



April 09, 2019

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

The Honorable Michael J. Desmond
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 Desmond:

The American Institute of CPAs (AICPA) appreciates the efforts of the Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) to address the need for guidance related to the new Internal Revenue Code section 199A² as enacted under Pub. L. No. 115-97, commonly referred to as the Tax Cuts and Jobs Act (TCJA or “the Act”) and to consider our prior recommendations.³

Treasury and the IRS issued corrected final regulations REG-107892-18 (released February 1, 2019) on the “Qualified Business Income Deduction” and IRS Notice 2019-07 (released January 18, 2019) on “Section 199A Trade or Business Safe Harbor: Rental Real Estate.”

Specifically, the AICPA submits comments in the following areas related to the regulations and notice:

- I. Safe Harbor for Rental Real Estate
- II. Deemed Trade or Business for All Commonly-Owned Arrangements
- III. Allocation Based Upon Gross Receipts
- IV. Unadjusted Basis Immediately After Acquisition (UBIA) on Section 734(b) Adjustments
- V. Definition of Qualified Business Income (QBI)

¹ Includes Treasury and the IRS’s corrected final regulations [REG-107892-18](#) (issued February 1, 2019) on the “Qualified Business Income Deduction” and the IRS [Notice 2019-07](#) on “Section 199A Trade or Business Safe Harbor: Rental Real Estate.”

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

³ AICPA Comment Letter “[Guidance Concerning the Deduction for Qualified Business Income Under Section 199A of the Internal Revenue Code](#),” submitted October 1, 2018.

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

Sincerely,

A handwritten signature in black ink, appearing to read "Annette Nellen". The signature is fluid and cursive, with the first name being more prominent.

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

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

AMERICAN INSTITUTE OF CPAs

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

April 09, 2019

I. Safe Harbor for Rental Real Estate

Overview:

To minimize uncertainty related to rental real estate enterprises and section 199A,⁴ proposed revenue procedure Notice 2019-07 provides a safe harbor for when a rental real estate enterprise is treated as a trade or business under section 162 for purposes of section 199A. Our comments below seek additional clarity while also recommending options to reduce taxpayer burden in complying with the provisions.

Recommendations:

The Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) should provide additional consideration around the proposed revenue procedure as follows:

1. Allow for aggregation of commercial and residential rental real estate activities;
2. Allow taxpayers that enter into triple net lease arrangements to qualify under the revenue procedure, in situations where the activities of the taxpayer surrounding the triple net lease would otherwise satisfy the requirements outlined in the revenue procedure;
3. Provide clarity around the taxpayer’s use of real property as a residence in which the taxpayer rents a portion and resides in a portion of the real property;
4. Clarify that the time spent by a professional real estate management company would qualify toward the 250-hour requirement;
5. Reduce the 250-hour requirement;
6. Reduce the requirements of contemporaneous documentation as it relates to independent contractors and agents of the taxpayer; and
7. Provide additional clarity around reporting, specify what a taxpayer needs to include in the reporting statement, and remove the signatory requirement.

Analysis:

1. *Allow for aggregation of commercial and residential rental real estate activities.*

Under the proposed safe harbor, taxpayers may treat each property held for the production of rents as separate enterprises or treat all “similar” properties held for the production of rents as a single enterprise. However, the safe harbor provides that taxpayers may not include commercial and residential real estate together as part of the same enterprise.

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

There is no precedent for segregating commercial from residential property. This separation is inconsistent with other areas of the Internal Revenue Code. For example, rental real estate is defined under the regulations of section 469 as “any real property used by customers or held for use by customers in a rental activity.”⁵ This definition does not separate between commercial and residential properties, thus allowing a taxpayer to group the activities of commercial and residential real estate together.

The separation of these two types of properties poses further complications in the context of mixed-use property, where both a component of residential and commercial rental activities exists within the same piece of property, which is an increasingly common arrangement in the rental real estate industry.

