

## **Reg. Section 1.199a-1(d)(4)(v), Example 5**

### Operational rules

#### (a) Overview.

(1) In general. This section provides operational rules for calculating the section 199A(a) qualified business income deduction (section 199A deduction) under section 199A of the Internal Revenue Code (Code). This section refers to the rules in §§1.199A-2 through 1.199A-6. This paragraph (a) provides an overview of this section. Paragraph (b) of this section provides definitions that apply for purposes of section 199A and §§1.199A-1 through 1.199A-6. Paragraph (c) of this section provides computational rules and examples for individuals whose taxable income does not exceed the threshold amount. Paragraph (d) of this section provides computational rules and examples for individuals whose taxable income exceeds the threshold amount. Paragraph (e) of this section provides special rules for purposes of section 199A and §§1.199A-1 through 1.199A-6. This section and §§1.199A-2 through 1.199A-6 do not apply for purposes of calculating the deduction in section 199A(g) for specified agricultural and horticultural cooperatives.

(2) Usage of term individual. For purposes of applying the rules of §§1.199A-1 through 1.199A-6, a reference to an individual includes a reference to a trust (other than a grantor trust) or an estate to the extent that the section 199A deduction is determined by the trust or estate under the rules of §1.199A-6.

#### (b) Definitions. For purposes of section 199A and §§ 1.199A-1 through 1.199A-6, the following definitions apply:

(1) Aggregated trade or business means two or more trades or businesses that have been aggregated pursuant to §1.199A-4.

(2) Applicable percentage means, with respect to any taxable year, 100 percent reduced (not below zero) by the percentage equal to the ratio that the taxable income of the individual for the taxable year in excess of the threshold amount, bears to \$50,000 (or \$100,000 in the case of a joint return).

(3) Net capital gain means net capital gain as defined in section 1222(11) plus any qualified dividend income (as defined in section 1(h)(11)(B)) for the taxable year.

(4) Phase-in range means a range of taxable income between the threshold amount and the threshold amount plus \$50,000 (or \$100,000 in the case of a joint return).

(5) Qualified business income (QBI) means the net amount of qualified items of income, gain, deduction, and loss with respect to any trade or business (or aggregated trade or business) as determined under the rules of §1.199A-3(b).

(6) QBI component means the amount determined under paragraph (d)(2) of this section.

(7) Qualified PTP income is defined in §1.199A-3(c)(3).

(8) Qualified REIT dividends are defined in §1.199A-3(c)(2).

(9) Reduction amount means, with respect to any taxable year, the excess amount multiplied by the ratio that the taxable income of the individual for the taxable year in excess of the threshold amount, bears to \$50,000 (or \$100,000 in the case of a joint return). For purposes of this paragraph (b)(9), the excess amount is the amount by which 20 percent of QBI exceeds the greater of 50 percent of W-2 wages or the sum of 25 percent of W-2 wages plus 2.5 percent of the UBIA of qualified property.

(10) Relevant passthrough entity (RPE) means a partnership (other than a PTP) or an S corporation that is owned, directly or indirectly, by at least one individual, estate, or trust. Other passthrough entities including common trust funds as described in §1.6032-1T and religious or apostolic organizations described in section 501(d) are also treated as RPEs if the entity files a Form 1065, U.S. Return of Partnership Income, and 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, W-2 wages, UBIA of qualified property, qualified REIT dividends, or qualified PTP income.

(11) Specified service trade or business (SSTB) means a specified service trade or business as defined in §1.199A-5(b).

(12) Threshold amount means, for any taxable year beginning before 2019, \$157,500 (or \$315,000 in the case of a taxpayer filing a joint return). In the case of any taxable year beginning after 2018, the threshold amount is the dollar amount in the preceding sentence increased by an amount equal to such dollar amount, multiplied by the cost-of-living adjustment determined under section 1(f)(3) of the Code for the calendar year in which the taxable year begins, determined by substituting "calendar year 2017" for "calendar year 2016" in section 1(f)(3)(A)(ii). The amount of any increase under the preceding sentence is rounded as provided in section 1(f)(7) of the Code.

(13) Total QBI amount means the net total QBI from all trades or businesses (including the individual's share of QBI from trades or business conducted by RPEs).

(14) Trade or business means a trade or business that is a trade or business under section 162 (a section 162 trade or business) other than the trade or business of performing services as an employee. In addition, rental or licensing of tangible or intangible property (rental activity) that does not rise to the level of a section 162 trade or business is nevertheless treated as a trade or business for purposes of section 199A, if the property is rented or licensed to a trade or business conducted by the individual or an RPE which is commonly controlled under §1.199A-4(b)(1)(i) (regardless of whether the rental activity and the trade or business are otherwise eligible to be aggregated under §1.199A-4(b)(1)).

(15) Unadjusted basis immediately after acquisition of qualified property (UBIA of qualified property) is defined in §1.199A-2(c).

(16) W-2 wages means W-2 wages of a trade or business (or aggregated trade or business) properly allocable to QBI as determined under §1.199A-2(b).

(c) Computation of the section 199A deduction for individuals with taxable income not exceeding threshold amount.

