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The propitious puzzle for small business owners: Understanding the Section 199A deduction

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THE PROPITIOUS PUZZLE FOR SMALL BUSINESS OWNERS: UNDERSTANDING THE SECTION 199A DEDUCTION

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Purpose

This paper will analyze how the new tax law changes passed by Congress that are effective beginning in the 2018 taxable year, specifically the Section 199A deduction, will impact small businesses. Research will be based on a survey of small business owners and tax professionals in the Cedar Valley area about their knowledge and opinion of the tax law changes. In order to make comparisons between the different businesses, questions will be geared towards how the businesses are planning to calculate the Section 199A deduction and what businesses are planning to do with the extra savings they may have after considering the deduction.

From these results, the overall effect of the new Section 199A deduction for small businesses will be shown along with how businesses are planning for the deduction and how tax professionals can help them plan for it. Any common confusions found among small business owners will signal to legislators and tax professionals where clarity still needs to be provided in order to maximize the tax benefit from Section 199A for their clients. When more guidance is provided, tax professionals will be able to better assist their small business clients. Small business owners and entrepreneurs could also profit as they become more aware of new information about potential tax savings.

Literature Review

The Tax Cuts and Jobs Act of 2017 (TCJA) signed into law by President Trump on December 22, 2017, is the biggest overhaul to the tax code since the Tax Reform Act of 1986 (Donaldson, 2018, p. 1). With this dramatic revision to the Internal Revenue Code (IRC) comes many changes that will affect all taxpayers, especially business owners. One of the most significant changes coming out of the TCJA is the reduction in the corporate tax rate from a maximum rate of 35 percent to a flat rate of 21 percent on all corporate taxable income (Donaldson, 2018, p. 12).

Considering this change to the tax code only impacted corporations, the TCJA provided a new deduction to owners of non-corporate entities. This new Section 199A deduction reduces the tax burden for sole proprietorships, partnerships, limited liability companies (LLC), and S corporations to simulate the reduction in the corporate tax rate for corporations. Sole proprietorships are business organizations formed by a single owner in which there is no legal distinction between the business and individual, which is the most simple business structure to form. A partnership is similar to a sole proprietorship except it is owned by two or more people. LLCs offer flexibility as the owner can choose whether they want to be taxed by the IRS as a sole proprietorship, partnership, or corporation. S corporations are a combination of sole proprietorships, partnerships, and C corporations; they have the limited liability protection of C corporations along with the tax benefits of sole proprietorships and partnerships (Quickbooks, 2017).

According to the IRC, the Section 199A deduction allows a taxpayer other than a corporation a deduction of up to 20 percent of qualified business income (QBI) (Section 199A(a)). As stated in Section 199A(c)(1), “qualified business income” is “the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer” and does not include any qualified real estate investment trust (REIT) dividends or qualified publicly traded partnership income. A qualified REIT dividend is any dividend from a taxable real estate investment trust that is not a capital gain dividend or qualified dividend income (Section 199A(e)(3)).

This 20 percent business deduction is effective beginning in 2018 and does not apply to taxable years beginning after December 31, 2025 (Section 199A(i)). It is a “below the line” deduction that reduces taxable income but is not considered an itemized deduction because the Section 199A deduction is available to both taxpayers who itemize deductions or claim the standard deduction (Sections 63(b)(3), 63(d)(3)).

Similar to other deductions, the Section 199A deduction phase-outs and limits apply to high-income taxpayers. These phase-outs and limits are put in place to avoid the conversion of compensation into business income that would be taxed at a lower rate (Kess, 2018). The threshold amount of taxable income determining how much of the deduction is phased out is set at $157,500 ($315,000 for a joint return) (Section 199A(e)(2)(A)). The Section 199A deduction is limited by “the greater of 50 percent of the W-2 wages with respect to the qualified trade or business or the sum of 25 percent of the W-2 wages with respect to the qualified trade or business, plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property” (Section 199A(b)(2)(B)). In other words, the amount on your books for property is the basis used to calculate 2.5 percent of all qualified property.

According to Section 199A(b)(6)(A), the term “qualified property” covers the tangible property of a character subject to the allowance for depreciation that is held by the qualified trade or business at the close of the taxable year and is used at any point during the taxable year in the production of QBI. The aggregate deductible amount of each qualified trade or business for a single taxpayer is then further limited by the excess of their taxable income over the sum of net capital gains for the year (Section 199A(a)(2)(B)). In spite of these limitations, the Section 199A deduction is expected to favor owners of non-corporate entities by lowering their effective tax rate.

With both the reduction in the corporate tax rate and the Section 199A deduction, new opportunities are available to businesses due to these potential tax savings. From the reduction in the corporate tax rate, the federal government is expected to lose $1.35 trillion in tax revenues over the next ten years and $414 billion from the Section 199A deduction over its lifetime (Donaldson, 2018, p. 3, 16). Accordingly, companies, big and small, across the nation have already started planning for these tax savings even though they will not take effect until the 2018 tax year, and businesses in Iowa are no exception to this. AT&T rewarded 541 Iowa employees with $1,000 bonuses and plans to increase capital expenditures by $1 billion nationwide, and the Anfinson Farm Store in Cushing, Iowa, followed suit by rewarding employees with a $1,000 bonus and an additional 5 percent pay raise (Kartch, 2018). Besides bonuses and pay raises, companies are hiring more employees, buying more equipment, contributing more to retirement plans, granting more stock options, investing in educational opportunities for employees, and making more charitable contributions all in response to the TCJA (Kartch, 2018).