2. *Allow taxpayers that enter into triple net lease arrangements to qualify under the revenue procedure, in situations where the activities of the taxpayer surrounding the triple net lease would otherwise satisfy the requirements outlined in the revenue procedure.*

The revenue procedure specifically prohibits taxpayers from using the safe harbor if the taxpayer rents or leases real estate under a triple net lease (defined as “an agreement that requires the tenant or lessee to pay taxes, fees, and insurance and to be responsible for the maintenance activities for a property in addition to rent and utilities.”)⁶

Precluding any triple net lease arrangement would have the effect of disallowing a rental real estate enterprise that would otherwise meet the requirements set forth in the proposed safe harbor, solely on the basis of the lease type. This result is not consistent with case law, as cases have relied on the actual activities performed related to the rental real estate enterprise. Many cases where the courts and the IRS have found that a taxpayer’s rental activities did not rise to the level of a trade or business, relied on the fact that there was a single property leased on a “net” basis to a single tenant.⁷ However, in cases where a trade or business was found, the courts gave the most weight to the number of properties rented and level of activities with respect to the property.⁸

For purposes of the safe harbor, Treasury and the IRS should consider the level of activities performed rather than basing the application of the safe harbor solely on the type of lease.

⁵ See Treas. Reg. § 1.469-9(b)(3).

⁶ IRS Notice 2019-07 section 3.05.

⁷ See, *Neill v. C.I.R.*, 46 B.T.A. 197 (1942) (single property rented to single tenant who was responsible for operating the property and paying all taxes and insurance); *Grier v. U.S.*, 120 F. Supp. 395 (D.C. Conn. 1954), *aff’d*, 218 F.2d 603 (2nd Cir. 1955) (rental of a single property to a single tenant for entire duration of ownership; maintenance generally handled by having tenant secure services and receive reimbursement); Rev. Rul. 73-522, 1973-2 C.B. 226 (triple net lease of a single property to a single tenant); P.L.R. 8350008 (Aug. 23, 1983) (triple net lease of a single hotel property to a single tenant).

⁸ See, e.g., *Pinchot v. C.I.R.*, 113 F.2d 718 (2nd Cir. 1940) (11 New York buildings; through agent, services were presumed considerable as well as continuous and regular); *Fackler v. C.I.R.*, 133 F.2d 509 (6th Cir. 1943) (single six-story property with numerous tenants; management involved alterations and repairs commensurate with the number of tenants who occupied the property); *Gilford v. C.I.R.*, 201 F.2d 735 (2nd Cir. 1953) (8 New York buildings; ground floors retail and upper floors apartments; agents of owner spent appreciable time in managing the property).

3. *Provide clarity around the taxpayer's use of real property as a residence in which the taxpayer rents a portion and resides in a portion of the real property.*

The proposed revenue procedure is not available to taxpayers who use the real estate as a residence for any part of the year. However, taxpayers may want to utilize, and arguably should benefit from, the safe harbor when a taxpayer owns a duplex, fourplex, or other rental property and lives within one of the adjoining units as a principal residence. We recommend that Treasury and the IRS clarify that the disallowance solely applies to the portion of the property in which the taxpayer resided during the taxable year and does not extend to contiguous units simply because of a commonly-shared wall.

4. *Clarify that the time spent by a professional real estate management company qualifies toward the 250-hour requirement.*

The proposed revenue procedure provides eligibility only for taxpayers who perform 250 or more hours of rental services related to the rental enterprise per year for tax years beginning prior to January 1, 2023. Thereafter, taxpayers must meet the 250-hour requirement in any three of five consecutive tax years, ending with the taxable year. In calculating the hour requirement, the safe harbor allows for the inclusion of rental services performed by others, including employees, agents, and independent contractors of the owners. Similarly, time incurred by a professional real estate management company on the owner's behalf should count towards the 250 hours. Please confirm the treatment of a professional real estate management company.

5. *Reduce the 250-hour requirement.*

In tracking the hours spent, a taxpayer must keep contemporaneous documentation, including details of the hours of services performed. If an enterprise fails to satisfy the requirements of the safe harbor, the rental real estate enterprise may still receive treatment as a trade or business for purposes of section 199A if the enterprise otherwise meets the definition of trade or business in Treas. Reg. § 1.199A-1(b)(14). A trade or business is established if the taxpayer pursues the activity with the intent of making a profit and the taxpayer's responsibility (personally or through agents) is regular and continuous.⁹ Requiring 250 hours as the threshold for meeting the safe harbor is excessive. Under Treas. Reg. § 1.469-5T(c)(2), a taxpayer is not passive with respect to her activity if she significantly participates for more than 100 hours during the year. Accordingly, we recommend an approach which reduces the 250 hours to "more than 100 hours" as consistent with passive activity standards.

