



*Tax Cuts and Jobs Act: Implementation of
the Qualified Business Income Deduction*

March 18, 2019

Reference Number: 2019-44-022

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

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2 = Law Enforcement Techniques/ Procedures and Guidelines for Law Enforcement Investigations or Prosecutions

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HIGHLIGHTS

TAX CUTS AND JOBS ACT: IMPLEMENTATION OF THE QUALIFIED BUSINESS INCOME DEDUCTION

Highlights

Final Report issued on March 18, 2019

Highlights of Reference Number: 2019-44-022 to the Commissioner of Internal Revenue.

IMPACT ON TAXPAYERS

The Tax Cuts and Jobs Act of 2017 includes Internal Revenue Code Section 199A, which provides individuals with a new tax deduction for qualified business income. Section 199A provides a deduction of up to 20 percent for an individual's domestic qualified business income from their taxable income. The IRS estimates that almost 23.7 million taxpayers may be eligible to claim the deduction. In addition, the Joint Committee on Taxation estimates a reduction in tax from this provision of \$27.7 billion in Fiscal Year 2018 and \$47.1 billion in Fiscal Year 2019, and totaling \$414.5 billion over Fiscal Years 2018 through 2027.

WHY TIGTA DID THE AUDIT

This review is part of TIGTA's overall audit strategy assessing the IRS's implementation of the Tax Cuts and Jobs Act. TIGTA performed this separate review of the IRS's implementation of the Section 199A Qualified Business Income Deduction because of its complexities and impact on taxpayers.

WHAT TIGTA FOUND

The IRS took proactive steps to implement the Qualified Business Income Deduction including establishing an implementation team, creating an action plan, and developing a communication strategy. However, IRS management indicated that due to the timing of the release of guidance, the IRS was unable to develop a tax form for the deduction. IRS management indicated that delaying the development of a tax form until Tax Year 2019 allowed the IRS to receive comments on the guidance, consider those comments before finalizing the guidance, and gain some

experience with the first filing season. As an alternative, the IRS developed a worksheet to assist taxpayers with calculating the Qualified Business Income Deduction.

In addition, IRS management responded that they would like to ensure an appropriate balance between compliance risk and taxpayer burden. IRS management plans to develop a post-processing compliance plan. Near the conclusion of our fieldwork, the IRS prepared a computer programming request. IRS management, management plans to develop a post-processing compliance plan. Near the conclusion of our fieldwork, the IRS prepared a computer programming request.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS ensure that computer programming, and timely implement the post-processing compliance plan.

IRS management agreed with all three recommendations and plans to take appropriate corrective actions.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 18, 2019

MEMORANDUM FOR COMMISSIONER OF INTERNAL REVENUE

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Tax Cuts and Jobs Act: Implementation of the
Qualified Business Income Deduction (Audit # 201840435)

This report presents the results of our review to assess the Internal Revenue Service’s actions to implement Provision 11011 of the Tax Cuts and Jobs Act of 2017.¹ This review is included in our Fiscal Year 2019 Annual Audit Plan and addresses the major management challenge of Implementing the Tax Cuts and Jobs Act and Other Tax Law Changes.

Management’s complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. If you have any questions, please contact me or Russell P. Martin, Assistant Inspector General for Audit (Returns Processing and Account Services).

¹ Pub. L. No. 115-97. Officially known as “An act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for Fiscal Year 2018.”



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Abbreviations

IRS	Internal Revenue Service
SB/SE	Small Business/Self-Employed
TY	Tax Year



*Tax Cuts and Jobs Act: Implementation
of the Qualified Business Income Deduction*

Background

The Tax Cuts and Jobs Act,¹ signed into law on December 22, 2017, includes Provision 11011 which creates a new Internal Revenue Code Section 199A, *i.e.*, Qualified Business Income Deduction. This provision provides individuals with a new tax deduction for qualified business income. On March 23, 2018, the President also signed into law the Consolidated Appropriations Act of 2018² which requires patrons of specified cooperatives³ to reduce their Qualified Business Income Deduction when receiving certain income from the specified cooperatives. Section 199A provides a deduction for taxable years beginning after December 31, 2017, of up to 20 percent of an individual's domestic qualified business income plus 20 percent of qualified real estate investment trust dividends and qualified publicly traded partnership income from their taxable income. The deduction is for owners of domestic businesses operated as a sole proprietorship or through a partnership, S corporation, trust, or estate. Individual taxpayers claim this deduction on their Form 1040, *U.S. Individual Income Tax Return*. In addition to individual taxpayers, some estates and trusts can also take the Section 199A deduction. A Section 199A deduction is not available for wage income or for business income earned through a C corporation.