The TCJA was passed with three objectives in mind: (1) tax relief and simplification for families, (2) competitiveness and growth for job creators, and (3) global competitiveness (Donaldson, 2018, p. 2). The goal was for a simpler taxation process, but with great change comes great confusion, and the Section 199A deduction is no exception to this confusion.

On account of the Section 199A deduction being so new, there are unknown aspects surrounding who is eligible, how to calculate, and how to maximize the benefit. In addition, there is not much prior research related to this deduction. Tony Nitti, CPA, outlined many of these possible confusions in his article, "Understanding the New Sec. 199A Business Income Deduction." Part of the uncertainty is due to the unclear definitions of 'qualified trade or business' and 'specified services.'

Section 199A(d)(1) generally defines “qualified trade or business” as “any trade or business other than a specified service trade or business, or the trade or business of performing services as an employee.” This means only the owner of the business is allowed to take the deduction, not employees. The definition provided for ‘qualified trade or business’ fails to address how involved the owner has to be in the business in order to qualify for the deduction. There are many levels of involvement an owner of a business can take on in order to run a business; some are very involved and others are only passively involved. This could pose a problem for rental property owners who are only passively involved. These passive rental owners would likely qualify for the deduction because of the second limitation, which is “the sum of 25 percent of the W-2 wages with respect to the qualified trade or business, plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property” (Section 199A(b)(2)(B)(ii); Nitti, 2018). This was added specifically to assist rental property owners. Other business owners, who may be more involved in the activities of their business, might miss out on the deduction based on other factors besides involvement.

On top of that, the term ‘specified service’ is not clearly defined within the IRC. A “specified service trade or business” includes “any trade or business involving the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset or such trade or business is the reputation or skill of one or more of its employees” (Section 1202(e)(3)(A)). Section 199A(d)(2)(A) modifies the definition found in Section 1202 by removing “engineering” and “architecture” from the list of businesses and substituting “employees or owners” for “employees” at the end. The first portion of the definition listing the trade or businesses labeled as specified services seems straightforward. If your business is an accounting firm, you will not qualify for the full Section 199A deduction, but not all businesses are going to fit neatly into these listed categories. For example, consulting is a broad category. Typically, consulting is comprised of law, accounting, and finance professionals who advise their clients on certain matters, but fortune tellers could possibly fall under the category of consulting since they also give advice to their clients.

The second portion of the definition "any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners" also poses an issue (Section 1202(e)(3)(A)). Just because your business is not operating in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, or brokerage does not mean you are entitled to the Section 199A deduction. Many trades or businesses not considered services may be excluded from the deduction on the grounds that the principal asset of their business is an employee or owner. In his article, "Understanding the New Sec. 199A Business Income Deduction," Tony Nitti gave the example of a restaurant run by a five-star chef. The restaurant's principal asset is the skill of the chef and would not operate the same if the chef decided to leave. Based on the definition of a specified service, the restaurant would not qualify for the Section 199A deduction even though the food industry is not listed as a disqualifying trade or business.

Both of these terms surrounding the changes made for the 2018 taxable year have already caused confusion. In response, the American Institute of Certified Public Accountants (AICPA) sent a request to the Department of the Treasury (USDT) and the Internal Revenue Service (IRS) to provide guidance about the issues within Section 199A. The following was their recommendation:

> The Department of the Treasury and Internal Revenue Service should provide clarity on the definition of the term "qualified business income" by defining what activities constitute a qualified trade or business under section 199A. This request includes defining a trade or business that generates QBI and clarifying what activities are excluded as a specified service trade or business. ("Request for Immediate Guidance Regarding IRC Section 199A - Deduction for Qualified Business Income of Pass-Through Entities (Pub. L. No. 115-97, Sec. 11011)," 2018)

With the ambiguity surrounding these two terms, business owners might think they are eligible for the deduction when they, in fact, are not. Many questions will continue to be directed towards the IRS to address these concerns.

As a result of these two unclear definitions, calculating the Section 199A deduction may prove to be a challenging task. Michael Gentile laid out the following six steps to calculate the Section 199A deduction and any recognizable issues with completing the step in his article "Proposed Computational Framework for Internal Revenue Code §199A" featured in the *Tax Development Journal*.

"<u>Step 1: Determine whether the taxpayer is engaged in a qualified trade or business.</u>"

> As previously stated, there is already a lot of confusion surrounding the definitions of 'qualified trade or business' and 'specified service' making it difficult for taxpayers to determine whether or not they are a qualified trade or business. Since applying the terms is already difficult in step 1, this will only further complicate the calculation process.

"Step 2: If the taxpayer engages in a specified service trade or business, determine what portion, if any, of the specified service trade or business is treated as a qualified trade or business."

According to Section 199A(d)(3), a specified service may be treated as a qualified trade or business depending on the taxpayer's taxable income. Based on the threshold amount of $157,500 ($315,000 for married filing jointly), there are three different income brackets a specified service taxpayer could be in that determine whether or not they can claim any of the Section 199A deduction.

1. If an owner of a specified service trade or business has a taxable income of less than $157,500 ($315,000 for those filing jointly), then their specified service is now treated as a qualified trade or business, therefore, they are eligible for the Section 199A deduction.
2. If an owner of a specified service trade or business has a taxable income between $157,500 and $207,500 ($315,000 and $415,000 for those filing jointly), then the specified service is treated as a qualified trade or business but only a certain percentage is. This percentage is the ratio of the excess taxable income over $157,500 ($315,000 for joint filers) to $50,000 ($100,000 for joint filers), therefore, they are only eligible for a percentage of the total Section 199A deduction.
3. If an owner of a specified service trade or business has a taxable income above $207,500 ($415,000 for those filing jointly), then their specified service is not treated as a qualified trade or business, therefore, they are not eligible for the Section 199A deduction.

