448 prohibits certain taxpayers from computing taxable income under the cash receipts and disbursements method of accounting. Qualified personal services corporations are excluded from this prohibition. Section 448(d)(2) defines the term qualified personal service corporation to include certain employee-owned corporations, substantially all of the activities of which involve the performance of services in the fields of health, law, engineering architecture, accounting, actuarial sciences, performing arts, or consulting.

By contrast, section 199A provides a deduction based on QBI from a qualified trade or business. For taxpayers with taxable income above the phase-in range, an SSTB is not a qualified trade or business. Section 199A, through reference to section 1202, defines an SSTB as a trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners. The trade or business of the performance of services that consist of investing and investment management, trading, or dealing in securities (as defined in section 475(c)(2)), partnership interests, or commodities (as defined in section 475(e)(2)) is also defined as an SSTB for purposes of section 199A. Further, section 199A looks to the trade or business of performing services involving one or more of the listed fields, and not the performance of services themselves in determining whether a trade or business is an SSTB. The designation of a trade or business as an SSTB applies to owners of the trade or business, regardless of whether the owner is passive or participated in any specified service activity. Accordingly, it is both necessary and consistent with the statute and the legislative history to expand the definitions of the fields of services listed in section 199A(d)(1) and (2) and §1.199A-5 beyond those provided in §1.448-1T(e)(4).

One commenter suggested that in order to provide certainty and further economic growth, the final regulations should include a franchising example to clarify that a franchisor will not be considered to be an SSTB based solely on the selling of a franchise in a listed field of service. The Treasury Department and the IRS adopt this comment and have included a franchising example in the final regulations.

Finally, the final regulations add two rules of general application. First, the final regulations specify that the rules for determining whether a business is an SSTB within the meaning of section 199A(d)(2) apply solely for purposes of section 199A and therefore, may not be taken into account for purposes of applying any other provision of law, except to the extent that another provision expressly refers to section 199A(d). Second, the final regulations include a hedging rule that is applicable to any trade or business conducted by an individual or an RPE. The hedging rule provides that income, deduction, gain, or loss from a hedging transaction entered into in the normal course of a trade or business is included as income, deduction, gain, or loss from that trade or business. A hedging transaction for these purposes is defined in §1.1221-2(b) and the timing rules of §1.446-4 are also applicable.

The remainder of this part VI.A. responds to those comments advocating that a specific category of trade or business should be excluded from one of the listed fields in section 199(d)(2) or from the SSTB provisions entirely.

## 2. Health

Multiple commenters submitted comments requesting additional guidance on the meaning of performance of services in the field of health. Several commenters recommended that the definition of the performance of services in the field of health should differentiate between institutional health care providers (such as skilled nursing homes), which bill on a fee-for-service or per diem-basis, versus health care providers who provide and bill for professional services (such as a physician's practice). Another commenter suggested a distinction between these types of providers based on whether the trade or business had made the capital investment necessary to function as a

custodial institution. One commenter recommended the definition be restricted to health care providers who derive a majority of their revenue from billing patients and third party payers for professional services, thereby excluding health care providers who derive a majority of their revenue from billing for institutional services (skilled nursing facilities, hospitals, ambulatory surgery centers, home health care agencies, outpatient radiology centers, and hospice agencies).

Commenters noted the many services that skilled nursing facilities and assisted living facilities provide are unrelated to health care, including housing, meals, laundry facilities, security, and socialization activities. In some cases, skilled nursing and similar facilities may make available independent contractors who provide services related to health care available to patients, without the facility receiving any payment or revenue with respect to such services. Another commenter suggested that skilled nursing facilities, assisted living, and similar facilities should be excluded from the definition of services in the field of health unless 95 percent or more of the time spent by employees of the facility are directly related to providing medical care.

The Treasury Department and the IRS agree that skilled nursing, assisted living, and similar facilities provide multi-faceted services to their residents. Whether such a facility and its owners are in the trade or business of performing services in the field of health requires a facts and circumstances inquiry that is beyond the scope of these final regulations. The final regulations provide an additional example of one such facility offering services that the Treasury Department and the IRS do not believe rises to the level of the performance of services in the field of health.

Several commenters asked for clarification regarding when two separate activities would generally be viewed separately, particularly in the context of health care facilities such as emergency centers, urgent care centers, and surgical centers that provide improved real estate and equipment but do not directly provide treatment or diagnostic care to service recipients. One commenter noted that there is precedent under section 469 for distinguishing between the provision of direct treatment and diagnostic care versus the business of providing services or facilities ancillary to direct care, even if the physicians own an interest in the entity owning the facilities. The commenter suggested that the final regulations provide examples or other clarification regarding when these and similar facilities will be treated as performing services in the field of health, particularly if one of the owners of a facility also performs medical services in the facility. The final regulations provide an additional example of an outpatient surgical center demonstrating a fact pattern that the Treasury Department and the IRS do not believe is a trade or business providing services in the field of health.

Several commenters requested clarification regarding whether a retail pharmacy selling pharmaceuticals or medical devices is engaged in a health service trade or business. One commenter suggested that final regulations include an example of when a pharmacist would be considered in the health profession. The commenter agreed that a pharmacist working as an independent contractor at various pharmacies, a pharmacist providing inoculations directly to the patient, and a consulting pharmacist working as an independent contractor would all be examples of a pharmacist engaged in an SSTB. Another commenter stated that the inclusion of pharmacists in the

definition might be overbroad, suggesting that a pharmacist who was also a pharmacy owner generating revenue from selling pharmaceuticals or medical devices would not be engaged in an SSTB while a pharmacist operating as a consultant and paid as an independent contractor would be engaged in an SSTB. A third commenter suggested that a pharmacist working as an independent contractor for several pharmacies would not be performing services in the field of health unless the pharmacist provides medical services, such as inoculations, directly to a patient.

The Treasury Department and the IRS agree that the sale of pharmaceuticals and medical devices by a retail pharmacy is not by itself a trade or business performing services in the field of health. As the commenters note, however, some services provided by a retail pharmacy through a pharmacist are the performance of services in the field of health. The final regulations provide an additional example of a pharmacist performing services in the field of health.

Another commenter argued that gene therapy and similar injectable products such as stem cell therapy and RNA-based therapies manufactured or produced from the patient's body itself should be treated in the same manner as pharmaceuticals. The commenter argued that their manufacture and production should not be treated as an SSTB, regardless of whether they take place in a hospital or in a separate production facility. The Treasury Department and the IRS decline to adopt this recommendation as this is a question of facts and circumstances.

Another commenter argued that veterinary medicine should not be considered an SSTB. The commenter stated that delivery of veterinary care is different than delivery of human health care because veterinary patients are property and the nature of the

animal may dictate the level of veterinary care provided by the owner. Most veterinary practices have other streams of income such as retail, laboratory and diagnostic services, boarding and grooming services, and pharmacies, and the commenter expressed concern that it would be difficult for veterinarians to segregate those other streams of income. The commenter noted that animal boarding and grooming would ordinarily generate income eligible for the deduction and that should not change when services are provided by a veterinarian. The commenter also stated that Federal health legislation does not apply to veterinarians unless the legislation specifically refers to veterinarians, veterinary medicine, or animal health. Finally, the commenter noted that §1.448-1(T)(e)(4)(ii) does not reference veterinarians, suggesting that this is an indication that Congress did not intend for veterinary medicine to be treated as a business in the field of health.

Issued nearly three decades ago, Rev. Rul. 91-30, 1991-1 C.B. 61, described a corporation in which employees spend all of their time in the performance of veterinary services, including diagnostic and recuperative services as well as activities, such as the boarding and grooming of animals, that are incident to the performance of these services. The ruling also describes the definition of the performance of services in the field of health contained in §1.448-1T(e)(4)(ii) and holds that a corporation whose employees perform veterinary services is a qualified personal service corporation within the meaning of sections 448(d)(2) and 11(b)(2) and a personal service corporation within the meaning of section 441(i). Accordingly, the Treasury Department and the IRS believe that it is appropriate to continue the long-standing treatment of veterinary

services as the performance of services in the field of health for purposes of section 199A and these final regulations.

Another commenter noted that there is a dividing line between physical therapists and other health-related occupations. For example, reimbursement rates from third-party payers are higher for doctors, nurses, and dentists. The commenter also noted that Congress initially attempted to exclude physical therapists from participating in Medicare and Medicaid incentive programs and health service student loan forgiveness programs. The Treasury Department and the IRS decline to adopt this comment as multiple health services are reimbursed differently, but are still within the field of health.

One commenter suggested that services are not performed in the field of health unless services are performed directly to a patient. As an example, the commenter argued that a physician who reads x-rays for another physician but does not work directly with the patient would not be performing a service in the field of health. Another commenter stated that defining services in the field of health by proximity to patients could lead to arbitrary results, pointing out that a radiologist who acts as an expert consultant to a physician engages in the same exercise of medical skills and judgment as a physician who sees patients. The commenter suggested that technicians who operate medical equipment or test samples, but are not required to exercise medical judgment should not be considered as performing services in the field of health. The Treasury Department and the IRS agree with the second commenter that proximity to patients is not a necessary component of providing services in the field of health. Accordingly, the final regulations remove the requirement that medical services be provided directly to the patient. The final regulations do not adopt the suggestion that

technicians who operate medical equipment or test samples are not considered to be performing services in the field of health as this is a question of fact. However, the final regulations do include an additional example related to laboratory services.