(1) In general. The section 199A deduction is determined for individuals with taxable income for the taxable year that does not exceed the threshold amount by adding 20 percent of the total QBI amount (including the individual's share of QBI from an RPE and QBI attributable to an SSTB) and 20 percent of the combined amount of qualified REIT dividends and qualified PTP income (including the individual's share of qualified REIT dividends and qualified PTP income from RPEs and qualified PTP income attributable to an SSTB). That sum is then compared to 20 percent of the amount by which the individual's taxable income exceeds net capital gain. The lesser of these two amounts is the individual's section 199A deduction.

(2) Carryover rules.

(i) Negative total QBI amount. If the total QBI amount is less than zero, the portion of the individual's section 199A deduction related to QBI is zero for the taxable year. The negative total QBI amount is treated as negative QBI from a separate trade or business in the succeeding taxable years of the individual for purposes of section 199A and this section. This carryover rule does not affect the deductibility of the loss for purposes of other provisions of the Code.

(ii) Negative combined qualified REIT dividends/qualified PTP income. If the combined amount of REIT dividends and qualified PTP income is less than zero, the portion of the individual's section 199A deduction related to qualified REIT dividends and qualified PTP income is zero for the taxable year. The negative combined amount must be carried forward and used to offset the combined amount of REIT dividends and qualified PTP income in the succeeding taxable years of the individual for purposes of section 199A and this section. This carryover rule does not affect the deductibility of the loss for purposes of other provisions of the Code.

(3) Examples. The following examples illustrate the provisions of this paragraph (c). For purposes of these examples, unless indicated otherwise, assume that all of the trades or businesses are trades or businesses as defined in paragraph (b)(14) of this section and all of the tax items are effectively connected to a trade or business within the United States within the meaning of section 864(c). Total taxable income does not include the section 199A deduction.

(i) Example (1). A, an unmarried individual, owns and operates a computer repair shop as a sole proprietorship. The business generates \$100,000 in net taxable income from operations in 2018. A has no capital gains or losses. After allowable deductions not relating to the business, A's total taxable income for 2018 is \$81,000. The business's QBI is \$100,000, the net amount of its qualified items of income, gain, deduction, and loss. A's section 199A deduction for 2018 is equal to \$16,200, the lesser of 20% of A's QBI from the business ( $\$100,000 \times 20\% = \$20,000$ ) and 20% of A's total taxable income for the taxable year ( $\$81,000 \times 20\% = \$16,200$ ).

(ii) Example (2). Assume the same facts as in Example 1 of paragraph (c)(3)(i) of this section, except that A also has \$7,000 in net capital gain for 2018 and that, after allowable deductions not relating to the business, A's taxable income for 2018 is \$74,000. A's taxable income minus net capital gain is \$67,000 ( $\$74,000 - \$7,000$ ). A's section 199A deduction is equal to \$13,400, the lesser of 20% of A's QBI from the business ( $\$100,000 \times 20\% = \$20,000$ ) and 20% of A's total taxable income minus net capital gain for the taxable year ( $\$67,000 \times 20\% = \$13,400$ ).

(iii) Example (3). B and C are married and file a joint individual income tax return. B earns \$50,000 in wages as an employee of an unrelated company in 2018. C owns 100% of the shares of X, an S corporation that provides landscaping services. X generates \$100,000 in net income from operations in 2018. X pays C \$150,000 in wages in 2018. B and C have no capital gains or losses. After allowable deductions not related to X, B and C's total taxable income for 2018 is \$270,000. B's and C's wages are not considered to be income from a trade or business for purposes of the section 199A deduction. Because X is an S corporation, its QBI is determined at the S corporation level. X's QBI is \$100,000, the net amount of its qualified items of income, gain, deduction, and loss. The wages paid by X to C are considered to be a qualified item of deduction for purposes of determining X's QBI. The section 199A deduction with respect to X's QBI is then determined by C, X's sole shareholder, and is claimed on the joint return filed by B and C. B and C's section 199A deduction is equal to \$20,000, the lesser of 20% of C's QBI from the business ( $\$100,000 \times 20\% = \$20,000$ ) and 20% of B and C's total taxable income for the taxable year ( $\$270,000 \times 20\% = \$54,000$ ).

(iv) Example (4). Assume the same facts as in Example 3 of paragraph (c)(3)(iii) of this section except that B also earns \$1,000 in qualified REIT dividends and \$500 in qualified PTP income in 2018, increasing taxable income to \$271,500. B and C's section 199A deduction is equal to \$20,300, the lesser of:

- (A) 20% of C's QBI from the business ( $\$100,000 \times 20\% = \$20,000$ ) plus 20% of B's combined qualified REIT dividends and qualified PTP income ( $\$1,500 \times 20\% = \$300$ ); and
- (B) 20% of B and C's total taxable for the taxable year ( $\$271,500 \times 20\% = \$54,300$ ).

(d) Computation of the section 199A deduction for individuals with taxable income above threshold amount.

(1) In general. The section 199A deduction is determined for individuals with taxable income for the taxable year that exceeds the threshold amount by adding the QBI component described in paragraph (d)(2) of this section and the qualified REIT dividends/qualified PTP income component described in paragraph (d)(3) of this section (including the individual's share of qualified REIT dividends and qualified PTP income from RPEs). That sum is then compared to 20 percent of the amount by which the individual's taxable income exceeds net capital gain. The lesser of these two amounts is the individual's section 199A deduction.