“Step 3: Calculate the taxpayer’s QBI for each qualified trade or business.”

The QBI of a taxpayer is computed separately for each qualified trade or business (Section 199A(b)(2)). All of the QBI from each separate trade or business is then combined. This is done to determine whether the net amount is negative or not. If the amount is positive, you can move on to step 4. If the amount is negative, then there is no need to go to step 4, and the amount is treated as a loss from a qualified trade or business in the succeeding taxable year (Section 199A(c)(2)).

“Step 4: Calculate the deductible amount for each qualified trade or business.”

For each qualified trade or business, the deductible amount is 20 percent of QBI from the trade or business and is limited by “the greater of (1) 50 percent of the W-2 wages with respect to the qualified trade or business, or (2) the sum of 25 percent of the W-2 wages with respect to the qualified trade or business, plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property” (Section 199A(b)(2)(B)). These two limits combined are known as the Wages/Capital limit (Gentile, 2018, p. 26).

“Step 5: Calculate the taxpayer’s combined QBI amount.”

Section 199A(b)(1) defines the “combined qualified business income amount” as the amount equal to the sum of the amounts determined in step 4 for each qualified trade or business carried on by the taxpayer, plus 20 percent of the aggregate amount of the qualified REIT dividends and qualified publicly traded partnership income of the taxpayer for the taxable year (Section 199A(b)(1)). Since QBI includes losses, there is extra consideration for losses carried over from previous tax years. As noted previously, the losses are treated as losses from a qualified trade or business in the succeeding taxable year (Section 199A(c)(2)).

"Step 6: Calculate the taxpayer's deduction under Section 199A" (Gentile, 2018).

The final step is calculating the total deduction taken under Section 199A. The deduction equals "the sum of the lesser of (1) the taxpayer's combined qualified business income found in step 5 or (2) 20 percent of the amount by which the taxpayer's taxable income exceeds net capital gains, plus the lesser of (1) 20 percent of the taxpayer's qualified cooperative dividends for the year or (2) the taxpayer's income less net capital gains" (Section 199A(a)). Further, this amount cannot be greater than the taxpayer's taxable income minus net capital gains for the year.

Following these six steps, taxpayers and their tax advisors will have calculated their total Section 199A deduction. After analyzing the six steps, it is easy to see where issues are likely to pop up surrounding the definitions of 'qualified business income' and 'specified service,' the determination of the phase-in percentages for both qualified and specified trade or business, and the consideration of carryover losses.

Considering all the Section 199A deduction offers to small business owners, it comes as no surprise that there are concerns surrounding this new deduction and the IRS and USDT have already been asked to provide guidance on these concerns. Many companies have anticipated the future tax savings and have responded accordingly by hiring more employees and giving bonuses, but smaller businesses may have different plans in mind. With the confusion surrounding the terms of 'qualified business income' and 'specified service,' business owners might think they are eligible for the deduction when they are not. This further complicates the business strategies owners may be planning for these tax savings, which they might not actually receive. Despite what may seem like a simple six-step process, business owners and even tax professionals are likely unaware of how to calculate and plan for the Section 199A deduction.

Research Questions to be Answered

1. Do business owners understand the qualifications and how to calculate the Section 199A deduction?
2. How are small business owners planning for the Section 199A deduction? What are business owners planning to do with the tax savings from the deduction?
3. How are tax professionals planning to advise their clients about the Section 199A deduction?

Methodology

Participants

For the "Impact of the Tax Cuts and Jobs Act on Small Businesses" survey (Impact Survey), the total sample consisted of thirteen small business owners recruited using an email list of local businesses and through the social media platforms of LinkedIn and Facebook. Only businesses within the Cedar Valley area (located in Black Hawk, Bremer, Buchanan, Butler, Chickasaw, Fayette, Grundy, or Tama County) were selected for this survey. Due to the criteria set to make sure the businesses could potentially qualify for the Section 199A deduction, five of the small business owners' responses were disregarded because they noted their business was organized as a corporation, and corporations are not eligible for the Section 199A deduction. This left 8 total responses to analyze. Of the individuals who participated, two (25 percent) were sole proprietors and six (75 percent) were organized as limited liability companies (LLC). Most of the participants employed, on average, one to ten people with only 25 percent employing more than ten employees. With participants from Waterloo, Cedar Falls, and Denver, all small businesses were located within the Cedar Valley area as described above.

For the “Advising Small Business Owners” survey (Advising Survey), the total sample consisted of six tax professionals who were recruited by phone and then sent an electronic survey to fill out via email. To match the sample for local small business owners, the tax professionals surveyed were selected from the same counties within the Cedar Valley area. Due to the criteria set to make sure the person answering the survey was actually a tax professional working at a local accounting firm, one of the responses was disregarded as a result of them noting they did not work in the tax department at their place of employment. This left five total responses to analyze.

Procedure

The study was approved by the Institutional Review Board (IRB) at the University of Northern Iowa. For both the Impact Survey and Advising Survey, data were collected during the fall of 2018. Small business participants chose whether or not they would like to participate in the study after reading a short script in the Google Forms survey sent to them via email. Tax professional participants chose whether or not they would like to participate in the study after receiving a phone call and providing an email to send the survey to. They also read a short script at the start of the survey to verify they were still interested in participating.