### 3. Accounting

One commenter suggested that real estate settlement agents should be excluded from the definition of those who perform services in the field of accounting. The commenter recommended that final regulations define the performance of services in the field of accounting as the performance of core accounting services such as bookkeeping (including data entry), write-up work, review services, and attest functions, as well as tax preparation and similar functions. As an alternative, the commenter recommends that settlement agents be added as not constituting the practice of accounting. A second commenter stated that the definition of accounting should be narrowed to the ordinary meaning of accounting. This comment noted that the field of accounting should include bookkeeping and financial statement preparation, but not tax return advice and preparation. A third commenter noted that the proposed regulations treat bookkeeping services, which do not require professional training or license, as an accounting service. The commenter argued that if the intent of section 199A is to create parity between C corporations and passthrough entities, the regulations should narrowly define SSTBs, as was done for reputation and skill, and not expand the definitions beyond what was expressly contemplated by Congress.

The Treasury Department and the IRS decline to adopt these comments. As noted in the preamble to the proposed regulations, the provision of services in the field of accounting is not limited to services requiring state licensure. It is based on a

common understanding of accounting, which includes tax return and bookkeeping services. Whether a real estate settlement agent is engaged in the performance of services in the field of accounting depends on the facts and circumstances including the specific services offered and performed by the trade or business.

#### 4. Actuarial Science

The proposed regulations provide that the performance of services in the field of actuarial science means the provision of services by individuals such as actuaries and similar professionals performing services in their capacity as such. One commenter stated that the definition creates uncertainty for businesses that employ actuaries but do not separately bill for the services (such as insurance businesses). The commenter recommended providing a rule similar to the rule for consulting services related to the manufacture and sale of goods for actuarial science. The Treasury Department and the IRS decline to adopt this comment as section 199A looks to the trade or business of performing services rather than the performance of services themselves. As stated in the preamble to the proposed regulations, the field of actuarial science does not include the provision of services by analysts, economists, mathematicians, and statisticians not engaged in analyzing or assessing the financial cost of risk or uncertainty of events. The mere employment of an actuary does not itself cause a trade or business to be treated as performing services in the field of actuarial science. Whether a trade or business is providing actuarial services is a question of fact and circumstance.

#### 5. Performing Arts

Multiple commenters stated that the definition of performance of services in the field of performing arts should be limited to the definition in §1.448-1T(e)(4)(iii). One

commenter argued that the position in the proposed regulations that includes individuals who participate in the creation of the performing arts is not supported by the legislative history, namely the Statement of Managers that references the section 448 regulations. As described in part VII.A.1. of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS decline to limit the definition of the performance of services in the field of performing arts to the definition in §1.448-1T(e)(4)(iii). Another commenter suggested that writers should fall outside the definition of the performance of services in the field of performing arts because writing does not require a skill unique to the creation of performing arts. Further, writers create a wide variety of works not intended to be performed before an audience. The Treasury Department and the IRS also decline to adopt this comment. To the extent that a writer is paid for written material, such as a song or screenplay, that is integral to the creation of the performing arts, the writer is performing services in the field of performing arts.

#### 6. Consulting

One commenter suggested that proposed §1.199A-5(b)(3), Example 3, should be modified to clarify that C, a taxpayer in the business of providing services that assist unrelated entities in making their personnel structures more efficient, does not provide any temporary workers, and C's compensation and fees are not affected by whether C's clients use temporary workers. The commenter argued that such a change would prevent the example from being interpreted as treating any recommendation for a business to use temporary workers as consulting services. The commenter also suggested that the final regulations include an additional example similar to Example 7 of §1.448-1T(e)(4)(iv)(B) related to staffing firms. The commenter recommended that

the example provide that a business that assists other businesses in meeting their personnel needs by referring job applicants to them does not engage in the performance of services in the field of consulting when the compensation for the business referring job applicants is based on whether the applicants accept employment positions with the businesses searching for employees. The final regulations adopt these suggestions.

Another commenter suggested that final regulations clarify whether services provided by engineers and architects could be considered to be an SSTB if their services meet the definition of consulting services. The Treasury Department and the IRS adopt this comment. Section 1.199A-5(b)(2)(vii) of the final regulations provides that services within the fields of architecture and engineering are not treated as consulting services for purposes of section 199A.

One commenter suggested that the definition of consulting should be narrowed to stand-alone advice and counsel with no link to production, manufacturing, sales, or licensing of products. The Treasury Department and the IRS decline to adopt this suggestion as it would be difficult to administer and subject to manipulation. Another commenter suggested that the phrase “provision of professional advice and counsel to clients to assist the client in achieving goals and solving problems” is overly broad as it could apply to almost any service-based business that assists clients in achieving goals and solving problems. The commenter stated that applying the ancillary rule would be difficult where a taxpayer is required to separately bill for embedded consulting services under state or local sales tax laws. The commenter suggested that the consulting field should be limited to taxpayers that fall under a consulting-related business activity code

under the North American Industry Classification Systems (NAICS). The Treasury Department and the IRS agree with the commenter that many service-based businesses could be construed as providing professional advice and counsel to clients to assist the client in achieving goals and solving problems; however, the Treasury Department and the IRS decline to adopt the recommendation to limit the consulting field based on NAICS codes. Section 1.199A-5(b)(2)(vii) excludes the performance of services other than providing advice and counsel from the field of consulting. At issue is whether advice and counsel is provided in the context of the provision of goods or services (that are not otherwise SSTBs). This is a question of facts and circumstances. Consulting services that are separately billed are generally not considered to be provided in the context of the provisions of goods or services.

## 7. Athletics

A few commenters suggested that the definition of a trade or business involving the performance of services in the field of athletics should not include the trade or business of owning a professional sports team. One commenter stated that the definition should be limited to entities that are either owned or controlled by, or whose primary beneficiaries are, professional athletes or that involve the performance of services by those athletes; in other words, the definition should apply solely to athletes' personal services companies.

Another commenter recommended that §1.199A-5(b)(3) Example 2 be revised to reflect that neither sports clubs nor club owners perform services described in section 1202(e)(3)(A). The commenter stated that a professional sports club and its owners do not perform services in the field of athletics. Instead, a sports club sells tickets,

licenses, sponsorships, and other intellectual property, creates digital content, engages in community activities, manages a stadium, and produces an entertainment product. The commenter argued that Congress intended through the SSTB rules to prevent W-2 wage income from being converted to QBI and that only the trade or business of an athlete involves W-2 wage income from athletic performance. The commenter continued, stating that professional sports clubs are not described in section 1202(e)(3)(A) or provided in section 448(d)(2)(A).

The Treasury Department and the IRS decline to adopt this comment. As described in part VII.A.1. of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS do not believe that definitional guidance should be limited to that provided in §1.448-1T(e)(4)(i) (by analogy to performing arts for athletics). While sports club and team owners are not performing athletic services directly, that is not a requirement of section 199A, which looks to whether there is income attributable to a trade or business involving the performance of services in a specified activity, not who performed the services. A professional sports club may operate more than one trade or business. For example, a team may operate its concession services as a separate trade or business. The Treasury Department and the IRS agree that such concession services generally would not be a trade or business of performing services in the field of athletics. Nonetheless, a professional sports club's operation of an athletic team is a trade or business of performing services in the field of athletics. Income from that trade or business, including income from ticket sales and broadcast rights, is income from a trade or business of performing services in the field of athletics. The performance of services in the field of athletics does not include the

provision of services by persons who broadcast or otherwise disseminate video or audio of athletic events to the public.

## 8. Financial Services

Several commenters suggested that final regulations clarify that financing, including taking deposits, making loans, and entering into financing contracts, is not a financial service. One commenter requested an explicit rule clarifying that non-bank mortgage bankers are not SSTBs and that customary activities of mortgage bankers including mortgage loan origination, sales of mortgage loans, mortgage loan servicing, and sale of mortgage servicing rights are not financial services. The preamble to the proposed regulations provides that the provision of financial services does not include taking deposits or making loans. The final regulations clarify that the provision of financial services does not include taking deposits or making loans.

One commenter stated that the determination that banking is not a financial service appears to be wrong and inconsistent with statutory construction since any common definition of financial services includes banking services. As stated in the preamble to the proposed regulations, banking is listed in section 1202(e)(3)(B) but not section 1202(e)(3)(A). As a matter of statutory construction, the Treasury Department and the IRS believe that banking must therefore be excluded from the definition of financial services for purposes of section 199A. Another commenter suggested that insurance should be categorically excluded from the meaning of financial services because insurance is described in section 1202(e)(3)(B). The Treasury Department and the IRS agree that by operation of section 1202(e)(3)(B), insurance cannot be considered a financial service for purposes of section 199A. The commenter also

suggested that a rule similar to the ancillary services rule for consulting should be extended to cover financial services. Another commenter argued that insurance agents and others who provide investment advice are not in the field of financial services, unless the agent receives a fee for the advice, rather than a commission on the sale. The Treasury Department and the IRS decline to categorically exclude services provided by insurance agents from the definition of financial services as financial services such as managing wealth, advising clients with respect to finances, and the provision of advisory and other similar services that can be provided by insurance agents. However, the Treasury Department and the IRS note that the provision of these services to the extent that they are ancillary to the commission-based sale of an insurance policy will generally not be considered the provision of financial services for purposes of section 199A.