(2) QBI component. An individual with taxable income for the taxable year that exceeds the threshold amount determines the QBI component using the following computational rules, which are to be applied in the order they appear.

(i) SSTB exclusion. If the individual's taxable income is within the phase-in range, then only the applicable percentage of QBI, W-2 wages, and UBIA of qualified property for each SSTB is taken into account for all purposes of determining the individual's section 199A deduction, including the application of the netting and carryover rules described in paragraph (d)(2)(iii) of this section. If the individual's taxable income exceeds the phase-in range, then none of the individual's share of QBI, W-2 wages, or UBIA of qualified property attributable to an SSTB may be taken into account for purposes of determining the individual's section 199A deduction.

(ii) Aggregated trade or business. If an individual chooses to aggregate trades or businesses under the rules of §1.199A-4, the individual must combine the QBI, W-2 wages, and UBIA of qualified property of each trade or business within an aggregated trade or business prior to applying the netting and carryover rules described in paragraph (d)(2)(iii) of this section and the W-2 wage and UBIA of qualified property limitations described in paragraph (d)(2)(iv) of this section.

(iii) Netting and carryover-

(A) Netting. If an individual's QBI from at least one trade or business (including an aggregated trade or business) is less than zero, the individual must offset the QBI attributable to each trade or business (or aggregated trade or business) that produced net positive QBI with the QBI from each trade or business (or aggregated trade or business) that produced net negative QBI in proportion to the relative amounts of net QBI in the trades or businesses (or aggregated trades or businesses) with positive QBI. The adjusted QBI is then used in paragraph (d)(2)(iv) of this section. The W-2 wages and UBIA of qualified property from the trades or businesses (including aggregated trades or businesses) that produced net negative QBI are not taken into account for purposes of this paragraph (d) and are not carried over to the subsequent year.

(B) Carryover of negative total QBI amount. If an individual's QBI from all trades or businesses (including aggregated trades or businesses) combined is less than zero, the QBI component is zero for the taxable year. This negative amount is treated as negative QBI from a separate trade or business in the succeeding taxable years of the individual for purposes of section 199A and this section. This carryover rule does not affect the deductibility of the loss for purposes of other provisions of the Code. The W-2 wages and UBIA of qualified property from the trades or businesses (including aggregated trades or businesses) that produced net negative QBI are not taken into account for purposes of this paragraph (d) and are not carried over to the subsequent year.

(iv) QBI component calculation-

(A) General rule. Except as provided in paragraph (d)(2)(iv)(B) of this section, the QBI component is the sum of the amounts determined under

this paragraph (d)(2)(iv)(A) for each trade or business (or aggregated trade or business). For each trade or business (or aggregated trade or business) (including trades or businesses operated through RPEs) the individual must determine the lesser of-

(1) 20 percent of the QBI for that trade or business (or aggregated trade or business); or

(2) The greater of-

(i) 50 percent of W-2 wages with respect to that trade or business (or aggregated trade or business); or

(ii) The sum of 25 percent of W-2 wages with respect to that trade or business (or aggregated trade or business) plus 2.5 percent of the UBIA of qualified property with respect to that trade or business (or aggregated trade or business).

(B) Taxpayers with taxable income within phase-in range. If the individual's taxable income is within the phase-in range and the amount determined under paragraph (d)(2)(iv)(A)(2) of this section for a trade or business (or aggregated trade or business) is less than the amount determined under paragraph (d)(2)(iv)(A)(1) of this section for that trade or business (or aggregated trade or business), the amount determined under paragraph (d)(2)(iv)(A) of this section for such trade or business (or aggregated trade or business) is modified. Instead of the amount determined under paragraph (d)(2)(iv)(A)(2) of this section, the QBI component for the trade or business (or aggregated trade or business) is the amount determined under paragraph (d)(2)(iv)(A)(1) of this section reduced by the reduction amount as defined in paragraph (b)(9) of this section. This reduction amount does not apply if the amount determined in paragraph (d)(2)(iv)(A)(2) of this section is greater than the amount determined under paragraph (d)(2)(iv)(A)(1) of this section (in which circumstance the QBI component for the trade or business (or aggregated trade or business) will be the unreduced amount determined in paragraph (d)(2)(iv)(A)(1) of this section).

(3) Qualified REIT dividends/qualified PTP income component.

(i) In general. The qualified REIT dividend/qualified PTP income component is 20 percent of the combined amount of qualified REIT dividends and qualified PTP income received by the individual (including the individual's share of qualified REIT dividends and qualified PTP income from RPEs).

(ii) SSTB exclusion. If the individual's taxable income is within the phase-in range, then only the applicable percentage of qualified PTP income generated by an SSTB is taken into account for purposes of determining the individual's section 199A deduction, including the determination of the combined amount of qualified REIT dividends and qualified PTP income described in paragraph (d)(1) of this section. If the individual's taxable income exceeds the phase-in range, then none of the individual's share of qualified PTP income generated by an SSTB may be

taken into account for purposes of determining the individual's section 199A deduction.

