

Example: Prop. Reg. § 199A-6(d)(3)(vi)

(vi) Example. (i) Computation of DNI and inclusion and deduction amounts.

(A) Trust's distributive share of partnership items. Trust, an irrevocable testamentary complex trust, is a 25% partner in PRS, a family partnership that operates a restaurant that generates QBI and W-2 wages. In 2018, PRS properly allocates gross income from the restaurant of \$55,000, and expenses directly allocable to the restaurant of \$50,000 (including W-2 wages of \$25,000, miscellaneous expenses of \$20,000, and depreciation deductions of \$5,000) to Trust. These items are properly included in Trust's DNI. Trust's share of PRS' unadjusted basis of qualified depreciable property is \$125,000. PRS distributes \$5,000 of cash to Trust in 2018.

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(B) Trust's activities. In addition to its interest in PRS, Trust also operates a family bakery conducted through an LLC wholly-owned by the Trust that is treated as a disregarded entity. In 2018, the bakery produced \$100,000 of gross income and \$150,000 of expenses directly allocable to operation of the bakery (including W-2 wages of \$50,000, rental expense of \$75,000, and miscellaneous expenses of \$35,000). (The net loss from the bakery operations is not subject to any loss disallowance provisions outside of section 199A.)

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Trust also has zero unadjusted basis of qualified depreciable property in the bakery. For purposes of computing its section 199A deduction, Trust has properly chosen to aggregate the family restaurant conducted through PRS with the bakery conducted directly by Trust under § 1.199A-4. Trust also owns various investment assets that produce portfolio-type income consisting of dividends (\$25,000), interest (\$15,000), and tax-exempt interest (\$15,000).

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Accordingly, Trust has the following items which are properly included in Trust's DNI:

Interest Income	15,000
Dividends	25,000
Tax-exempt interest	15,000
Net business loss from PRS and bakery	(45,000)
Trustee commissions	3,000
State and local taxes	5,000

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(C) Allocation of deductions under §1.652(b)-3. (1) Directly attributable expenses. In computing Trust's DNI for the taxable year, the distributive share of expenses of PRS are directly attributable under §1.652(b)-3(a) to the distributive share of income of PRS. Accordingly, Trust has gross business income of \$155,000 (\$55,000 from PRS and \$100,000 from the bakery) and direct business expenses of \$200,000 (\$50,000 from PRS and \$150,000 from the bakery). In addition, \$1,000 of the trustee commissions and \$1,000 of state and local taxes are directly attributable under §1.652(b)-3(a) to Trust's business income.

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Accordingly, Trust has excess business deductions of \$47,000. Pursuant to its authority recognized under §1.652(b)-3(d), Trust allocates the \$47,000 excess business deductions as follows: \$15,000 to the interest income, resulting in \$0 interest income, \$25,000 to the dividends, resulting in \$0 dividend income, and \$7,000 to the tax exempt interest.

(2) Non-directly attributable expenses. The trustee must allocate the sum of the balance of the trustee commissions (\$2,000) and state and local taxes (\$4,000) to Trust's remaining tax-exempt interest income, resulting in \$2,000 of tax exempt interest.

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(D) Amounts included in taxable income. For 2018, Trust has DNI of \$2,000. Pursuant to Trust's governing instrument, Trustee distributes 50%, or \$1,000, of that DNI to A, an individual who is a discretionary beneficiary of Trust. In addition, Trustee is required to distribute 25%, or \$500, of that DNI to B, a current income beneficiary of Trust. Trust retains the remaining 25% of DNI. Consequently, with respect to the \$1,000 distribution A receives from Trust, A properly excludes \$1,000 of tax-exempt interest income under section 662(b). With respect to the \$500 distribution B receives from Trust, B properly excludes \$500 of tax-exempt interest income under section 662(b). Because the DNI consists entirely of tax-exempt income, Trust deducts \$0 under section 661 with respect to the distributions to A and B.

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(ii) Section 199A deduction. (A) Trust's W-2 wages and QBI. For the 2018 taxable year, Trust has \$75,000 (\$25,000 from PRS + \$50,000 of Trust) of W-2 wages. Trust also has \$125,000 of unadjusted basis in qualified depreciable property. Trust has negative QBI of (\$47,000) (\$155,000 gross income from aggregated businesses less the sum of \$200,000 direct expenses from aggregated businesses and \$2,000 directly attributable business expenses from Trust under the rules of §1.652(b)-3(a)).