#### 9. Brokerage Services

One commenter stated that the ordinary definition of a broker is any person who buys and sells goods or services for others, including agents, and argued that nothing in the statute limits this to stock brokers. The commenter said that the definition in the proposed regulations artificially narrows the standard to appease special interests without any justification. The definition provided for in the proposed regulations applies more broadly than stock brokers and includes all services in which a person arranges transactions between a buyer and a seller with respect to securities (as defined in section 475(c)(2)) for a commission or fee. While the term “broker” is sometimes used in a broad sense to include anyone who facilitates the purchase and sale of goods for a fee or commission, the term “brokerage services” is most commonly associated with

services, such as those provided by brokerage firms, involving the facilitation of purchases and sales of stock and other securities.

Another commenter suggested that final regulations clarify that life insurance products are not securities for purposes of section 199A or that life insurance brokers engaged in their capacity as such are not brokers in securities for purposes of section 199A. Other commenters requested the final regulations clarify that the business of financing or making loans, including the services provided by mortgage banking companies, does not fall within the definition of brokerage services. The Treasury Department and the IRS address this comment in the final regulations by explicitly stating that although the performance of services in the field of financial services does not include taking deposits or making loans, it does include arranging lending transactions between a lender and borrower. The final regulations define securities by reference to section 475(c)(2).

#### 10. Investing and Investment Management

One commenter recommended that the performance of services that consist of investing and investment management be limited to investment management and investment advisory businesses whose income is principally attributable to the performance of personal services involving the provision of investment advice or the regular and contemporaneous management of investors' assets by individual employees or owners of the business. The commenter recommended that the definition exclude large, diversified asset managers that invest significant capital in and derive significant income from the research, development, and sale of investment products. The commenter suggested that rather than making business-by-business

determinations, the final regulations should look to rules such as the regulations under now repealed section 1348, which did not treat income from a business in which capital is a material income producing factor as earned income. As an alternative, the commenter suggested that the final regulations could provide a safe harbor for firms that research, develop, and sell investment products, including changes to the de minimis and incidental rules necessary to effectuate the safe harbor. An example of such a rule could be similar to the rule provided for ancillary consulting services.

The Treasury Department and the IRS decline to adopt this comment as the regulations under now repealed section 1348 looked to earned income including fees received by taxpayers engaged in a professional occupation. Section 199A is focused on a trade or business, not a profession of an individual. Accordingly, the determination of whether a trade or business in an SSTB must be made on a business-by-business basis.

Another commenter suggested that final regulations clarify that investing and investment management does not include the sale of life insurance products and that life insurance products are not investments for purposes of section 199A. The Treasury Department and the IRS decline to define investment for purposes of section 199A but note that commission-based sales of insurance policies generally will not be considered the performance of services in the field of investing and investment management for purposes of section 199A.

Another commenter recommended that final regulations clarify that directly managing real property includes management through agents and affiliates acting as agents for the property manager. The SSTB limitations apply to direct and indirect

owners of a trade or business that is an SSTB, regardless of whether the owner is passive or participated in any specified service activity. Accordingly, direct and indirect management of real property includes management through agents, employees, and independent contractors.

## 11. Dealing

### a. Mortgage Banking, Credit Sales, and Non-Bank Lending

Several commenters suggested that the provisions regarding dealing in securities should exclude mortgage banking and other lending activities in which lending is the primary business focus. Several of these commenters noted that the plain language meaning of “purchasing securities” does not include making loans. One commenter suggested that the reference to the definition of negligible sales should be clarified to explain that negligible sales as defined in §1.475(c)-1(c)(2) and (4) does not apply if the loan is in connection with mortgage servicing contracts as excluded in section 451(b)(1)(B). Another commenter suggested that portfolio lenders should also be able to use the negligible sales exemption and all sales of loans outside the ordinary course of business should be excluded from consideration in applying the negligible sales test. A third commenter suggested that the regulation clarify that the negligible sales exception is simply an exception to the general definition of dealing in securities. Another commenter suggested that application of dealing in securities should be limited to taxpayers engaged in broker-dealer activities for which registration under Federal law would be required. Another commenter suggested that the creation of a loan should not be construed as a purchase and a taxpayer should be considered a dealer in securities only if they both purchase and sell securities. As an alternative, this commenter

suggested that negligible sales could be defined in terms of the number of customers that the lender sells loans to each year. For this purpose, the Government National Mortgage Association (GNMA) would be considered to be the customer for purpose of sales of GNMA mortgage pools through the issuance of mortgage backed securities. Another commenter suggested that sales of retail installment contracts or loans for purposes of liquidity, portfolio diversification, and similar purposes should be considered to be outside of recurring business activity and thus not dealing in securities. In response to these comments, the final regulations provide that for purposes of section 199A and the definition of performing services that consist of dealing in securities, the performance of services to originate a loan is not treated as the purchase of a security from the borrower. Additionally, the final regulations remove the reference to the negligible sales exception under §1.475(c)-1(c)(2) and (4) from the definition of dealing in securities.

Another commenter suggested that under section 199A, the term “securities” should be defined by reference to section 475 but not the terms “dealer” or “dealer in securities.” The commenter suggested that a lender should be considered to be a dealer in securities for purposes of section 199A only to the extent that loans, including retail sales contracts, acquired by the lender are held in inventory or held for sale to customers in the ordinary course of a trade or business within the meaning of section 1221. The commenter also suggested that when a loan is acquired with a view towards holding the loan to maturity in the lender’s portfolio and the loan is later sold outside the normal course of business; such a sale should not result in the lender being viewed as a dealer in securities. Another commenter suggested that the meaning of sales to

customers should be clarified in the context of a mortgage finance business. This commenter requested that the regulations clarify that a mortgage loan originator which transfers mortgages to an agency or broker/dealer for cash or mortgage-backed securities does not engage in a sale by the originator to a customer for purposes of section 199A.

In response to these comments, the final regulations provide that the performance of services to originate a loan is not treated as the purchase of a security from the borrower in determining whether the lender is performing services consisting of dealing in securities. The comment regarding the definition of a dealer in securities, however, is not accepted, as the definition of a securities dealer has never depended on whether securities were held in inventory. The final regulations also do not address loans that are sold outside the normal course of business, which is an inherently factual question. Similarly, the Treasury Department and the IRS decline to address the question of whether a person is a customer as this is a subject which is beyond the scope of these regulations.

b. Banking

Many commenters recommended that traditional banking activities be excluded entirely from the definition of an SSTB, including the performance of services that consist of dealing in securities. The commenters argued that Congress intended banks that elect under section 1362(a) to be S corporations (subchapter S banks) to have the same relative reduction in taxes as C corporation banks after enactment of the TCJA. Many commenters noted that subchapter S bank activities are already strictly limited by the Bank Holding Company Act and this effectively serves as a guardrail against abuse

of the section 199A deduction. As an alternative, commenters suggested that the definition of SSTB should be more narrowly drawn to exclude bank services such as trust or fiduciary services, securities brokerage, and the origination and sale of mortgages and loans. Commenters also expressed concern that the de minimis rule is insufficient to protect banks. These commenters suggested revisions including raising the de minimis threshold to 25 percent regardless of the amount of gross receipts and using net income rather than gross receipts for the measure.

The Treasury Department and the IRS decline to accept these comments. Although the final regulations continue to exclude taking deposits or making loans from the definition of an SSTB involving the performance of financial services, and exclude the origination of loans from the definition of dealing in securities for purposes of section 199A, the Treasury Department and the IRS do not believe that there is a broad exemption from the listed SSTBs with respect to all services that may be legally permitted to be performed by banks. Therefore, to the extent a bank operates a single trade or business that involves the performance of services listed as SSTBs outside of the de minimis exception, such as investing and investment management, the bank's single trade or business will be treated as an SSTB. However, as noted previously, an RPE, including a subchapter S bank, may operate more than one trade or business. Thus, a subchapter S bank could segregate specified service activities from an existing trade or business and operate such specified service activities as an SSTB separate from its remaining trade or business, either within the same legal entity or in a separate entity.

c. Commodities

Several commenters suggested that the final regulations provide that a trade or business is not engaged in the performance of services of investing, trading, or dealing in commodities if it regularly takes physical possession of the underlying commodity in the ordinary course of its trade or business. These commenters also argued that a business that takes physical possession of the commodity should not be treated as an SSTB if it hedges its risk with respect to the commodity as part of the ordinary course of its trade or business. The commenters state that dealing in commodities for purposes of section 199A should be understood to mean an activity similar to dealing in securities and should be limited to the dealing in financial instruments referenced to commodities, such as commodities futures or options that are traded on regulated exchanges. One commenter argued that if the regulations were to apply to physical commodities it would result in different tax treatment depending on whether the commodity is actively traded and that Congress intended the definition of commodities to apply only to commodities derivatives. Another commenter suggested that manufacturing activities as defined under the now repealed section 199 should be expressly excluded from the definition of both trading in commodities and dealing in commodities.

The Treasury Department and the IRS agree with commenters that the definition of dealing in commodities for purposes of section 199A should be limited to a trade or business that is dealing in financial instruments or otherwise does not engage in substantial activities with respect to physical commodities. To distinguish a trade or business that performs substantial activities with physical commodities from a trade or business that engages in a commodities trade or business by dealing or trading in financial instruments that are commodities (within the meaning of section 475(e)(2)), or

a trade or business that otherwise does not perform substantial activities with commodities, the final regulations adopt rules similar to the rules that apply to qualified active sales of commodities in §1.954-2(f)(2)(iii). Those rules generally require a person to be engaged in the active conduct of a commodities business as a producer, processor, merchant, or handler of commodities and to perform certain activities with respect to those commodities.

