

Do Triple Net Leases Qualify for the New Business Tax Deduction (Section 199A)?

If you use triple-net leases for your rental properties, you may wonder whether you'll get your Section 199A deduction.

We don't have a clear answer for you, so we are going to go with "maybe." As you'll see, we need more information.

A triple-net lease requires the lessee to pay the landlord rent as well as take care of real estate taxes, building insurance, and property maintenance costs. Therefore, in a triple-net lease, the lessee bears all the burdens of ownership, and the landlord usually has little to no involvement in the property management.

A rental property qualifies for the Section 199A deduction if

1. the rental property qualifies as a trade or business under tax code Section 162, or
2. you rent the property to a commonly controlled trade or business.

Assuming you can't use the commonly controlled route, your rental properties need to rise to the level of a trade or business to get your Section 199A deduction.

To meet that requirement, you'll generally need to have regular and continuous involvement with your rental activities. And the proposed regulations require you to look at each rental activity separately when determining whether it is a trade or business—aggregation doesn't help you with this.

Many triple-net lease rental activities likely fail the regular and continuous activity test and won't qualify for the Section 199A deduction. For example, in *Neill*, the Board of Tax Appeals (the precursor to the Tax Court) held that a single property leased on a triple-net basis is not a Code Section 162 trade or business.

In the preamble to the Code Section 1411 regulations, the IRS gives you other factors to consider when determining whether your rental activity is a trade or business:

- Type of property (commercial vs. residential vs. personal property)
- Number of properties rented
- Day-to-day involvement of the owner or its agent
- Type of lease (net vs. traditional, short-term vs. long-term)

Depending on the particular circumstances of your triple-net lease rental activities, they may rise to the level of a trade or business, even if your involvement with each lease individually is minimal.

You can see why we are in "maybe" land and hoping for more information from the IRS.

If you would like us to review your net leases with you, please don't hesitate to reach out to us at Kennedy Financial Services.

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