6. *Reduce the requirements of contemporaneous documentation as it relates to independent contractors and agents of the taxpayer.*

The safe harbor requirement to keep documentation of the hours of all services performed is unduly burdensome on the taxpayer as well as the taxpayer's agents and independent contractors. As a standard practice, many independent contractors and most property managers do not include hourly billing in their invoices, and only bill a total amount for the contractual services performed.

⁹ *Comm'r v. Groetzinger*, 107 S.Ct. 980, 2/24/1987.

Thus, taxpayers relying on the safe harbor would have to require their agents and independent contractors to provide detailed time in the invoices. This requirement may add additional burdens on independent contractors and hinder taxpayers from finding competent service providers. Therefore, we recommend a reduction in the contemporaneous documentation requirements as it relates to independent contractors and agents of the taxpayer.

7. *Provide additional clarity around reporting, specify what a taxpayer needs to include in the reporting statement, and remove the signatory requirement.*

In order to utilize the safe harbor, taxpayers must include a statement noting that the requirements of the revenue procedure are satisfied. The statement also requires a signature from the taxpayer or authorized representative, and it must provide the following specific language:

“Under penalties of perjury, I (we) declare that I (we) have examined the statement, and, to the best of my (our) knowledge and belief, the statement contains all the relevant facts relating to the revenue procedure, and such facts are true, correct, and complete.”

This signatory requirement adds burdens on taxpayers. Furthermore, Treasury and the IRS have worked hard over the years to remove requirements for a separate signature in order to accommodate electronically filing returns.¹⁰ Above the signature line of tax returns, the taxpayer (or the taxpayer representative) already signs under penalties of perjury to confirm that the taxpayer has reviewed the return, included accompanying schedules and statements, and provided accompanying schedules and statements that are true, correct, and complete. Therefore, the required language in the safe harbor statement, along with the additional signatory requirement, are redundant. We recommend that Treasury and the IRS remove the signatory requirement from the final revenue procedure and clarify what specific statements the election attachment must contain.

If Treasury and the IRS determine that the signatory requirement is necessary, clarity is needed on exactly what the declaratory statement entails. Outside of including the penalties of perjury language above, it is unclear what specific additional assertions the safe harbor statement must contain. Guidance does not provide whether taxpayers may simply meet the requirements listed in the statement or if they must also provide a detailed description of how the listed requirements were satisfied. The penalties of perjury language implies that the statement must contain additional details surrounding how the taxpayer met the requirements contained in the revenue procedure.

II. Deemed Trade or Business for All Commonly-Owned Arrangements

Overview

Taxpayers may operate closely-held businesses through multiple legal entities for business reasons, including separating assets from exposure to risks. However, taxpayers often may manage these legal entities as one trade or business. Treasury Reg. § 1.199A-1(b)(14) recognizes

¹⁰ For instance, in 2017, Treasury and the IRS proposed to amend the section 754 regulations to remove the signatory requirement on section 754 elections to aid electronic filing. *See* 82 Fed. Reg. at 47408.

this concept in deeming real estate operations commonly-owned with operating entities as trades or businesses, even though the real estate operation would not otherwise rise to the level of a trade or business. This deemed status does not depend upon aggregation under Treas. Reg. § 1.199A-4. Also, the deemed status is not available if the real estate is leased to a commonly-owned C corporation. The tax filing classification of the tenant operating business should not matter in respect to the deemed treatment as one managed trade or business.

Recommendation

Treasury and the IRS should modify Treas. Reg. § 1.199A-1(b)(14) to include rentals to a commonly-owned C corporation as a deemed trade or business for the rental activity. However, aggregation under Treas. Reg. § 1.199A-4(b)(1)(i) should continue to deny aggregation with a commonly-owned C corporation.

Analysis

The Preamble to the section 199A regulation (Treasury Decision (TD) 9847)¹¹ and in the earlier proposed regulations (REG-107892-18)¹² recognize the difficulties of defining the term “trade or business” for purposes of sections 162 and 199A. Taxpayers often manage their trade or business affairs across the lines of separate legal entities (*e.g.*, disregarded entities are utilized to reduce exposure to legal liabilities, real estate is leased to the operating entity, supply chains are often operated through S or C corporations separate from the manufacturing entity, etc.). Treasury and the IRS recognized that a closely-held business may cross entity boundaries in adopting Prop. Reg. § 1.199A-1(b)(13) and Treas. Reg. § 1.199A-1(b)(14). The final regulations define a trade or business, solely for purposes of section 199A, as including the rental or licensing of tangible or intangible property to a related trade or business, commonly controlled under Treas. Reg. § 1.199A-4(b)(1)(i). The Preamble to the regulations (at page 19) clarifies that the commonly controlled entity must exist as an individual or relevant pass-through entity (RPE) or multiple RPEs.

