

PUBLICATION

Spotlight on Franchising: Expanded Information Reporting Requirements Affect Franchise Fees and Other Payments

August 05, 2010

The Patient Protection and Affordable Care Act (the "Act"), although focused primarily on health care reform, included an expansion of the information reporting requirements under Section 6041 of the Internal Revenue Code. This provision mandates the delivery of IRS Form 1099 when certain payments are made by a business to an individual or another business. The Act amended Section 6041 to extend the reporting requirement to include any corporation other than tax exempt organizations. The Act also modifies the information reporting requirements to include payments of "gross proceeds" and "amounts in consideration for property." These new rules will apply to payments made after December 31, 2011.

Prior to enactment of the Act, the Treasury Regulations generally exempted payments to corporations from the information reporting requirements under Section 6041 of the Code. Additionally, the payments subject to the information reporting requirements were limited to rent, salaries, wages, premiums, annuities, compensation, remuneration, emoluments, or other fixed or determinable gains, profits, and income (other than certain exempt payments). These provisions will continue to apply to all payments made on or before December 31, 2011.

As amended by the Act, and unless the IRS issues regulations and other guidance exempting certain payments, all businesses will need to collect taxpayer identification numbers from vendors and send each of them who receive more than \$600 annually a Form 1099 by each January 31, based on the prior year's payments. If the vendor doesn't supply a taxpayer identification number, the payor must withhold for federal income taxes from payments to the vendor, in accordance with the backup withholding requirements.

In view of the amendments to Section 6041 by the Act, franchisees will likely be required to issue a Form 1099 to their franchisor for the initial franchise fee and the continuing royalties and other fee payments typically made under a franchise agreement, unless the regulations to be issued by the IRS provide different guidance. This Form 1099 requirement applies regardless of the form of entity used by the franchisor. The more likely interpretation of the Act's revision of Section 6041 by the IRS will produce regulations that mean franchise fee and other vendor payments to franchisors made after December 31, 2011 will require delivery of Form 1099 to the franchisor and other vendors to the business.

The information reporting requirements, however, are not yet settled and the IRS is seeking taxpayer input. Specifically, the IRS recently issued Notice 2010-51 soliciting public comments regarding information that it intends to consider in preparing regulations and other guidance with respect to the expanded information reporting requirements under Section 6041. Individuals and businesses interested in submitting comments must do so by September 29, 2010.

Notice 2010-51 was issued in an effort to collect information to assist the IRS in promulgating regulations and other guidance that will help minimize the taxpayer burden under the expanded information reporting requirements and to avoid duplicative reporting. The IRS is seeking comments primarily with respect to (1) circumstances in which duplicative reporting might occur under the new law and other sections of the Code, (2) the burden the new law will place on various types of businesses and industries, (3) the appropriate scope of the terms "gross proceeds" and "amounts in consideration of property," (4) how the new law should apply to

payments between affiliated corporations, (5) the appropriate time and manner for reporting payments, (6) what changes, if any, should be made to Form W-9, Request for Taxpayer Identification Number and Certification, for purposes of complying with the new law, and (7) how the backup withholding requirements for missing taxpayer identification numbers should be administered under the new law.

Should your company wish to discuss the expanded information reporting requirements or seek assistance in preparing a written response to Notice 2010-51 before the September 29, 2010 deadline, please contact any Baker Donelson attorney.