Those who agreed to participate and fit the inclusion criteria of being either a small business owner or tax professional were provided an online consent form. Participants also had the option to skip a question or opt out of the survey at any point. As noted above, five of the small business owner responses and one of the tax professional responses were excluded from this study because they did not meet all of the qualifications to be a study participant. If the participant consented, they could continue with the online survey. Both survey group participants completed an online survey using Google Forms, which inquired about their knowledge and opinion of the TCJA, as well as any confusions they had pertaining to the tax reform changes and the Section 199A deduction. Those who completed the survey were not compensated for their participation.

Two different surveys were sent out: one to business owners and one to tax professionals. The surveys were structured in which all of the businesses and tax professionals were asked the same series of questions in the same order to allow for greater comparison between the responses given. In the surveys, the questions asked were a variety of both closed- and open-ended questions. The closed-ended questions were designed to be easier for the respondent to answer. Additionally, the closed-ended questions were easier for analysis purposes since the number of responses was limited. The open-ended questions were included to allow the respondent to display their feelings towards and understanding of the Section 199A deduction without being limited by their choice in response.

To gather the necessary information to answer the research questions noted in the previous section, the questions asked in the survey were geared towards the business owner's and tax professional's knowledge and understanding of the Section 199A deduction. The business owners were asked about their overall feelings towards the new tax laws and whether or not they thought they would actually benefit from these changes. They were also asked specifically about Section 199A: what they knew about the deduction and how they are planning for it. Tax professionals were asked about their knowledge and feelings towards the new tax law changes and how they are helping small business owners plan for this new deduction.

To analyze the survey results, I looked for common confusions pertaining to the new tax laws among business owners and ways in which tax professionals are helping to plan for the Section 199A deduction.

Results

Through inquiry of small business owners and tax professionals, the issues and complications associated with the TCJA, specifically the new Section 199A deduction, have become more evident. These areas of confusion are indicators of improvements that can be made by legislators and tax professionals when it comes to passing tax reform. Legislators should consider informing the general public about how these changes will impact taxpayers, as well as provide the proper guidance to tax professionals, so they can best advise their clients. Tax professionals are more aware of the confusions surrounding tax legislation than small business owners and are responsible for assisting their small business clients to help them receive the greatest possible tax deduction. Evaluation of these small business owner and tax professional surveys has created generalizations which legislators and tax professionals can use to better inform taxpayers and small business clients, respectively. As outlined throughout this report, more work needs to be done by legislators and tax professionals to provide small business owners with the necessary information to take advantage of this opportunity.

Though the sample size was relatively small for both surveys, noteworthy conclusions were made from the data collected. It should also be mentioned since participants had the option to skip a question or opt out of the survey at any point, not all responses noted below will add up to a 100 percent response rate.

Small Business Owners

In total, there were eight responses analyzed for the small business owners who participated in the Impact Survey. The data revealed, overall, small business owners have positive feelings towards the TCJA but are not fully aware of the benefits the act provides, specifically the Section 199A deduction.

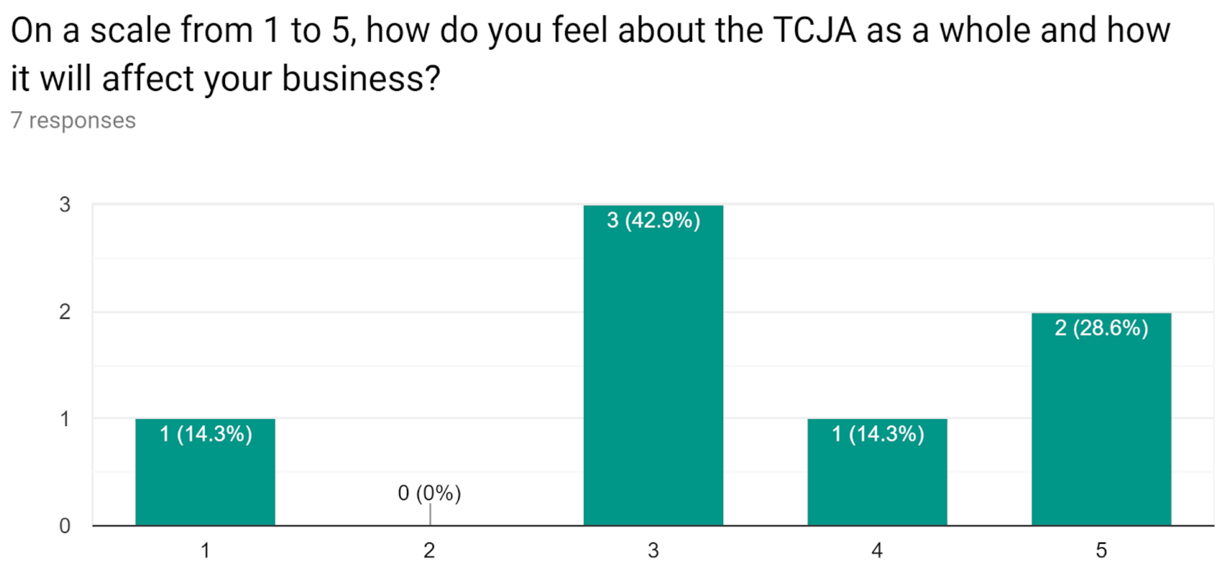

Figure 1

When asked the question "On a scale from 1 to 5, how do you feel about the TCJA as a whole and how it will affect your business?" with 1 being 'strongly dislike the TCJA' and 5 being 'strongly like the TCJA,' only one participant (12.5 percent) responded with a '1' and six of the respondents (75 percent) gave a rank of '3' or higher (See Figure 1). This indicates the majority of small business owners in the Cedar Valley have an optimistic outlook when thinking about the tax law changes.