Qualified business income is the total amount of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer. The Qualified Business Income Deduction may be subject to limitations based on the type of trade or business, the taxpayer's taxable income, the amount of Form W-2, *Wage and Tax Statement*, wages paid with respect to the qualified trade or business, and the unadjusted basis of qualified property held by the trade or business. For purposes of the deduction, there are two business categories:

- **Specified service trade or business:** Any domestic trade or business, other than a C corporation, involving the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any business where the principal asset is the reputation of its employees.
- **Qualified trade or business:** Any domestic trade or business, other than a C corporation, that is not a specified service trade or business and does not perform services as an employee.

¹ Pub. L. No. 115-97. Officially known as "An act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for Fiscal Year 2018."

² Pub. L. No. 115-141.

³ An organization that engages in: 1) the manufacturing, production, growth, or extraction of any agricultural or horticultural products, and 2) the marketing of these products.



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This review is part of our overall audit strategy assessing the Internal Revenue Service's (IRS) implementation of the Tax Cuts and Jobs Act. We performed this separate review of the IRS's implementation of the Section 199A Qualified Business Income Deduction because of the complex nature of the provision, the millions of taxpayers eligible to claim the deduction, and the billions of dollars in tax potentially reduced by taxpayers claiming this deduction. This review was performed at the Small Business/Self-Employed (SB/SE) Division, Headquarters Examination function in New Carrollton, Maryland; the Wage and Investment Division in Atlanta, Georgia; and the Office of Chief Counsel in Washington D.C., during the period May through October 2018. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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Results of Review

The IRS initiated a number of proactive steps regarding the implementation of the Qualified Business Income Deduction. For example:

- The IRS established an implementation team with representatives from both the SB/SE and the Large Business and International Divisions. Both divisions focused jointly on implementing the deduction as defined in the Tax Cuts and Jobs Act and the revisions made by the Consolidated Appropriations Act of 2018.
- The Tax Reform Implementation Office has centralized responsibility for leading and coordinating IRS implementation efforts. The Tax Reform Implementation Office worked with the business units to identify impacted areas, *i.e.*, tax products, employee training, *etc.*, and to track the progress of the implementation efforts.
- The IRS also created an action plan outlining necessary actions to update existing forms, instructions, and publications; determine necessary computer programming updates; communicate changes externally; provide training to employees, *etc.*
- The IRS developed a communication strategy to provide taxpayers information about the Qualified Business Income Deduction. The IRS plans to provide information through various outreach platforms including IRS.gov, videos, webinars, social media, and events. Outreach began in July 2018 with the start of the Tax Forums, and communication will continue throughout Calendar Years 2018 and 2019.

However, IRS management indicated that timing in the issuance of guidance did not provide sufficient time to develop a separate Qualified Business Income Deduction tax form. A separate tax form would allow the IRS to capture data to assist in evaluating compliance with the deduction requirements. The IRS could use information from a form to improve systemic identification of erroneous deduction amounts.

*****2*****
*****2*****
*****2*****
*****2*****. The IRS estimates that almost 23.7 million taxpayers may be eligible to claim the deduction. In addition, the Joint Committee on Taxation estimates a reduction in tax from this provision of \$27.7 billion in Fiscal Year⁴ 2018 and \$47.1 billion in Fiscal Year 2019, and totaling \$414.5 billion over Fiscal Years 2018 through 2027.

⁴ Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.



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**Timing of the Release of Guidance Adversely Affected the Ability to
Develop a Qualified Business Income Deduction Tax Form**

IRS management *****7*****
*****7*****
*****7*****
*****7*****
*****7*****. For example, the implementation team needed clarification on the treatment of a partner’s guaranteed payments and how income or loss is reported when a taxpayer has multiple qualified trades or businesses.

*****7*****. As such, the implementation team believed there would not be sufficient time to develop and program the requirements for a new tax form, especially because the initial due date for completing these tasks was April 30, 2018. Programming of requirements involves developing a Work Request Notification to create the new tax form, identifying business requirements and other programming changes, and submitting this information to the Information Technology organization for review and approval.

As an alternative, the IRS developed a worksheet to assist taxpayers with calculating the Qualified Business Income Deduction because this would not require a Work Request Notification or other programming needed to develop a new form. The IRS indicated that the worksheet was not due to the Tax Forms and Publications Office until September 1, 2018, *****7*****
*****7*****. The IRS will not require the worksheet to be attached with the taxpayer’s filed tax return in support of the deduction. Figure 1 provides a timeline for the IRS’s implementation activities for the Qualified Business Income Deduction.