Treasury and the IRS recognize (by adopting the deemed treatment of rentals to related entities) that one trade or business may operate across legal entity boundaries. Closely-held businesses, whether operated in pass-through entity form or as a C corporation, are usually managed similarly. A taxpayer, family group, or other group of owners may commonly own multiple entities, one or more of which may exist as a C corporation. These owners may also commonly own real estate leased to an operating C corporation. This management as one trade or business is functionally no different than rentals to related C corporations.

Treasury Reg. § 1.469-4(d)(5)(ii) allow a taxpayer conducting an activity through a C corporation that is subject to section 469 to group the C corporation activity with another activity of the taxpayer, but only for purposes of determining whether the taxpayer materially or significantly participates in the other activity. This allowance is in recognition of taxpayers that operate

¹¹ See Treasury Decision (TD) 9847, “[Qualified Business Income Deduction](#),” dated February 8, 2019.

¹² See Notice of Proposed Rulemaking REG-107892-18, “[Qualified Business Income Deduction](#),” dated August 16, 2018.

businesses across entity lines. Recognition, however, is also needed for taxpayers' involvement in multiple entities regardless of entity type.

If this deemed trade or business status for property leased to an operating C corporation is not adopted, we recommend acknowledging that taxpayers may establish, depending upon facts and circumstances, that property leased to an operating C corporation is a trade or business due to common management and control. This provision would include triple net leases and other leasing arrangements that might not otherwise rise to the level of a trade or business.

To clarify, our recommendation does not include the aggregation of qualified business income (QBI) components with C corporations. It also does not include any changes to the aggregation rules under Treas. Reg. § 1.199A-4(b)(1)(i).

III. Allocation Based Upon Gross Receipts

Overview

Individual taxpayers may pay or incur deductions that apply to more than one business. Treasury Reg. § 1.199A-3(b)(1)(vi) provides guidance for allocating the deductions between the taxpayer's multiple businesses. We believe the methodology provided is flawed.

Recommendation

Treasury and the IRS should modify Treas. Reg. § 1.199A-3(b)(1)(vi). Specifically, we recommend that taxpayers allocate the various deductions, which are not direct deductions of the trade or business, proportionately to the businesses based upon relative positive QBI – not gross receipts.

Analysis

Self-employment income may generate from one or more sole proprietorships and partnerships. One or more of the partnerships may generate QBI without self-employment income. For example, a limited partner may receive QBI, but the income may not derive from self-employment income. Also, a general partner of a specified service trade or business (SSTB) may generate self-employment income, which is not QBI in the case where the taxpayer is fully phased-out of the QBI deduction because of excess taxable income over the applicable threshold. A guaranteed payment, which is not QBI, may also generate self-employment income. In each of these cases, the relative gross receipts of the trade or business is irrelevant to the determination of the self-employment income and irrelevant to the determination of QBI.

The same analysis applies to qualified retirement plan contributions under section 404.

Section 162(l) allows a trade or business deduction for the self-employed person's health insurance paid or reimbursed by the business. A partnership reports the payment of the health insurance as a guaranteed payment to the partner. An S corporation reports the payment of the health insurance as additional wage income in box 1 of Form W-2, Wage and Tax Statement. The guaranteed

payment of the partnership, however, is not QBI. The wage income of the S corporation shareholder is not QBI. Consequently, the only self-employed health insurance deduction to reduce QBI is the deduction from a sole proprietorship. The determination of the deduction is directly traceable to the SSTB that adopted the health insurance plan and paid the amount. Gross receipts are not relevant to the determination.

Example:

Jean has two sole proprietorships (SP). SP1 is not an SSTB, generating \$1 of net income. SP2 is an SSTB generating \$100,000 of SSTB income. SP1 has gross receipts of \$900,000; SP2 has gross receipts of \$100,000. Under the final regulation, the 50% self-employment tax deduction under section 164(f) is allocated 90% to SP1, even though SP1 did not generate any self-employment tax.