Likewise, when asked directly if they thought the TCJA would benefit small businesses, five participants (62.5 percent) said ‘yes,’ one participant (12.5 percent) said ‘maybe,’ and one participant (12.5 percent) said ‘no’ (See Figure 2). This further goes to show the small business owners feel confident about tax reform and what it can do for their business. The one respondent who gave a ‘1’ when ranking their feelings towards the TCJA and did not think the TCJA would benefit small businesses noted their business would not qualify for the Section 199A deduction, which could have played a role in their negative response towards the TCJA. Overall, the responses were positive, which is surprising considering most were not aware of the beneficial Section 199A deduction.

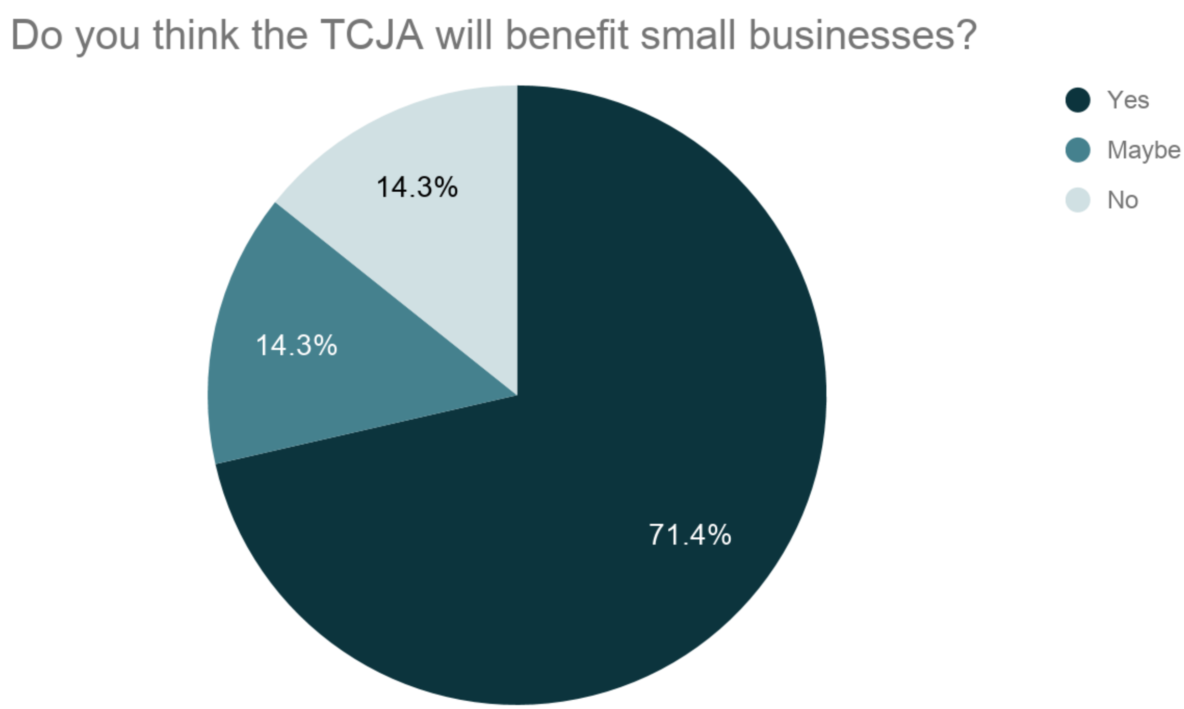

Figure 2

While most small business owners know about the TCJA as a whole, results indicate most small business owners are not aware of the Section 199A deduction. When asked “Are you aware of the new 20 percent pass-through deduction for small business owners provided by the

TCJA?," six participants (75 percent) responded 'no' (See Figure 3).

