



# Rental Real Estate QBI Safe Harbor

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## Qualified Business Income (QBI) Deduction

For tax years 2018 through 2025, you may deduct up to 20% of qualified business income from each of your qualified trades or businesses, including those operated through a sole proprietorship, or a pass-through entity, such as a partnership, LLC, or S corporation.

In general, income from rental real property held for investment purposes and reported on Schedule E (Form 1040) is not eligible for the QBI deduction. However, you may be eligible for the QBI deduction if you are operating the activity as a real estate business.

There is uncertainty for some as to whether rental real estate qualifies as a trade or business for purposes of the QBI deduction. The IRS has provided a safe harbor under which a rental real estate enterprise will be treated as a trade or business solely for purposes of the QBI deduction.

**Note:** The rental or licensing of tangible or intangible property to a related trade or business qualifies if both businesses are commonly controlled.

## Rental Real Estate Enterprise

Solely for purposes of the safe harbor, a rental real estate enterprise is defined as an interest in real property held for the production of rents and may consist of an interest in multiple properties. That is, you may own just one rental property or multiple rental properties that could potentially qualify as a rental real estate enterprise.

You or the relevant pass-through entity (RPE) such as a partnership or S corporation, relying on the safe harbor must hold the interest directly or through an entity disregarded as separate from its owner, such as a limited liability company (LLC).

You 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. However, commercial and residential real estate may not be part of the same enterprise. Once you chose to combine or keep properties separate, you may not vary this treatment from year-to-year unless there has been a significant change in facts and circumstances.

## Safe Harbor

Solely for purposes of the QBI deduction, your rental real estate enterprise will be treated as a trade or business under the safe harbor, if all of the following requirements are satisfied during the tax year.

- Separate books and records are maintained to reflect income and expenses for each rental real estate enterprise,
- 250 or more hours of rental services are performed per year for the rental enterprise for tax years beginning prior to 2023, and
- You maintain contemporaneous records, including time reports, logs, or similar documents, regarding:
  - Hours of all services performed,
  - Description of all services performed,
  - Dates on which such services were performed, and
  - Who performed the services.

**Note:** The contemporaneous record requirement does not apply to 2018. It does apply for tax years after 2018.



## Rental Real Estate QBI Safe Harbor

**Rental services.** For purposes of the safe harbor, rental services include the following activities.

- Advertising to rent or lease the real estate,
- Negotiating and executing leases,
- Verifying information contained in prospective tenant applications,
- Collection of rent,
- Daily operation, maintenance, and repair of the property,
- Management of the real estate,
- Purchase of materials, and
- Supervision of employees and independent contractors.

Rental services may be performed by owners or by employees, agents, and/or independent contractors of the owners.

The term rental services does 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.

**Example:** Jill owns a condo that she rents out during 2018 and she does not use a management company. She receives rent deposits directly from the tenant during the year. In May, she made arrangements for repairs to be completed at the condo. She had no other contact with the tenant and did not visit the property during the year. In this scenario, Jill's rental real estate enterprise probably does not rise to the level of a trade or business under the safe harbor because it is unlikely she spent 250 hours performing rental services. She would not be entitled to claim the QBI deduction for her rental income under the safe harbor.

**Excluded rental real estate arrangements.** The safe harbor does not apply to real estate used by you as a residence for any part of the year. This exclusion would include vacation homes.

Real estate rented or leased under a triple net lease is also not eligible for the safe harbor. A triple net lease is a lease agreement that requires the tenant or lessee to pay directly, in addition to rent, some or all of the expenses typically paid by the property owner. These expenses include property taxes, insurance, maintenance, and other expenses.

This brochure contains general information for taxpayers and should not be relied upon as the only source of authority. Taxpayers should seek professional tax advice for more information.

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**Statement attached to the return.** To use the safe harbor, a signed statement must be attached to your tax return that states the requirements of Notice 2019-07 have been satisfied. The statement must include the following:

“Under penalties of perjury, I (we) declare that I (we) have examined the statement, and, to the best of my (our) knowledge and belief, the statement contains all the relevant facts relating to the revenue procedure, and such facts are true, correct, and complete.”

The signer(s) must have personal knowledge of the facts and circumstances related to the statement.

### Trade or Business

If your rental real estate enterprise fails to satisfy the safe harbor requirements, it may still be treated as a trade or business for purposes of QBI deduction if the enterprise otherwise meets the definition of a trade or business. However, this has never been defined by the IRS and has been left up to the courts, which have produced differing opinions depending on the facts and circumstances of the situation.

Generally, a trade or business activity does not include a rental activity or the rental of property that is incidental to an activity of holding the property for investment.

## Contact Us

There are many events that occur during the year that can affect your tax situation. Preparation of your tax return involves summarizing transactions and events that occurred during the prior year. In most situations, treatment is firmly established at the time the transaction occurs. However, negative tax effects can be avoided by proper planning. Please contact us in advance if you have questions about the tax effects of a transaction or event, including the following:

- Pension or IRA distributions.
- Significant change in income or deductions.
- Job change.
- Marriage.
- Attainment of age 59½ or 70½.
- Sale or purchase of a business.
- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of \$5,000.