

Addendum: Business Tax Update: QBI and Choosing a Business Entity

Revision 1:

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The example has been modified and corrected.

Income before other Payroll	242,500
Other Payroll	85,000
Net Income	157,500
Unadjusted Basis in Assets	1,000,000
Other Combined Income of Taxpayer and Spouse	-
Standard / Itemized Deductions + 1/2 SE Tax	(20,326)
Taxable Income Before CQBI Deduction	137,174
CQBI Deduction	(27,435)
Taxable Income	109,739
Maximum CQBI Deduction	
A) 20% of net Income:	31,500
B) 50% of Payroll	N/A
C) 25% of Wages + 2.5% of Assets	N/A
D) Greater of B or C	-
E) Lesser of A or D	31,500
Lesser of E or 20% of taxable income	27,435
Phaseout Starts	157,500
Phaseout Ends	207,500
Threshold Range	50,000
Phaseout Allowed Percentage	100.00%
Allowed Limited CQBI Deduction	27,435

The limited CQBI deduction of \$27,435 is allowed, A's taxable income is \$109,739 resulting in tax of \$20,627 (plus \$16,652 SE tax); B's taxable income is \$230,500 resulting in tax of about \$56,364 for total tax of \$76,991, so tax is not saved by filing separate in this case to take advantage of the higher CQBI deduction.

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The example has been modified and corrected.

In 2018, each owner reports compensation of \$300,000 plus \$18,500 as their share of net business income. Using the same MFJ assumption above, the tax to each owner would be about \$44,170 (plus \$450 additional Medicare tax on earned income, or \$44,620 net of the 20% CQBI deduction).

Income before other Payroll	368,500
Other Payroll	50,000
Net Income	318,500
Unadjusted Basis in Assets	-
Other Combined Income of Taxpayer and Spouse	-
Standard / Itemized Deductions + 1/2 SE Tax	(24,000)
Taxable Income Before CQBI Deduction	294,500
CQBI Deduction	(58,900)
Taxable Income	235,600
Maximum CQBI Deduction	
A) 20% of net Income:	63,700
B) 50% of Payroll	N/A
C) 25% of Wages + 2.5% of Assets	N/A
D) Greater of B or C	-
E) Lesser of A or D	63,700
Lesser of E or 20% of taxable income	58,900
Phaseout Starts	315,000
Phaseout Ends	415,000
Threshold Range	100,000
Phaseout Allowed Percentage	100.00%
Allowed Limited CQBI Deduction	58,900

For purposes of computing CQBI, net business income is not reduced by owner reasonable compensation. Therefore, each partner would be able to claim a CQBI deduction of \$58,900. This would reduce their taxable income to \$235,600 and at MFJ rates, income tax of \$44,170.

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The example has been modified and corrected.

Income before other Payroll	190,000
Other Payroll	25,000
Net Income	240,000
Unadjusted Basis in Assets	-
Other Combined Income of Taxpayer and Spouse	-
Standard / Itemized Deductions + 1/2 SE Tax	(36,329)
Taxable Income Before CQBI Deduction	203,671
CQBI Deduction	(40,734)
Taxable Income	162,937
Maximum CQBI Deduction	
A) 20% of net Income:	40,734
B) 50% of Payroll	50,000
C) 25% of Wages + 2.5% of Assets	N/A
D) Greater of B or C	50,000
E) Lesser of A or D	40,734
Lesser of E or 20% of taxable income	40,734
Phaseout Starts	315,000
Phaseout Ends	415,000
Threshold Range	100,000
Phaseout Allowed Percentage	100.00%
Allowed Limited CQBI Deduction	40,734

On combined taxable income after CQBI deduction of \$162,937, Harry and Sally would pay \$26,772 income tax plus \$24,659 SE tax for a total of \$51,431.

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