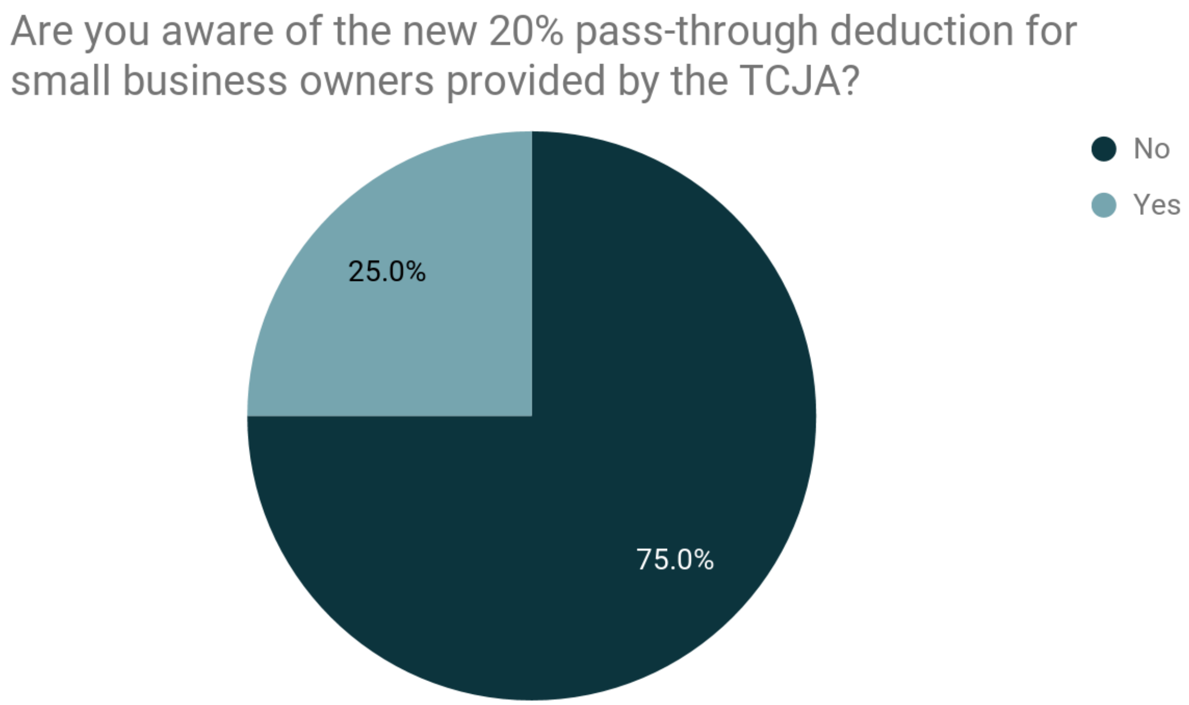

Figure 3

Throughout the whole research, this statistic was the most concerning. The main purpose of passing the new tax reform at the end of 2017 was to contribute to the success of businesses, both big and small, while increasing employment nationwide. This can be better accomplished if as many business owners as possible are informed about how tax reform can advance their business. It is nearly impossible for everyone to be informed. Recognizing the small sample size, the majority of small business owners surveyed were not aware of the Section 199A deduction; therefore, many were unaware of how to calculate and plan for the deduction.

As noted in the Literature Review, the calculation of the Section 199A deduction comes with its own confusions, but once you get past those confusions, the savings from the deduction could be used in many different ways. Whether it be to hire more employees, give pay raises or bonuses, buy more equipment, or make more charitable contributions, all of these go to further stimulate the economy. Now, the specific reasons as to why 75 percent of small business owners are not aware of the Section 199A deduction are unknown, but it can be concluded more needs to be done to inform small business owners of this potentially beneficial deduction.

Tax Professionals

In total, there were 5 responses analyzed for the tax professionals who participated in the Advising Survey. The data revealed, overall, tax professionals have positive feelings towards the TCJA and think it will help small business owners; however, they are not fully informed about how to aggregate their clients' income from multiple sources when calculating the deduction. Along with this, tax professionals are not advising all of their small business clients in the same way when it comes to planning for this deduction.

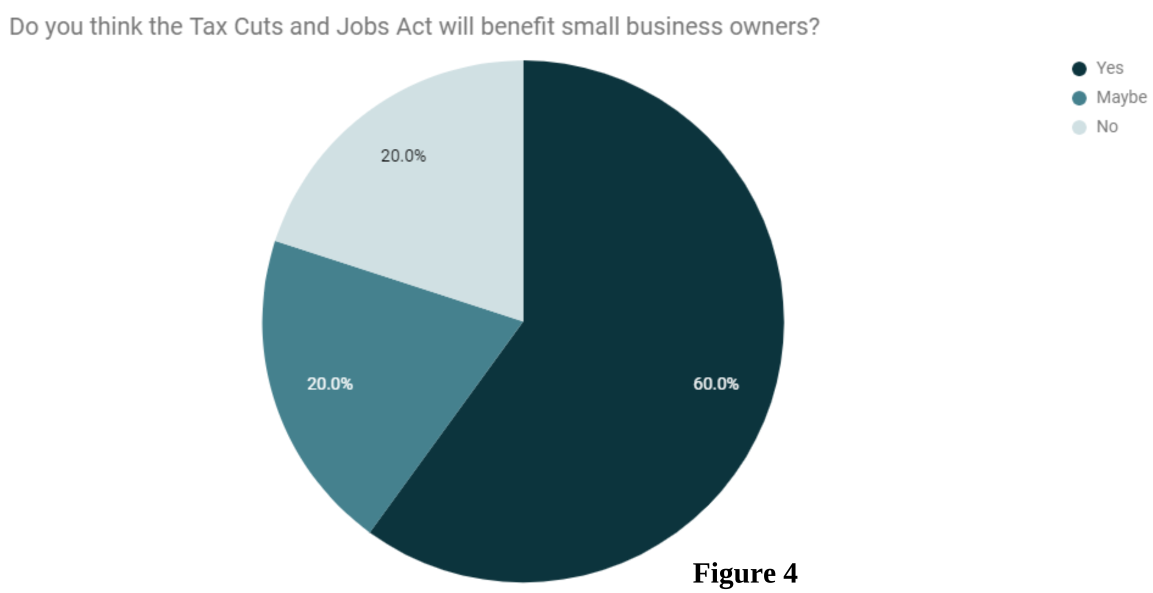

Figure 4

When asked if they thought the TCJA would benefit small business owners, three tax professionals (60 percent) responded 'yes,' one (20 percent) responded 'maybe,' and one (20 percent) responded 'no' (See Figure 4). This goes to show that tax professionals, overall, have positive feelings towards tax reform, which can be passed on when advising their small business clients.

When asked the question "On a scale from 1 to 5, how well do you feel you can advise small business owners about the Section 199A deduction?" with 1 being 'not well' and 5 being 'extremely well,' two participants (40 percent) responded with a '3.' The other three respondents (60 percent) gave a rank of '4' showing the majority of tax professionals have the confidence and ability to advise their small business clients well (See Figure 5). This is somewhat surprising given the fact the IRS still has a great deal of guidance to provide surrounding the Section 199A deduction, but it is optimistic to see tax professionals feel positive about this deduction even if there is some uncertainty.

