Qualified business income deduction

Many owners of sole proprietorships, partnerships, S corporations and some trusts and estates may be eligible for a qualified business income (QBI) deduction – also called the Section 199A deduction – for tax years beginning after December 31, 2017. The deduction allows eligible taxpayers to deduct up to 20 percent of their QBI, plus 20 percent of qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income. Income earned through a C corporation or by providing services as an employee is not eligible for the deduction. For more information on what qualifies as a trade or business, see Determining your qualified trades or businesses in the Instructions for Form 8995-A or Form 8995.

The deduction is available regardless of whether taxpayers itemize deductions on Schedule A or take the standard deduction. Eligible taxpayers can claim the deduction for tax years beginning after December 31, 2017, and ending on or before December 31, 2025.

The deduction has two components.

1. **QBI component.** This component of the deduction equals 20 percent of QBI from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust, or estate. The QBI Component is subject to limitations, depending on the taxpayer's taxable income which may include the type of trade or business, the amount of W-2 wages paid by the qualified trade or business, and the unadjusted basis immediately after acquisition (UBIA) of qualified property held by the trade or business. It may also be reduced by the patron reduction if the taxpayer is a patron of an agricultural or horticultural cooperative.
2. **REIT/PTP component.** This component of the deduction equals 20 percent of qualified REIT dividends and qualified PTP income. This component is not limited by W-2 wages or the UBIA of qualified property. Depending on the taxpayer's taxable income, the amount of PTP income that qualifies may be limited depending on the type of the PTP's trade or business.

The deduction is limited to the lesser of the QBI component plus the REIT/PTP component or 20 percent of the taxpayer's taxable income minus net capital gain.

QBI is the net amount of qualified items of income, gain, deduction, and loss from any qualified trade or business, including income from partnerships, S corporations, sole proprietorships, and certain trusts. Generally, this includes, but is not limited to, the deductible part of self-employment tax, self-employed health insurance, and deductions for contributions to qualified retirement plans (e.g., SEP, SIMPLE and qualified plan deductions).

QBI does not include items such as:

- Items that are not properly includable in taxable income
- Investment items such as capital gains or losses
- Interest income not properly allocable to a trade or business
- Wage income
- Income that is not effectively connected with the conduct of business within the United States
- Commodities transactions or foreign currency gains or losses
- Certain dividends and payments in lieu of dividends
- Income, loss, or deductions from notional principal contracts
- Annuities, unless received in connection with the trade or business
- Amounts received as reasonable compensation from an S corporation
- Amounts received as guaranteed payments from a partnership
- Payments received by a partner for services other than in a capacity as a partner
- Qualified REIT dividends
- PTP income

Solely for the purposes of section 199A, a safe harbor is available to individuals and owners of passthrough entities who seek to claim the deduction under section 199A with respect to a rental real estate enterprise. Under the safe harbor a rental real estate enterprise will be treated as a trade or business for purposes of the QBI deduction if certain criteria are met. For more information on the safe harbor, see News Release IR-2019-158

An interest in rental real estate that does not meet the requirements of the safe harbor may still be treated as a trade or business for purposes of the QBI deduction if it otherwise is a section 162 trade or business.

In addition, the rental or licensing of tangible or intangible property that does not rise to the level of a section 162 trade or business is nevertheless treated as a qualified trade or business for purposes of section 199A if the rental or licensing of property is to a commonly controlled trade or business operated by the individual or a passthrough entity as provided in Treas. Reg. § 1.199A-1(b)(14).

More information

- FAQs
- Final regulations PDF
- Notice 2018-64
- Instructions to Form 1040 PDF
- Instructions to Form 8995-A PDF
- Instructions to Form 8995 PDF
- Tax Reform Basics for the Qualified Business Income Deduction (199A)

Qualified Business Income Deduction

Transcript

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