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(B) Section 199A deduction computation. (1) A's computation. Because the \$1,000 Trust distribution to A equals one-half of Trust's DNI, A has W-2 wages from Trust of \$37,500. A also has W-2 wages of \$2,500 from a trade or business outside of Trust (computed without regard to A's interest in Trust), which A has properly aggregated under §1.199A-4 with the Trust's trade or businesses (the family's restaurant and bakery), for a total of \$40,000 of W-2 wages from the aggregate trade or businesses. A has \$100,000 of QBI from non-Trust trade or businesses in which A owns an interest. Because the \$1,000 Trust distribution to A equals one-half of Trust's DNI, A has (negative) QBI from Trust of (\$23,500). A's total QBI is determined by combining the \$100,000 QBI from non-Trust sources with the (\$23,500) QBI from Trust for a total of \$76,500 of QBI. Assume that A's taxable income exceeds the threshold amount for 2018 by \$200,000. A's tentative deduction is \$15,300 ($.20 \times \$76,500$), limited under the W-2 wage limitation to \$20,000 ($50\% \times \$40,000$ W-2 wages). Accordingly, A's section 199A deduction for 2018 is \$15,300.

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(2) B's computation. For 2018, B's taxable income is below the threshold amount so B is not subject to the W-2 wage limitation. Because the \$500 Trust distribution to B equals one-quarter of Trust's DNI, B has a total of (\$11,750) of QBI. B also has no QBI from non-Trust trades or businesses, so B has a total of (\$11,750) of QBI. Accordingly, B's section 199A deduction for 2018 is zero. The (\$11,750) of QBI is carried over to 2019 as a loss from a qualified business in the hands of B pursuant to section 199A(c)(2).

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(3) Trust's computation. For 2018, Trust's taxable income is below the threshold amount so it is not subject to the W-2 wage limitation. Because Trust retained 25% of Trust's DNI, Trust is allocated 25% of its QBI, which is (\$11,750). Trust's section 199A deduction for 2018 is zero. The (\$11,750) of QBI is carried over to 2019 as a loss from a qualified business in the hands of Trust pursuant to section 199A(c)(2).

Permissive Aggregation of Trades and Businesses

Proposed Regulations allow – but do not mandate (except in certain circumstances) – the aggregation of multiple QTBs owned directly by individuals and/or the individual's share of QBI, W-2 wages, and UBI of qualified property from trades or businesses operated through RPEs.

- RPEs cannot aggregate; only individuals, estates, and trusts can aggregate

Four factors to aggregate

(1) same person, or group of persons, must directly or indirectly, own 50% or more of each trade or business to be aggregated for a majority of the taxable year in which the items attributable to each trade or business to be aggregated are included in income

- No attribution between siblings

(2) all the items attributable to each trade or business to be aggregated must be reported on returns within the same taxable year, not considering short taxable years

Four factors to aggregate

- (3) none of the aggregated trades or businesses may be an SSTB
- (4) two out of three of the following enumerated factors demonstrating that the businesses are in fact part of a larger, integrated trade or business must exist
 - (a) the trades or businesses provide products and services that are the same or customarily offered together
 - (b) the trades or businesses share facilities or share significant centralized business elements, such as personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources
 - (c) the trades or businesses are operated in coordination with, or reliance upon, one or more of the businesses in the aggregated group (for example, supply chain interdependencies)

Operational Rules for Aggregating

- If an individual chooses to aggregate, it must combine the QBI, W-2 wages, and UBIA of qualified property for all aggregated trades or businesses for purposes of applying the wage and property limitations
- Owners of RPE do not have to aggregate in same manner

Consistency and Reporting Requirements:

- Once aggregated must consistently report aggregated trades or businesses in all subsequent taxable years, but can add a new business to the aggregation and can disaggregate under certain factual changes
- If one chooses to aggregate, one must attach statement to return with certain information
- IRS can disaggregate for failure to provide information

How To Determine Which Trades Or Businesses MAY Be Aggregated

Ownership →

Does the same person or group of persons, directly or indirectly, own 50% or more of each trade or business to be aggregated?

Taxable year →

Does such ownership exist for the majority of the applicable taxable year?

Are all items attributable to each trade or business to be aggregated reported on returns with the same taxable year?

No SSTB →

Are any of the trades or businesses to be aggregated an SSTB?

Necessary factors

Do the trades or businesses exhibit at least 2 of the following 3 factors?

- 1). Products and services provided are the same or customarily provided together
- 2). Shared facilities or shared significant centralized business elements
- 3). Operated in coordination with, or reliance on, one or more of the businesses in the aggregated group

Selected Clarifications In Proposed Regulations

- “Reasonable compensation” concept does not apply outside the context of S corporations for purposes of section 199A
 - Concept is not extended to partnerships
 - Wage income received by an employee is never QBI

Selected Clarifications In Proposed Regulations

- Narrow construction of what constitutes a trade or business where the principal asset of such trade or business is the reputation or skills of one or more of its employees or owners, thereby causing it to be characterized as an SSTB
 - Trade or business in which a person receives fees, compensation, or other income for endorsing products or services
 - Trade or business in which a person licenses or receives fees, compensation, or other income for the use of an individual's likeness, name, signature, voice, trademark, or any other symbols associated with an individual's identity
 - Receiving fees, compensation, or other income for appearing at an event or on radio, television, or another media format
 - Fees, compensation, or other income is defined to include receipt of a partnership interest or receipt of stock in an S corporation and the corresponding income, deductions, gains or losses