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Take Care Defining Health Services Under IRC Section 199A

By **Marc Finer** (February 15, 2019, 5:18 PM EST)

One of the most publicized changes made by 2017's Tax Cuts and Jobs Act was the creation of a new 20 percent qualified business income deduction under new Section 199A of the Internal Revenue Code. This new provision generally permits the owners of pass-through businesses, such as sole proprietorships, partnerships, limited liability companies and S corporations, to deduct up to 20 percent of their share of the business' QBI in determining their personal U.S. federal income tax liability.



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In general, to benefit from the QBI deduction, a business must be a "qualified trade or business," defined, in part, as any trade or business other than a specified service trade or business. Included in the list of specified service trades or businesses are businesses that perform services in the field of health. This includes 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.

On Jan. 18, 2019, the Internal Revenue Service issued final regulations that should help taxpayers determine their eligibility to benefit from the QBI deduction. Included in the guidance provided by the final regulations is a clarification of the meaning of "performance of services in the field of health." The preamble to the final regulations begins by acknowledging that certain facilities, such as assisted living facilities and skilled nursing facilities, provide multi-faceted services to their residents and indicates that a determination of whether such facilities and their owners "perform services in the field of health" requires a facts and circumstances inquiry. To assist taxpayers with this determination, the final regulations provide a number of examples of apparent health services that would not be considered services in the field of health.

Such examples are summarized below:

- A senior living facility that offers domestic services, such as housing management and maintenance, meals, laundry, entertainment and other similar services while contracting with local professional healthcare organizations that offer residents medical and health services at the facility, and that bills the residents directly, does not perform services in the field of health.
- A surgical center that does not employ physicians, nurses, and medical assistants, but rather enters into agreements with other professional medical organizations or

directly with medical professionals who perform the procedures, provide all medical care and bill the patients directly for the cost of the procedure conducted by the physician and medical support team, does not perform services in the field of health.

- A developer and provider of a patented test used to detect a particular medical condition is not treated as performing services in the field of health because the developer's employees do not contact patients and do not diagnose, treat or manage any aspects of patient care.

In contrast to the above examples, a board-certified pharmacist who contracts with a medical facility and who receives and reviews orders from physicians providing medical care at the facility, makes recommendations on dosing and alternatives to the ordering physician, performs inoculations, checks for drug interactions and fills pharmaceutical orders for patients receiving care at the facility is engaged in the performance of services in the field of health.

This conclusion may also apply because the final regulations remove the requirement from the proposed regulations that the services be provided directly to patients. By comparison, the preamble to the final regulations states that the sale of pharmaceuticals and medical devices by a retail pharmacy is not, by itself, a trade or business that is performing services in the field of health.

Interestingly, the final regulations affirm that a taxpayer can operate both a nonhealth-related business and a health-related business within a single pass-through entity without the former being tainted by the latter. In a new example in the final regulations, a limited liability company provides veterinarian services through licensed staff and also develops and sells its own line of organic dog food at the veterinary clinic and online. The example concludes that the veterinary services are services in the field of health but that the dog food business should not be similarly treated because the dog food business is operated through separate employees who are not otherwise affiliated with the veterinary clinic, and the company maintains separate books and records for each business.

The final regulations, primarily through the use of examples, clearly demonstrate the IRS' recognition that a trade or business can be associated with the field of health and still qualify for the QBI deduction because it is not performing services in the field of health under the IRS standards. However, a careful analysis of the facts and circumstances will be critical to this determination, and health-related businesses that operate with facts that are even slightly different than those in the new examples should proceed with caution.

For example, the fact that a senior living facility provides nursing care to its residents in addition to domestic services could be viewed as a significant difference from the senior living facility in the above example and result in the facility being treated as performing services in the field of health. Moreover, because a lack of proximity to the patient is no longer determinative of whether an individual is performing services in the field of health, as it was under the proposed regulations, more trades or businesses may be viewed as providing services in the field of health under the final regulations.

For taxpayers that are operating multiple trades or businesses in a health-related field, some of which would be considered specified service trades or businesses and others that would not, a detailed analysis of the separate activities should be made to demonstrate the existence of multiple trades or businesses — e.g., complete and separate books and records and separate employees — or document the income that is specifically related to the performance of services in the field of health.

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