

## RENTAL REAL ESTATE AND THE QBID - UPDATE

On January 18, the IRS sent out Notice 2019-07 about a proposed revenue procedure which allows individuals and entities who own rental real estate directly or through a disregarded entity to treat a rental real estate enterprise as a trade or business for purposes of the Code Section 199A Qualified Business Income Deduction (QBID), if certain requirements are met. Taxpayers can rely on this safe harbor until a final revenue procedure is issued. Prior to this, it was questionable as to whether rental real estate rose to the level of a trade or business, and therefore qualified for the deduction.

This revenue procedure provides a safe harbor under which a rental real estate enterprise will be treated as a trade or business for purposes of section 199A of the Internal Revenue Code (Code) and §§ 1.199A-1 through 1.199A-6 of the Income Tax Regulations (26 CFR Part I). The safe harbor provided by this revenue procedure applies solely for purposes of section 199A. If an enterprise fails to satisfy the requirements of this safe harbor, the rental real estate enterprise may still be treated as a trade or business for purposes of section 199A if the enterprise otherwise meets the definition of trade or business in §1.199A-1(b)(14).

If the safe harbor requirements are met, the real estate enterprise will be treated as a trade or business as defined in section 199A(d) for purposes of applying the regulations under section 199A. Relevant pass-through entities (RPEs) as defined in §1.199A-1(b)(10) may also use this safe harbor in order to determine whether a rental real estate enterprise is a trade or business as defined in section 199A(d).

### OVERVIEW OF SAFE HARBOR PROVISIONS

The proposed procedure is 10 pages long, with multiple sections. This is just an overview of the major provisions.

Solely for purposes of this safe harbor, a rental real estate enterprise (RREE) is defined as an interest in real property held for the production of rents and may consist of an interest in multiple properties. The individual or RPE relying on this revenue procedure must hold the interest directly or through an entity disregarded as an entity separate from its owner under §301.7701-3. Taxpayers must either treat each property held for the production of rents as a separate enterprise or treat all similar properties held for the production of rents as a single enterprise. Commercial and residential real estate may not be part of the same enterprise. Real estate used as residence for any part of the year and triple net lease arrangements do NOT qualify. Taxpayers may not vary this treatment from year-to-year unless there has been a significant change in facts and circumstances. The following requirements must be met during each taxable year:

1. Separate books and records are maintained for each RREE
2. 250 or more hours must be spent each year providing “rental services” with respect to each RREE. “Rental services” include advertising, negotiating & executing leases, verifying tenant application information, rent collection, daily operation, maintenance and repair of the property; management of the real estate, purchase of materials, and supervision of employees and contractors. Rental services may be performed by owners or by employees, agents and/or contractors of the owners. “Rental services” do NOT include financial or investment management activities, such as arranging financing; procuring property; studying and reviewing financial statements or reports on operations;

planning, managing, or constructing long-term capital improvements; or hours spent traveling to and from the real estate.

3. The taxpayer maintains contemporaneous records, including time reports, logs, or similar documents, regarding the following: (i) hours of all services performed; (ii) description of all services performed; (iii) dates on which such services were performed; and (iv) who performed the services. Such records are to be made available for inspection at the request of the IRS. The contemporaneous records requirement will not apply to taxable years beginning prior to January 1, 2019.
4. A taxpayer or RPE must include a statement attached to the return on which it claims the section 199A deduction or passes through section 199A information that the requirements in Section 3.03 of this revenue procedure have been satisfied.