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Figure 1: Timeline of the IRS's Implementation Activities

Date	Description of IRS Action Taken
*****7*****	*****7***** *****7***** *****7***** *****7***** *****7***** *****7***** *****7*****.
February 14, 2018	The IRS prepared an action plan that continued evolving over time and identified 11 tax forms, 14 instructions, and five publications that required updates for Tax Year (TY) 2018. The primary form that required updating was Form 1040 in which taxpayers would claim the Qualified Business Income Deduction. Other key forms the IRS updated include: Schedule K-1, <i>Partner's Share of Income, Deductions, Credits, etc.</i> , of Form 1065, <i>U.S. Return of Partnership Income</i> ; and Schedule K-1, <i>Shareholder's Share of Income, Deductions, Credits, etc.</i> , of Form 1120S, <i>U.S. Income Tax Return for an S Corporation</i> . For example, these additional forms were updated because taxpayers involved in flow-through entities needed to be informed of their allocable portion of the elements needed to calculate the Qualified Business Income Deduction.
*****7*****	*****7***** *****7***** *****7***** . Because of concerns regarding the ability to develop a form, the implementation team recommended developing a worksheet.
April 30, 2018	The IRS's due date for submission of new tax forms and programming requirements.
June 29, 2018	The IRS completed initial draft updates to the 11 tax forms identified in the action plan for the Qualified Business Income Deduction.
August 8, 2018	The Department of the Treasury and the IRS published guidance needed to clarify key definitional terms and the deduction calculation.
August 20, 2018	The IRS circulated draft Form 1040 instructions for TY 2018, which includes a worksheet and instructions to calculate the Qualified Business Income Deduction.
September 25, 2018	The IRS submitted proposed business rules *****2***** *****2***** *****2*****.

Source: Treasury Inspector General for Tax Administration analysis of the IRS's Qualified Business Income Deduction implementation efforts.



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When we raised our concern about the lack of a tax form for TY 2018 filings, IRS management stated that they had already considered the risk of not having a tax form and continued to believe that the development of a computational worksheet, in lieu of a new form, was the optimal decision for TY 2018 filings. Furthermore, IRS management indicated that delaying the development of a tax form until TY 2019 allowed the IRS to receive comments on the proposed regulations, consider those comments before finalizing the regulations as required by law, and gain some experience with the first filing season. The proposed regulations were not issued until August 8, 2018, more than three months past the IRS's original due date for submitting new tax forms and programming requirements.

Development of the simplified worksheet will help reduce taxpayer burden

The IRS estimates that more than 22.2 million (94 percent) of the 23.7 million taxpayers eligible for the Qualified Business Income Deduction will qualify for the deduction without having to perform a complex calculation. The initial worksheet the IRS developed contained three parts and four schedules to be used when determining the deduction.⁵ Some taxpayers will need this to address the complexity of their tax scenarios when calculating their deduction. Because the majority of impacted taxpayers would not be subject to a complex deduction calculation, we suggested that the IRS consider a simplified worksheet. Management indicated that a similar concern was raised within the IRS, and they had in fact developed a simplified worksheet.⁶ As a result, the IRS now has two worksheets to assist taxpayers in calculating the Qualified Business Income Deduction. This includes the:

- **Simplified worksheet.** This worksheet is for taxpayers whose taxable income does not exceed \$157,500 (\$315,000 Married Filing Joint) and who are not a patron in a farmers' cooperative.⁷ The IRS plans to include the simplified worksheet within the Form 1040 instructions.
- **Worksheet for more complex calculations.** The IRS designed a worksheet for complex calculations that can be used by taxpayers with income in excess of \$157,500 (\$315,000 for Married Filing Joint) and taxpayers who are patrons in a farmers' cooperative. The worksheet assists with the complex calculations such as applicable Form W-2 wages and qualified depreciable property limitations, limitations for specified service trades or businesses, and patronage reductions⁸ for taxpayers who are members in

⁵ See Appendix IV.

⁶ See Appendix V.

⁷ Farmers' cooperatives are tax-exempt associations organized and operated on a cooperative basis to market products of members and return the proceeds, less the necessary marketing expenses, to the members. A cooperative may also involve purchasing equipment and providing it to the members at actual cost.

⁸ A patronage reduction is a calculation used by members of farmers' cooperatives. It reduces total qualified business income based on payments received from cooperatives.



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a cooperative. The IRS plans to publish the worksheet for more complex calculations in Publication 535, *Business Expenses*.

The IRS circulated draft instructions to the Form 1040 for TY 2018, which include the simplified worksheet and instructions, for review and expects to release final instructions to the public in December 2018. In comparison, the IRS scheduled the final release of Publication 535, containing the worksheet for complex calculations, in March 2019. When we brought to management’s attention our concerns that individuals subject to the complex calculations would only be provided limited time to accurately calculate their estimated tax payments and complete their tax returns by April 15, management subsequently moved the target release date for Publication 535 to January 2019.