(iii) Negative combined qualified REIT dividends/qualified PTP income. If the combined amount of REIT dividends and qualified PTP income is less than zero, the portion of the individual's section 199A deduction related to qualified REIT dividends and qualified PTP income is zero for the taxable year. The negative combined amount must be carried forward and used to offset the combined amount of REIT dividends/qualified PTP income in the succeeding taxable years of the individual for purposes of section 199A and this section. This carryover rule does not affect the deductibility of the loss for purposes of other provisions of the Code.

(4) Examples. The following examples illustrate the provisions of this paragraph (d). For purposes of these examples, unless indicated otherwise, assume that all of the trades or businesses are trades or businesses as defined in paragraph (b)(14) of this section, none of the trades or businesses are SSTBs as defined in paragraph (b)(11) of this section and §1.199A-5(b); and all of the tax items associated with the trades or businesses are effectively connected to a trade or business within the United States within the meaning of section 864(c). Also assume that the taxpayers report no capital gains or losses or other tax items not specified in the examples. Total taxable income does not include the section 199A deduction.

(i) Example (1). D, an unmarried individual, operates a business as a sole proprietorship. The business generates \$1,000,000 of QBI in 2018. Solely for purposes of this example, assume that the business paid no wages and holds no qualified property for use in the business. After allowable deductions unrelated to the business, D's total taxable income for 2018 is \$980,000. Because D's taxable income exceeds the applicable threshold amount, D's section 199A deduction is subject to the W-2 wage and UBIA of qualified property limitations. D's section 199A deduction is limited to zero because the business paid no wages and held no qualified property.

(ii) Example (2). Assume the same facts as in Example 1 of paragraph (d)(4)(i) of this section, except that D holds qualified property with a UBIA of \$10,000,000 for use in the trade or business. D reports \$4,000,000 of QBI for 2020. After allowable deductions unrelated to the business, D's total taxable income for 2020 is \$3,980,000. Because D's taxable income is above the threshold amount, the QBI component of D's section 199A deduction is subject to the W-2 wage and UBIA of qualified property limitations. Because the business has no W-2 wages, the QBI component of D's section 199A deduction is limited to the lesser of 20% of the business's QBI or 2.5% of its UBIA of qualified property. Twenty percent of the \$4,000,000 of QBI is \$800,000. Two and one-half percent of the \$10,000,000 UBIA of qualified property is \$250,000. The QBI component of D's section 199A deduction is thus limited to \$250,000. D's section 199A deduction is equal to the lesser of:

(A) 20% of the QBI from the business as limited (\$250,000); or

(B) 20% of D's taxable income ( $\$3,980,000 \times 20\% = \$796,000$ ).

Therefore, D's section 199A deduction for 2020 is \$250,000.

(iii) Example (3). E, an unmarried individual, is a 30% owner of LLC, which is classified as a partnership for Federal income tax purposes. In 2018, the LLC has a single trade or business and reports QBI of \$3,000,000. The LLC pays total W-2 wages of \$1,000,000, and its total UBIA of qualified property is \$100,000. E is allocated 30% of all items of the partnership. For the 2018 taxable year, E reports \$900,000 of QBI from the LLC. After allowable deductions unrelated to LLC, E's taxable income is \$880,000. Because E's taxable income is above the threshold amount, the QBI component of E's section 199A deduction will be limited to the lesser of 20% of E's share of LLC's QBI or the greater of the W-2 wage or UBIA of qualified property limitations. Twenty percent of E's share of QBI of \$900,000 is \$180,000. The W-2 wage limitation equals 50% of E's share of the LLC's wages (\$300,000) or \$150,000. The UBIA of qualified property limitation equals \$75,750, the sum of 25% of E's share of LLC's wages (\$300,000) or \$75,000 plus 2.5% of E's share of UBIA of qualified property (\$30,000) or \$750. The greater of the limitation amounts (\$150,000 and \$75,750) is \$150,000. The QBI component of E's section 199A deduction is thus limited to \$150,000, the lesser of 20% of QBI (\$180,000) and the greater of the limitations amounts (\$150,000). E's section 199A deduction is equal to the lesser of 20% of the QBI from the business as limited (\$150,000) or 20% of E's taxable income ( $\$880,000 \times 20\% = \$176,000$ ). Therefore, E's section 199A deduction is \$150,000 for 2018.

