Who gets the 20% small-business tax deduction? It's complicated

By Marcy Gordon

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WASHINGTON - Architects and engineers are still in. Accountants, doctors and lawyers remain out - mostly. New rules floated by the Trump administration lay out what kinds of businesses can take a 20 percent deduction against income taxes under the new tax law.

With the proposed rules issued Wednesday, the Treasury Department and the IRS had worked for six months to bring clarity to Congress' blueprint. But as with many aspects of the sweeping Republican tax law hustled through Congress last year, the requirements for the millions of 'pass-through' businesses to score generous tax breaks are stunningly complex.

Some business owners earning over certain income levels, for example, are excluded, as are companies that are organized in certain ways or that lease their equipment rather than own it.

'They've attempted to draw lines that are clearer than the language' of the tax law, said Andrew Howlett, an attorney at law firm Miller& Chevalier who specializes in tax issues. 'There are still questions that remain to be answered for taxpayers.'

Steven Rosenthal, a senior fellow at the nonpartisan Urban-Brookings Tax Policy Center, said the new regulations 'allow a lot of different businesses the 20 percent deduction. ... They allowed a lot of latitude for businesses to claim it.'

At the same time, Rosenthal found the protections in the rules against abuse by businesses of the special tax break to be inadequate. 'I think there'll be a lot of gaming of the rules,' he said.

There is concern, for example, that to qualify for the deduction, individuals would quit their jobs and then contract their services back to their former employers as independent contractors. Now the government appears to have prohibited that in the new rules, said Kyle Pomerleau, director of the Center for Quantitative Analysis at the conservative Tax Foundation.

The new rules affirm the requirement in the tax law that certain business owners like lawyers, accountants, doctors and consultants can't qualify for the full deduction if their annual income exceeds $157,000 for single tax filers and $315,000 for couples filing jointly. The amount of the deduction to be claimed declines as taxpayers' income rises. The same is true for interior designers, investment managers, therapists and others.

Many small-business owners around the country have been yearning for months to know whether they'll be pass-through winners or losers. Even with the new regulations, many owners still will likely be turning to tax accountants and other specialists to cut through the confusion.

Millions of businesses - from the mom-and-pop grocery store or florist to big law firms, hedge funds and the sprawling Trump Organization - are organized as pass-throughs in which company profits are pipelined into the owners' personal tax bucket. The owners pay individual, not corporate, tax rates on the income. The vast majority of U.S. businesses, big and small, are taxed this way.

The Republican architects of the tax plan and President Trump portrayed the new pass-through tax break as a boon to Main Street businesses and entrepreneurs.