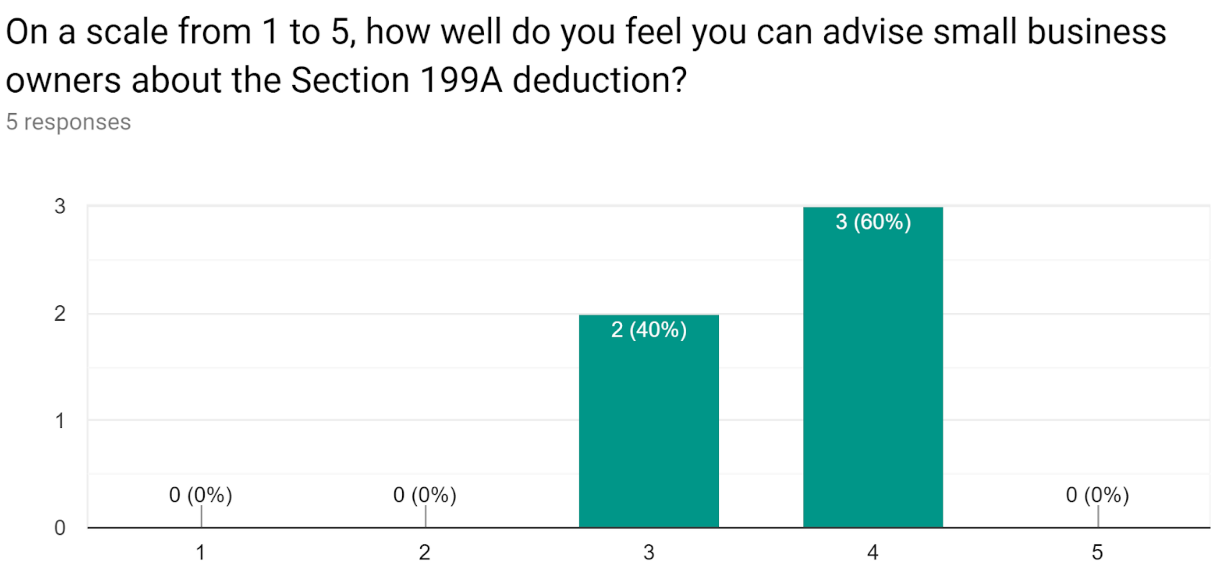

Figure 5

Whenever a large-scale change is made, there is generally a learning curve to overcome before the change can be effective. When asked the question "On a scale from 1 to 5, how well do you understand the new Section 199A deduction?" with 1 being 'do not understand at all' and 5 being 'understand it completely,' only one participant (20 percent) responded with a '2' and the other four respondents (80 percent) gave a rank of '3' or '4' showing the majority of tax professionals have a general understanding when it comes to the tax law changes (See Figure 6).

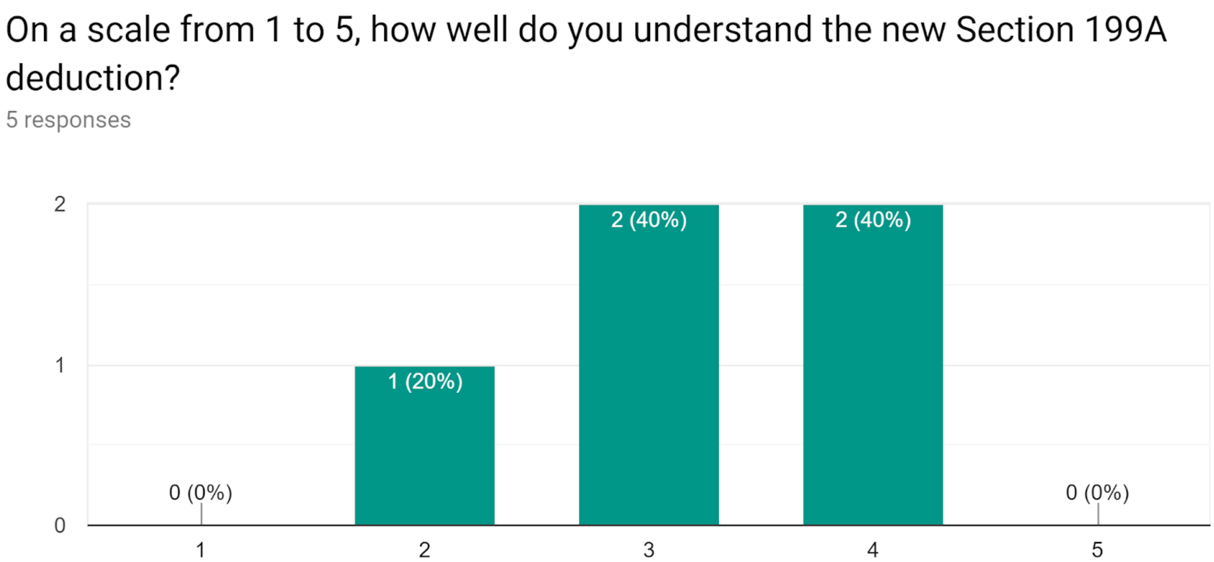

Figure 6

Tax professionals were confused about how to aggregate income from various activities, how to maximize the deduction, and the impact of the agricultural cooperative deduction. The Section 199A deduction allows small business owners a deduction of up to 20 percent of qualified business income (QBI). QBI is "the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer" excluding any qualified REIT dividends or qualified publicly traded partnership income (Section 199A(a),(c)(1)). On account of this deduction being based on the net amount of qualified items, tax professionals need to be aware of their client's income from all qualified sources. The way income is classified, either 'qualified business income' or 'specified service income,' determines the basis for calculating the deduction. The ambiguity of these two terms complicates matters for tax professionals when helping clients maximize the benefits of the Section 199A deduction.

