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Proposed 199A Regulations Changes

Proposed regulations issued on August 8, 2018 could limit the availability of the §199A deduction, also known as the 20% or pass-through deduction. In the original legislation passed by Congress and signed into law last December, dental services wouldn't qualify for this special deduction unless certain income levels were met. However, until now it appeared that rental income and management services would still qualify. Under the proposed regulations issued on August 8, 2018, reorganizing a business in order to break out the non-dental services, will still not allow the separate business income to qualify for the 20% or pass-through deduction.

SSTB = a specified service trade or business income such as a dental practice or law firm. Income from an SSTB doesn't qualify for the 20% deduction if the individual's taxable income is over $415,000 (Married filing joint) or $207,500 (single)

Examples from the proposed regulation:

Example 1
A dentist, owns a dental practice and also owns an office building. The dentist rents half the building to the dental practice and half the building to unrelated persons. Under proposed §1.199A-5(c)(2), the renting of half of the building to the dental practice will be treated as an SSTB.

Example 2
A Law Firm is a partnership that provides legal services to clients, it owns its own office building and employs its own administrative staff. The Law Firm divides into three partnerships.

Partnership 1 performs legal services to clients. Partnership 2 owns the office building and rents the entire building to Partnership 1.
Partnership 3 employs the administrative staff and through a contract with Partnership 1 provides

administrative services to Partnership 1 in exchange for fees.

All three of the partnerships are owned by the same people (the original owners of Law Firm). Because there is 50% or more common ownership of each of the three partnerships, Partnership 2 provides substantially all of its property to Partnership 1, and Partnership 3 provides substantially all of its services to Partnership 1, Partnerships 1, 2, and 3 will be treated as one SSTB under paragraph (a)(6) of this section.

With this new proposed 199A regulations, if you were thinking of setting up a management company only to take advantage of the tax deduction, we advise you to contact our office before proceeding.