Processes Have Not Been Developed to *****2*****
*****2*****

Our review identified that the IRS *****2*****
*****2*****
*****2****. On June 12, 2018, we brought to management’s attention our concerns *****2*****
*****2*****
*****2*****. Specifically, we noted that the IRS could:

- *****2*****
*****2*****
*****2***** , 9 *****2*****
*****2*****
*****2*****
*****2*****. Taxpayers report the income associated with business income on Form 1040, Schedule 1, *Additional Income and Adjustments to Income*. This includes:
 - Line 12, Business income or (loss). Taxpayers use this line to report income from Schedule C, *Profit or Loss From Business*. Schedule C is used to report income or loss from a business operated or profession practiced as a sole proprietor.
 - Line 17, Rental real estate, royalties, partnerships, S corporations, trusts, *etc.* Taxpayers use this line to report income from Schedule E, *Supplemental Income and Loss*. Schedule E is used to report a taxpayer’s share of income or loss from partnerships, S corporations, rental real estate, estates, and trusts.
 - Line 18, Farm income or (loss). Taxpayers use this line to report income or loss from Schedule F, *Profit or Loss From Farming*. Schedule F is used to report a taxpayer’s

9 *****2*****
*****2*****.



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net profit or loss from regular farming operations. This also includes qualified cooperative dividends.

- *****2*****
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*****2*****
*****2*****
*****2*****
*****2*****
*****2*****.

In response to our concerns, IRS management responded that they would like to ensure an appropriate balance between compliance risk and taxpayer burden. As such, they agreed to consider whether *****2*****
However, because TY 2018 is the first year of the Qualified Business Income Deduction, IRS management believed that it would be *****2*****
*****2*****. IRS management also stated that it could not require taxpayers to submit a worksheet (any required documents must have OMB approval and an associated number) and that a worksheet would not assist the IRS in *****2***** and would increase taxpayer burden.
*****2*****
*****2*****, management plans to develop a post-processing compliance plan. The compliance plan will *****2*****
*****2*****. The IRS will compare TYs 2018 and 2019 tax returns to identify trends and audit tax returns across two years. As the IRS gains more experience and as more information becomes available, it will continue to review and revise its post-filing actions, striking a balance between compliance risk and taxpayer burden.

Near the conclusion of our fieldwork, the IRS prepared a computer programming request to add a new error code that would *****2*****
*****2*****
*****2*****. Because of the late submission, the IRS elevated the request for approval to both the Commissioner, Wage and Investment Division, and the Associate Chief Information Officer on September 14, 2018. The Commissioner, Wage and Investment Division, approved the request on September 24, 2018. As of October 3, 2018, the request had been submitted to the Information Technology organization for review. In the justification for this computer programming request, the IRS noted the following, “if we do not pursue this programming for Processing Year 2019, *****2*****
*****2*****
*****2*****.”



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As part of our upcoming filing season review,10 we plan to *****2***** . In addition, we will continue to monitor the IRS’s implementation of this provision, including post-processing compliance efforts and development of a tax form and associated error conditions for Processing Year 2020.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 1: Ensure that computer programming is *****2***** .

Management’s Response: The IRS agreed with this recommendation and has submitted programming requirements to detect returns *****2***** .

Recommendation 2: *****2***** .

Management’s Response: The IRS agreed with this recommendation. IRS management responded that in conjunction with the introduction of new forms on which Qualified Business Income Deduction computations will be provided with filed tax returns, *****2***** .

Office of Audit Comment: In the IRS’s response, management cites their disagreement with our statement that processes *****2***** . This action was taken in response to concerns that we brought to management’s attention that *****2***** .

10 Treasury Inspector General for Tax Administration, Audit No. 201940401, Filing Season Individual Tax Return Processing.



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The Commissioner, Small Business/Self-Employed Division, should:

Recommendation 3: Ensure the timely implementation of the post-processing compliance plan to identify individuals that do not meet eligibility requirements and erroneously claim the Qualified Business Income Deduction.

Management's Response: The IRS agreed with this recommendation and plans to develop post-processing business rules to identify individuals that do not meet eligibility requirements and erroneously claim the Qualified Business Income Deduction.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to assess the IRS's actions to implement Provision 11011 of the Tax Cuts and Jobs Act of 2017.¹ To accomplish our objective, we:

- I. Evaluated the accuracy and completeness of the IRS's plans to implement the Qualified Business Income Deduction provision.
 - A. Met with members of the Tax Reform Implementation Office and SB/SE Division management to discuss specific actions to implement the new tax law.
 - B. Reviewed the IRS's action items for implementation of the Qualified Business Income Deduction provision to ensure that they are complete and accurate.
 - C. Independently identified tax forms and publications that are affected by the Qualified Business Income Deduction provision.
 - D. Reviewed the IRS Implementation Plan for Forms and Publications to identify tax forms and publications that the IRS deems necessary to update to implement the Qualified Business Income Deduction provision.
 - E. Compared our list of forms and publications (Step I. C.) to IRS forms and publications (Step I. D.) to ensure that the IRS has identified all forms and publications.
 - F. Reviewed the IRS's drafts of revised tax forms and publications on the Composition Process Management system² to identify changes made due to the Qualified Business Income Deduction provision and to ensure the accuracy of changes.
 - G. Determined whether the IRS is accurately tracking and updating the implementation of the Tax Cuts and Jobs Act – Qualified Business Income Deduction through the Legislative Affairs Tracking Implementation Services system³ and associated action plans.
 - H. Identified and evaluated the IRS's process to develop rules and regulations.

