



It's Final: Staffing Services Are Eligible for New Tax Deduction

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The Treasury Department and Internal Revenue Service issued final regulations Jan. 17 confirming the ASA position that staffing companies can take advantage of the new tax deduction for “passthrough” businesses provided for in the Tax Cuts and Jobs Act of 2017. The great majority of staffing companies are passthrough businesses and should substantially benefit from the deduction.

The deduction applies to businesses such as sole proprietorships, partnerships, trusts, and S corporations in which the owners are taxed as individuals. Those individuals can take a deduction, up to 20%, for their qualified business income (QBI) subject to certain limitations (e.g., if the W-2 wages with respect to the trade or business are below a specified amount). QBI is the net amount of qualified items of income, gain, deduction, and loss from any qualified U.S. trade or business, except for certain “specified service trades or businesses” (“excepted SSTBs”) in fields such as health, law, accounting, and consulting. Also excepted is any business whose principal asset is the reputation or skill of one or more of its employees or owners. Individual taxpayers who make less than \$157,500 (\$315,000 for married couples filing jointly) are not subject to these exceptions.

The final rules are effective on the date of publication in the *Federal Register* and are generally applicable to taxable years ending after such date; but taxpayers may rely on the final rules, or on the proposed rules issued Aug. 16, 2018, for taxable years ending in calendar year 2018.

Staffing Is Recognized as a Separate, Non-SSTB Service

The final regulations reflect the positions advocated by ASA with senior Treasury Department officials and in subsequent written comments and hearing testimony. ASA asserted that staffing services should be eligible for the deduction because staffing is not on the list of excepted SSTBs and because it is a service that is separate and distinct from the services temporary employees provide to staffing company clients. As such, the business of staffing should be eligible for the deduction even if the services performed by temporary employees are in the field of excepted SSTBs. Stated another way, providing clients with employees who perform excepted SSTBs does not make the staffing company an excepted SSTB because the staffing company is not directly providing those services. The final regulations confirm this view in the following example, which demonstrates that providing staffing services to a consulting business (an excepted SSTB) is not itself considered an excepted SSTB.

E is an individual who owns and operates a temporary worker staffing company 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

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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.

Likewise, based on this example, if a staffing company supplies clients with temporary lawyers, nurses, or individuals to perform other excepted SSTBs involving facts similar to those described in the example, the company will not be viewed as an excepted SSTB engaged in performing such services.

Pure Workforce Consulting Will Be Considered an Excepted SSTB

If a staffing company separately engages in the business of advising clients on how to best manage their workforces that does not involve supplying temporary workers, the final regulations provide that the staffing company will be viewed as engaged in the excepted SSTB of consulting, as illustrated in the following example.

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.

Although most staffing companies don't provide separate consulting services, to the extent that they do, they may still qualify for the deduction if those services are de minimis (i.e., less than 10% for businesses with gross receipts of \$25 million or less; less than 5% if gross receipts exceed \$25 million). Otherwise, to avoid having the consulting services adversely affect the staffing company's eligibility for the deduction, the consulting services must be operated as a distinctly separate business with its own books and records. Staffing companies should consult with their tax advisers on the requirements for maintaining the appropriate separation.

Reputation or Skill Exception Is Narrowly Construed

The final rules also make clear that the "reputation or skill" exception, as ASA had urged, will be construed to apply only to a narrow set of trades or businesses such that staffing clearly is not subject to the exception. Specifically, the exception will apply only to those trades or businesses in which an individual receives income for endorsing products or services; for licensing his or her image, likeness, name, signature, voice, trademark, or any other symbols associated with the individual's identity; or for making appearances.

The final regulations are a significant victory for the staffing industry and a direct result of the association's advocacy on behalf of the industry. It is important to note that the regulations are complex and companies should consult their tax advisers to determine how the rules apply to them—including the provisions that may limit the deduction, and how the rules apply to companies engaged in one or more trades or businesses.