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Section 199A implications for cooperatives under appropriations legislation

The Consolidated Appropriations Act, 2018 (Pub. L. No. 115-141) that the president signed into law on Friday, March 23, 2018, includes changes to section 199A regarding the application of the new deduction for certain cooperatives and grain companies.

As enacted in Pub. L. No. 115-97 (December 22, 2017), section 199A generally provides a deduction for qualifying income of certain noncorporate owners of some pass-through entities and sole proprietorships.

The provision in the Consolidated Appropriations Act attempts to address certain concerns raised within the agricultural industry that farmers selling their farm commodities to cooperatives were significantly tax-advantaged over similarly situated farmers selling to non-cooperatives. Section 199A(a)(2), as initially enacted, had provided for a 20% gross deduction for “qualified cooperative dividends,” and this term was defined as including per-unit retain allocations paid in money (essentially the sales price of the commodities delivered for marketing to a cooperative).

The new provisions are effective retroactively from January 1, 2018.

Overview of new provision

With enactment of the new measures, section 199A:

- Restores prior-law section 199 treatment for specified agricultural and horticultural cooperatives under new section 199A(g). The U.S. Treasury is instructed to base new guidance on regulations under the prior-law version of section 199.
- Allows eligible patrons to claim a deduction passed through from a specified agricultural and horticultural cooperative. Eligible patrons include all non-corporate

taxpayers, S corporations, and other specified agricultural and horticultural cooperatives.

- Revises the farmer-level deduction to 20% of taxable income or qualified business income (in line with all other non-corporate taxpayers), with limitations for farmers with high taxable incomes or capital gains.

Under the new law, for farmers who enter into transactions with a cooperative:

- The 20% deduction will be reduced by the lesser of: (1) 9% of qualified business income allocable to qualified payments received from cooperatives; or (2) 50% of wages allocable to such qualified payments.
- This reduction applies regardless of the amount of section 199A(g) deduction passed through by the cooperative. This treatment is intended to replicate the deduction the farmer had foregone by dealing with the cooperative under prior-law section 199.
- The cooperative member's total deduction for the year will be the pass-through deduction plus the modified 20% deduction.

Taxpayers, including patrons of cooperatives structured as C corporations, are not eligible for the 199A deduction including the pass-through deduction under section 199A(g) from specified agricultural and horticultural cooperatives.

Special rules are provided for cooperatives with oil-related qualified production activities income.

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