



October 1, 2018

The Honorable David J. Kautter
Assistant Secretary for Tax Policy
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Mr. William M. Paul
Acting Chief Counsel
Internal Revenue Service
1111 Constitution Ave, NW
Washington, DC 20224

RE: Guidance Concerning the Deduction for Qualified Business Income Under Section 199A of the Internal Revenue Code¹

Dear Messrs. Kautter and Paul:

The American Institute of CPAs (AICPA) offers the following comments and recommendations related to the Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) notice of proposed rulemaking REG-107892-18 (issued August 16, 2018) on the “Qualified Business Income Deduction,” the IRS Notice 2018-64 on “Methods for Calculating W-2 Wages for Purposes of Section 199A,”² and the IRS Frequently Asked Questions (FAQs) on the “Tax Cuts and Jobs Act, Provision 11011 Section 199A – Deduction for Qualified Business Income.” The proposed guidance provides rules addressing how the regulations will affect individuals, partnerships, S corporations, trusts, and estates engaged in domestic trades or businesses.

Our letter includes both the AICPA priority questions as well as our suggested responses to those questions. We have also attached an appendix of other issues affecting qualified business income (QBI) that warrant guidance.

Specifically, we recommend that Treasury and the IRS provide guidance on the following issues:

- I. Qualification of Rental Real Estate as a Trade or Business
- II. Modification of the Rental Property Recharacterization Rule (Prop. Reg. §1.199A-5(c)(2))
- III. Clarification of the *de Minimis* Rule in the Allocation Between specified service trade or business (SSTB) and Non-SSTB Activities
- IV. Clarification on the Definition of QBI
- V. Treatment of the Ordering Rule for Sections 465, 469, 704(d), and 1366(d)

¹ Including Treasury and the IRS’s notice of proposed rulemaking [REG-107892-18](#) (issued August 16, 2018) on the “Qualified Business Income Deduction,” the IRS [Notice 2018-64](#) on “Methods for Calculating W-2 Wages for Purposes of Section 199A,” and the IRS [Frequently Asked Questions](#) (FAQs) on the “Tax Cuts and Jobs Act, Provision 11011 Section 199A – Deduction for Qualified Business Income.”

² Unless otherwise indicated, hereinafter, all section references are to the Internal Revenue Code of 1986, as amended, or to Treasury Regulations promulgated thereunder.

- VI. Interaction of Section 199A with Section 461(l) for Purposes of Calculating QBI
- VII. Treatment of Relevant Passthrough Entities (RPEs)
- VIII. Clarification on the Aggregation Rules
- IX. Effect of Sections 743(b) and 734(b) Basis Adjustments on Unadjusted Basis Immediately After Acquisition (UBIA) of Qualified Property
- X. Effect of Sections 351, 721, and 1031 on UBIA of Qualified Property and the Depreciable Period
- XI. Disclosure of Section 199A Information When Owners of RPEs Are Below the Taxable Income Threshold

In the interest of fairness, the AICPA has also urged Congress to reconsider the exclusion of SSTBs from the lower effective tax rates allowed for individuals operating other types of businesses.³

The AICPA is the world's largest member association representing the accounting profession with more than 418,000 members in 143 countries and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

We appreciate your consideration of these comments and welcome the opportunity to discuss these issues further. If you have any questions, please contact me at (408) 924-3508 or Annette.Nellen@sjsu.edu; Troy Lewis, Chair, AICPA Qualified Business Income Task Force, at (801) 523-1051 or tlewis@sisna.com; or Amy Wang, AICPA Senior Manager – Tax Policy & Advocacy, at (202) 434-9264 or Amy.Wang@aicpa-cima.com.

Sincerely,



Annette Nellen, CPA, CGMA, Esq.
Chair, AICPA Tax Executive Committee

Encl.

cc: The Honorable Charles Rettig, Commissioner, Internal Revenue Service
Mr. Thomas A. Barthold, Chief of Staff, Joint Committee on Taxation

³ AICPA comment letter "[Tax Reform 2.0](#)," dated September 25, 2018.

AMERICAN INSTITUTE OF CPAs

**Guidance Concerning the Deduction for Qualified Business Income Under Section 199A of
the Internal Revenue Code**

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Guidance Concerning the Deduction for Qualified Business Income Under Section 199A of the Internal Revenue Code

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I. Qualification of Rental Real Estate as a Trade or Business

Overview

Proposed Reg. §1.199A-1(b)(13) (“proposed regulations”) provide that a trade or business is defined under a section 162⁴ judicial definition. As a result, the trade or business status of a real estate rental activity is uncertain and may lead to inconsistent treatment amongst taxpayers attempting to claim the section 199A qualified business income (QBI) deduction.

Recommendation

The Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) should provide assurance that rental real estate activities are generally considered a trade or business. Further, guidance is needed on whether there are specific circumstances in which rental real estate activities would not generate qualified trade or business income under the adopted section 162 trade or business standard.

Analysis

The preamble to the proposed regulations provides that for purposes of section 199A, the definition of a trade or business is provided under section 162(a). The large body of existing case law and administrative guidance interpreting the meaning of trade or business in the context of a broad range of industries is cited as support for utilizing this definition. Specifically, Prop. Reg. §1.199A-1(a)(13) provides that a trade or business is defined as a section 162 trade or business other than the trade or business of performing services as an employee.

However, the term “trade or business” is not defined in the Internal Revenue Code (IRC), Treasury regulations, or IRS guidance. As a result, no uniform standard definition exists and the determination of trade or business status is made on a case-by-case basis, sometimes with discrepancies within industries.

The Supreme Court adopted the notions of regularity (*i.e.*, activity over a certain period) and a profit motive as factors that other courts have widely accepted as establishing a trade or business.⁵ However, unlike several other industries, determining the extent to which the rental of real estate rises to the level of a section 162 trade or business is particularly difficult. In a Private Letter

⁴ Unless otherwise indicated, hereinafter, all section references are to the Internal Revenue Code of 1986, as amended, or to Treasury Regulations promulgated thereunder.

⁵ *Groetzinger*, 480 U.S. 23, 35 (1987) (See also *Higgins*, 312 U.S. 212 (1941); and *Dagres*, 136 T.C. 263 (2011)).

Ruling (PLR), the IRS readily admitted that there are no uniform standards for the rental of real estate, noting:

“The issue of whether the rental of property is a trade or business of a taxpayer is ultimately one of fact in which the scope of a taxpayer’s activities, either personally or through agents, in connection with the property, are extensive enough as to rise to the stature of a trade or business.”⁶

Consistent with this position, some real estate rentals have been historically considered by the IRS as section 212 activity rather than trades or businesses.⁷

In addition, the courts have long struggled to draw definitive lines on the trade or business issue. In *Murtaugh v. Commissioner*, 74 T.C.M. 75 (1997), the court ruled in favor of the taxpayer, a married couple, which was found engaged in a section 162 trade or business despite owning only a 25 percent time-share interest in two condominium units with the majority of the management work performed by an outside company acting as their agent.⁸ In *Anderson v. Commissioner*, 44 T.C.M. 1305 (1982), the court ruled for the IRS in the case of a taxpayer that rented a farm to a tenant farmer where the rental was deemed an investment because the taxpayer’s efforts were limited to paying bills related to the farm, depositing rent checks, keeping minimal records, and talking to the tenant occasionally on the phone.⁹ Despite similar fact patterns, the courts have issued contrary decisions on the trade or business issue.

