



## **OKLAHOMA INCOME TAX CONFORMITY WITH THE QUALIFIED BUSINESS INCOME DEDUCTION UNDER INTERNAL REVENUE CODE SECTION 199A**

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The question of allowance of the federal income tax deduction of qualified business income of pass-through entities by owners other than corporations under section 199A of the Internal Revenue Code (“Code”) for purposes of the Oklahoma income tax has been raised and discussed by some tax advisers and their clients. That discussion has included correspondence and comments sent and shared by and between members of the Oklahoma Society of CPAs in which the author of this note participated.

At the time this note was written, the [Oklahoma Tax Commission had published a question and answer](#), stating the section 199A qualified business income deduction is not an allowable deduction for Oklahoma (the “OTC/Individual QBI Q&A”). The reason given by the Tax Commission in the OTC/Individual QBI Q&A is the deduction is not a modification to federal adjusted gross income (which is Oklahoma’s starting point), but rather a modification to federal taxable income. (The Oklahoma Tax Commission also more recently published a separate question and answer on Oklahoma income tax conformity with the section 199A deduction for an Oklahoma trust. This note is furnished to discuss the OTC/Individual QBI Q&A, as described, and with respect to an individual taxpayer as an owner of a pass-through entity such a partnership, S corporation or sole proprietorship, rather than a trust.)

The allowance of the section 199A deduction for Oklahoma income tax presumably is dependent upon application of the provisions of the Oklahoma Income Tax Act, 68 O. S. §§2351-2397 (the “Act”) and the Code. This note discusses how the provisions of the Act may support a different result than what is stated in the OTC/Individual QBI Q&A, and that under the Act the section 199A deduction could be considered as allowable for Oklahoma income tax.

The Act has been interpreted as in effect providing that a federal income tax deduction allowed under the Code and lawfully claimed on an individual taxpayer's federal income tax return is allowed in arriving at "taxable income" of the taxpayer and is in turn also allowed in arriving at "Oklahoma taxable income" of the taxpayer, subject to further adjustments, if any, provided with respect to the deduction under the Act. The Act does not appear to contain any specific provision that prevents or avoids this result for the section 199A deduction, or any specific statutory adjustment that limits or disallows the section 199A deduction for Oklahoma.

Thus, under that interpretation the Act appears to provide that federal "taxable income" reported by an individual taxpayer on the taxpayer's federal income tax return is the "Oklahoma taxable income" of the taxpayer. This seems to make federal "taxable income" the substantive tax base for conformity of Oklahoma income tax with federal income for individual taxpayers, although federal "adjusted gross income" has been referred to as the "starting point" for computing and reporting that conformity. As indicated, the Act has been interpreted as providing that the Code and deductions allowed under it are integrated into the Act by the statutory definitions of "taxable income" and "Oklahoma taxable income" in the Act. A deduction allowed under the Code and lawfully claimed on an individual taxpayer's federal income tax return to arrive at federal "taxable income" is also allowed in arriving at the taxpayer's "Oklahoma taxable income," absent any specific statutory adjustment to the taxpayer's "Oklahoma adjusted gross income" or "taxable income" provided under the Act that limits or denies the deduction for Oklahoma. The interpretation states Oklahoma accepts all lawful deductions taken on the taxpayer's federal return, pursuant to the Code, as adjustments to "adjusted gross income," prior to the determination of "Oklahoma taxable income." Thus, under the Act, as interpreted, a federal income tax deduction that is allowed under the Code in arriving at the amount of federal "taxable income," (as defined in 68 O. S. § 2353(10)) of an individual taxpayer and as lawfully reported to the federal government by the taxpayer becomes a deduction allowed in arriving at "Oklahoma taxable income" (as defined in 68 O. S. §2353(12), and the Act does not repeat or state the terms of such federal deduction because it is already stated in and allowed under the Code.

The Act does not specifically allow the section 199A deduction for Oklahoma, which is consistent with treatment of other federal income tax deductions, as described above, and the Act also does not provide for any specific statutory adjustment to an individual's "adjusted gross income" or "taxable income" that limits or disallows a section 199A deduction lawfully claimed and allowed on an individual taxpayer's federal return. Thus, the governing tax conformity provisions of the Act defining and correlating "taxable income" and "Oklahoma taxable income," as so interpreted, presumably should result in allowance of the section 199A deduction to the same extent as any other federal deduction under the Code that is lawfully claimed and allowed on an individual taxpayer's federal income tax return. The Act also does not contain any provision stating that result is changed because the section 199A deduction under the Code reduces "taxable income," rather than being an "above-the-line" deduction allowed in computation of federal "adjusted gross income," or a federal "itemized" deduction.

The published OTC/ Individual QBI Q&A does not specifically explain how the answer given in it is based upon the provisions of the Act. The OTC/ Individual QBI Q&A also does not explain why the section 199A deduction is not be allowed for Oklahoma pursuant to the Act if the deduction is, as indicated in the answer given, a “modification of federal taxable income,” and there is no specific statutory adjustment in the Act that limits or denies the section 199A deduction in arriving at “Oklahoma taxable income” of an individual taxpayer who is allowed the deduction under the Code and has lawfully claimed it on the taxpayer’s federal return.

In summary, the statutory provisions of the Act, as so interpreted, seemingly could support an answer that the Oklahoma income tax conforms with section 199A. The Oklahoma Tax Commission published information in the OTC/ Individual QBI Q&A indicates a different answer that Oklahoma income tax is not conformed to the section 199A deduction. Hopefully, the discussion in and made available by this note will help in finding the correct answer.

[Click here](#) for a more detailed discussion of the question and application of the Act written by the author.

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