(iv) Example (4). F, an unmarried individual, owns a 50% interest in Z, an S corporation for Federal income tax purposes that conducts a single trade or business. In 2018, Z reports QBI of \$6,000,000. Z pays total W-2 wages of \$2,000,000, and its total UBIA of qualified property is \$200,000. For the 2018 taxable year, F reports \$3,000,000 of QBI from Z. F is not an employee of Z and receives no wages or reasonable compensation from Z. After allowable deductions unrelated to Z and a deductible qualified net loss from a PTP of (\$10,000), F's taxable income is \$1,880,000. Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction will be limited to the lesser of 20% of F's share of Z's QBI or the greater of the W-2 wage and UBIA of qualified property limitations. Twenty percent of F's share of Z's QBI (\$3,000,000) is \$600,000. The W-2 wage limitation equals 50% of F's share of Z's W-2 wages (\$1,000,000) or \$500,000. The UBIA of qualified property limitation equals \$252,500, the sum of 25% of F's share of Z's W-2 wages (\$1,000,000) or \$250,000 plus 2.5% of E's share of UBIA of qualified property (\$100,000) or \$2,500. The greater of the limitation amounts (\$500,000 and \$252,500) is \$500,000. The QBI component of F's section 199A deduction is thus limited to \$500,000, the lesser of 20% of QBI (\$600,000) and the greater of the limitations amounts (\$500,000). F reports a qualified loss from a PTP and has no qualified REIT dividend. F does not net the (\$10,000) loss from the PTP against QBI. Instead, the portion of F's section 199A deduction related to qualified REIT dividends and qualified PTP income is zero for 2018. F's section 199A deduction is equal to the lesser of 20% of the QBI from the business as limited (\$500,000) or 20% of F's taxable income over net capital gain ( $\$1,880,000 \times 20\% = \$376,000$ ). Therefore, F's section 199A deduction is \$376,000 for 2018. F must also carry forward the (\$10,000) qualified loss from a PTP to be netted against F's qualified REIT dividends and qualified PTP income in the succeeding taxable year.





(v) Example (5). Phase-in range.

(A) B and C are married and file a joint individual income tax return. B is a shareholder in M, an entity taxed as an S corporation for Federal income tax purposes that conducts a single trade or business. M holds no qualified property. B's share of the M's QBI is \$300,000 in 2018. B's share of the W-2 wages from M in 2018 is \$40,000. C earns wage income from employment by an unrelated company. After allowable deductions unrelated to M, B and C's taxable income for 2018 is \$375,000. B and C are within the phase-in range because their taxable income exceeds the applicable threshold amount, \$315,000, but does not exceed the threshold amount plus \$100,000, or \$415,000. Consequently, the QBI component of B and C's section 199A deduction may be limited by the W-2 wage and UBIA of qualified property limitations but the limitations will be phased in.

(B) Because M does not hold qualified property, only the W-2 wage limitation must be calculated. In order to apply the W-2 wage limitation, B and C must first determine 20% of B's share of M's QBI. Twenty percent of B's share of M's QBI of \$300,000 is \$60,000. Next, B and C must determine 50% of B's share of M's W-2 wages. Fifty percent of B's share of M's W-2 wages of \$40,000 is \$20,000. Because 50% of B's share of M's W-2 wages (\$20,000) is less than 20% of B's share of M's QBI (\$60,000), B and C must determine the QBI component of their section 199A deduction by reducing 20% of B's share of M's QBI by the reduction amount.

(C) B and C are 60% through the phase-in range (that is, their taxable income exceeds the threshold amount by \$60,000 and their phase-in range is \$100,000). B and C must determine the excess amount, which is the excess of 20% of B's share of M's QBI, or \$60,000, over 50% of B's share of M's W-2 wages, or \$20,000. Thus, the excess amount is \$40,000. The reduction amount is equal to 60% of the excess amount, or \$24,000. Thus, the QBI component of B and C's section 199A deduction is equal to \$36,000, 20% of B's \$300,000 share M's QBI (that is, \$60,000), reduced by \$24,000. B and C's section 199A deduction is equal to the lesser of 20% of the QBI from the business as limited (\$36,000) or 20% of B and C's taxable income ( $\$375,000 \times 20\% = \$75,000$ ). Therefore, B and C's section 199A deduction is \$36,000 for 2018.

(vi) Example (6).

(A) Assume the same facts as in Example 5 of paragraph (d)(4)(v) of this section, except that M is engaged in an SSTB. Because B and C are within the phase-in range, B must reduce the QBI and W-2 wages allocable to B from M to the applicable percentage of those items. B and C's applicable percentage is 100% reduced by the percentage equal to the ratio that their taxable income for the taxable year (\$375,000) exceeds their threshold amount (\$315,000), or \$60,000, bears to \$100,000. Their applicable percentage is 40%. The applicable percentage of B's QBI is ( $\$300,000 \times$

40% =) \$120,000, and the applicable percentage of B's share of W-2 wages is (\$40,000 x 40% =) \$16,000. These reduced numbers must then be used to determine how B's section 199A deduction is limited.

(B) B and C must apply the W-2 wage limitation by first determining 20% of B's share of M's QBI as limited by paragraph (d)(4)(vi)(A) of this section. Twenty percent of B's share of M's QBI of \$120,000 is \$24,000. Next, B and C must determine 50% of B's share of M's W-2 wages. Fifty percent of B's share of M's W-2 wages of \$16,000 is \$8,000. Because 50% of B's share of M's W-2 wages (\$8,000) is less than 20% of B's share of M's QBI (\$24,000), B and C's must determine the QBI component of their section 199A deduction by reducing 20% of B's share of M's QBI by the reduction amount.

