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July 25, 2018

Via E-mail: WI.1040.Comments@IRS.gov

The Honorable David J. Kautter
Acting Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

The Honorable William M. Paul
Acting Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: IRS Draft Form 1040

Dear Messrs. Kautter and Paul:

Nareit appreciates the opportunity to offer our comments regarding the Internal Revenue Service (IRS) IRS Draft Form 1040, which the IRS released on June 29, 2018.

Nareit is the worldwide representative voice for real estate investment trusts (REITs) and publicly traded real estate companies with an interest in U.S. real estate and capital markets. Nareit advocates for REIT-based real estate investment with policymakers and the global investment community.

REITs are real estate working for you. Through the properties they own, finance and operate, REITs help provide the essential real estate we need to live, work and play. All U.S. REITs own approximately $3 trillion in gross assets, public U.S. REITs account for $2 trillion in gross assets, and stock-exchange listed REITs have an equity market capitalization of over $1 trillion. In addition, more than 80 million Americans invest in REIT stocks through their 401(k) and other investment funds.

Executive Summary

With the enactment of Pub. L. 115-97 (also known as the Tax Cuts and Jobs Act, or TCJA), section 199A, entitled “Qualified business income,” was added to the Internal Revenue Code.[1] The Consolidated Appropriations Act, 2018, Pub. L. 115-141, further refined section 199A.

[1] Unless otherwise noted, references to “section” in this letter refer to sections of the Internal Revenue Code of 1986, as amended (the Code).

As relevant to Form 1040 and REITs, section 199A generally entitles individual taxpayers to a deduction equal to 20% of, among other things, their "qualified REIT dividends." The Draft Form 1040 includes Line 9 entitled "Qualified business income deduction (see instructions)." However, the draft Form 1040 does not provide instructions as to how Line 9 should be calculated.

Nareit understands that the IRS will release a revised version of the Form 1040, along with instructions, later this year. Nareit requests that the Form 1040 instructions explicitly state that the 20% deduction provided by line 9 of Form 1040 (or the appropriate line of any modification to the current draft of Form 1040) applies to qualified REIT dividends.

Discussion

While section 199A is entitled "**Qualified business income**" in the Code, the section 199A(a) deduction combines a number of items of which the defined term "qualified business income" is a part. Specifically, section 199A(a) provides a deduction generally equal to the lesser of: 1) the combined qualified business income amount (CQBIA) of the taxpayer, or, 2) an amount equal to 20% of the excess (if any) of the taxable income of the taxpayer for the taxable year, over the net capital gain of the taxpayer for such taxable year.[2]

CQBIA generally is defined as 20% of qualified business income with respect to each qualified trade or business through a partnership, S corporation, or sole proprietorship (potentially with certain wage and basis limitations) of the taxpayer, plus 20% of the aggregate amount of the qualified REIT dividends and qualified publicly traded partnership income of the taxpayer for the taxable year.

Section 199A(e)(3) defines a "qualified REIT dividend" as any dividend from a real estate investment trust received during the taxable year which is not a capital gain dividend, as defined in section 857(b)(3), and is not qualified dividend income, as defined in section 1(h)(11).

Corporations, including REITs and regulated investment companies (RICs or mutual funds), report their dividends to individual shareholders on Form 1099-DIV.[3] Partnerships, including publicly traded partnerships, may hold interests in REITs and would report qualified REIT dividends to their partners on Form 1065, Schedule K-1.[4] Because the tax treatment of qualified REIT dividends differs from other income of the partnership, we recommend that qualified REIT dividends be reported as a separately stated item on Form 1065, Schedule K-1.

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[2] Section 199A(g) also provides for a "deduction for income attributable to domestic production activities of specified agricultural or horticultural cooperatives." This letter does not address the calculation of that deduction.
[3] The most recent version of Form 1099-DIV was posted on the IRS website on July 17, 2018.
[4] The most recent version of Form 1065, Schedule K-1 was posted on the IRS website on Dec. 4, 2017. Thus, it does not reflect the provisions of Pub. L. 115-97 or Pub L. 115-141.