Accordingly, for purposes of section 199A, gains and losses from the sale of commodities in the active conduct of a commodities business as a producer, processor, merchant, or handler of commodities will be qualified active sales and gains and losses from qualified active sales are not taken into account in determining whether a person is engaged in the trade or business of dealing in commodities. Similarly, income, deduction, gain, or loss from a hedging transaction (as defined in §1.1221-2(b)) entered into in the normal course of a commodities business conducted by a producer, processor, merchant, or handler of commodities will be treated as gains and losses from qualified active sales that are part of that trade or business. Qualified active sales generally require a taxpayer to hold commodities as inventory or similar property and to satisfy specified conditions regarding substantial and significant activities described in the final regulations. A sale by a trade or business of commodities held for investment or speculation is not a qualified active sale.

### 13. Reputation/Skill

Many commenters expressed support for the position in the proposed regulations that reputation or skill was intended to describe a narrow set of trades or businesses not otherwise covered by the other listed SSTBs, often writing that a more broad

interpretation would be inherently complex and unworkable. Other commenters disagreed with the definition in the proposed regulations, expressing concern that the narrowness of the definition is contrary to the language of the statute and Congressional intent.

The Treasury Department and the IRS remain concerned that a broad interpretation of the reputation and skill clause would result in substantial uncertainty for both taxpayers and the IRS. As stated in the preamble to the proposed regulations, it would be inconsistent with the text, structure, and purpose of section 199A to potentially exclude income from all service businesses from qualifying for the section 199A deduction for taxpayers with taxable income above the threshold amount. If Congressional intent was to exclude all service businesses, Congress clearly could have drafted such a rule. Accordingly, the final regulations retain the proposed rule limiting the meaning of the reputation or skill clause to fact patterns in which an individual or RPE is engaged in the trade or business of receiving income from endorsements, the licensing of an individual's likeness or features, and appearance fees.

One commenter requested additional clarification regarding whether advertising income received for on air advertising spots in which a program host reads a script describing the positive qualities of a product or service, and may also choose to describe his or her own positive experiences with the product, is endorsement income as described in §1.199A-5(b)(2)(xiv)(A). The commenter argued that such income should not be considered endorsement income because it is not received in connection with a separate trade or business of making endorsements. The Treasury Department

and the IRS decline to adopt this suggestion as §1.199A-5(b)(2)(xiv)(A) looks to whether the individual or RPE is receiving income from the endorsement of products or services, not whether the income is received in connection with a separate trade or business of making endorsements. Whether a taxpayer endorses a product or services is dependent on the facts and circumstances.

#### B. De Minimis Rule

The proposed regulations provide that for a trade or business with gross receipts of \$25 million or less for the taxable year, a trade or business is not an SSTB if less than 10 percent of the gross receipts of the trade or business are attributable to a specified service field. The percentage is reduced to 5 percent in the case of trades or businesses with gross receipts in excess of \$25 million. Several commenters requested clarification regarding whether the entire trade or business is designated an SSTB if the threshold is exceeded. Some of these commenters suggested that the rule be modified so that the deduction could be claimed on the portion of the trade or business activity that was not an SSTB. A few suggested that an allocation similar to that in now repealed section 199 could be used. One commenter suggested using the cost accounting principles of section 861 with a safe harbor allowing a simplified method for entities with average annual gross receipts less than \$25 million. Another commenter stated that treating the entire trade or business as an SSTB is a trap for the unwary because well-advised taxpayers could avoid application of the rule by rearranging their activities into separate entities. One commenter suggested that the de minimis rule allow for minor year-to-year changes in gross receipts for businesses that are close to the de minimis thresholds. The commenter also suggested that the thresholds be

## **Services or Property Provided to an SSTB Summary**

service activity in excess of the de minimis threshold are considered to be SSTBs. The final regulations retain the proposed rule but add an additional example demonstrating the result in which a trade or business has income from a specified service activity in excess of the de minimis threshold.

As discussed in part II of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS acknowledge that an RPE can have more than one trade or business for purposes of section 162 and thus for section 199A. However, each trade or business is required under section 199A to be separately tested to determine whether that trade or business is an SSTB. Similarly, the de minimis threshold is applied to each trade or business of an RPE separately, not in the aggregate to all the trades or businesses of the RPE. Thus, to the extent that an individual or RPE has more than one trade or business, the presence of specified service activity in one of those trades or business will not cause the individual's or RPE's other trades or businesses to be considered SSTBs except to the extent that the rules in §1.199A-5(c)(2) (services or property provided to an SSTB) apply.

C. Services or Property Provided to an SSTB.

The proposed regulations provide special rules for service or property provided to an SSTB by a trade or business with common ownership. A trade or business that provides more than 80 percent of its property or services to an SSTB is treated as an SSTB if there is 50 percent or more common ownership of the trades or businesses. In cases in which a trade or business provides less than 80 percent of its property or services to a commonly owned SSTB, the portion of the trade or business providing

property to the commonly owned SSTB is treated as part of the SSTB with respect to the related parties.

One commenter suggested that the provision is warranted because of abuse potential but is overbroad and prevents legitimate transactions. The commenter recommended that the rule be modified into a presumption that a taxpayer could rebut with evidence demonstrating that the property or services provided to the SSTB by the related RPE are (1) comparable to those available from competing organizations and (2) that prices charged by the RPE and paid by the SSTB are comparable to those charged in the market. The commenter also suggested that the IRS could examine the totality of facts and circumstances, including historic conduct between the SSTB and RPE. Another commenter suggested that the final rule add an exception to the rule for taxpayers that can demonstrate they have a substantial purpose (apart from Federal income tax effects) for structuring their trade or business in a particular manner. For example, title to a skilled nursing facility could be held by one passthrough entity that is operated by a related passthrough entity in order to satisfy Department of Housing and Urban Development lending requirements. The Treasury Department and the IRS decline to adopt these recommendations. Creating a presumption or substantial purpose test would lead to greater complexity and administrative burden for both taxpayers and the IRS.

A few commenters requested clarification regarding whether the rule applies when the property or services are provided to a commonly-owned C corporation. One commenter also asked for clarification on the meaning of 50 percent or more common ownership, examples of how ownership is determined, and whether the definition is

different than the 50 percent or more common ownership test used in the aggregation rules. One commenter suggested that the rule should apply only to those owners who make up the 50 percent ownership test. Another commenter suggested that the rule should not apply to real estate rentals to a commonly owned SSTB. Another commenter suggested that structures that existed before December 22, 2017, be grandfathered so that the rule would not apply. In response to comments, the final regulations clarify that the rule applies only to those who make up the 50 percent test. As discussed in section V.B. of this Summary of Comments and Explanation of Revisions, the final regulations provide that sections 267(b) and 707(b) apply in determining common ownership for purposes of the aggregation rules. The Treasury Department and the IRS decline to exempt real estate rentals or to structures that existed before December 22, 2017, as the rule is intended to address goods and services that are provided to an SSTB regardless of the type of good or service provided or the date on which the structure was put into place.

One commenter stated that the rule is overbroad and not based on statutory authority and unfairly punishes related party transactions. Other commenters suggested that the rule automatically treating a trade or business that provides more than 80 percent of its goods or services to a commonly owned SSTB as an SSTB is unnecessary, as there are no abuse concerns regarding the portions of goods or services provided to a third party. The Treasury Department and the IRS agree with this comment and have removed the 80 percent rule in the final regulations. Accordingly, the final regulations provide that if a trade or business provides property or services to an SSTB and there is 50 percent or more common ownership of the trade or

business, the portion of the trade or business providing property or services to the 50 percent or more commonly-owned SSTB will be treated as a separate SSTB with respect to related parties.

D. Incidental to a Specified Service Trade or Business

The proposed regulations provide that if a trade or business (that would not otherwise be treated as an SSTB) has both 50 percent or more common ownership with an SSTB and shared expenses with an SSTB, then the trade or business is treated as incidental to and, therefore, part of the SSTB, if the gross receipts of the trade or business represent no more than five percent of the total combined gross receipts of the trade or business and the SSTB in a taxable year. One commenter recommended that this rule be removed because it is unnecessary and causes administrative difficulties for taxpayers who must determine whether a trade or business is incidental in order to apply the rule. If the rule is retained, the commenter recommended that final regulations define gross receipts and shared expenses, make adjustments to avoid double counting the same gross receipts, clarify what businesses are taken into account for purposes of the rule, and treat a trade or business to which the anti-abuse rule applies as a separate SSTB rather than as part of the SSTB. Another commenter suggested that the final regulations add an exception for start-ups such as a three to five year grace period and also clarify the ownership standard, how the rule would apply if the trades or business have different tax years, and how shared expenses would be determined. In accordance with the comments, the rule is removed from the final regulations.

E. Trade or Business of Performing Services as an Employee

Multiple commenters expressed support for the rule in the proposed regulations that provides that an individual who was previously treated as an employee and is subsequently treated as other than an employee while performing substantially the same services to the same person, or a related person, will be presumed to be in the trade or business of performing services as an employee for purposes of section 199A. The commenters noted that the presumption furthers the public policy goal of preventing worker misclassification, preserves agency resources, and prevents a decline in Federal and state tax revenues. The commenters also state that regulations should not incentivize workers to accept misclassification by their employer in order to obtain a tax benefit.