The delineating factors establishing a real estate activity as a trade or business are not clear in the proposed regulations. Proposed Reg. §1.199A-1(d)(4) example 1 provides as a fact pattern a taxpayer renting what appears as undeveloped land to tenants in which no wages are paid and no depreciable property is present. The example, however, seems to assume away the trade or business issue by stating that the “business generated \$1,000,000 of QBI in 2018,” despite the lack of any operating expenses or mention of management activities. Further, example 2 in that section continues with the same facts, maintaining no paid wages but providing that \$10,000,000 of depreciable property was expended. These two examples under Prop. Reg. §1.199A-1(d)(4) suggest that the rental of vacant land rises to the level of a trade or business and generates QBI designation in example 1, despite no wages paid and no depreciable property.

Without further guidance clarifying when the rental of real estate would fail to rise to the level of a section 162 trade or business, unnecessary ambiguity exists that will likely create a divergence in practice. Taxpayers are thus left to pursue their own interpretation of the rules under section 199A and the IRS will likely face greater complexity of administration.

⁶ PLR 9840026.

⁷ See the commentary in Treasury Decision (TD) 9644, at 5.E.iii, effective date: December 2, 2013: “However, for several reasons, the Treasury Department and the IRS do not believe that every real estate professional is necessarily engaged in the trade or business of rental real estate.”

⁸ *Murtaugh*, T.C. Memo 1997-319.

⁹ *Anderson*, T.C. Memo 1982-576.

II. Modification of the Rental Property Recharacterization Rule (Prop. Reg. §1.199A-5(c)(2))

Overview

Proposed Reg. §1.199A-5 contains two anti-abuse rules designed to prevent the fracturing of a specified service trade or business (SSTB) in an attempt to qualify those separated parts for the section 199A deduction.

Recommendations

The AICPA agrees with the need for anti-abuse rules. However, we recommend modifications to those rules as follows:

1. Remove the 50 percent/80 percent rule from Prop. Reg. §1.199A-5(c)(2).
2. Clarify that the Prop. Reg. §1.199A-5(c)(2) rule only applies to common owners that form the greater than 50 percent ownership test.

Analysis

1. *Remove the 50 percent/80 percent rule from Prop. Reg. §1.199A-5(c)(2).*

Proposed Reg. §1.199A-5(c) has two anti-abuse rules. First, Prop. Reg. §1.199A-5(c)(2) provides that an SSTB includes any trade or business with 50 percent or more common ownership (directly or indirectly) that provides 80 percent or more of its property or services to an SSTB. Second, if a trade or business has 50 percent or more common ownership with an SSTB, to the extent that the trade or business provides property or services (but less than 80 percent) to the commonly-owned SSTB, the portion of the property or services provided to the SSTB is treated as an SSTB (meaning the income is treated as income from an SSTB).

For example, A, a dentist, owns a dental practice and an office building. A rents half the building to the dental practice and the other half to unrelated persons. Under Prop. Reg. §1.199A-5(c)(2), the renting of half of the building to the dental practice is treated as an SSTB.

The first rule (“50 percent/80 percent rule”) is not necessary. In the example, if the dentist rents 90 percent of the building to the dental practice, there is no abuse concern that the other 10 percent is not QBI. In a common situation in which several partners of an accounting firm acquire an 11-story building for the accounting firm to use, the individuals rent floors two through 11 to the accounting firm and the first floor to a deli, dry cleaner, and hair salon. If only the second rule described above is retained, the rent from the accounting firm is deemed an SSTB, but not the rent from the deli, dry cleaner, and hair salon. Even if the building is held by the accounting firm directly and rented to the deli, dry cleaner and hair salon, these amounts are separately reported on the accounting firm’s tax return as rental income. As separate books are required to accurately report the net rental income for section 469 purposes, it would likely qualify for QBI. Thus, the second rule provides the same protection as the first rule to address the government’s concern of

abuse. In fact, the example in the regulations regarding the law firm would have the same result if the 50 percent/80 percent rule was removed and the second rule was the only rule in place.

Therefore, removing the 50 percent/80 percent rule creates minimal risk while providing simplification for both taxpayers and the IRS.

2. *Clarify that the Prop. Reg. §1.199A-5(c)(2) rule only applies to common owners that form the greater than 50 percent ownership test.*

The operation of the rule for the non-common owner appears to treat the non-common owner of the business that provides property or service to an SSTB as the owner of an SSTB even if that person does not own an interest in the SSTB. In effect, the rule apparently recharacterizes the business as an SSTB to all owners. This interpretation is overreaching and Treasury and the IRS should revise the guidance.

Example:

Accounting Firm (AF) is a partnership that provides accounting services to clients and owns an office building housing its administrative staff. AF has three partners, A, B, and C. PRS, a partnership, owns the building solely occupied by AF. PRS has three equal partners, B, C, and D. D is unrelated to A, B, or C.

Based on Prop. Reg. §1.199A-5(c), because PRS and AF are owned more than 50 percent by A and B (because A & B collectively own 66.6 percent of both AF and PRS), the rule provides that PRS is a SSTB.

The intention of the rule is to provide that PRS is a SSTB with respect to income allocable to B and C. However, the rule appears to provide that PRS is an SSTB with respect to D's distributable share of rental income. Therefore, D is denied QBI treatment of the net rental income. If our interpretation is accurate with respect to D, Treasury and the IRS should reconsider the rule.

The recharacterization of an entire business as an SSTB based on ownership is too extensive. Treasury and the IRS can retain the proposed rule in its current form, but should clarify that it only applies to the common owners that make up the 50 percent ownership test.

By comparison, our recommendation is akin to a section 469 recharacterization rule. In the section 469 recharacterization rules (*e.g.*, Treas. Reg. §1.469-2(f)(6)), only the taxpayer's interest in the lessor activity is recharacterized as nonpassive because it is nonpassive in the lessee. The section 469 self-rental rule has no relevance to a taxpayer that is an owner of the lessor but not an owner of the lessee. The same result should apply to an owner of a business that provides services or property to an SSTB if the owner is not also an owner in the SSTB.

III. Clarification of the *de Minimis* Rule in the Allocation Between SSTB and Non-SSTB Activities

Overview

Section 199A(b)(2) provides that the deductible amount under section 199A is determined for each trade or business. Section 199A(d)(1) provides that a qualified trade or business does not include an SSTB. A *de minimis* rule is provided in Prop. Reg. §1.199A-5(c). If the trade or business has gross receipts of no more than \$25 million, a trade or business is not an SSTB if less than ten percent of the gross receipts are attributable to the performance of SSTB services. If the gross receipts are greater than \$25 million, the *de minimis* provision is applied at the five percent level.

No guidance is provided with respect to determining the QBI of a business that has SSTB income greater than the *de minimis* levels.

Recommendation

Treasury and the IRS should allow a single trade or business to determine its QBI based upon guidance provided for section 199. The taxpayer should have the ability to determine its income from SSTB activities and allocate costs to the SSTB activities in a manner similar to Treas. Reg. §1.199-4, with costs allocable to domestic production gross receipts. We recommend that taxpayers with average annual gross receipts not greater than \$25 million (determined at the entity level and considering related party aggregation of gross receipts) allocate between SSTB and non-SSTB based upon the small business simplified overall method of Treas. Reg. §1.199-4(f).

