The Section 199A Deduction Formula

In a nutshell, the Section 199A "pass-through entity" tax cut gives the owners of pass-through businesses like sole proprietors, partnerships, S corporations, and some real estate investors a deduction equal to 20% of qualified business income.[2]

For example, if each of the following "pass-through" taxpayers earns $10,000 of qualified business income, each potentially gets a $2,000 tax deduction, calculated as 20% of $10,000:

- a sole proprietor making $10,000
- a partner earning $10,000 from a partnership
- an S corporation shareholder earning $10,000 from an interest in an S corporation
- a rental property investor earning $10,000 from a real estate investment portfolio

No limit exists, though some restrictions and special requirements kick in when a taxpayer's income rises.

Accordingly, someone who earns $100,000 may receive a $20,000 deduction. Someone who earns $1,000,000 may receive a $200,000. Some who receives $10,000,000 may receive a $2,000,000 deduction and so on.[3]

In addition to a deduction based on the business income from a pass-through entity, Section 199A also gives a taxpayer a deduction equal to 20% of any qualified real estate investment trust (REIT) dividends and 20% of any qualified publicly traded partnership business income. A taxpayer receiving $10,000 of REIT dividends or $10,000 of qualified publicly traded partnership income also potentially gets a $2,000 tax deduction.

Finally, Section 199A also gives qualified agricultural and horticultural cooperatives as well as their members a deduction. That deduction sort of equals 20% of the business income subject to some complicated rules.

---

[2] Sec. 199A(a) and Sec. 199A(b).

[3] The Sec. 199A deduction reduces alternative minimum taxable income, too.