

October 1, 2018

Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

**Re: Comments on Proposed Regulations under Section 199A of the Internal Revenue Code;
IRS and REG-107892-18**

Ladies and Gentlemen:

The American Financial Services Association (“AFSA”) appreciates the opportunity to comment on the Internal Revenue Service’s (“IRS”) recent notice of proposed rulemaking (the “Proposed Rule”). The Proposed Rule establishes regulations to implement the 20 percent deduction for qualified business income for individuals, partnerships, S corporations, trusts, and estates under Section 199A of the Internal Revenue Code, as established by the Tax Cuts and Jobs Act of 2017.¹

Founded in 1916, AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including traditional installment loans, mortgages, direct and indirect vehicle financing, payment cards, and retail sales finance. AFSA members are licensed and regulated at the state level. Many of AFSA’s members are also supervised by federal regulators. Those that are not supervised at the federal level are still subject to oversight by the Bureau of Consumer Financial Protection (“BCFP”).

AFSA members provide indirect financing for the purchase of vehicles, furniture, and other consumer products. As the only national trade association representing indirect lenders, AFSA is uniquely qualified to present a problem with the Proposed Rule regarding the definitions of “financial services” and “loans.”

As defined in the Proposed Rule, “financial services” includes many things, such as advising clients in wealth management, and expressly excludes making loans. Businesses that offer “financial services” are not eligible for the 20 percent deduction. The definition of financial services is therefore critical. Many AFSA members make “loans” that are excluded from the definition of financial services, and are therefore eligible for the deductions. However, many others engage in credit sales transactions, which are not expressly excluded from the definition of “financial services,” but should be.

The technical distinction between loans and extensions of credit, for purposes of the Proposed Rule and the Tax Cuts and Jobs Act of 2017, is, however, irrelevant. “Loans” are made when a creditor extends credit to a consumer by giving the consumer *money*, and the consumer promises to pay back the money with money and interest over time at periodic intervals. “Credit sales transactions” are made when a creditor extends credit to a consumer by giving the consumer *goods*, and the consumer promises to pay for the goods with money and interest (called finance charges) over time at periodic intervals. Thus, credit extensions are, for the IRS’s purposes, the functional equivalent of lending money.

¹ Pub. Law 115-97, Dec. 22, 2017.

Given the importance to businesses that extend credit, and that the distinction between loans and credit sales is functionally only semantics in this instance, we respectfully request that the IRS clarify that the term “loans” includes “credit sales transactions.” We also ask that the IRS make clear that the sale of a loan or of a credit sales transaction does not constitute a “financial service.”

I. Overview - What Businesses Qualify for the Deduction

To be specific, section 199A of the Proposed Rule states that a taxpayer can deduct 20 percent of qualified business income from a partnership, S corporation, or sole proprietorship. Businesses that do not qualify for the deduction are referred to as “specified service trade or businesses” or SSTBs. What businesses are SSTBs? The Proposed Rule states that financial service businesses, among others, are SSTBs. The IRS rightly limits the definition of financial services, which AFSA believes was Congress’ intent.

The Proposed Rule limits the definition of financial services to those:

“... typically performed by financial advisors and investment bankers and provides that the field of financial services includes 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 the client’s agent in the issuance of securities, and similar services. This includes services provided by financial advisors, investment bankers, wealth planners, and retirement advisors and other similar professionals, *but does not include taking deposits or making loans.*” [emphasis added]

Thus, as Congress intended, the Proposed Rule recognizes that businesses that make “loans” are not SSTBs. Additionally, while financial services are SSTBs, it seems clear that banking, insurance, financing, leasing, investing, or similar business are not. Non-bank lenders that licensed and regulated should be treated on par with banks.

II. Indirect Lenders Should Qualify for the Deduction

Our primary reason for submitting this letter centers on the definition of “loan,” and our purpose is to ensure that the Proposed Rule recognizes the reality of what many think: that credit sales of any type are the functional equivalent of loans, so that extenders of credit will also expressly be excluded from the definition of financial services.