Self-employment tax and qualified retirement plan contributions may result from multiple activities and require allocation. Taxpayers should allocate the amount based on the relative self-employment income or earned income on which qualified retirement plan contributions are based, respectively.

Taxpayers should directly allocate the section 162(l) deduction to the business that paid or reimbursed the health insurance of the self-employed person.

Each of these deductions may, or may not, reduce QBI depending upon the respective businesses' contribution to QBI.

IV. Unadjusted Basis Immediately After Acquisition (UBIA) on Section 734(b) Adjustment

Overview

The proposed section 199A regulations denied an increase in UBIA of qualified property for adjustments under sections 734(b) and 743(b). The final regulations allow a limited adjustment for excess section 743(b) adjustments, but not for similar adjustments under section 734(b). The Preamble of the regulations notes that Treasury and the IRS continue to study the issue.

Recommendation

Treasury and the IRS should provide that an excess section 734(b) adjustment generates UBIA in the same manner as an excess section 743(b) adjustment.

Analysis

In the Preamble to the final regulations, Treasury and the IRS state that they do not believe a section 734(b) adjustment is an acquisition of qualified property for purposes of section 199A. However, we believe that a partnership should have treatment as acquiring the distributee partner's portion of partnership property to the extent that the partner recognizes gain under section 731(a)(1). Section 731(a) provides that any gain or loss recognized under this subsection is

considered a gain or loss from the sale or exchange of the partnership interest of the distributee partner, presumably by the partnership.

Other provisions have provided special rules on how to treat section 734(b) basis adjustments. For example, increases to basis of section 197 intangibles pursuant to section 734(b) are treated as separate section 197 intangibles.¹³

Generally, upon the redemption of a partner's partnership interest for cash, a partnership with a section 754 election in effect will adjust the basis of the underlying assets of the partnership. This adjustment is based upon the amount of gain or loss recognized by the distributee partner under section 731(a). Rules for allocating the special basis adjustments under section 734(b) are provided under Treas. Reg. § 1.755-1(c). To the extent an increase in basis is allocated to qualified property under section 199A(b)(6), regulations should allow the ability to adjust the UBIA. This adjustment is applicable, for example, if the fair market value of the underlying qualified property is greater than the original unadjusted basis of the property (an excess section 734(b) adjustment).

The partnership should determine the adjustment in question without regard to earlier adjustments for partners under section 743(b), as those adjustments are partner-specific and do not affect the other partners of the partnership.

Example:

Consider a three-person partnership (A, B, and C) that acquires qualified property for \$15,000. The partners are each one-third owners. Ignore adjustments for depreciation, because the UBIA is applicable only if and to the extent of increases in fair market value over original cost. Initially, Partner B's interest is acquired for \$6,000 by new Partner D. The partnership has a section 754 election in effect. Partner D has an excess section 743(b) adjustment of \$1,000. Its share of partnership UBIA is \$5,000, plus its \$1,000 excess section 743(b) adjustment, for a total UBIA of \$6,000.

Subsequently, Partner A is redeemed by the partnership for \$7,000. The partnership records a section 734(b) adjustment for \$2,000, equal to Partner A's gain recognized under section 731(a). This adjustment should have recognition as an excess section 734(b) adjustment, generating UBIA for the partnership.

As a result of the adjustments, UBIA of the qualified property is \$17,000 (the original \$15,000 plus excess section 734(b) adjustment of \$2,000). The partnership now has two partners, C and D. Partner C's share of the partnership's UBIA is \$8,500 (\$7,500 is the 50% interest in the original \$15,000, plus \$1,000 from the excess section 734(b) adjustment). Partner D's share of the partnership's UBIA is also \$8,500. In addition, Partner D has an excess section 743(b) adjustment of \$1,000 from its earlier acquisition of Partner B's partnership interest; Partner D has a total UBIA of \$9,500.

The total UBIA associated with the qualified property is \$18,000, which reflects the economic transactions of gains recognized by A and B upon the redemption and sale of the

¹³ Treas. Reg. § 1.197-2(g)(3).

partnership interests, respectively. Partners C and D should benefit from these acquisitions that result in each partner's economic sharing in the qualified property to increase.

V. Definition of QBI

Overview

QBI is the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business. The taxpayer (individual, estate, or trust) may recognize items of income, gain, deduction, and loss from multiple sources. Some items may originate from multiple trades or businesses (see item III above).