¹ Pub. L. No. 115-97. Officially known as "An act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for Fiscal Year 2018."

² A centralized composition system to store, manage, and transform electronic products from a single-source file into output files used for print or viewing electronically.

³ The Legislative Affairs Tracking Implementation Services system is used to manage, coordinate, and track the actions the IRS takes to implement legislative provisions.



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1. Determined how long it will take the IRS to develop rules and regulations.
 2. Identified if the IRS will obtain comments from stakeholders.
- II. Evaluated the IRS's procedures to ensure that tax forms, instructions, and publications are timely and accurately updated.
- A. Met with IRS management to discuss the IRS's procedures for updating instructions, forms, and publications. This included determining how far in advance impacted parties need to be notified regarding the creation of a new tax form to calculate the deduction.
 - B. Reviewed the new worksheets to determine if they provide a reasonable method for calculating the deduction.
 - C. Met with IRS management to discuss the process for the development and issuance of guidance. This included determining how far in advance impacted parties need to be notified regarding the development of guidance, who within the IRS is responsible, and which type of guidance is needed.
 - D. Assessed the IRS's outreach and collaboration with internal and external stakeholders.
- III. Evaluated the IRS's plans to ensure that taxpayers' claims for the Qualified Business Income Deduction are accurate and allowable both at the time tax returns are processed and during post-processing.
- A. Met with IRS management to determine what types of business rules are being considered to identify potentially fraudulent or improper claims for the Qualified Business Income Deduction at the time tax returns are filed.
 - B. Met with IRS management to determine their plans for post-processing compliance.
 - C. Assessed IRS plans for providing training to employees to assist taxpayer compliance with the provision and post-compliance activities.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. *****2*****
*****2*****
*****2***** at the time of our review.



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Appendix II

Major Contributors to This Report

Russell P. Martin, Assistant Inspector General for Audit (Returns Processing and Account Services)

Diana M. Tengesdal, Director

Darryl J. Roth, Audit Manager

Benjamin D. Meeks, Lead Auditor

John L Hawkins, Senior Auditor



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Appendix III

Report Distribution List

Deputy Commissioner for Services and Enforcement
Commissioner, Small Business/Self-Employed Division
Commissioner, Wage and Investment Division
Director, Customer Account Services, Wage and Investment Division
Director, Headquarters Exam, Small Business/Self-Employed Division
Director, Office of Audit Coordination



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Appendix IV

*Qualified Business Income Deduction -
Complex Worksheet*

Worksheet 12-A. **Qualified Business Income Deduction Worksheet**

Keep for Your Records



Part I: Trade, Business, or Aggregation Information				
1. (a) Name	(b) Check if specified service	(c) Check if Aggregated	(d) Taxpayer identification number	(e) Check if Patron
A. _____	<input type="checkbox"/>	<input type="checkbox"/>	_____	<input type="checkbox"/>
B. _____	<input type="checkbox"/>	<input type="checkbox"/>	_____	<input type="checkbox"/>
C. _____	<input type="checkbox"/>	<input type="checkbox"/>	_____	<input type="checkbox"/>

Part II: Determine Your Qualified Business Income Component			
	A	B	C
2. Qualified business income from the trade, business, or aggregation (see instructions)			
3. Multiply line 2 by 20% (0.20). If your taxable income is \$157,500 or less (\$315,000 if married filing jointly), skip lines 4 through 12 and enter line 3 on line 13			
4. Allocable share of W-2 wages from the trade, business, or aggregation			
5. Multiply line 4 by 50% (0.50)			
6. Multiply line 4 by 25% (0.25)			
7. Allocable share of the unadjusted basis of all qualified property			
8. Multiply line 7 by 2.5% (0.025)			
9. Add lines 6 and 8			
10. Enter the greater of line 5 or line 9			
11. W-2 wage and qualified property limitation. Enter the smaller of line 3 or line 10			
12. Phased-in reduction. Enter amount from Part III, line 26, if any. See instructions			
13. Qualified business income deduction before patron reduction. Enter the greater of line 11 or line 12			
14. Patron reduction. Enter the amount from Schedule D, line 6, if any			
15. Qualified business income component. Subtract line 14 from line 13			
16. Total qualified business income component. Add all amounts reported on line 15			

Source: Publication 535, Business Expenses, dated January 25, 2019.