Other commenters recommended that the presumption be removed arguing that the common law test under current law is sufficient for determining whether a former employee is properly classified as an employee and that the presumption would impede the objective of ensuring similar treatment of similarly situated taxpayers because two similarly situated taxpayers who provide services to the same company would be treated differently if one was a former employee of the company and the other was not. The commenter also notes that the presumption would create uncertainty for taxpayers and would cause former employees to not claim the deduction in order to avoid a dispute with the IRS.

Another commenter expressed concern that the presumption as written in the proposed regulations could create a dual standard for worker classification under the Code, in which a worker could be classified as an independent contractor for employment tax purposes, and an employee for purposes of claiming section 199A

deduction. This could result in an independent contractor being held liable for self-employment taxes and unable to claim the section 199A deduction on income that would otherwise qualify as QBI. The commenter suggested that if the presumption is retained, it should include an exemption for certain independent contractors based on factors including income, source of income, industry practice, and timeframe.

A different commenter suggested that the presumption should provide that an independent contractor is operating as such and that it is up to the relevant Federal agencies to determine whether the business misclassified the individual. The commenter also noted that the IRS is barred from issuing regulations with respect to the employment status of any individual for employment tax purposes under Section 530(b) of the Revenue Act of 1978 (P.L. 95-600), as amended by section 9(d)(2) of P.L. 96-167, section 1(a) of P.L. 96-541, and section 269(c) of P.L. 97-248, and that the presumption could result in an individual otherwise subject to self-employment tax to not get the benefit of the section 199A deduction. Another commenter argued that an employee who changes his status from employee to independent contractor so he may deduct business expenses on Schedule C and claim a section 199A deduction is exercising his right to structure his business transactions to minimize his tax liability.

Another commenter questioned how the rule would be applied, asking for clarification on whether the rule is intended to prohibit employers from firing employees and rehiring them as independent contractors; whether it applies to former employees regardless of current relationship; and how far the IRS would look back at prior employees. Another commenter suggested that a new example be added to the final regulations demonstrating that the presumption is inapplicable when the facts

demonstrate that a service recipient and a service provider have materially modified their relationship such that its proper classification is that of a service recipient and a partner.

The Treasury Department and the IRS believe that the presumption is necessary to prevent misclassifications but agree that some clarification of the presumption is necessary. In accordance with commenter's suggestions, the final regulations provide a three-year look back rule for purposes of the presumption. The final regulations provide that an individual may rebut the presumption by showing records, such as contracts or partnership agreements, that are sufficient to corroborate the individual's status as a non-employee for three years from the date a person ceases to treat the individual as an employee for Federal employment taxes. Finally, the final regulations contain an additional example demonstrating the application of the presumption for the situation in which an employee has materially modified his relationship with his employer such that the employee can successfully rebut the presumption.

## VII. Relevant Passthrough Entities, Publicly Traded Partnerships, Trusts, and Estates

### A. Reporting Rules

The proposed regulations provide that an RPE must determine and separately report QBI, W-2 wages, UBIA of qualified property, and whether the trade or business is an SSTB for each of the RPE's trades or businesses. To help simplify the administration and compliance burden, several commenters suggested that there be an option to compute, aggregate, and report activities at the RPE or entity level. As discussed in part V of this Summary of Comments and Explanation of Revisions, the final regulations allow an RPE to aggregate its trades or businesses provided the rules

## **Specified Service Trade or Business Examples**

(e) Effective/ applicability date--(1) General rule. Except as provided in paragraph (e)(2) of this section, the provisions of this section apply to taxable years ending after **[INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

(2) Exception for non-calendar year RPE. For purposes of determining QBI, W-2 wages, and UBIA of qualified property, and the aggregate amount of qualified REIT dividends and qualified PTP income, if an individual receives any of these items from an RPE with a taxable year that begins before January 1, 2018, and ends after December 31, 2017, such items are treated as having been incurred by the individual during the individual's taxable year in which or with which such RPE taxable year ends.

Par. 7. Section 1.199A-5 is added to read as follows:

§1.199A-5 Specified service trades or businesses and the trade or business of performing services as an employee.

(a) Scope and effect--(1) Scope. This section provides guidance on specified service trades or businesses (SSTBs) and the trade or business of performing services as an employee. This paragraph (a) describes the effect of a trade or business being an SSTB and the trade or business of performing services as an employee. Paragraph (b) of this section provides definitional guidance on SSTBs. Paragraph (c) of this section provides special rules related to SSTBs. Paragraph (d) of this section provides guidance on the trade or business of performing services as an employee. The provisions of this section apply solely for purposes of section 199A of the Internal Revenue Code (Code).

(2) Effect of being an SSTB. If a trade or business is an SSTB, no qualified business income (QBI), W-2 wages, or unadjusted basis immediately after acquisition

(UBIA) of qualified property from the SSTB may be taken into account by any individual whose taxable income exceeds the phase-in range as defined in §1.199A-1(b)(4), even if the item is derived from an activity that is not itself a specified service activity. The SSTB limitation also applies to income earned from a publicly traded partnership (PTP). If a trade or business conducted by a relevant passthrough entity (RPE) or PTP is an SSTB, this limitation applies to any direct or indirect individual owners of the business, regardless of whether the owner is passive or participated in any specified service activity. However, the SSTB limitation does not apply to individuals with taxable income below the threshold amount as defined in §1.199A-1(b)(12). A phase-in rule, provided in §1.199A-1(d)(2), applies to individuals with taxable income within the phase-in range, allowing them to take into account a certain “applicable percentage” of QBI, W-2 wages, and UBIA of qualified property from an SSTB. The phase-in rule also applies to income earned from a PTP. A direct or indirect owner of a trade or business engaged in the performance of a specified service is engaged in the performance of the specified service for purposes of section 199A and this section, regardless of whether the owner is passive or participated in the specified service activity.

(3) Trade or business of performing services as an employee. The trade or business of performing services as an employee is not a trade or business for purposes of section 199A and the regulations thereunder. Therefore, no items of income, gain, deduction, or loss from the trade or business of performing services as an employee constitute QBI within the meaning of section 199A and §1.199A-3. No taxpayer may claim a section 199A deduction for wage income, regardless of the amount of taxable income.

(b) Definition of specified service trade or business. Except as provided in paragraph (c)(1) of this section, the term specified service trade or business (SSTB) means any of the following:

(1) Listed SSTBs. Any trade or business involving the performance of services in one or more of the following fields:

(i) Health as described in paragraph (b)(2)(ii) of this section;

(ii) Law as described in paragraph (b)(2)(iii) of this section;

(iii) Accounting as described in paragraph (b)(2)(iv) of this section;

(iv) Actuarial science as described in paragraph (b)(2)(v) of this section;

(v) Performing arts as described in paragraph (b)(2)(vi) of this section;

(vi) Consulting as described in paragraph (b)(2)(vii) of this section;

(vii) Athletics as described in paragraph (b)(2)(viii) of this section;

(viii) Financial services as described in paragraph (b)(2)(ix) of this section;

(ix) Brokerage services as described in paragraph (b)(2)(x) of this section;

(x) Investing and investment management as described in paragraph (b)(2)(xi) of this section;

(xi) Trading as described in paragraph (b)(2)(xii) of this section;

(xii) Dealing in securities (as defined in section 475(c)(2)), partnership interests, or commodities (as defined in section 475(e)(2)) as described in paragraph (b)(2)(xiii) of this section; or

(xiii) Any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners as defined in paragraph (b)(2)(xiv) of this section.

(2) Additional rules for applying section 199A(d)(2) and paragraph (b) of this section--(i) In general--(A) No effect on other tax rules. This paragraph (b)(2) provides additional rules for determining whether a business is an SSTB within the meaning of section 199A(d)(2) and paragraph (b) of this section only. The rules of this paragraph (b)(2) apply solely for purposes of section 199A and therefore may not be taken into account for purposes of applying any provision of law or regulation other than section 199A and the regulations thereunder, except to the extent such provision expressly refers to section 199A(d) or this section.

(B) Hedging transactions. Income, deduction, gain or loss from a hedging transaction (as defined in §1.1221-2(b)) entered into by an individual or RPE in the normal course of the individual's or RPE's trade or business is treated as income, deduction, gain, or loss from that trade or business for purposes of this paragraph (b)(2). See also §1.446-4.

(ii) Meaning of services performed in the field of health. For purposes of section 199A(d)(2) and paragraph (b)(1)(i) of this section only, the performance of services in the field of health means the provision of medical services by individuals such as physicians, pharmacists, nurses, dentists, veterinarians, physical therapists, psychologists, and other similar healthcare professionals performing services in their capacity as such. The performance of services in the field of health does not include the provision of services not directly related to a medical services field, even though the services provided may purportedly relate to the health of the service recipient. For example, the performance of services in the field of health does not include the operation of health clubs or health spas that provide physical exercise or conditioning to

their customers, payment processing, or the research, testing, and manufacture and/or sales of pharmaceuticals or medical devices.

(iii) Meaning of services performed in the field of law. For purposes of section 199A(d)(2) and paragraph (b)(1)(ii) of this section only, the performance of services in the field of law means the performance of legal services by individuals such as lawyers, paralegals, legal arbitrators, mediators, and similar professionals performing services in their capacity as such. The performance of services in the field of law does not include the provision of services that do not require skills unique to the field of law; for example, the provision of services in the field of law does not include the provision of services by printers, delivery services, or stenography services.