We recommend the use of the section 448 aggregation and related party tests to prevent the abusive use of the *de minimis* provision in the proposed regulations. Treasury and the IRS should also expand this *de minimis* rule. We recommend that if the non-SSTB gross receipts are less than 10 percent for a trade or business (determined before the separation between SSTB and non-SSTB), non-SSTB gross receipts are ignored and the entire trade or business is considered an SSTB. If the business has average annual gross receipts greater than \$25 million, Treasury and the IRS should apply a *de minimis* threshold of five percent rather than ten percent.

Analysis

Proposed Reg. §1.199A-5(c)(3)(ii) provides the example of a dermatologist with *de minimis* sales of skin care products. The example does not inform the taxpayer, however, as to the qualification for the 20 percent section 199A deduction if the sales of skin care products exceed the *de minimis* threshold. Treasury and the IRS should include an example illustrating the SSTB treatment if the skin care products exceed the *de minimis* threshold.

Taxpayers and the IRS require an administrable determination of QBI. Mechanisms are needed to reduce conflicts. Congress has determined that the 20 percent deduction for QBI is not available for businesses defined as SSTBs. Congress has also determined taxpayers with tentative taxable income above the threshold levels must determine the QBI amount based upon each separate trade or business.

Taxpayers may have engagement in more than one business with different methods of accounting for each trade or business.¹⁰ No trade or business is considered separate and distinct for purposes of determining its method of accounting unless a complete and separable set of books and records is kept for such trade or business, per Treas. Reg. §1.446-1(d)(2). The regulation does not require separate books and records for each trade or business, or keeping the books and records separate. It merely requires that the books and records are separable, implying that the taxpayer may employ means of separating aspects of its trades and businesses from one set of books and records.

Businesses determine gross receipts or gross revenues based on different revenue streams, including those derived from an SSTB and a non-SSTB. To the extent a revenue stream is a separable trade or business, the taxpayer must allocate costs and expenses to the separable trade or business. Treasury has provided for this mechanism before in Treas. Reg. §1.199-4, with costs allocable to domestic production gross receipts (DPGR). When determining qualified production activities income, the taxpayer must subtract from DPGR the costs of goods sold allocable to the DPGR.¹¹ Other deductions may allocate based upon the section 861 method¹² or the simplified deduction method.¹³ Qualifying small taxpayers were allowed to use the small business simplified overall method to allocate costs of goods sold and other costs and deductions based upon relative gross receipts.

IV. Clarification on the Definition of QBI

Overview

Section 199A(c)(1) provides that “qualified business income” is the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer. Left unstated in the Code and in the proposed regulations is the definition of the word “qualified” as a modifier to the phrase “items of income, gain, deduction and loss.”

Recommendations

Treasury and the IRS should provide guidance with respect to the many items of income, gain, deduction and loss (“Items”) reported on tax returns beyond that reported on Schedules C, F and K-1. Guidance should treat items reported on Form 4797, for which depreciation was claimed against QBI, as QBI (*e.g.*, sections 1245 and 1250 gain and section 1231 losses not otherwise netted against section 1231 gains).

Specifically, Treasury and the IRS should address the following Items:

1. Treatment of qualified retirement plan contributions as not associated with a trade or business;
2. Reduction in QBI by the interest expense to acquire partnership and S corporation interests;

¹⁰ See Treas. Reg. §1.446-1(d)(1).

¹¹ See Treas. Reg. §1.199-4(b).

¹² See Treas. Reg. §1.199-4(d).

¹³ See Treas. Reg. §1.199-4(e).

3. Reduction in QBI for deduction of unreimbursed partnership expenses;
4. Treatment of section 1244 losses;
5. Simplification of the rules for self-employed health insurance under section 162(l);
6. Allocation of the deduction for one-half of self-employment tax under section 164(f); and
7. Disregard for state income tax associated with QBI.

Analysis

The above Items are included as examples of income, gains, deductions, and losses that appear on forms or schedules of an individual tax return as taxable or deductible business items. Taxpayers may have uncertainty as to how to treat these items under section 199A.

To the extent that depreciation reduced QBI in prior years, we recommend that the gain associated with depreciation recapture under sections 1245 and 1250 restore the reduction to income as QBI. The taxpayer should assign the depreciation recapture gain to the taxpayer's trade or business from which the depreciation was deducted.

1. *Treatment of qualified retirement plan contributions as not associated with a trade or business.*

Section 172(d)(4)(D) provides that for purposes of the net operating loss (NOL) computation, deductions allowed under section 404 (deduction for contributions of an employer to an employee's trust or annuity plan and compensation under a deferred-payment plan) are not treated as attributable to the trade or business of the individual. We recommend following the treatment under section 172 as evidence of Congressional intent to consider qualified retirement plan contributions as not associated with a trade or business.

2. *Reduction in QBI by the interest expense to acquire partnership and S corporation interests.*

IRS Notice 89-35 provides guidance on how to treat interest expense attributable to passthrough entities. Interest expense incurred to acquire partnership and S corporation ownership interests is deductible as a business expense if associated with the business assets of the passthrough entity. The taxpayer is allowed to use any reasonable method in allocating the interest expense among the assets of the entity. The taxpayer must have made the determination that the interest expense is associated with the business or rental activity of the passthrough entity. Since there is minimal complexity associated with the QBI determination of this interest expense, we recommend that the interest expense to acquire the ownership of a business passthrough entity reduce QBI.

3. *Reduction in QBI for deduction of unreimbursed partnership expenses.*

Partners are allowed to deduct unreimbursed partnership expenses.¹⁴ The deduction mandates that the partnership agreement (pursuant to partnership practice) require that a partner pay certain partnership expenses out of his or her own funds. To prevent abuse of this rule, Treasury and the

¹⁴ Revenue Ruling (Rev. Rul.) 70-253 (pursuant to the partnership agreement); *Fred S. Klein v. Comm.*, 25 T.C. 1045 (1956), acq. 1956-2 CB 6 (pursuant to partnership practice); IRS Pub. 587.

IRS should provide that QBI is reduced to the extent the partner is allowed a deduction for unreimbursed partnership expenses.

4. Treatment of section 1244 losses.

A loss on section 1244 stock issued to an individual or to a partnership is treated as an ordinary loss. The loss originates from the sale or exchange of a capital asset. Capital losses for purposes of the exception from QBI listed at section 199A(c)(3)(B)(i) should include all items initially defined as capital losses, even though treated as ordinary losses.

5. Simplification of the rules for self-employed health insurance under section 162(l).

Section 162 provides for the deduction of all ordinary and necessary expenses paid or incurred in carrying on any trade or business. Section 162(l) includes certain medical insurance expenses as deductions under section 162. Insurance that constitutes medical care for the taxpayer, the taxpayer's spouse, the taxpayer's dependents and any child (as defined in section 152(f)(1)) of the taxpayer who has not attained age 27 at the end of the year is a deduction under section 162. Although guidance requires that these deduction amounts are associated with specific trades or businesses, Treasury and the IRS should simplify the rules by not including these amounts in the determination of QBI.

6. Allocation of the deduction for one-half of self-employment tax under section 164(f).

Section 164(f)(2) provides that the deduction for one-half of the self-employment tax is a deduction attributable to a trade or business for purposes of this chapter. "This chapter" is Chapter 1, which includes section 199A. However, in support of simplicity, Treasury and the IRS should disregard the deduction for one-half of the self-employment tax in the determination of QBI. Otherwise, taxpayers with multiple trades or businesses subject to self-employment tax must allocate the deduction to the many businesses (partnerships and proprietorships) generating self-employment income (which may include both SSTB and non-SSTB businesses).