(C) B and C are 60% through the phase-in range (that is, their taxable income exceeds the threshold amount by \$60,000 and their phase-in range is \$100,000). B and C must determine the excess amount, which is the excess of 20% of B's share of M's QBI, as adjusted in paragraph (d)(4)(vi)(A) of this section or \$24,000, over 50% of B's share of M's W-2 wages, as adjusted in paragraph (d)(4)(vi)(A) of this section, or \$8,000. Thus, the excess amount is \$16,000. The reduction amount is equal to 60% of the excess amount or \$9,600. Thus, the QBI component of B and C's section 199A deduction is equal to \$14,400, 20% of B's share M's QBI of \$24,000, reduced by \$9,600. B and C's section 199A deduction is equal to the lesser of 20% of the QBI from the business as limited (\$14,400) or 20% of B's and C's taxable income (\$375,000 x 20% = \$75,000). Therefore, B and C's section 199A deduction is \$14,400 for 2018.

(vii) Example (7).

(A) F, an unmarried individual, owns as a sole proprietor 100 percent of three trades or businesses, Business X, Business Y, and Business Z. None of the businesses hold qualified property. F does not aggregate the trades or businesses under § 1.199A-4. For taxable year 2018, Business X generates \$1 million of QBI and pays \$500,000 of W-2 wages with respect to the business. Business Y also generates \$1 million of QBI but pays no wages. Business Z generates \$2,000 of QBI and pays \$500,000 of W-2 wages with respect to the business. F also has \$750,000 of wage income from employment with an unrelated company. After allowable deductions unrelated to the businesses, F's taxable income is \$2,722,000.

(B) Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction is subject to the W-2 wage and UBIA of qualified property limitations. These limitations must be applied on a business-by-business basis. None of the businesses hold qualified property, therefore only the 50% of W-2 wage limitation must be calculated. Because QBI from each business is positive, F applies the limitation by determining the lesser of 20% of QBI and 50% of W-2 wages for each business. For Business X, the lesser of 20% of QBI (\$1,000,000 x 20 percent = \$200,000) and 50% of Business X's W-2

wages ( $\$500,000 \times 50\% = \$250,000$ ) is  $\$200,000$ . Business Y pays no W-2 wages. The lesser of 20% of Business Y's QBI ( $\$1,000,000 \times 20\% = \$200,000$ ) and 50% of its W-2 wages (zero) is zero. For Business Z, the lesser of 20% of QBI ( $\$2,000 \times 20\% = \$400$ ) and 50% of W-2 wages ( $\$500,000 \times 50\% = \$250,000$ ) is  $\$400$ .

(C) Next, F must then combine the amounts determined in paragraph (d)(4)(vii)(B) of this section and compare that sum to 20% of F's taxable income. The lesser of these two amounts equals F's section 199A deduction. The total of the combined amounts in paragraph (d)(4)(vii)(B) of this section is  $\$200,400$  ( $\$200,000 + \text{zero} + 400$ ). Twenty percent of F's taxable income is  $\$544,400$  ( $\$2,722,000 \times 20\%$ ). Thus, F's section 199A deduction for 2018 is  $\$200,400$ .

(viii) Example (8).

(A) Assume the same facts as in Example 7 of paragraph (d)(4)(vii) of this section, except that F aggregates Business X, Business Y, and Business Z under the rules of § 1.199A-4.

(B) Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction is subject to the W-2 wage and UBIA of qualified property limitations. Because the businesses are aggregated, these limitations are applied on an aggregated basis. None of the businesses holds qualified property, therefore only the W-2 wage limitation must be calculated. F applies the limitation by determining the lesser of 20% of the QBI from the aggregated businesses, which is  $\$400,400$  ( $\$2,002,000 \times 20\%$ ) and 50% of W-2 wages from the aggregated businesses, which is  $\$500,000$  ( $\$1,000,000 \times 50\%$ ). F's section 199A deduction is equal to the lesser of  $\$400,400$  and 20% of F's taxable income ( $\$2,722,000 \times 20\% = \$544,400$ ). Thus, F's section 199A deduction for 2018 is  $\$400,400$ .

(ix) Example (9).

(A) Assume the same facts as in Example 7 of paragraph (d)(4)(vii) of this section, except that for taxable year 2018, Business Z generates a loss that results in  $(\$600,000)$  of negative QBI and pays  $\$500,000$  of W-2 wages. After allowable deductions unrelated to the businesses, F's taxable income is  $\$2,120,000$ . Because Business Z had negative QBI, F must offset the positive QBI from Business X and Business Y with the negative QBI from Business Z in proportion to the relative amounts of positive QBI from Business X and Business Y. Because Business X and Business Y produced the same amount of positive QBI, the negative QBI from Business Z is apportioned equally among Business X and Business Y. Therefore, the adjusted QBI for each of Business X and Business Y is  $\$700,000$  ( $\$1 \text{ million plus } 50\% \text{ of the negative QBI of } \$600,000$ ). The adjusted QBI in Business Z is  $\$0$ , because its negative QBI has been fully apportioned to Business X and Business Y.

(B) Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction is subject to the W-2 wage and UBI of qualified property limitations. These limitations must be applied on a business-by-business basis. None of the businesses hold qualified property, therefore only the 50% of W-2 wage limitation must be calculated. For Business X, the lesser of 20% of QBI ( $\$700,000 \times 20\% = \$140,000$ ) and 50% of W-2 wages ( $\$500,000 \times 50\% = \$250,000$ ) is  $\$140,000$ . Business Y pays no W-2 wages. The lesser of 20% of Business Y's QBI ( $\$700,000 \times 20\% = \$140,000$ ) and 50% of its W-2 wages (zero) is zero.