(iv) Meaning of services performed in the field of accounting. For purposes of section 199A(d)(2) and paragraph (b)(1)(iii) of this section only, the performance of services in the field of accounting means the provision of services by individuals such as accountants, enrolled agents, return preparers, financial auditors, and similar professionals performing services in their capacity as such.

(v) Meaning of services performed in the field of actuarial science. For purposes of section 199A(d)(2) and paragraph (b)(1)(iv) of this section only, the performance of services in the field of actuarial science means the provision of services by individuals such as actuaries and similar professionals performing services in their capacity as such.

(vi) Meaning of services performed in the field of performing arts. For purposes of section 199A(d)(2) and paragraph (b)(1)(v) of this section only, the performance of services in the field of the performing arts means the performance of services by

individuals who participate in the creation of performing arts, such as actors, singers, musicians, entertainers, directors, and similar professionals performing services in their capacity as such. The performance of services in the field of performing arts does not include the provision of services that do not require skills unique to the creation of performing arts, such as the maintenance and operation of equipment or facilities for use in the performing arts. Similarly, the performance of services in the field of the performing arts does not include the provision of services by persons who broadcast or otherwise disseminate video or audio of performing arts to the public.

(vii) Meaning of services performed in the field of consulting. For purposes of section 199A(d)(2) and paragraph (b)(1)(vi) of this section only, the performance of services in the field of consulting means the provision of professional advice and counsel to clients to assist the client in achieving goals and solving problems. Consulting includes providing advice and counsel regarding advocacy with the intention of influencing decisions made by a government or governmental agency and all attempts to influence legislators and other government officials on behalf of a client by lobbyists and other similar professionals performing services in their capacity as such. The performance of services in the field of consulting does not include the performance of services other than advice and counsel, such as sales (or economically similar services) or the provision of training and educational courses. For purposes of the preceding sentence, the determination of whether a person's services are sales or economically similar services will be based on all the facts and circumstances of that person's business. Such facts and circumstances include, for example, the manner in which the taxpayer is compensated for the services provided. Performance of services

in the field of consulting does not include the performance of consulting services embedded in, or ancillary to, the sale of goods or performance of services on behalf of a trade or business that is otherwise not an SSTB (such as typical services provided by a building contractor) if there is no separate payment for the consulting services. Services within the fields of architecture and engineering are not treated as consulting services.

(viii) Meaning of services performed in the field of athletics. For purposes of section 199A(d)(2) and paragraph (b)(1)(vii) of this section only, the performance of services in the field of athletics means the performance of services by individuals who participate in athletic competition such as athletes, coaches, and team managers in sports such as baseball, basketball, football, soccer, hockey, martial arts, boxing, bowling, tennis, golf, skiing, snowboarding, track and field, billiards, and racing. The performance of services in the field of athletics does not include the provision of services that do not require skills unique to athletic competition, such as the maintenance and operation of equipment or facilities for use in athletic events. Similarly, the performance of services in the field of athletics does not include the provision of services by persons who broadcast or otherwise disseminate video or audio of athletic events to the public.

(ix) Meaning of services performed in the field of financial services. For purposes of section 199A(d)(2) and paragraph (b)(1)(viii) of this section only, the performance of services in the field of financial services means the provision of financial services to clients including managing wealth, advising clients with respect to finances, developing retirement plans, developing wealth transition plans, the provision of advisory and other

similar services regarding valuations, mergers, acquisitions, dispositions, restructurings (including in title 11 or similar cases), and raising financial capital by underwriting, or acting as a client's agent in the issuance of securities and similar services. This includes services provided by financial advisors, investment bankers, wealth planners, retirement advisors, and other similar professionals performing services in their capacity as such. Solely for purposes of section 199A, the performance of services in the field of financial services does not include taking deposits or making loans, but does include arranging lending transactions between a lender and borrower.

(x) Meaning of services performed in the field of brokerage services. For purposes of section 199A(d)(2) and paragraph (b)(1)(ix) of this section only, the performance of services in the field of brokerage services includes services in which a person arranges transactions between a buyer and a seller with respect to securities (as defined in section 475(c)(2)) for a commission or fee. This includes services provided by stock brokers and other similar professionals, but does not include services provided by real estate agents and brokers, or insurance agents and brokers.

(xi) Meaning of the provision of services in investing and investment management. For purposes of section 199A(d)(2) and paragraph (b)(1)(x) of this section only, the performance of services that consist of investing and investment management refers to a trade or business involving the receipt of fees for providing investing, asset management, or investment management services, including providing advice with respect to buying and selling investments. The performance of services of investing and investment management does not include directly managing real property.

(xii) Meaning of the provision of services in trading. For purposes of section 199A(d)(2) and paragraph (b)(1)(xi) of this section only, the performance of services that consist of trading means a trade or business of trading in securities (as defined in section 475(c)(2)), commodities (as defined in section 475(e)(2)), or partnership interests. Whether a person is a trader in securities, commodities, or partnership interests is determined by taking into account all relevant facts and circumstances, including the source and type of profit that is associated with engaging in the activity regardless of whether that person trades for the person's own account, for the account of others, or any combination thereof.

(xiii) Meaning of the provision of services in dealing--(A) Dealing in securities. For purposes of section 199A(d)(2) and paragraph (b)(1)(xii) of this section only, the performance of services that consist of dealing in securities (as defined in section 475(c)(2)) means regularly purchasing securities from and selling securities to customers in the ordinary course of a trade or business or regularly offering to enter into, assume, offset, assign, or otherwise terminate positions in securities with customers in the ordinary course of a trade or business. Solely for purposes of the preceding sentence, the performance of services to originate a loan is not treated as the purchase of a security from the borrower in determining whether the lender is dealing in securities.

(B) Dealing in commodities. For purposes of section 199A(d)(2) and paragraph (b)(1)(xii) of this section only, the performance of services that consist of dealing in commodities (as defined in section 475(e)(2)) means regularly purchasing commodities from and selling commodities to customers in the ordinary course of a trade or business

or regularly offering to enter into, assume, offset, assign, or otherwise terminate positions in commodities with customers in the ordinary course of a trade or business. Solely for purposes of the preceding sentence, gains and losses from qualified active sales as defined in paragraph (b)(2)(xiii)(B)(1) of this section are not taken into account in determining whether a person is engaged in the trade or business of dealing in commodities.

(1) Qualified active sale. The term qualified active sale means the sale of commodities in the active conduct of a commodities business as a producer, processor, merchant, or handler of commodities if the trade or business is as an active producer, processor, merchant or handler of commodities. A hedging transaction described in paragraph (b)(2)(i)(B) of this section is treated as a qualified active sale. The sale of commodities held by a trade or business other than in its capacity as an active producer, processor, merchant, or handler of commodities is not a qualified active sale. For example, the sale by a trade or business of commodities that were held for investment or speculation would not be a qualified active sale.

(2) Active conduct of a commodities business. For purposes of paragraph (b)(2)(xiii)(B)(1) of this section, a trade or business is engaged in the active conduct of a commodities business as a producer, processor, merchant, or handler of commodities only with respect to commodities for which each of the conditions described in paragraphs (b)(2)(xiii)(B)(3), (4), and (5) of this section is satisfied.

(3) Directly holds commodities as inventory or similar property. The commodities trade or business holds the commodities directly, and not through an agent or independent contractor, as inventory or similar property. The term inventory or similar

property means property that is stock in trade of the trade or business or other property of a kind that would properly be included in the inventory of the trade or business if on hand at the close of the taxable year, or property held by the trade or business primarily for sale to customers in the ordinary course of its trade or business.

(4) Directly incurs substantial expenses in the ordinary course. The commodities trade or business incurs substantial expenses in the ordinary course of the commodities trade or business from engaging in one or more of the following activities directly, and not through an agent or independent contractor--

(i) Substantial activities in the production of the commodities, including planting, tending or harvesting crops, raising or slaughtering livestock, or extracting minerals;

(ii) Substantial processing activities prior to the sale of the commodities, including the blending and drying of agricultural commodities, or the concentrating, refining, mixing, crushing, aerating or milling of commodities; or

(iii) Significant activities as described in paragraph (b)(2)(xiii)(B)(5) of this section.

(5) Significant activities for purposes of paragraph (b)(2)(xiii)(B)(4)(iii). The commodities trade or business performs significant activities with respect to the commodities that consists of--

(i) The physical movement, handling and storage of the commodities, including preparation of contracts and invoices, arranging transportation, insurance and credit, arranging for receipt, transfer or negotiation of shipping documents, arranging storage or warehousing, and dealing with quality claims;

(ii) Owning and operating facilities for storage or warehousing; or

(iii) Owning, chartering, or leasing vessels or vehicles for the transportation of the commodities.

(C) Dealing in partnership interests. For purposes of section 199A(d)(2) and paragraph (b)(1)(xii) of this section only, the performance of services that consist of dealing in partnership interests means regularly purchasing partnership interests from and selling partnership interests to customers in the ordinary course of a trade or business or regularly offering to enter into, assume, offset, assign, or otherwise terminate positions in partnership interests with customers in the ordinary course of a trade or business.

(xiv) Meaning of trade or business where the principal asset of such trade or business is the reputation or skill of one or more employees or owners. For purposes of section 199A(d)(2) and paragraph (b)(1)(xiii) of this section only, the term any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners means any trade or business that consists of any of the following (or any combination thereof):

(A) A trade or business in which a person receives fees, compensation, or other income for endorsing products or services,

(B) A trade or business in which a person licenses or receives fees, compensation, or other income for the use of an individual's image, likeness, name, signature, voice, trademark, or any other symbols associated with the individual's identity,

(C) Receiving fees, compensation, or other income for appearing at an event or on radio, television, or another media format.