For the reasons stated above, it is clear that lending money and extending credit are functionally equivalent. Consider for example, that when most consumers buy a car, they talk about getting a “loan,” even though it is really a credit sales transaction.² Or that when reporters write about the vehicle finance industry—(also referred to as indirect auto lending), they often write about auto “loans,” even though they should write about extensions of credit secured by autos. Or that the BCFP, which supervises vehicle finance companies, uses the terms, “auto lender” and “loan” when referring to financing of goods. Even though “loans” are not being made; credit is being extended. These examples highlight that when people want to buy things, they neither make nor understand—nor

² We note that while a fraction of vehicle finance transactions are loans made by banks, credit unions, and other lenders directly to borrowers who then pay the money to the seller, the vast majority of auto finance transactions occur in an auto dealership between a dealer (*i.e.*, seller) and a buyer (*i.e.*, vehicle finance company), and are structured as credit sale transactions (also referred to as retail installment sales contracts).

care about—the technical distinction between loans and extensions of credit. Thus, we believe that indirect finance companies are not SSTBs because they can be considered lenders who make loans.

Credit sales (consummated by use of installment sales contracts) are also used extensively in the financing of other products including farm equipment, furniture, and other consumer products. Like automobile financing, all forms of indirect lending are governed by state and federal laws.

For the purposes of 199A, we ask the IRS to acknowledge that loans and credit sales are functionally the same. There is no reason to exempt loans from the definition of financial services but not credit sales transactions. Thus, we ask that the IRS clarify that both loans and credit sales are not financial services.

We respectfully suggest that the IRS add the underlined language to the following definition of financial services: “This includes services provided by financial advisors, investment bankers, wealth planners, and retirement advisors and other similar professionals, but does not include taking deposits or making loans or credit sales.”

III. The Sale of Loans or Retail Installment Sales Contracts Does not Constitute a “Financial Service”

In addition to clarifying the definition of “loan,” we respectfully request that the IRS make clear that taxpayers who make loans or extend credit not be classified as SSTBs regardless of whether they hold the loans or sales contracts in portfolio or sell them. In other words, the sale of such loans or contracts should not result in a taxpayer being re-classified as a financial service provider and so designated as an SSTB. For the purposes of the pass-through deduction, there is no meaningful difference between the two. Many indirect lenders sell loans in whole, in part, or in securitized pools in order to maintain liquidity and diversification. This enables the finance company to extend credit to more borrowers. Often, the finance company retains the servicing rights.

To be more specific—for purposes of the Proposed Rule, the performance of services that consist of dealing in securities 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. The Proposed Rule specifies that a taxpayer that regularly originates loans in the ordinary course of a trade or business of making loans but engages in no more than negligible sales of the loans is not dealing in securities.

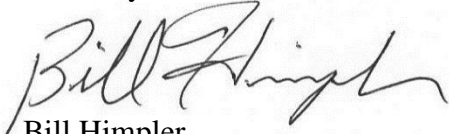
AFSA emphasizes that all sales of loans outside the ordinary course of business should be excluded from consideration in applying the negligible sales test. As noted in the previous paragraph, the definition of negligible sales currently provides that sales of securities that are necessitated by exceptional circumstances and that are not undertaken as recurring business activities are not considered in applying the mechanical negligible sales test.

This language may have the same effect as excluding all transactions outside the ordinary course of business. However, it is also possible that this language does not cover transactions outside the ordinary course of business that are not strictly necessary (for example, loans that no longer meet the taxpayer’s regulatory requirements, charged-off loans, or loans sold in connection with the closure of an underperforming branch). At any rate, these types of sales lack the regularity to be considered as sales in connection with the business of dealing in securities. Therefore, they should be excluded from the mechanical test. These clarifications are consistent with congressional intent because the suggested treatment of the items is consistent with existing banking/lending practices.

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AFSA appreciates the opportunity to provide comments on the Proposed Rule. We hope you find our recommendations useful. Please contact me by phone, 202-466-8616, or email, bhimpler@afsamail.org, with any questions.

Sincerely,

A handwritten signature in black ink that reads "Bill Himpler". The signature is written in a cursive style with a large, stylized initial "B".

Bill Himpler
Executive Vice President
American Financial Services Association