7. Disregard for state income tax associated with QBI.

State income tax associated with business income is a business deduction for computing the taxpayer's NOL under section 172.¹⁵ Including this state income tax amount in the QBI computation requires the determination of which tax is included in the \$10,000 limitation under section 164(b)(6) (state income associated with business income, state income tax associated with nonbusiness income, real property tax). We recommend that the determination of QBI ignores state income tax.¹⁶

¹⁵ Rev. Rul. 70-40.

¹⁶ Additionally, to carry out this recommendation, a modification of Part C of the example in Prop. Reg. 1.199A-6(d)(3)(iv) is needed. We recommend that the "...and \$1,000 of state and local taxes are directly attributable under §1.652(b)-3(a) to Trust's business income" is stricken. This statement is inconsistent with Rev. Rul. 81-188 (providing certain types of taxes as above-the-line taxes that are not taxes of general applicability) and inconsistent with Treas. Reg. §1.652(b)-3(c) which functionally should produce the same result as Treas. Reg. §1.62-1T(d) for estates and trusts.

V. Treatment of the Ordering Rule for Sections 465, 469, 704(d), and 1366(d)

Overview

Proposed Reg. §1.199A-3(b)(1)(iv) provides that, to the extent that any previously disallowed losses or deductions are allowed in the taxable year, they are treated as items attributable to the trade or business. However, losses or deductions that were disallowed for taxable years beginning before January 1, 2018, are not taken into account for purposes of computing QBI in a later taxable year.

Recommendations

Loss items suspended by other code provisions prior to the creation of QBI should not have an impact on the calculation of the new section 199A deduction. We understand the need for the rule. However, the rule as written is too ambiguous to serve effectively. For the rule to provide a mechanically viable purpose, Treasury and the IRS should expand the final Prop. Reg. §1.199A-3(b)(1)(iv) to take into account the following:

1. Provide an ordering rule to address suspended amounts within sections 465, 469, 704(d), and 1366(d) that occur post-2017 and pre-2018.
2. Provide an ordering rule to address suspended amounts within sections 465, 469, 704(d), and 1366(d) that occur post-2017 but contain QBI and non-QBI items.
3. Clarify that an amount originating in a trade or business prior to 2018 will retain its status as a pre-2018 item as it moves through sections 465, 469, 704(d), and 1366(d).
4. Provide a rule clarifying the treatment of suspended SSTB losses.

Analysis

1. *Provide an ordering rule to address suspended amounts within sections 465, 469, 704(d), and 1366(d) that occur post-2017 and pre-2018.*

Prior to the release of these proposed regulations, we are not aware of any situation within the history of sections 465, 469, 704(d), and 1366(d) where taxpayers were required to track “vintages” of losses similar to the requirement in sections 170 and 172. In order for the proposed rule to operate effectively, Treasury and the IRS should adopt a first-in, first-out rule (FIFO) that aligns with the carryover rules in sections 170 and 172.

2. *Provide an ordering rule to address suspended amounts within sections 465, 469, 704(d), and 1366(d) that occur post-2017 but contain QBI and non-QBI items.*

Our second recommendation is to provide an ordering rule to address suspended amounts within sections 465, 469, 704(d), and 1366(d) that occur post-2017 but contain QBI and non-QBI items. On its face, this recommendation appears similar to the suggestion in the paragraph above, but it serves a different purpose. A single suspended item, such as an ordinary loss from business operations, could comprise QBI and non-QBI amounts.

The following two examples illustrate the issue:

Example 1:

Assume PRS, a domestic partnership, has a business loss of \$120, which is comprised of a \$90 loss from domestic sources (which is negative QBI) and a \$30 loss from non-US sources (which is not QBI). This loss is fully suspended by section 469. When the taxpayer has passive income of \$50 from operations in the following year that releases \$50 of the loss, the rules should consider the \$50 suspended loss. Treasury and the IRS should treat some portion of that \$50 as QBI and some portion not as QBI. We suggest that a rule that provides that 75 percent of the loss (90/120) is treated as negative QBI is a reasonable approach.

Example 2(A):

Assume XYZ, a domestic S corporation, has a business loss of \$30 which is comprised of a \$90 loss from domestic sources (which is negative QBI) and \$60 of net income from non-US sources (which is not QBI). This \$30 loss is fully suspended by section 469. In Year 2, the domestic S corporation has net income of \$40 from domestic sources and \$10 of income from foreign sources. In this situation, such a rule would provide that 100 percent of the \$30 loss is negative QBI when ultimately released. Thus, QBI is \$10 in Year 2.¹⁷

Example 2(B):

Assume the opposite of Example 2(A). The S corporation has a business loss of \$30 which is comprised of \$60 of income from domestic sources (which is QBI) and \$90 of loss income from non-US sources (which is not QBI). This \$30 loss is fully suspended by section 469. It appears in this case that the taxpayer would have \$60 of QBI in Year 1. In Year 2, the domestic S corporation has net income of \$40 from domestic sources and \$10 of income from foreign sources. In this case, the rule would provide that the \$30 passive activity loss (PAL) is fully utilized, but the shareholder's QBI for the year is \$40.

It may appear unusual for a taxpayer to have QBI (\$60 in Year 1 and \$40 in Year 2) that is greater than the overall income from the activity (\$0 in Year 1 and \$20 in Year 2), but there is no rule in the statute or regulations to prevent this occurrence. However, this issue does not create significant concern because the overall limitation of 20 percent of ordinary taxable income will take into account the netting of the foreign and domestic amounts.

3. *Clarify that an amount originating in a trade or business prior to 2018 will retain its status as a pre-2018 item as it moves through sections 465, 469, 704(d), and 1366(d).*

The ordering rule, for example, should provide that a loss incurred in a partnership in 2016 that was suspended by section 465 retains its status as a pre-2018 loss if the taxpayer has sufficient

¹⁷Prop. Reg. §1.199A-1(c)(2) would treat the \$60 domestic loss that is deducted in the current year as negative QBI that could carryover to Year 2 (assuming the taxpayer has no QBI from other sources). Therefore, our proposed rule dealing with identifying the QBI imbedded in the passive loss should only consider negative QBI after Prop. Reg. §1.199A-1(c)(2) is applied. As a result, although the taxpayer would have \$10 of QBI under the PAL rule in Year 2, Prop. Reg. §1.199A-1(c)(2) would then cause the \$60 carryover to apply and reduce the QBI to \$0. Accordingly, Prop. Reg. §1.199A-1(c)(2) would cause \$50 of negative QBI to carryforward into Year 3. There are no PALs coming into Year 3, so the PAL rule is simply not applicable.

amounts at-risk in 2018 to allow the loss, but the loss is suspended by section 469. We recommend that the rule clarify that, even though the amount is suspended by section 469 in 2018, the loss originated in 2016 and thus will not reduce QBI when it is ultimately allowed under the section 469 rules in a post-2017 year.

