**Understanding the 199A Deduction After The New IRS Final Regulations**

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Despite being in the midst of a government shutdown, the Internal Revenue Service (IRS) was just able to release a [247 page document](https://www.irs.gov/pub/irs-drop/td-reg-107892-18.pdf) describing and cementing final rules around section 199A. For those of you who are unfamiliar with 199A, the section provides for a new deduction of up to 20 percent of qualified domestic business income for pass through entities such as sole-proprietorships, partnerships, S-corporations, trusts, or estates. 199A was solidified as part of the tax reform legislation that was passed late in 2017 on December 22nd. Much like the official title of the tax cut act itself, entitled “An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2019” – and less formally known as the Tax Cuts and Jobs Act (TCJA) – it fell short on the original message of simplification. While 199A remains extremely complex, the new regulations help to explain a lot of the questions that arose from the original legislation. Let’s look at how the law stands now after the new regulations.

Like most of the individual tax code provision passed in the TCJA, they went effective for the tax year 2018 and expire after 2025. While all laws are somewhat temporary in nature as they can be changed, this one goes away unless further action is taken, which could occur before 2025. However, with 2018 in the books, we know that 199A is at least applicable to last year.

The 199A deduction allows for up to a “20% deduction” of qualified business income for certain business owners, trusts, and estates. However, the deduction comes with significant qualifications. First, you need to determine if your business entity qualifies for the deduction. Remember, this is only for pass-through entities. Additionally, the deduction is only on qualified business income (discussed more later), and not available for wage income (i.e. W-2 reported income). The deduction could also be limited by the type of business in which you are engaged, your taxable income, W-2 wages paid, and the unadjusted basis immediately after acquisition (UBIA) of qualified property.

To be a section 162 business that receives the 199A deduction you need to be engaged in the activity with some regularity. Generally, if you think you are running a business you probably are running a business. One area of concern with 199A had been if rental property qualified as a business. Under the new regulations, Revenue Procedure 2019-7, the IRS offered a safe harbor in determining what is rental activity. For instance, if separate books and records are maintained for each rental activity, and if 250 hours or more of rental services are provided for the year. You lose the rental safe harbor if you use the rental for yourself for more than 14 days a year (think your beach house or mountain cabin). If you rent it most of year but spend three weeks there, it’s not available.

Further complicating the matter is that generally the 199A deduction requires you to treat each trade or business (even within a single entity) as separate for reporting purposes. For each trade or business, you must be able to compute qualified business income.