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Via Electronic Submission:
www.regulations.gov

CC:PA:LPD:PR (REG-107892-18)
Courier's Desk
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Comments Regarding REG-107892-18, Qualified Business Income Deduction, 83 Fed. Reg. 40884 (Aug. 16, 2018)

To Whom It May Concern:

The International Franchise Association ("IFA") respectfully submits the comments contained in this letter and the letter's attachment above to the Department of the Treasury ("Treasury") and the Internal Revenue Service (the "IRS"). The comments are with respect to the proposed regulations published in the Federal Register on August 16, 2018, regarding section 199A of the Internal Revenue Code (the "Proposed Regulations").[1] Specifically, the comments relate to the application to the franchise industry of Prop. Treas. Reg. § 1.199A-5 and its definition of a "specialized service trade or business" ("SSTB") for purposes of section 199A(d)(2).

The attachment is simply a reprint of IFA's pre-proposed-rule submission on this subject to Treasury and the IRS. As can be seen, the bulk of our comments are included in that attachment, rather than in the body of this letter. We are proceeding in this manner because in our view the earlier submission – which still reflects our basic position – is in substantial agreement with the terms and reasoning of the Proposed Regulations. We thought it would be most efficient, therefore, to reflect the extent of that agreement by attaching the earlier submission and to focus the text of the letter on one additional IFA request.

[1] REG-107892-18, Qualified Business Income Deduction, 83 Fed. Reg. 40884 (Aug. 16, 2018). All section references are to the Internal Revenue Code of 1986, as amended and currently in effect.

That request is that the final rule should add a "franchising example" to the examples used by the Proposed Regulations that define "SSTB."[2] We believe the examples currently in the proposal are used effectively by the drafters to particularize the rule's requirements. They serve largely to narrow the construction of statutory terms that, without such narrowing, could inadvertently impose SSTB treatment on large numbers of taxpayers never intended to receive such treatment. For instance, while the Internal Revenue Code sections relevant to SSTBs, if read literally, could have the effect of imposing SSTB status on "*any* trade or business involving the performance of services in the field of health" (emphasis added) – a result never intended by the Congress – the "health example" in the Proposed Regulations would impose that status only on healthcare trades or businesses in which "healthcare professionals . . . provide medical services directly to a patient."[3] Similar restrictive language is provided for other fields of business in several of the rule's other SSTB examples.[4]

We believe that these provisions, taken together, will have the effect of excluding franchisors from any SSTB designation under the Proposed Regulations that is based solely on the selling of franchises in a listed field of service. That activity cannot reasonably be interpreted as the direct providing of services by a professional in the listed field to a consumer of those services. We think it would be preferable, however, if the rule in final form could explicitly say just that – either by way of a "franchising example" or any other approach the drafters might find acceptable.

The example could be very short, along the following lines:

> F is in the business of franchising a brand of medical clinics, which involve doctors and nurses providing primary care to patients. F does not operate the medical clinics herself; rather, she licenses the medical clinic brand and operations manual to third party franchisees in exchange for an up-front fee and a royalty based on the franchisees' gross revenue. F is not engaged in the performance of services in an SSTB in the field of medicine within the meaning of paragraphs (b)(1)(i) and (b)(2)(ii) of this section.

There are essentially two reasons why we believe a rule that included this feature would best serve the interests we believe Treasury and the IRS wish to pursue in this rulemaking. First, one of those interests relates to the need for certainty. On many occasions the proponents of tax reform have listed certainty as a major reform objective, and the preamble of the Proposed Regulations makes clear that this objective is a priority for the rule's drafters.[5] A franchising

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[2] *See* Prop. Treas. Reg. § 1.199A-5(b).

[3] Prop. Treas. Reg. § 1.199A-5(b)(2)(ii).

[4] *See* Prop. Treas. Reg. § 1.199A-5(b)(2)(iii)-(vi), (ix).

[5] 83 Fed. Reg. at 40897 ("Most importantly, section 199A is a new Code provision intended to benefit a wide range of businesses, and taxpayers need certainty in determining whether their trade or business generates income that is eligible for the section 199A deduction.").

company's certainty regarding its future tax liability would no doubt be enhanced by an example of the kind just described. In fact, there is a greater need for certainty where franchisors, as opposed to other business taxpayers, are involved. The franchisor community consists largely of small businesses that typically are not in a position to hire expensive tax advisors and litigators.[6] Regulations that provide a maximum degree of certainty and clarity are therefore particularly valuable to this business sector.

Second, this approach would provide an essentially hassle-free way to promote another major tax-reform objective – economic growth. As noted in our pre-proposed-rule submission, the franchising model supports close to 7.6 million direct jobs, is responsible for 2.5 percent of the nation's GDP, and has been an important contributor to the current U.S. economic recovery. Franchisors in effect leverage their business investment activity through franchising agreements, a practice that can typically be relied on to create considerable employment and economic expansion.

We believe, therefore, that any favorable signal to franchising companies regarding the tax certainty and growth potential associated with their businesses would promote investment by those companies and further enhance the nation's economy. Moreover, it would do so without actually affecting the substance of the new section 199A regime. What would change would not be the requirements of that regime, but rather, in many cases, the perception of those requirements. We respectfully submit that any such approach could be expected to amount to a no-lose proposition.

Thank you for your consideration of these suggestions, as well as for your responsiveness to IFA's earlier proposals in this rulemaking. We would be delighted to discuss any of these matters further with you at your convenience.

Yours sincerely,

Matt Haller
Senior Vice President of Government
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Enclosure

[6] We recognize that if those businesses are small enough, their income levels may be below the thresholds that trigger the application of the SSTB provisions. Most of the small franchisors we are familiar with, however, have incomes that exceed those levels.

cc: Thomas West
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