4. Provide a rule clarifying the treatment of suspended SSTB losses.

We recommend that the final regulations clarify the treatment of a suspended SSTB loss when it is ultimately released. For example, the taxpayer has taxable income of \$500,000 in 2019, when the taxpayer incurs a \$10,000 loss from an SSTB suspended under section 469. If the loss is released in 2020, when the taxpayer has income of \$140,000, the regulations should address whether the loss is negative QBI. It was not QBI when it was suspended because the taxpayer was over the threshold; therefore, it is reasonable to conclude that the year of origination tests SSTB status and it remains in SSTB until the loss is ultimately allowed. Conversely, if the taxpayer only has \$90,000 of taxable income, the net loss from a suspended SSTB is treated as QBI because the taxpayer's taxable income is under the threshold. If the suspended SSTB loss is released when the taxpayer has taxable income of \$500,000, consistency requires that it is treated as negative QBI.

We recognize that the taxpayer could also test a rule that provides the SSTB status of a loss when it is ultimately allowed. However, this alternative is more complex for taxpayers and the IRS to administer.

VI. Interaction of Section 199A with Section 461(l) for Purposes of Calculating QBI

Overview

Proposed Reg. §1.199A-1(d)(2)(iii) contains negative QBI carryover rules. In addition, Prop. Reg. §1.199A-3(b)(1)(v) contains a unique NOL rule. The proposed regulations provide that generally, a deduction under section 172 for an NOL is not considered attributable to a trade or business and, therefore, is not taken into account in computing QBI. However, to the extent the NOL is comprised of amounts attributable to a trade or business that were disallowed under section 461(l), the NOL is considered attributable to that trade or business and will constitute negative QBI. For the rule to properly address the concern expressed in the preamble, Treasury and the IRS should make modifications. Currently, it is not clear how the negative QBI carryover rules operate.

Recommendations

Treasury and the IRS should clarify the negative QBI carryover rules to provide that the amount considered negative QBI under Prop. Reg. §1.199A-3(b)(1)(v) is the lesser of:

1. The negative total QBI amount carried over to the following year under Prop. Reg. §1.199A-1(d)(2)(iii); or
2. The amount disallowed under section 461(l).

Additionally, in the preamble to the section 199A proposed regulations, Treasury and the IRS requested comments regarding the interaction of section 199A and 461(l) generally. Guidance

should clarify that the section 199A deduction is not a business loss considered in the excess business loss of section 461(l) computation.

Analysis

The following example illustrates the need for a modification to these rules:

Example 1:

If an individual has an operating loss of \$600,000 from a non-SSTB, section 461(l) will result in \$100,000 as disallowed in the current year, and subsequently convert that loss to an NOL in the following year. In this case, the regulation appears to conclude that the negative total QBI rule in Prop. Reg. §1.199A-1(d)(2)(iii) will result in treatment of \$500,000 as a carryover QBI attribute. The NOL section 461(l) rule in Prop. Reg. §1.199A-3(b)(1)(v) will treat the \$100,000 as negative QBI in the following year. As a result, the taxpayer has \$600,000 of total QBI loss next year.

What is not clear from Prop. Reg. §1.199A-3(b)(1)(v) is what happens when the taxpayer has a QBI loss of \$400,000 and a non-QBI loss of \$200,000 (assume the non-QBI loss is from an SSTB). The section 461(l) excess business loss disallowance is \$100,000 (similar to Example 1 above) that is treated as an NOL in the following year. However, it is not clear how much of that section 461(l) NOL reduces QBI. The taxpayer's \$400,000 negative QBI is carried over under the general rule in Prop. Reg. §1.199A-1(d)(2)(iii). Therefore, the section 461(l) disallowance is not necessary to add to the negative QBI. The lesser of (A) \$0 or (B) \$100,000 would result in no portion of the section 461(l) NOL considered negative QBI in the following year under Prop. Reg. §1.199A-3(b)(1)(v).

A simpler approach is to provide that the negative QBI carryover rule in Prop. Reg. §1.199A-1(d)(2)(iii) is determined without regard to section 461(l) (*i.e.*, before the application of section 461(l)). This approach would eliminate the need for Prop. Reg. §1.199A-3(b)(1)(v) because it would result in \$600,000 of negative QBI in the first example and \$400,000 of negative QBI in the second example. It would remove a pre-2018, QBI related, or non QBI related NOL, to exist as is, untouched by section 199A. This approach is simpler and retains the two carryover systems independent from one another.

VII. Treatment of Relevant Passthrough Entities (RPEs)

Overview

According to Prop. Reg. §1.199A-1(b)(9), an RPE is a partnership, other than a publicly traded partnership (PTP), or an S corporation that is owned directly or indirectly by at least one individual, estate, or trust. A trust or estate is treated as an RPE to the extent it passes through QBI, Form W-2 wages, Unadjusted Basis Immediately After Acquisition (UBIA) of qualified property, qualified real estate investment trust (REIT) dividends, or qualified PTP income.

Recommendations

Treasury and the IRS should provide the following guidance:

1. Expand the definition of an RPE to include a regulated investment company (RIC)¹⁸ and a common trust fund (CTF).¹⁹
2. Clarify that estates and trusts are not considered RPEs for the aggregation rules.

Specifically, we recommend that trusts and estates have the ability to aggregate businesses under Prop. Reg. §1.199A-4 in the same manner as that of an individual, regardless of whether the trust or estate distributes income during the year.

Analysis

1. *Expand the definition of an RPE to include a RIC and a CTF.*

Allowing the QBI pass through nature of RICs and CTFs is consistent with the overall legislative scheme embodied in sections 851-855 (for RICs) and section 584 (for CTFs). These entities are not often considered fully fiscally transparent entities for federal tax purposes. There is a long history of allowing shareholders to look through these entities for purposes of identifying income with preferential tax rates. Although Congress did not alter section 1 to provide for a special tax rate for QBI, congressional intent behind the QBI deduction is to create a preferential rate for QBI. Therefore, not recognizing RICs and CTFs as RPE is potentially in opposition to the legislative intent.

2. *Clarify that estates and trusts are not considered RPEs for the aggregation rules.*

Estates and trusts share many characteristics with S corporations and partnerships that can result in consideration of estates and trusts as RPEs. However, Treasury and the IRS should consider trusts and estates as RPEs solely for the allocation of QBI, Form W-2 wages, UBI of qualified property, qualified REIT dividends, or qualified PTP income between the entity and the beneficiary. Trusts and estates should have the ability to aggregate businesses under Prop. Reg. §1.199A-4 in the same manner as that of an individual, regardless of whether the trust or estate distributes income during the year.

The example in Prop. Reg. §1.199A-6 provides that the trust aggregates before distributing income. However, it appears that Prop. Reg. §1.199A-6(d)(1) would allow aggregation only after distributions. The hybrid nature of trusts and estates as partial RPEs adds unnecessary complexities that aggregation could alleviate.

¹⁸ As defined in section 851.

¹⁹ As defined in section 584.

VIII. Clarification on the Aggregation Rules

Overview

Proposed Reg. §1.199A-4 sets forth aggregation rules for when taxpayers may treat multiple trades or businesses as a single trade or business for purposes of applying the limitations in Prop. Reg. §1.199A-1(d)(2)(iv). Proposed Reg. §1.199A-4(b)(3) sets forth the family attribution rules that attributes ownership by a taxpayer's spouse or children, grandchildren, and parents to the taxpayer.

Recommendations

Treasury and the IRS should provide the following guidance:

1. Clarify that aggregation is permitted at the RPE level; and
2. Provide guidance that Prop. Reg. §1.199A-4(b)(3) should use existing attribution rules under sections 267 and 707 rather than creating a new operating rule.