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Part III: Phased-in Reduction			
Caution. Complete Part III only if your taxable income is more than \$157,500 but not \$207,500 (\$315,000 and \$415,000 if married filing jointly), and line 10 is less than line 3. Otherwise, skip Part III.			
	A	B	C
17. Enter amounts from line 3			
18. Enter the amount from line 10			
19. Subtract line 18 from line 17			
20. Taxable income before qualified business income deduction			
21. Threshold. Enter \$157,500 (\$315,000 if married filing jointly)			
22. Subtract line 21 from line 20			
23. Phase-in range. Enter \$50,000 (\$100,000 if married filing jointly)			
24. Phase-in percentage. Divide line 22 by line 23			
25. Total phase-in reduction. Multiply line 19 by line 24			
26. Qualified business income after phase-in reduction. Subtract line 25 from line 17. Enter this amount on line 12 for the corresponding trade or business			

Part IV: Determine Your Qualified Business Income Deduction			
27. Total qualified business income component from all qualified trades, businesses, or aggregations. Enter the amount from Part II, line 16	27.		
28. Qualified REIT dividends and qualified PTP income or (loss) (see instructions)	28.		
29. Qualified REIT dividends and qualified PTP loss carryforward from prior years. Enter as a negative number	29.		
30. Total qualified REIT dividends and qualified PTP income. Add lines 28 and 29. If less than zero, enter -0-	30.		
31. REIT and PTP component. Multiply line 30 by 20% (0.20)	31.		
32. Qualified business income deduction before the income limitation. Add lines 27 and 31		32.	
33. Taxable income before qualified business income deduction	33.		
34. Net capital gain (see instructions)	34.		
35. Subtract line 34 from line 33. If zero or less, enter -0-	35.		
36. Income limitation. Multiply line 35 by 20% (0.20)		36.	
37. Qualified business income deduction. Enter the smaller of line 32 or line 36		37.	
38. Total qualified REIT dividend and qualified PTP loss carryforward. Add lines 28 and 29, if zero or greater enter -0-		38.	
39. DPAD under section 199A(g) allocated from an agricultural or horticultural cooperative. Don't enter more than line 33 minus line 37. Enter this deduction on Form 1040, line 10. See the instructions for Form 1040, line 10		39.	



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Schedule A—Specified Service Trades or Businesses (SSTB)

Keep for Your Records



Caution. Complete Schedule A only if your trade or business is a specified service trade or business and your taxable income is more than \$157,500 but not \$207,500 (\$315,000 and \$415,000 if married filing jointly). If your taxable income isn't more than \$157,500 (\$315,000 if married filing jointly), and you aren't a patron of agricultural or horticultural cooperative, don't use this worksheet; instead, use the Qualified Business Income Deduction—Simplified Worksheet in the Instructions for Form 1040. Otherwise, complete Schedule D before beginning Part I. If your taxable income is more than \$207,500 (\$415,000 if married filing jointly), your specified service business doesn't qualify for the deduction.

Part I—Non-Publicly Traded Partnership

	SSTB 1	SSTB 2	SSTB 3
1a. Trade or business name:	_____	_____	_____
1b. Taxpayer identification number	_____	_____	_____
2. Qualified business income from the trade or business	_____	_____	_____
3. Allocable share of W-2 wages from the trade or business	_____	_____	_____
4. Allocable share of the unadjusted basis of all qualified property	_____	_____	_____
5. Taxable income before qualified business income deduction	_____	_____	_____
6. Threshold. Enter \$157,500 (\$315,000 if married filing jointly)	_____	_____	_____
7. Subtract line 6 from line 5	_____	_____	_____
8. Phase-in range. Enter \$50,000 (\$100,000 if married filing jointly)	_____	_____	_____
9. Divide line 7 by line 8	_____	_____	_____
10. Applicable percentage. Subtract line 9 from 100%	_____	_____	_____
11. Applicable percentage of qualified business income. Multiply line 2 by line 10. Enter this amount on Schedule C or Part II, line 2, for the corresponding trade or business, as appropriate	_____	_____	_____
12. Applicable percentage of W-2 wages. Multiply line 3 by line 10. Enter this amount on Part II, line 4, for the corresponding trade or business, as appropriate	_____	_____	_____
13. Applicable percentage of the unadjusted basis of qualified property. Multiply line 4 by line 10. Enter this amount on Part II, line 7, for the corresponding trade or business, as appropriate	_____	_____	_____

Part II—Publicly Traded Partnership

	PTP SSTB 1	PTP SSTB 2	PTP SSTB 3
14. Trade or business name	_____	_____	_____
15. Taxpayer identification number	_____	_____	_____
16. Qualified PTP income or loss	_____	_____	_____
17. Taxable income before qualified business income deduction	_____	_____	_____
18. Threshold. Enter \$157,500 (\$315,000 if married filing jointly)	_____	_____	_____
19. Subtract line 18 from line 17	_____	_____	_____
20. Phase-in range. Enter \$50,000 (\$100,000 if married filing jointly)	_____	_____	_____
21. Divide line 19 by line 20	_____	_____	_____
22. Applicable percentage. Subtract line 21 from 100%	_____	_____	_____
23. Applicable percentage of qualified PTP income or loss. Multiply line 16 by line 22. Enter this amount on Part IV, line 28	_____	_____	_____



*Tax Cuts and Jobs Act: Implementation
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Schedule B—Aggregation of Business Operations