(D) For purposes of paragraph (b)(2)(xiv)(A) through (C) of this section, the term fees, compensation, or other income includes the receipt of a partnership interest and the corresponding distributive share of income, deduction, gain, or loss from the partnership, or the receipt of stock of an S corporation and the corresponding income, deduction, gain, or loss from the S corporation stock.

(3) Examples. The following examples illustrate the rules in paragraphs (a) and (b) of this section. The examples do not address all types of services that may or may not qualify as specified services. Unless otherwise provided, the individual in each example has taxable income in excess of the threshold amount.

(i) Example 1 to paragraph (b)(3). B is a board-certified pharmacist who contracts as an independent contractor with X, a small medical facility in a rural area. X employs one full time pharmacist, but contracts with B when X's needs exceed the capacity of its full-time staff. When engaged by X, B is responsible for receiving and reviewing orders from physicians providing medical care at the facility; making recommendations on dosing and alternatives to the ordering physician; performing inoculations, checking for drug interactions, and filling pharmaceutical orders for patients receiving care at X. B is engaged in the performance of services in the field of health within the meaning of section 199A(d)(2) and paragraphs (b)(1)(i) and (b)(2)(ii) of this section.

(ii) Example 2 to paragraph (b)(3). X is the operator of a residential facility that provides a variety of services to senior citizens who reside on campus. For residents, X offers standard domestic services including housing management and maintenance, meals, laundry, entertainment, and other similar services. In addition, X contracts with local professional healthcare organizations to offer residents a range of medical and health services provided at the facility, including skilled nursing care, physical and occupational therapy, speech-language pathology services, medical social services, medications, medical supplies and equipment used in the facility, ambulance transportation to the nearest supplier of needed services, and dietary counseling. X receives all of its income from residents for the costs associated with residing at the facility. Any health and medical services are billed directly by the healthcare providers to the senior citizens for those professional healthcare services even though those services are provided at the facility. X does not perform services in the field of health within the meaning of section 199A(d)(2) and paragraphs (b)(1)(i) and (b)(2)(ii) of this section.

(iii) Example 3 to paragraph (b)(3). Y operates specialty surgical centers that provide outpatient medical procedures that do not require the patient to remain overnight for recovery or observation following the procedure. Y is a private organization that owns a number of facilities throughout the country. For each facility, Y ensures compliance with state and Federal laws for medical facilities and manages the facility's operations and performs all administrative functions. Y does not employ physicians, nurses, and medical assistants, but enters into agreements with other professional medical organizations or directly with the medical professionals to perform the procedures and provide all medical care. Patients are billed by Y for the facility costs relating to their procedure and by the healthcare professional or their affiliated organization for the actual costs of the procedure conducted by the physician and medical support team. Y does not perform services in the field of health within the meaning of section 199A(d)(2) and paragraphs (b)(1)(i) and (b)(2)(ii) of this section.

(iv) Example 4 to paragraph (b)(3). Z is the developer and the only provider of a patented test used to detect a particular medical condition. Z accepts test orders only from health care professionals (Z's clients), does not have contact with patients, and Z's employees do not diagnose, treat, or manage any aspect of patient care. A, who manages Z's testing operations, is the only employee with an advanced medical degree. All other employees are technical support staff and not healthcare professionals. Z's workers are highly educated, but the skills the workers bring to the job are not often useful for Z's testing methods. In order to perform the duties required by Z, employees receive more than a year of specialized training for working with Z's test, which is of no use to other employers. Upon completion of an ordered test, Z analyses the results and provides its clients a report summarizing the findings. Z does not discuss the report's results, or the patient's diagnosis or treatment with any health care provider or the patient. Z is not informed by the healthcare provider as to the healthcare provider's diagnosis or treatment. Z is not providing services in the field of health within the meaning of section 199A(d)(2) and paragraphs (b)(1)(i) and (b)(2)(ii) of this section or where the principal asset of the trade or business is the reputation or skill of one or more of its employees within the meaning of paragraphs (b)(1)(xiii) and (b)(2)(xiv) of this section.

(v) Example 5 to paragraph (b)(3). A, a singer and songwriter, writes and records a song. A is paid a mechanical royalty when the song is licensed or streamed. A is also paid a performance royalty when the recorded song is played publicly. A is engaged in the performance of services in an SSTB in the field of performing arts within the meaning of section 199A(d)(2) or paragraphs (b)(1)(v) and (b)(2)(vi) of this section. The royalties that A receives for the song are not eligible for a deduction under section 199A.

(vi) Example 6 to paragraph (b)(3). B is a partner in Movie LLC, a partnership. Movie LLC is a film production company. Movie LLC plans and coordinates film production. Movie LLC shares in the profits of the films that it produces. Therefore, Movie LLC is engaged in the performance of services in an SSTB in the field of performing arts within the meaning of section 199A(d)(2) or paragraphs (b)(1)(v) and

(b)(2)(vi) of this section. B is a passive owner in Movie LLC and does not provide any services with respect to Movie LLC. However, because Movie LLC is engaged in an SSTB in the field of performing arts, B's distributive share of the income, gain, deduction, and loss with respect to Movie LLC is not eligible for a deduction under section 199A.

(vii) Example 7 to paragraph (b)(3). C is a partner in Partnership, which solely owns and operates a professional sports team. Partnership employs athletes and sells tickets and broadcast rights for games in which the sports team competes. Partnership sells the broadcast rights to Broadcast LLC, a separate trade or business. Broadcast LLC solely broadcasts the games. Partnership is engaged in the performance of services in an SSTB in the field of athletics within the meaning of section 199A(d)(2) or paragraphs (b)(1)(vii) and (b)(2)(viii) of this section. The tickets sales and the sale of the broadcast rights are both the performance of services in the field of athletics. C is a passive owner in Partnership and C does not provide any services with respect to Partnership or the sports team. However, because Partnership is engaged in an SSTB in the field of athletics, C's distributive share of the income, gain, deduction, and loss with respect to Partnership is not eligible for a deduction under section 199A. Broadcast LLC is not engaged in the performance of services in an SSTB in the field of athletics.

(viii) Example 8 to paragraph (b)(3). D is in the business of providing services that assist unrelated entities in making their personnel structures more efficient. D studies its client's organization and structure and compares it to peers in its industry. D then makes recommendations and provides advice to its client regarding possible changes in the client's personnel structure, including the use of temporary workers. D does not provide any temporary workers to its clients and D's compensation and fees are not affected by whether D's clients used temporary workers. D is engaged in the performance of services in an SSTB in the field of consulting within the meaning of section 199A(d)(2) or paragraphs (b)(1)(vi) and (b)(2)(vii) of this section.

(ix) Example 9 to paragraph (b)(3). E is an individual who owns and operates a temporary worker staffing firm primarily focused on the software consulting industry. Business clients hire E to provide temporary workers that have the necessary technical skills and experience with a variety of business software to provide consulting and advice regarding the proper selection and operation of software most appropriate for the business they are advising. E does not have a technical software engineering background and does not provide software consulting advice herself. E reviews resumes and refers candidates to the client when the client indicates a need for temporary workers. E does not evaluate her clients' needs about whether the client needs workers and does not evaluate the clients' consulting contracts to determine the type of expertise needed. Rather, the client provides E with a job description indicating the required skills for the upcoming consulting project. E is paid a fixed fee for each temporary worker actually hired by the client and receives a bonus if that worker is hired permanently within a year of referral. E's fee is not contingent on the profits of its clients. E is not considered to be engaged in the performance of services in the field of

consulting within the meaning of section 199A(d)(2) or (b)(1)(vi) and (b)(2)(vii) of this section.

(x) Example 10 to paragraph (b)(3). F is in the business of licensing software to customers. F discusses and evaluates the customer's software needs with the customer. The taxpayer advises the customer on the particular software products it licenses. F is paid a flat price for the software license. After the customer licenses the software, F helps to implement the software. F is engaged in the trade or business of licensing software and not engaged in an SSTB in the field of consulting within the meaning of section 199A(d)(2) or paragraphs (b)(1)(vi) and (b)(2)(vii) of this section.

(xi) Example 11 to paragraph (b)(3). G is in the business of providing services to assist clients with their finances. G will study a particular client's financial situation, including, the client's present income, savings, and investments, and anticipated future economic and financial needs. Based on this study, G will then assist the client in making decisions and plans regarding the client's financial activities. Such financial planning includes the design of a personal budget to assist the client in monitoring the client's financial situation, the adoption of investment strategies tailored to the client's needs, and other similar services. G is engaged in the performance of services in an SSTB in the field of financial services within the meaning of section 199A(d)(2) or paragraphs (b)(1)(viii) and (b)(2)(ix) of this section.

(xii) Example 12 to paragraph (b)(3). H is in the business of franchising a brand of personal financial planning offices, which generally provide personal wealth management, retirement planning, and other financial advice services to customers for a fee. H does not provide financial planning services itself. H licenses the right to use the business tradename, other branding intellectual property, and a marketing plan to third-party financial planner franchisees that operate the franchised locations and provide all services to customers. In exchange, the franchisees compensate H based on a fee structure, which includes a one-time fee to acquire the franchise. H is not engaged in the performance of services in the field of financial services within the meaning of section 199A(d)(2) or paragraphs (b)(1)(viii) and (b)(2)(ix) of this section.