Analysis

1. *Clarify that aggregation is permitted at the RPE level.*

Treasury Reg. §1.469-4(d)(5) allows a partnership or S corporation the option to group activities at the entity level. Once grouping is determined by the partnership or S corporation, the partner or shareholder must follow that grouping. If grouping is not determined by the partnership or S corporation, the partner or shareholder may thereafter select a proper grouping. We recommend a similar rule for aggregation under Prop. Reg. §1.199A-4.

Allowing the RPE the option to aggregate at the entity level may avoid unnecessary reporting in certain circumstances. The RPE will generally select aggregation at the entity level when such a grouping would broadly benefit the RPE partners or shareholders. The RPE may select aggregation at the entity level when Treasury and the IRS would have permitted such aggregation at the individual partner or shareholder level. Once aggregation is determined by the RPE, the partner or shareholder is bound by that aggregation. Under this elective regime, if the RPE has not determined aggregation, then the partner or shareholder may thereafter apply the aggregation rules under Prop. Reg. §1.199A-4 on such individual's separate return.

Within the existing proposed section 199A aggregation regime, non-majority owners may benefit from common ownership in allowing for aggregation on the individual return of such non-majority investor. Presumably, such non-majority owners will require the RPE to provide information on the common ownership necessary to allow for this aggregation. Comments were requested on whether Treasury and the IRS should require reporting or other information sharing requirements. In response to the request for comments, we think that by allowing the RPE to aggregate at the RPE level, it potentially avoids the requirement to provide further ownership information (including attribution information) to non-majority owners, in certain circumstances.

Example:

Assume an upper-tier RPE is owned by eighty-five partners (80 percent owned by founder and 20 percent owned by employees of the company). The RPE has multiple trades or businesses that sell products that are customarily offered together, and each trade or business shares significant centralized business elements with one another. Providing the option for the upper-tier RPE to aggregate all of the lower-tier trades or businesses together would simplify the reporting otherwise required on separate schedules K-1, by likely arriving at the same result as if Treasury and the IRS had not allowed RPE aggregation.

The preamble to the proposed regulations stated that if the reporting requirements allowed for aggregation at the entity level, it would result in complexity for both taxpayers and the IRS. To the contrary, we think that providing the RPE with the option to aggregate would simplify the reporting process.

To the extent that the IRS believes that aggregation at the RPE level has more burdens and risks than benefits, we recommend that the guidance allows one exception to the prohibition on RPE aggregation. This sole exception applies if the RPE is (A) owned solely by individuals, estates and trusts (and disregarded entities owned by those entities, as defined in Treas. Reg. §301.7701-3), and (B) the owners would have the option to aggregate because the relevant requirements in Prop. Reg. 1.199A-4(b)(1) have been satisfied.

2. *Provide guidance that Prop. Reg. §1.199A-4(b)(3) should use existing attribution rules under sections 267 and 707 rather than creating a new operating rule.*

Multiple advantages exist for utilizing the attribution rules under sections 267 and 707 instead of creating a new attribution rule under section 199A.

First, the rules under sections 267 and 707 are well-established and familiar to most practitioners. Therefore, using those rules for attribution for purposes of aggregation under section 199A would result in improved compliance. Having a different family attribution rule for section 199A could result in confusion and inadvertent misapplication of the rule.

Second, many family businesses include siblings. To exclude siblings from the attribution rule would arbitrarily disadvantage businesses that have sibling ownership. Sibling ownership is more likely in a business held and operated by the second or later generation. As there are already obstacles for family businesses that are run by a successive generation, treating them differently for tax purposes would further disadvantage such a business.

Congress intended section 199A to benefit businesses that are not organized as C corporations; many of these businesses are family owned. There is no policy reason to treat businesses owned primarily by the first generation and their children differently from a business owned primarily by the children after the parents are deceased or have transferred their ownership to their children.

For this reason, the AICPA recommends that the attribution rule under Prop. Reg. §1.199A-4(b)(3) reference attribution under sections 267 and 707 instead of creating a new attribution rule.

IX. Effect of Sections 743(b) and 734(b) Basis Adjustments on UBIA of Qualified Property

Overview

Proposed Reg. §1.199A-2(c)(1)(iii) provides that sections 734(b) and 743(b) are not treated as qualified property for purposes of section 199A.

Recommendations

Treasury and the IRS should provide the following guidance:

1. Section 743(b) adjustment:
Allow a transferee partner to treat a section 743(b) basis adjustment allocable to depreciable tangible property as separate qualified property; and
2. Section 734(b) adjustment:
Provide the remaining partners with the ability to treat their respective share of a section 734(b) basis adjustment allocable to depreciable tangible property as separate qualified property for section 199A purposes; or
3. Alternative option:
If the two recommendations above are not adopted, Treasury and the IRS should allow taxpayers to exclude the amount of depreciation attributable to a section 734(b) or 743(b) basis adjustment from QBI.

Analysis

In the preamble to the proposed regulations, Treasury and the IRS explain that treating partnership special basis adjustments as qualified property could result in duplication of the UBIA of qualified property. For example, the proposed regulations provide a case where the fair market value of the property has not increased and the depreciable period has not ended at the time that the basis adjustment is generated.

1. Section 743(b) adjustment.

Section 743(b) basis adjustments arise when a partnership interest is sold or exchanged and either the partnership has a valid section 754 election in effect or the partnership has a substantial built-in loss.²⁰ A positive section 743(b) adjustment results to the extent that the transferee partner's basis in the partnership interest (outside basis) exceeds the transferee's share of the partnership's adjusted basis of partnership property (inside basis); a negative section 743(b) adjustment results to the extent inside basis exceeds outside basis. This basis adjustment is made with respect to the transferee partner only (*i.e.*, the partnership does not adjust the common basis in the partnership property).

²⁰ Section 743(d) defines a substantial built-in loss as either (1) the partnership's adjusted basis in the partnership property exceeding its fair market value by more than \$250,000 or (2) the transferee partner allocation of more than \$250,000 of losses if the partnership assets were sold for its fair market value.

A transferee partner's initial outside basis in the purchased interest is its cost. Section 743(b) provides a transferee partner the ability of treatment as if it had acquired a direct interest in the partnership's assets. Thus, the transferee's basis in the partnership assets should equal its outside basis in the partnership interest immediately after acquisition. In this respect, partners should treat a section 743(b) basis adjustment allocable to depreciable property as separate qualified property if the fair market value of the depreciable property at the time that the transferee partner acquires the partnership interest exceeds the partner's share of the adjusted tax basis at the time that the partnership originally acquired the property.

2. Section 734(b) adjustment.

Section 734(b) basis adjustments arise when property is distributed by a partnership and either a valid section 754 election is in effect or there is a substantial basis reduction.²¹ A positive section 734(b) adjustment results to the extent that (1) a distributee partner recognizes gain under section 731(a)(1) and (2) the partnership's adjusted basis in distributed property exceeds the distributee partner's basis in such property. A negative section 734(b) adjustment results to the extent that (1) a distributee partner recognizes loss under section 731(a)(2) and (2) the distributee partner's basis in distributed property exceeds the partnership's adjusted basis in such property. The basis adjustment is made to the common basis of the partnership property and benefits the continuing partners of the partnership after the distribution event.