(C) F must combine the amounts determined in paragraph (d)(4)(ix)(B) of this section and compare the sum to 20% of taxable income. F's section 199A deduction equals the lesser of these two amounts. The combined amount from paragraph (d)(4)(ix)(B) of this section is  $\$140,000$  ( $\$140,000 + \text{zero}$ ) and 20% of F's taxable income is  $\$424,000$  ( $\$2,120,000 \times 20\%$ ). Thus, F's section 199A deduction for 2018 is  $\$140,000$ . There is no carryover of any loss into the following taxable year for purposes of section 199A.

(x) Example (10).

(A) Assume the same facts as in Example 9 of paragraph (d)(4)(ix) of this section, except that F aggregates Business X, Business Y, and Business Z under the rules of § 1.199A-4.

(B) Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction is subject to the W-2 wage and UBI of qualified property limitations. Because the businesses are aggregated, these limitations are applied on an aggregated basis. None of the businesses holds qualified property, therefore only the W-2 wage limitation must be calculated. F applies the limitation by determining the lesser of 20% of the QBI from the aggregated businesses ( $\$1,400,000 \times 20\% = \$280,000$ ) and 50% of W-2 wages from the aggregated businesses ( $\$1,000,000 \times 50\% = \$500,000$ ), or  $\$280,000$ . F's section 199A deduction is equal to the lesser of  $\$280,000$  and 20% of F's taxable income ( $\$2,120,000 \times 20\% = \$424,000$ ). Thus, F's section 199A deduction for 2018 is  $\$280,000$ . There is no carryover of any loss into the following taxable year for purposes of section 199A.

(xi) Example (11).

(A) Assume the same facts as in Example 7 of paragraph (d)(4)(vii) of this section, except that Business Z generates a loss that results in  $(\$2,150,000)$  of negative QBI and pays  $\$500,000$  of W-2 wages with respect to the business in 2018. Thus, F has a negative combined QBI of  $(\$150,000)$  when the QBI from all of the businesses are added together ( $\$1$  million plus  $\$1$  million minus the loss of  $(\$2,150,000)$ ). Because F has a negative combined QBI for 2018, F has no section 199A deduction with respect to any trade or business for 2018. Instead, the negative combined QBI of  $(\$150,000)$  carries forward and will be treated as negative QBI from a

separate trade or business for purposes of computing the section 199A deduction in the next taxable year. None of the W-2 wages carry forward. However, for income tax purposes, the \$150,000 loss may offset F's \$750,000 of wage income (assuming the loss is otherwise allowable under the Code).

(B) In taxable year 2019, Business X generates \$200,000 of net QBI and pays \$100,000 of W-2 wages with respect to the business. Business Y generates \$150,000 of net QBI but pays no wages. Business Z generates a loss that results in (\$120,000) of negative QBI and pays \$500 of W-2 wages with respect to the business. F also has \$750,000 of wage income from employment with an unrelated company. After allowable deductions unrelated to the businesses, F's taxable income is \$960,000. Pursuant to paragraph (d)(2)(iii)(B) of this section, the (\$150,000) of negative QBI from 2018 is treated as arising in 2019 from a separate trade or business. Thus, F has overall net QBI of \$80,000 when all trades or businesses are taken together (\$200,000) plus \$150,000 minus \$120,000 minus the carryover loss of (\$150,000). Because Business Z had negative QBI and F also has a negative QBI carryover amount, F must offset the positive QBI from Business X and Business Y with the negative QBI from Business Z and the carryover amount in proportion to the relative amounts of positive QBI from Business X and Business Y. Because Business X produced 57.14% of the total QBI from Business X and Business Y, 57.14% of the negative QBI from Business Z and the negative QBI carryforward must be apportioned to Business X, and the remaining 42.86% allocated to Business Y. Therefore, the adjusted QBI in Business X is \$45,722 (\$200,000 minus 57.14% of the loss from Business Z (\$68,568), minus 57.14% of the carryover loss (\$85,710)). The adjusted QBI in Business Y is \$34,278 (\$150,000, minus 42.86% of the loss from Business Z (\$51,432) minus 42.86% of the carryover loss (\$64,290)). The adjusted QBI in Business Z is \$0, because its negative QBI has been apportioned to Business X and Business Y.

(C) Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction is subject to the W-2 wage and UBI of qualified property limitations. These limitations must be applied on a business-by-business basis. None of the businesses hold qualified property, therefore only the 50% of W-2 wage limitation must be calculated. For Business X, 20% of QBI is \$9,144 (\$45,722 x 20%) and 50% of W-2 wages is \$50,000 (\$100,000 x 50%), so the lesser amount is \$9,144. Business Y pays no W-2 wages. Twenty percent of Business Y's QBI is \$6,856 (\$34,278 x 20%) and 50% of its W-2 wages (zero) is zero, so the lesser amount is zero.