(xiii) Example 13 to paragraph (b)(3). J is in the business of executing transactions for customers involving various types of securities or commodities generally traded through organized exchanges or other similar networks. Customers place orders with J to trade securities or commodities based on the taxpayer's recommendations. J's compensation for its services typically is based on completion of the trade orders. J is engaged in an SSTB in the field of brokerage services within the meaning of section 199A(d)(2) or paragraphs (b)(1)(ix) and (b)(2)(x) of this section.

(xiv) Example 14 to paragraph (b)(3). K owns 100% of Corp, an S corporation, which operates a bicycle sales and repair business. Corp has 8 employees, including K. Half of Corp's net income is generated from sales of new and used bicycles and related goods, such as helmets, and bicycle-related equipment. The other half of Corp's net income is generated from bicycle repair services performed by K and Corp's

other employees. Corp's assets consist of inventory, fixtures, bicycle repair equipment, and a leasehold on its retail location. Several of the employees and G have worked in the bicycle business for many years, and have acquired substantial skill and reputation in the field. Customers often consult with the employees on the best bicycle for purchase. K is in the business of sales and repairs of bicycles and is not engaged in an SSTB within the meaning of section 199A(d)(2) or paragraphs (b)(1)(xiii) and (b)(2)(xiv) of this section.

(v) Example 15 to paragraph (b)(3). L is a well-known chef and the sole owner of multiple restaurants each of which is owned in a disregarded entity. Due to L's skill and reputation as a chef, L receives an endorsement fee of \$500,000 for the use of L's name on a line of cooking utensils and cookware. L is in the trade or business of being a chef and owning restaurants and such trade or business is not an SSTB. However, L is also in the trade or business of receiving endorsement income. L's trade or business consisting of the receipt of the endorsement fee for L's skill and/or reputation is an SSTB within the meaning of section 199A(d)(2) or paragraphs (b)(1)(xiii) and (b)(2)(xiv) of this section.

(xvi) Example 16 to paragraph (b)(3). M is a well-known actor. M entered into a partnership with Shoe Company, in which M contributed her likeness and the use of her name to the partnership in exchange for a 50% interest in the partnership and a guaranteed payment. M's trade or business consisting of the receipt of the partnership interest and the corresponding distributive share with respect to the partnership interest for M's likeness and the use of her name is an SSTB within the meaning of section 199A(d)(2) or paragraphs (b)(1)(xiii) and (b)(2)(xiv) of this section.

(c) Special rules--(1) De minimis rule--(i) Gross receipts of \$25 million or less.

For a trade or business with gross receipts of \$25 million or less for the taxable year, a trade or business is not an SSTB if less than 10 percent of the gross receipts of the trade or business are attributable to the performance of services in a field described in paragraph (b) of this section. For purposes of determining whether this 10 percent test is satisfied, the performance of any activity incident to the actual performance of services in the field is considered the performance of services in that field.

(ii) Gross receipts of greater than \$25 million. For a trade or business with gross receipts of greater than \$25 million for the taxable year, the rules of paragraph (c)(1)(i)

## **Presumption of Employee Examples**

performing services as an employee refers to all wages (within the meaning of section 3401(a)) and other income earned in a capacity as an employee, including payments described in §1.6041-2(a)(1) (other than payments to individuals described in section 3121(d)(3)) and §1.6041-2(b)(1).

(2) Employer's Federal employment tax classification of employee immaterial.

For purposes of determining whether wages are earned in a capacity as an employee as provided in paragraph (d)(1) of this section, the treatment of an employee by an employer as anything other than an employee for Federal employment tax purposes is immaterial. Thus, if a worker should be properly classified as an employee, it is of no consequence that the employee is treated as a non-employee by the employer for Federal employment tax purposes.

(3) Presumption that former employees are still employees--(i) Presumption.

Solely for purposes of section 199A(d)(1)(B) and paragraph (d)(1) of this section, an individual that was properly treated as an employee for Federal employment tax purposes by the person to which he or she provided services and who is subsequently treated as other than an employee by such person with regard to the provision of substantially the same services directly or indirectly to the person (or a related person), is presumed, for three years after ceasing to be treated as an employee for Federal employment tax purposes, to be in the trade or business of performing services as an employee with regard to such services. As provided in paragraph (d)(3)(ii) of this section, this presumption may be rebutted upon a showing by the individual that, under Federal tax law, regulations, and principles (including common-law employee classification rules), the individual is performing services in a capacity other than as an

employee. This presumption applies regardless of whether the individual provides services directly or indirectly through an entity or entities.

(ii) Rebuttal of presumption. Upon notice from the IRS, an individual rebuts the presumption in paragraph (d)(3)(i) of this section by providing records, such as contracts or partnership agreements, that provide sufficient evidence to corroborate the individual's status as a non-employee.

(iii) Examples. The following examples illustrate the provision of paragraph (d)(3) of this section. Unless otherwise provided, the individual in each example has taxable income in excess of the threshold amount.

(A) Example 1 to paragraph (d)(3). A is employed by PRS, a partnership for Federal tax purposes, as a fulltime employee and is treated as such for Federal employment tax purposes. A quits his job for PRS and enters into a contract with PRS under which A provides substantially the same services that A previously provided to PRS in A's capacity as an employee. Because A was treated as an employee for services he provided to PRS, and now is no longer treated as an employee with regard to such services, A is presumed (solely for purposes of section 199A(d)(1)(B) and paragraphs (a)(3) and (d) of this section) to be in the trade or business of performing services as an employee with regard to his services performed for PRS. Unless the presumption is rebutted with a showing that, under Federal tax law, regulations, and principles (including the common-law employee classification rules), A is not an employee, any amounts paid by PRS to A with respect to such services will not be QBI for purposes of section 199A. The presumption would apply even if, instead of contracting directly with PRS, A formed a disregarded entity, or a passthrough entity, and the entity entered into the contract with PRS.

(B) Example 2 to paragraph (d)(3). C is an attorney employed as an associate in a law firm (Law Firm 1) and was treated as such for Federal employment tax purposes. C and the other associates in Law Firm 1 have taxable income below the threshold amount. Law Firm 1 terminates its employment relationship with C and its other associates. C and the other former associates form a new partnership, Law Firm 2, which contracts to perform legal services for Law Firm 1. Therefore, in form, C is now a partner in Law Firm 2 which earns income from providing legal services to Law Firm 1. C continues to provide substantially the same legal services to Law Firm 1 and its clients. Because C was previously treated as an employee for services she provided to Law Firm 1, and now is no longer treated as an employee with regard to such services, C is presumed (solely for purposes of section 199A(d)(1)(B) and paragraphs (a)(3) and (d) of this section) to be in the trade or business of performing services as an employee

with respect to the services C provides to Law Firm 1 indirectly through Law Firm 2. Unless the presumption is rebutted with a showing that, under Federal tax law, regulations, and principles (including common-law employee classification rules), C's distributive share of Law Firm 2 income (including any guaranteed payments) will not be QBI for purposes of section 199A. The results in this example would not change if, instead of contracting with Law Firm 1, Law Firm 2 was instead admitted as a partner in Law Firm 1.

(C) Example 3 to paragraph (d)(3). E is an engineer employed as a senior project engineer in an engineering firm, Engineering Firm. Engineering Firm is a partnership for Federal tax purposes and structured such that after 10 years, senior project engineers are considered for partner if certain career milestones are met. After 10 years, E meets those career milestones and is admitted as a partner in Engineering Firm. As a partner in Engineering Firm, E shares in the net profits of Engineering Firm, and also otherwise satisfies the requirements under Federal tax law, regulations, and principles (including common-law employee classification rules) to be respected as a partner. E is presumed (solely for purposes of section 199A(d)(1)(B) and paragraphs (a)(3) and (d) of this section) to be in the trade or business of performing services as an employee with respect to the services E provides to Engineering Firm. However, E is able to rebut the presumption by showing that E became a partner in Engineering Firm as a career milestone, shares in the overall net profits in Engineering Firm, and otherwise satisfies the requirements under Federal tax law, regulations, and principles (including common-law employee classification rules) to be respected as a partner.

(D) Example 4 to paragraph (d)(3). F is a financial advisor employed by a financial advisory firm, Advisory Firm, a partnership for Federal tax purposes, as a fulltime employee and is treated as such for Federal employment tax purposes. F has taxable income below the threshold amount. Advisory Firm is a partnership and offers F the opportunity to be admitted as a partner. F elects to be admitted as a partner to Advisory Firm and is admitted as a partner to Advisory Firm. As a partner in Advisory Firm, F shares in the net profits of Advisory Firm, is obligated to Advisory Firm in ways that F was not previously obligated as an employee, is no longer entitled to certain benefits available only to employees of Advisory Firm, and has materially modified his relationship with Advisory Firm. F's share of net profits is not subject to a floor or capped at a dollar amount. F is presumed (solely for purposes of section 199A(d)(1)(B) and paragraphs (a)(3) and (d) of this section) to be in the trade or business of performing services as an employee with respect to the services F provides to Advisory Firm. However, F is able to rebut the presumption by showing that F became a partner in Advisory Firm by sharing in the profits of Advisory Firm, materially modifying F's relationship with Advisory Firm, and otherwise satisfying the requirements under Federal tax law, regulations, and principles (including common-law employee classification rules) to be respected as a partner.