These basis adjustments arise only when the general nonrecognition rule under section 731(a) and the general carryover basis rule under section 732(a) do not apply. Thus, partners should treat their share of section 734(b) basis adjustment allocable to depreciable property as separate qualified property for section 199A purposes.

3. Alternative option.

In the interest of fairness and equity, if either or both sections 743(b) and 734(b) basis adjustments are not allowed as separate qualified property, Treasury and the IRS should allow taxpayers to exclude depreciation attributable to either basis adjustment from QBI. This guidance would provide parity between the determination of UBI of qualified property and the effect of depreciation associated with the basis adjustments on QBI.

Additionally, see Item 2 in the attached Appendix for additional basis altering provisions that Treasury and the IRS should consider.

²¹ Section 734(d) provides that a substantial basis reduction exists if the sum of any loss recognized under section 731(a)(2) and the excess of a distributee partner's basis in distributed property over the partnership's basis in such property exceeds \$250,000.

X. Effect of Sections 351, 721, and 1031 on UBIA of Qualified Property and the Depreciable Period

Overview

The UBIA of qualified property acquired in a like-kind exchange, involuntary conversion, or section 168(i)(7) transaction (*i.e.*, certain nonrecognition transactions, such as section 721 and section 351 transfers) equals the adjusted basis at the time of exchange, conversion, or transfer, except to the extent that the basis of the replacement property or transferred property in hands of the transferee exceeds the basis of the relinquished or transferred property in the hands of the transferor. Meanwhile, the depreciable period of the replacement property and transferred property begins on date the relinquished or original property was first placed into service.

Recommendations

Treasury and the IRS should align the UBIA and depreciable period of qualified property in order to allow the following:

1. The UBIA of replacement or section 168(i)(7) property equals the original cost basis that the transferor had in such property and the depreciable period begins on the date that the property was originally placed in service by the transferor; or
2. The UBIA of replacement or section 168(i)(7) property equals the adjusted basis on the date of the exchange, conversion, or transfer and the depreciable period begins on that date.

Analysis

The UBIA and the beginning of the depreciable period of qualified property that is acquired in either a section 168(i)(7) transaction or in a like-kind exchange or involuntary conversion are not afforded consistent treatment in Prop. Reg. §199A-2(c)(2) and (3), discussed as follows. We recommend providing taxpayers with the ability to determine both the UBIA and the start of the depreciable period of qualified property by reference to either:

1. The date of the like-kind exchange, involuntary conversion, or the section 168(i)(7) transaction; or
2. The date the underlying property was originally placed in service by the individual or RPE that relinquished or transferred the property.

For sections 1031 and 1033 property, Prop. Reg. §1.199A-2(c)(2)(iii) provides that the depreciable period of modified accelerated cost recovery system (MACRS) qualified property²² acquired in a like-kind exchange or involuntary conversion (*i.e.*, the replacement property) is bifurcated as follows:

²² See Treas. Reg. §1.168(i)-6(b)(1).

1. With respect to the exchanged basis, the date on which the relinquished property was first placed in service; and
2. With respect to the excess basis, the date on which replacement property was first placed in service.²³

However, the UBIA of the exchanged basis of the replacement property equals the adjusted basis on the date of the exchange or conversion.²⁴

For section 168(i)(7) property, Prop. Reg. §1.199A-2(c) provides that the depreciable period of the MACRS qualified property acquired in a section 168(i)(7) transaction (including transfers to a partnership pursuant to section 721 or a corporation pursuant to section 351) begins on the date that the transferred property was originally placed in service by the transferor to the extent that the transferee's basis in the transferred property equals the adjusted basis in the hands of the transferor. Meanwhile, the UBIA of the transferred property equals the basis determined under section 723 or section 362, as applicable, on the date of the transfer to the partnership or S corporation. Treasury and the IRS should align the UBIA and depreciable period of qualified property.

XI. Disclosure of Section 199A Information When Owners of RPEs Are Below the Taxable Income Threshold

Overview

Treasury and the IRS requested comments as to the administrability of providing a special rule with regards to the Section 199A deduction such that if none of the owners of an RPE have taxable income above the threshold amount, there is no requirement for the RPE to determine and report W-2 wages, UBIA of qualified property, or whether the trade or business is an SSTB.

Recommendations

Treasury and the IRS should consider the following recommendations:

1. All RPEs should provide the amounts of QBI, W-2 wages, and the UBIA of qualified property for each trade or business on Schedules K-1, in addition to the determination as to whether any trade or business is an SSTB;
2. The failure to provide the above information is a determination the RPE has no QBI, W-2 wages, and UBIA of qualified property (respectively); and
3. Guidance should provide who is responsible for corrections and penalties due to the failure to disclose the information on Schedules K-1 when the determination affects the individual owner's deduction for QBI.

²³ If the individual or RPE makes an election pursuant to Treas. Reg. §1.168-6(i)(1), the depreciable period of the exchanged basis and excess basis in the replacement MACRS property begins on the date that the replacement property is placed in service.

²⁴ Prop. Reg. §1.199A-2(c)(3).

Analysis

Partners and shareholders of RPEs will need to rely on information provided on Schedule K-1 to compute their section 199A deductions. We caution against providing a special rule to allow RPEs with only owners below the threshold to opt out of reporting. RPEs do not normally have knowledge of the taxable income of both direct and indirect partners and shareholders. A certification process by the owners will create administrative burdens. Regulations should provide the assumption that the failure to include an item necessary for the section 199A computation is a disclosure of “zero” for that item.



AMERICAN INSTITUTE OF CPAs
Guidance Concerning the Deduction for Qualified Business Income
Under Section 199A of the Internal Revenue Code

Developed by the AICPA Qualified Business Income Task Force

Item #	Topic	Description of Item	IRC Section
Additional Recommendations for Guidance			
1.	Charitable Remainder Trust (CRT)	<ul style="list-style-type: none"> • Provide guidance that the CRT should calculate the section 199A deduction at the trust level. In order to apply taxable income, wage and unadjusted basis immediately after acquisition (UBIA) thresholds and/or limitations, the CRT would calculate its taxable income each year (starting in 2018) and use that number solely for section 199A purposes. The Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) should treat the CRT as a single taxpayer for threshold purposes. <i>Example:</i> <ul style="list-style-type: none"> ○ In 2018, the CRT receives rental income from a 50 percent interest in a trade or business of \$200,000. The total wages paid by the business for 2018 was \$100,000. The unadjusted basis of the property held by the business was \$2,500,000. The CRT calculates its taxable income for the year, and it is \$300,000. Therefore, the CRT must apply the wage and UBIA limitations. The wage amount attributable to the CRT’s 50 percent interest is \$50,000 and the UBIA attributable to the CRT’s 50 percent interest is \$1,250,000. 20 percent of the rental income is \$40,000 (200,000 x 0.2). The first limitation (50 percent of wages) is \$25,000. The second limitation (25 percent of wages and 2.5 percent of UBIA) is \$43,750 ((50,000 x 0.25) + (1,250,000 x 0.025)). The greater of the two limitations is \$43,750; therefore, the 20 percent deduction is not limited. Moreover, as 20 percent of the CRT’s taxable income exceeds \$40,000, there is no further limitation. The CRT applies the \$40,000 deduction and records \$160,000 of ordinary income. • Confirm that if QBI is also unrelated business taxable income (UBTI) to the CRT, the 20 percent deduction would apply before application of the 100 percent excise tax. 	199A
2.	Gift Transactions	<ul style="list-style-type: none"> • Provide guidance on certain gift transactions that can affect UBIA. <ul style="list-style-type: none"> ○ Situations exist where basis is adjusted in non-sale transactions. ○ Basis is adjusted upward when there are gifts of assets that have suspended losses under sections 465 and 469. ○ Basis adjustments can also occur when gift tax is paid on gifts. 	199A, 465, 469