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Aggregation:					
1. Provide a description of the trade or business and an explanation of the factors met that allow the aggregation in accordance with Regulations section 1.199A-4. In addition, if you hold a direct or indirect interest in a relevant pass-through entity (RPE) that aggregates multiple trades or businesses you must attach a copy of the RPE's aggregations.					
2. Has this trade or business aggregation changed from the prior year? This includes changes in the aggregation due to a trade or business being formed, acquired, disposed, or ceasing operations. If yes, explain.					
3.	(a) Name of trade or business	(b) Taxpayer identification number	(c) Qualified business income/(loss)	(d) W-2 wages	(e) Unadjusted basis immediately after acquisition
4. Totals. Total columns (c), (d), and (e). Enter the total amounts on Schedule C or Parts II and IV of Worksheet 12-A, as appropriate. See instructions					
Note. If you have more than one aggregated group, attach additional Schedules B. Name the additional aggregations 2, 3, 4, and so forth.					

Schedule C—Loss Netting and Carryforward

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	(a) Qualified business income/(loss)	(b) Reduction for loss netting	(c) Adjusted qualified business income (combine (a) and (b); if zero or less, enter -0-)
1. _____			
2. Qualified business net loss carryforward from prior years			
3. Total trade or business losses. Combine the negative amounts on lines 1, column (a), and 2, for all trades and businesses. Enter as a negative number			
4. Total trade or business income. Add the positive amounts on line 1, column (a), for all trades and businesses			
5. Losses netted with income of other trades or businesses. Enter as a negative number, the smaller of the absolute value of line 3 or line 4. Allocate this amount to each trade or business on line 1, column (b). See instructions			
6. Qualified business net loss carryforward. Subtract line 5 from line 3. If greater than zero, enter -0-			



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Schedule D—Special Rules for Patrons of Agricultural or Horticultural Cooperatives (Coop)

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	Coop 1	Coop 2	Coop 3
Caution. Complete Schedule D only if you're a patron of an agricultural or horticultural cooperative.			
1a. Trade, business, or aggregation name:	_____	_____	_____
1b. Taxpayer identification number	_____	_____	_____
2. Qualified business income allocable to qualified payments received from cooperative	_____	_____	_____
3. Multiply line 2 by 9% (0.09)	_____	_____	_____
4. W-2 wages from trade or business allocable to the qualified payments	_____	_____	_____
5. Multiply line 4 by 50% (0.50)	_____	_____	_____
6. Patron reduction. Enter the smaller of line 3 or line 5. Enter this amount on Part II, line 14, for the corresponding trade or business	_____	_____	_____



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Appendix V

*Qualified Business Income Deduction -
Simplified Worksheet*

2018 Qualified Business Income Deduction—Simplified Worksheet

Keep for Your Records



Before you begin: This worksheet is for taxpayers who:

- ✓ Have qualified business income, REIT dividends, or PTP income.
- ✓ Are not a patron in a specified agricultural or horticultural cooperative.
- ✓ Have taxable income of \$157,500 or less (\$315,000 or less if married filing jointly).

	(a) Trade or business name	(b) Employer identification number	(c) Qualified business income or (loss)
1.			
	i.		
	ii.		
	iii.		
	iv.		
2.	Total qualified business income or (loss). Add the amounts in 1i through 1iv, column 1(c)		2. <input style="width: 100px;" type="text"/>
	<i>Note. If reporting qualified business income or (loss) from more than four trades or businesses, see the instructions for line 2 of this worksheet.</i>		
3.	Qualified business loss carryforward from the prior year		3. <input style="width: 100px;" type="text"/>
4.	Total qualified business income. Combine lines 2 and 3. If zero or less, enter -0-		4. <input style="width: 100px;" type="text"/>
5.	Qualified business income component. Multiply line 4 by 20% (0.20)		5. <input style="width: 100px;" type="text"/>
6.	Qualified REIT dividends and PTP income or (loss)		6. <input style="width: 100px;" type="text"/>
7.	Qualified REIT dividends and PTP loss carryforward from the prior year		7. (<input style="width: 50px;" type="text"/>)
8.	Total qualified REIT dividends and PTP income. Add lines 6 and 7. If zero or less, enter -0-		8. <input style="width: 100px;" type="text"/>
9.	REIT and PTP component. Multiply line 8 by 20% (0.20)		9. <input style="width: 100px;" type="text"/>
10.	Qualified business income deduction before the income limitation. Add lines 5 and 9		10. <input style="width: 100px;" type="text"/>
11.	Taxable income before qualified business income deduction		11. <input style="width: 100px;" type="text"/>
12.	Net capital gain (see instructions)		12. <input style="width: 100px;" type="text"/>
13.	Subtract line 12 from line 11. If zero or less, enter -0-		13. <input style="width: 100px;" type="text"/>
14.	Income limitation. Multiply line 13 by 20% (0.20)		14. <input style="width: 100px;" type="text"/>
15.	Qualified business income deduction. Enter the smaller of line 10 or line 14		15. <input style="width: 100px;" type="text"/>
16.	Total qualified business loss carryforward. Add lines 2 and 3. If more than zero, enter -0-		16. (<input style="width: 50px;" type="text"/>)
17.	Total qualified REIT dividends and PTP loss carryforward. Add lines 6 and 7. If more than zero, enter -0-		17. (<input style="width: 50px;" type="text"/>)

Source: TY 2018 Form 1040, U.S. Individual Income Tax Return, Instructions.