Looking at how the Section 199A deduction would impact agricultural cooperatives was not considered before conducting this research. This study finds local tax professionals are concerned about how this deduction will impact their farmer clients. The main concern for farmers is deciding which deduction will be the most advantageous, the QBI deduction or agricultural cooperative deduction.

If a farmer is selling their crops to a non-cooperative, they are entitled to the full 20 percent QBI deduction, which is calculated based on their net income from the sale (Tidgren, 2018). This is not the case if the farmer decides to sell to a cooperative. Within the revised version of the IRC, there is a special rule that must be considered with respect to income received from cooperatives (Section 199A(b)(7)). The amount received from a specified agricultural or horticultural cooperative is reduced by the lesser of "9 percent of so much of the qualified business income with respect to such trade or business as is properly allocable to qualified payments received from such cooperative" or "50 percent of so much of the W-2 wages with respect to such trade or business as are so allocable" (Section 199A(b)(7)). Depending on the circumstance, this special rule will advantage, disadvantage, or not affect farmers that decide to sell to cooperatives; consequently, this adds to the complexity and confusion surrounding the Section 199A deduction.

In order to fix the cooperative legislation included within Section 199A, subsection g was added. This new section applies to cooperatives as taxpayers must be engaged "in the manufacturing, production, growth, or extraction in whole or significant part of any agricultural or horticultural product" or "in the marketing of agricultural or horticultural products" (Section 199A(g)(4)(A)). A taxpayer involved in a specified agricultural or horticultural cooperative is eligible for an agricultural cooperative deduction equal to 9 percent of the lesser of "the qualified production activities income of the taxpayer for the taxable year" or "the taxable income of the taxpayer for the taxable year" (Section 199A(g)(1)(A)). Though similar to the 20 percent QBI, this deduction is based on "qualified production activities income," which is equal to domestic production gross receipts over the sum of cost of goods sold, other expenses, losses, and deductions from those receipts (Section 199A(g)(3)(A)). Consequently, tax professionals will need to determine whether the 20 percent deduction based on qualified business income or the 9 percent deduction based on qualified production activities income is the most auspicious for their client.

The research also reveals there is no universal advice tax professionals can provide to all of their small business clients about how to use tax savings and plan for the deduction. With each small business being unique in its own way, tax professionals will need to advise clients differently based on the business's circumstances. Some of the planning suggestions noted in the survey were to give pay raises for employees, increase owner's wages, keep the savings, and buy more equipment for their business.

Applying the Results

Looking at the responses from both small business owners and tax professionals, there are some conclusions that can be drawn between the two populations' opinions towards the TCJA. These opinions can be utilized to inform small business owners about the benefits of the Section 199A deduction and increase the services of tax professionals.

Both small business owners and tax professionals have positive feelings towards the TCJA. When asked whether or not they thought the TCJA would benefit small businesses, 62.5 percent of small business owners and 60 percent of tax professionals said it would benefit small business owners, while only 12.5 percent of small business owners and 20 percent of tax professionals felt the opposite. It is encouraging to see positive feelings surrounding new legislation that had such mixed reviews when passed by Congress at the end of 2017. For those who have negative opinions, learning more about the benefits of the TCJA could potentially transform those negative opinions into positive ones. The survey indicates the majority of small business owners were not aware of the Section 199A deduction yet responded positively towards the TCJA.

This presents an opportunity for tax professionals to tap into two new markets of potential clients: those with a negative outlook and those with a positive outlook concerning tax reform. Tax professionals that have a positive attitude towards the TCJA and confident knowledge about Section 199A can influence skeptical business owners by educating them on the benefits of the deduction. Once informed of the new Section 199A deduction, their negative outlook might subside. Looking at potential clients who already have a positive outlook on tax reform, tax professionals may also influence these prospects by keeping them informed and up-to-date on new tax reform, as well as provide them with tax savings strategies. Since 80 percent of the members of this positive-outlook group were also unaware of the new Section 199A deduction, tax professionals could provide them with guidance about how this deduction would help them grow their business and gain loyal customers along the way.

Conclusion

The TCJA has brought with it many changes affecting businesses and individuals and the tax professionals who advise small business clients. With the addition of the Section 199A deduction, small business owners have an opportunity to deduct 20 percent of their QBI. This reduction in a business's tax burden has the power to change the business's behavior in multiple ways. Giving pay raises to employees, buying more equipment for their business, and making more charitable contributions are a few ways small businesses are planning for this deduction.

Though this is advantageous for many owners of non-corporate entities, there are complications surrounding the deduction. Through the surveying of small business owners and tax professionals in the Cedar Valley, common concerns were identified. Understanding who is eligible for the deduction, how to calculate the deduction, and how to aggregate income from all sources are just some of the complexities. Business owners and tax professionals will need to overcome these complexities in order to maximize their benefit from this deduction. Additionally, tax professionals must consider how this deduction will impact farmers and determine whether it is best for their client to take the 20 percent qualified business income deduction or the 9 percent agricultural cooperative deduction. This study's results demonstrate trends that can be addressed by the USDT and IRS when providing guidance about Section 199A to tax professionals.

This study also reveals a new opportunity for tax professionals to advertise their services more and inform small business owners about a brand new deduction they previously may not have been aware of. This provides a mutual benefit as tax professionals could see an increase in business, and small business owners may see a reduction in their overall tax burden. Despite the challenges this deduction presents, new opportunities for both small businesses and tax professionals to grow their businesses are accessible as a possible result of the Section 199A deduction.

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