Item #	Topic	Description of Item	IRC Section
3.	Gross Receipt Indexing of the <i>de Minimis</i> Rule	<ul style="list-style-type: none"> • Adopt the section 448(c)(1) \$25 million gross receipts threshold standard for purposes of the <i>de minimis</i> rule of Prop. Reg. §1.199A-5(c)(1). <ul style="list-style-type: none"> ○ Prop. Reg. §1.199A-5(c)(1)(i) provides that for purposes of applying the gross receipts <i>de minimis</i> rule, a trade or business with gross receipts of \$25 million dollars or less for the taxable year is not considered a specified service trade or business (SSTB) if less than 10 percent of the gross receipts of the trade or business are attributable to the performances of services of an SSTB. Likewise, Prop. Reg. §1.199A-5(c)(1)(ii) also provides that the exemption threshold drops to 5 percent if the total gross receipts of the trade or business exceeds the \$25 million threshold. The \$25 million threshold itself is calculated on a per tax year basis and is not indexed for inflation. ○ For tax years beginning after December 31, 2017, a gross receipts threshold amount of \$25 million dollars (section 448(c)(1)) is also applied in determining whether certain “small business” taxpayers can use the cash method of accounting (section 448(b)(3)), are required to use inventory methods (section 471(c)(1)), are exempt from the application of the uniform capitalization (“UNICAP”) rules (section 263A(i)(1)), are not required to use the percentage of completion method for a small construction contract (section 460(e)(2)(A)), and are exempt from the application of the limitation of the deduction of business interest (section 163(j)(3)). ○ Unlike Prop. Reg. §1.199A-5(c)(1) which mandates an annual testing period, section 448(c)(1) provides that the \$25 million gross receipts test is calculated on an average annual basis for the 3-taxable year period ending with the taxable year that precedes such applicable taxable year. ○ The section 448(c)(4) \$25 million gross receipts threshold is adjusted annually for inflation for tax years beginning after December 31, 2018 using the Chained Consumer Price Index for All Urban Consumers (C-CPI-U) rounded to the nearest multiple of \$1,000,000 (section 448(c)(4) plus flush language).¹ ○ The maintenance of two separate and unique \$25 million dollars gross receipts threshold is unnecessary and will eventually produce confusion as the two standards diverge. • Provide guidance that the \$25 million gross receipts threshold utilized for purposes of the Prop. Reg. §1.199A-5(c)(1) <i>de minimis</i> rule adopts the \$25 million gross receipts threshold standard of section 448(c)(1). This guidance would promote simplicity, fairness, and consistency. 	199A, 448

¹ The flush language at section 448(c)(4) reads: “If any amount as increased under the preceding sentence is not a multiple of \$1,000,000, such amount shall be rounded to the nearest multiple of \$1,000,000.”

Item #	Topic	Description of Item	IRC Section
4.	Threshold Amount for Non-Grantor Trusts	<ul style="list-style-type: none"> • Replace language in Prop. Reg. §1.199A-6(d)(3)(iii) that currently states, “the taxable income of a trust or estate is determined <i>before</i> taking into account any distribution deduction under sections 651 or 661” with “the taxable income of a trust or estate is determined <i>after</i> taking into account any distribution deduction under sections 651 or 661.” <ul style="list-style-type: none"> ○ As the proposed regulations are currently drafted, the distribution deduction is ignored and potentially the same income - the amount of distributed taxable income - is counted twice for threshold purposes (both at the trust level and again at the beneficiary level). This same income is used to potentially disallow a QBI deduction for the estate/trust, and then used by the beneficiary again to determine taxable income at the individual level, which could partially or totally disallow the QBI deduction for the beneficiary. Treasury and the IRS should address this issue in revisions to the regulations. 	199A, 651, 661
5.	Presumption That Former Employees are Still Employees	<ul style="list-style-type: none"> • Provide guidance on an appropriate timeframe where a former employee is considered an employee when providing services to a former employer. Establish a reasonable timeframe whereby a former employee is no longer tainted by prior employment with a business. <ul style="list-style-type: none"> ○ Proposed Reg. §1.199A-5(d)(3) states that for purposes of section 199A(d)(1)(B) and Prop. Reg. §1.199A-5(d)(1), an individual that was formerly treated as an employee for federal employment tax purposes and subsequently provides the same services to the same individual but in a non-employee status is considered in the trade or business of providing services as an employee. • To the extent that a person is considered an employee under this provision, then any such compensation paid to such personal is considered W-2 wages of the payor business, despite the fact it is not reported on Form W-2. 	199A
6.	Common Ownership	<ul style="list-style-type: none"> • Replace the language: “... owns more than 50% ...” in the examples of Prop. Reg. §1.199A-4(d) to “... at least 50% ...” or “... 50% or more ...” in order to provide consistency with the common ownership requirement in Prop. Reg. §1.199A-4(b). • Replace the term “majority interest” in the Preamble to “at least 50%” or “50% or more.” <ul style="list-style-type: none"> ○ “Majority interest” implies that the common ownership test is more than 50 percent. This should read “at least 50%” or “50% or more” interest in ownership throughout the regulation to confirm and conform to the 50 percent common ownership threshold. 	199A
7.	Agriculture: Dealing in Commodities	<ul style="list-style-type: none"> • Provide guidance that excludes taxpayers who take physical possession of the commodity from SSTB status. They are in the storage or transporting businesses. <ul style="list-style-type: none"> ○ Proposed Reg. §1.199A-5(b)(2)(xiii) provides guidance with respect to dealing in commodities as defined in section 475(e)(2). A commodity for this purpose includes one that is actively traded within the meaning of section 1092(d)(1). This refers to personal 	199A, 1092

Item #	Topic	Description of Item	IRC Section
		<p>property that is actively traded, which refers to an established financial market (a national securities exchange, domestic board of trade, etc.) (Treas. Reg. §1.1092(d)-1)). This provision appears to treat certain agricultural traders and dealers as SSTBs. For example, a private grain elevator structured as a partnership purchases, stores and sells wheat. Because wheat is actively traded on established financial markets, this appears as dealing in commodities; the partnership income would not qualify as QBI because it is an SSTB. However, this private elevator would not have considered it possible that a middleman, taking physical possession, is considered a dealer in the notion contemplated by section 475. Section 475 appears as intended to address accounting and taxation for taxpayers who deal in paper transactions, but is not intended to address those who take physical possession. In the case of the grain elevator (in the example), physical possession entails risk of spoilage.</p> <ul style="list-style-type: none"> ○ Another example, on yet a smaller scale but important for the concept, is the purchaser of grain (actively traded on a national exchange) from a farmer-producer, who transports it to another farmer (livestock owner), who feeds the grain. This middleman is in the business of transporting commodities, but appears as an SSTB because of temporary ownership during the transport. 	
8.	Agriculture: Crop Share Arrangements	<ul style="list-style-type: none"> ● Provide guidance that a crop share arrangement between a land owner and a tenant is trade or business income for the landlord if the crop share arrangement is nonpassive under the provisions of section 1375. 	199A, 1375