Currently, the instructions to Box 1a of revised Form 1099-DIV requires inclusion of "total ordinary dividends that are taxable." Pursuant to the Form 1099-DIV instructions, Box 1b of Form 1099-DIV should equal the "**portion of the amount in box 1a** that may be eligible for reduced capital gains rates" (*i.e.*, "qualified dividend income" under section 1(h)(11)(B)) (Emphasis added). Box 2a "shows total capital gain distributions from a regulated investment company (RIC) or a . . . [REIT]."

If an individual taxpayer's Form 1099-DIV included only dividends from REITs, that taxpayer could calculate its section 199A(a) deduction with respect to "qualified REIT dividends" by subtracting the amount in Box 1b from the amount in Box 1a. The resulting amount would represent the dividends received from a REIT that are not capital gain dividends or qualified dividend income, in other words, "qualified REIT dividends."

However, many individual taxpayers receive Forms 1099-DIV that may include not just REIT dividends, but also RIC and dividends from corporations other than REITs and RICs. This might be the case if a taxpayer maintains an investment account comprised of a portfolio of stocks and securities at a specific broker or investment adviser. If so, Box 1a of Form 1099-DIV would aggregate all taxable ordinary dividends of the taxpayer from such investment account, and Box 1b would aggregate all qualified dividend income of the taxpayer from such investment account. For example, Box 1a may include $100 of dividends from a REIT and $50 of non-qualified dividend income from other sources, such as certain foreign dividends, and Box 1b may show an amount of $0. The amount resulting after subtracting Box 1b from Box 1a would be $150, but only $100 of that amount would represent a qualified REIT dividend for purposes of section 199A(e)(3). We appreciate that the revised version of Form 1099-DIV posted on the IRS website on July 17, 2018, includes a new Box 5 entitled "Section 199A dividends." Inclusion of Box 5 should assist both taxpayers as well as the IRS in matching the qualified REIT dividends from Form 1099-DIV with the qualified REIT dividends reported on Form 1040.

The Form 1099-DIV instructions regarding new Box 5 state: "Shows dividends eligible for the 20% qualified business income deduction under section 199A. See the Instructions for Form 1040." For effective matching (and clarity), it would be helpful if the instructions to the 2018 Form 1040 could include a worksheet for calculating the Line 9 deduction. In particular, because qualified REIT dividends are not subject to the limitation in section 199A(b)(2)(B), it seems reasonable and prudent to separate the reporting of qualified REIT dividends from that of qualified trade or business income.[5] Nareit recommends that the 2018 Form 1040 instructions be revised to describe clearly the calculation of

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[5] For the same reason, we recommend that Form 1065, Schedule K-1 be modified to include separate line items for section 199A REIT dividends and other qualified business income. This specificity should assist both taxpayers as well as the IRS in matching the qualified REIT dividends and qualified business income earned by the partnership with that reported by partners.

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qualified REIT dividends to be included on Line 9 of Form 1040. Such a revision would help to ensure accurate reporting of REIT dividends. [6]

We would be pleased to discuss these comments if you believe it would be helpful. Please feel free to contact me at (202) 739-9408, or tedwards@nareit.com; Cathy Barré, Nareit's Senior Vice President, Policy & Politics, at (202) 739-9422, or cbarre@nareit.com; or Dara Bernstein, Nareit's Senior Vice President and Tax Counsel, at (202) 739-9446 or dbernstein@nareit.com.

Respectfully submitted,

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[6] We note that, for over 20 years, Nareit has cooperated with The Investment Company Institute (ICI) (the trade association representing the mutual fund industry), and the securities and brokerage industry to facilitate the effective reporting of year-end dividend allocation information on Form 1099-DIV by providing each reporting company with a uniform spreadsheet for such information. Nareit member REITs upload year-end tax reporting data based on the Form 1099-DIV to the Nareit website on a voluntary basis as well as to organizations that in turn disseminate the data to mutual funds and brokers. Brokers access the information from the Nareit website and these spreadsheets electronically and pre-program their reporting processes to accurately incorporate the data. This Nareit project helps to ensure that the individual components of each REIT distribution are reported accurately by both mutual funds and brokers on Form 1099-DIV, and, accordingly, by individuals on Form 1040. Because any changes to the reporting process, such as the addition of Box 5 to the Form 1099-DIV, require time to re-program reporting processes, it is important that the revised Form 1040 instructions be issued as soon as possible to ensure accurate reporting.