(D) F must then compare the combined amounts determined in paragraph (d)(4)(xi)(C) of this section to 20% of F's taxable income. The section 199A deduction equals the lesser of these amounts. F's combined amount from paragraph (d)(4)(xi)(C) of this section is \$9,144 (\$9,144 plus zero) and 20% of F's taxable income is \$192,000 (\$960,000 x 20%) Thus, F's

section 199A deduction for 2019 is \$9,144. There is no carryover of any negative QBI into the following taxable year for purposes of section 199A.

(xii) Example (12).

(A) Assume the same facts as in Example 11 of paragraph (d)(4)(xi) of this section, except that F aggregates Business X, Business Y, and Business Z under the rules of § 1.199A-4. For 2018, F's QBI from the aggregated trade or business is (\$150,000). Because F has a combined negative QBI for 2018, F has no section 199A deduction with respect to any trade or business for 2018. Instead, the negative combined QBI of (\$150,000) carries forward and will be treated as negative QBI from a separate trade or business for purposes of computing the section 199A deduction in the next taxable year. However, for income tax purposes, the \$150,000 loss may offset taxpayer's \$750,000 of wage income (assuming the loss is otherwise allowable under the Code).

(B) In taxable year 2019, F will have QBI of \$230,000 and W-2 wages of \$100,500 from the aggregated trade or business. F also has \$750,000 of wage income from employment with an unrelated company. After allowable deductions unrelated to the businesses, F's taxable income is \$960,000. F must treat the negative QBI carryover loss (\$150,000) from 2018 as a loss from a separate trade or business for purposes of section 199A. This loss will offset the positive QBI from the aggregated trade or business, resulting in an adjusted QBI of \$80,000 (\$230,000 - \$150,000).

(C) Because F's taxable income is above the threshold amount, the QBI component of F's section 199A deduction is subject to the W-2 wage and UBIA of qualified property limitations. These limitations must be applied on a business-by-business basis. None of the businesses hold qualified property, therefore only the 50% of W-2 wage limitation must be calculated. For the aggregated trade or business, the lesser of 20% of QBI ( $\$80,000 \times 20\% = \$16,000$ ) and 50% of W-2 wages ( $\$100,500 \times 50\% = \$50,250$ ) is \$16,000. F's section 199A deduction equals the lesser of that amount (\$16,000) and 20% of F's taxable income ( $\$960,000 \times 20\% = \$192,000$ ). Thus, F's section 199A deduction for 2019 is \$16,000. There is no carryover of any negative QBI into the following taxable year for purposes of section 199A.

(e) Special rules.

(1) Effect of deduction. In the case of a partnership or S corporation, section 199A is applied at the partner or shareholder level. The rules of subchapter K and subchapter S of the Code apply in their entirety for purposes of determining each partner's or shareholder's share of QBI, W-2 wages, UBIA of qualified property, qualified REIT dividends, and qualified PTP income or loss. The section 199A deduction has no effect on the adjusted basis of a partner's interest in the partnership, the adjusted basis of a shareholder's stock in an S corporation, or an S corporation's accumulated adjustments account.

(2) Disregarded entities. An entity with a single owner that is treated as disregarded as an entity separate from its owner under any provision of the Code is disregarded for purposes of section 199A and §§1.199A-1 through 1.199A-6.

(3) Self-employment tax and net investment income tax. The deduction allowed under section 199A does not reduce net earnings from self-employment under section 1402 or net investment income under section 1411.

(4) Commonwealth of Puerto Rico. If all of an individual's QBI from sources within the Commonwealth of Puerto Rico is taxable under section 1 of the Code for a taxable year, then for purposes of determining the QBI of such individual for such taxable year, the term "United States" includes the Commonwealth of Puerto Rico.

(5) Coordination with alternative minimum tax. For purposes of determining alternative minimum taxable income under section 55, the deduction allowed under section 199A(a) for a taxable year is equal in amount to the deduction allowed under section 199A(a) in determining taxable income for that taxable year (that is, without regard to any adjustments under sections 56 through 59).

(6) Imposition of accuracy-related penalty on underpayments. For rules related to the imposition of the accuracy-related penalty on underpayments for taxpayers who claim the deduction allowed under section 199A, see section 6662(d)(1)(C).

(7) Reduction for income received from cooperatives. In the case of any trade or business of a patron of a specified agricultural or horticultural cooperative, as defined in section 199A(g)(4), the amount of section 199A deduction determined under paragraph (c) or (d) of this section with respect to such trade or business must be reduced by the lesser of:

(i) Nine percent of the QBI with respect to such trade or business as is properly allocable to qualified payments received from such cooperative; or

(ii) 50 percent of the W-2 wages with respect to such trade or business as are so allocable as determined under §1.199A-2.

(f) Applicability date.

(1) General rule. Except as provided in paragraph (f)(2) of this section, the provisions of this section apply to taxable years ending after February 8, 2019.

(2) Exception for non-calendar year RPE. For purposes of determining QBI, W-2 wages, UBIA of qualified property, and the aggregate amount of qualified REIT dividends and qualified PTP income, if an individual receives any of these items from an RPE with a taxable year that begins before January 1, 2018, and ends after December 31, 2017, such items are treated as having been incurred by the individual during the individual's taxable year in which or with which such RPE taxable year ends.