*Tax Cuts and Jobs Act: Implementation
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Appendix VI

Management's Response to the Draft Report

**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224**

**COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION**

February 13, 2019

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: *for* Mary Beth Murphy /s/ Lisa J. Beard-Niemann
Commissioner, Small Business/Self-Employed Division (SB/SE)

SUBJECT: Draft Audit Report - Tax Cuts and Jobs Act: Implementation of the
Qualified Business Income Deduction (Audit# 201840435)

Thank you for the opportunity to review and comment on the subject draft audit report. The Tax Cuts and Jobs Act (TCJA) represents the most comprehensive tax legislation in the last thirty years. Internal Revenue Code Section 199A, also known as the Qualified Business Income Deduction (QBID), was enacted as part of the TCJA. This code section provides individuals, and certain trusts and estates, with a deduction of up to twenty percent of their domestic qualified business income from their taxable income.

The QBID is quite complex and subject to various limitations and thresholds. It is expected to impact millions of taxpayers which will result in billions of dollars in tax deductions. We took several steps to ensure successful implementation of this code section and appreciate your acknowledgement of our efforts. For example, the IRS:

- Established an implementation team with participation from both SB/SE and the Large Business and International Division.
- Updated forms and publications, addressed computer programming changes, trained employees, and addressed a variety of other issues.
- Began providing critical information about QBID through various educational sources and events, such as, the Tax Forums.
- Created a "simple" and a "complex" worksheet to assist taxpayers with calculating the deduction.
- Began Information Technology programming *****2*****
*****2*****

Throughout, we have sought to balance compliance risk with taxpayer burden. We disagree with your statement that *****2*****
*****2*****
For the 2019 filing season, we have implemented programming that *****2*****



*Tax Cuts and Jobs Act: Implementation
of the Qualified Business Income Deduction*

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*****2*****. We will continue to evaluate whether additional system verification or business rules could be used during processing to enhance compliance. We also disagree with your suggestion that we instruct taxpayers to attach the QBID worksheets or risk having their returns rejected. Under the public protection provision of the Paperwork Reduction Act, taxpayers can only be required to provide information on a form displaying a valid Office of Management and Budget control number. While computational accuracy can be addressed during return processing *****2*****. Thus, we are establishing a post-processing compliance plan which will allow us to assess the level of compliance with the provision and improve our selection methods. We will continue to assess and implement new approaches to ensure proper implementation of the statute and compliance with the statute as we move forward.

Attached is a detailed response outlining our corrective actions to address your recommendations. If you have any questions, please contact me or Brenda Dial, Director, Examination Operations, SB/SE Division.

Attachment



*Tax Cuts and Jobs Act: Implementation
of the Qualified Business Income Deduction*

Attachment

RECOMMENDATION 1:

The Commissioner, Wage and Investment Division, should ensure that computer programming *****2*****.

CORRECTIVE ACTION:

We agree with this recommendation. Programming requirements were submitted to the Information Technology organization that *****2*****.

IMPLEMENTATION DATE:

Implemented

RESPONSIBLE OFFICIAL:

Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN:

N/A

RECOMMENDATION 2:

The Commissioner, Wage and Investment Division, should *****2*****.

CORRECTIVE ACTION:

We agree with this recommendation. In conjunction with the introduction of new forms on which the QBID computations will be provided with filed tax returns, we will implement processes that evaluate the additional data provided by those computations to identify *****2*****; however, implementation is dependent on limited budgetary and programming resources and is subject to competing priorities. We cannot provide an implementation date.

IMPLEMENTATION DATE:

N/A



*Tax Cuts and Jobs Act: Implementation
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RESPONSIBLE OFFICIAL:

Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN:

We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 3:

The Commissioner, Small Business/Self-Employed Division, should ensure the timely implementation of the post-processing compliance plan to identify individuals who do not meet eligibility requirements and erroneously claim the Qualified Business Income Deduction.

CORRECTIVE ACTION:

We agree with this recommendation. We will develop post-processing business rules to identify individuals who do not meet eligibility requirements and erroneously claim the QBID.

IMPLEMENTATION DATE:

March 15, 2020

RESPONSIBLE OFFICIAL:

Director, Exam Case Selection, Small Business/Self-Employed

CORRECTIVE ACTION MONITORING PLAN:

We will monitor this corrective action as part of our internal management control system.