

THE IRC SECTION 199A DEDUCTION: FREQUENTLY ASKED QUESTIONS

Under the Federal Tax Cuts and Jobs Act – IRC Section 199A for tax years after December 31, 2017, owners of sole proprietorships, S Corporations, or partnerships are permitted to deduct 20% of the income earned by a pass-through business. C Corporations are not entitled to this deduction.

Q: Can Business Income & Receipts Tax (BIRT) filers taking the federal deduction on pass-through income reduce the income reported to Philadelphia to reflect the same 20% reduction?

A: No.

- C Corporations are not entitled to the federal deduction, so there is no impact.
- Partnerships and S Corporations file the BIRT return at the entity level and pay the tax due, even though they are pass-through entities. The federal deduction does not apply
- Individuals report taxable income for BIRT based on Net Profit (Loss) from Federal Form 1040, Schedule C. The IRC Section 199A deduction is reported *after* Adjusted Gross Income on the Federal Form 1040 (the draft for 2018), so it would not be reflected as a reduction for BIRT Net Income purposes.

Q: Can Net Profits Tax (NPT) filers take the IRC Section 199A deduction to arrive at the net profits subject to tax?

A: No.

- Partnerships with nexus in Philadelphia would pay NPT based on the partnership income, without any deduction under IRC Section 199A. None of the income would be taxed to the partners.
- For partnerships without nexus in Philadelphia, a resident partner would file a NPT Return reporting its distributive share of the partnership income. The federal deduction is not allowed.

Q: Will this deduction affect Philadelphia Wage or Earnings Tax filers?

A: No. The Wage and Earnings Tax is not imposed on pass-through income.