Recommendations

Treasury and the IRS should expand Treas. Reg. § 1.199A-3(b)(1) to include items commonly reported by taxpayers owning or benefiting from RPEs. Treasury Reg. § 1.199A-3(b)(1) should include a sentence such as, "The following items are among the trade or business items that are or are not taken into account in computing QBI (not an all-inclusive list)."

Analysis

Taxpayers and tax preparers struggle with determining which items constitute QBI. To provide the clarity needed on items commonly reported by taxpayers owning RPEs, the regulations need additional examples. Specifically, we recommend adding examples to Treas. Reg. § 1.199A-3(b)(1) on the following issues:

1. Self-employed health insurance under section 162(l) is a reduction of QBI if the income associated with the expense is QBI (considering SSTB or non-SSTB status).
2. The deduction for one-half of the taxpayer's self-employment tax under section 164(f) is a reduction of QBI if the income associated with the self-employment tax was QBI (considering SSTB and non-SSTB status).
3. Interest expense attributable to the acquisition of a partnership or S corporation ownership interest is a reduction of QBI if and to the extent the partnership or S corporation activity generated QBI (considering SSTB and non-SSTB status).
4. Unreimbursed partner expenses are reductions of QBI if and to the extent the partnership activity generated QBI (considering SSTB and non-SSTB status).
5. Qualified retirement plan contributions of a sole proprietor or partner are reductions of QBI to the extent attributable to income generating QBI (considering SSTB and non-SSTB status).
6. The state income tax deduction on the Form 1040, Schedule A (Itemized Deductions) for the taxpayer could reduce QBI to the extent the deduction provided a tax benefit and was attributable to income generating a deduction under section 199A.
7. The QBI status of royalty income depends upon whether the property generating the royalty is a qualified trade or business of the taxpayer.

The examples below illustrate the effect on QBI based on income, gain, deduction, and loss from sources listed in Treas. Reg. § 1.199A-3(b):

Example 1:

Josephine is a partner in a partnership providing services in the field of law. The activity is an SSTB. Josephine, a single taxpayer, has 2018 tentative taxable income determined under section 199A(d)(3) of less than \$157,500. In accordance with Revenue Ruling (Rev. Rul.) 91-26, the partnership includes the self-employed deduction for health insurance cost as a guaranteed payment under section 707(c). The section 162(l) deduction for Josephine's health insurance, paid by the partnership, is not a reduction of QBI because it is associated with the guaranteed payment, which is not qualified income.

Example 2:

Jacob is a sole proprietor lawyer who provides his own health insurance, allowed as a deduction under section 162(l). His 2018 tentative taxable income determined under section 199A(d)(3) is \$197,500. The deduction under section 162(l) reduces his law firm income to arrive at the amount of taxpayer SSTB that qualifies as QBI.

Example 3:

Rachel is a shareholder in a law service S corporation. She also receives health insurance through her firm. In accordance with IRS Notice 2008-1, Rachel's Form W-2, Wage and Tax Statement, box 1 wage is increased by the amount of the health insurance. Her section 162(l) deduction does not reduce QBI because it is associated with her wage income, which is not qualified income.

Example 4:

Allison, a single person, reports \$200,000 self-employment income from her partnership, a medical clinic, which is an SSTB. She also receives \$50,000 of self-employment income from another partnership that is not an SSTB. Her tentative taxable income is over \$207,500 for 2018. Because 20% of her self-employment income is associated with QBI (none of the medical clinic's SSTB income qualifies as QBI), 20% of her section 164(f) deduction for one-half of her self-employment tax reduces QBI.

Example 5:

Alexander is a partner of a construction partnership. He receives a \$50,000 guaranteed payment and pass-through QBI of \$200,000. His self-employment income is \$250,000. The guaranteed payment is not QBI. Therefore, 80% of his self-employment tax deduction under section 164(f) reduces QBI.

Example 6:

Kate is an author who receives book royalties (as the author) of \$300,000. The royalties from the sale of her books are qualified business income. The QBI from the book royalties may reduce from the section 164(f) deduction for one-half of her self-employment tax, her qualified retirement plan contributions (including IRA deductions), her self-employed

health insurance under section 162(l), and other deductions attributable to her book royalty income activities.

Example 7:

Jack owns an investment in a producing oil well that generates royalty income. The oil well investment is not a working interest. This royalty income is not QBI as it is not a trade or business activity under section 162.