

## Airbnb and the "New" Qualified Business Income Deduction

**Take-Away:** An Airbnb owner can qualify for the qualified business income (QBI) income tax deduction if the Airbnb meets the definition of, and is classified as, a ‘trade or business,’ or the owner elects to fall within an IRS ‘safe harbor.’

**Background:** The recent One Big Beautiful Bill Act (OBBBA) for self-employed and small business owners made permanent the 20% federal income tax deduction for *qualified business income*. [IRC 199A.] In addition, the OBBBA expanded the adjusted gross income (AGI) limitations to become eligible to claim the *qualified business income* (QBI) tax deduction. Accordingly, the number of those individuals who can claim the QBI income tax deduction will be expanded under the OBBBA, including more Airbnb owners. These changes to IRC199A are effective for tax years that begin after December 31, 2025.

**The OBBBA Changes:** The phase-in thresholds for the owner’s W-2 wages, and/or capital investment limits and restrictions are widened under the OBBBA. The income phase-in range was increased from \$100,000 (under the prior law) to \$150,000 for married couples who file jointly. For single individuals, the income phase-in threshold was expanded from \$50,000 to \$75,000. For those individuals who have less than \$1,000 in *qualified business income* from an active trade-or-business in which they materially participate, a *floor* (so to speak) is created; those individuals will receive a minimum \$400 QBI income tax deduction. These amounts are indexed to inflation. [IRC 199A(b)(3); IRC 199A(i).]

These changes to the QBI eligibility rules are intended to provide access to the QBI deduction to more individuals who are small or moderate-income business owners.

**Trade or Business:** To be eligible to claim the QBI income tax deduction however, the Airbnb rental activity must be classified as a ‘trade-or-business’ rather than merely passive rental activity. This means that for most short-term rentals, the ‘trade or business’ determination will turn on how active the owner is in managing their property and the level of services that are provided by the owner to their guests who rent the Airbnb.

**QBI Eligibility:** The owner of the Airbnb must either meet the definition of a ‘trade-or-business’ provided in IRC 162, or the Airbnb must qualify under a specific IRS ‘safe harbor.’

**Schedule C:** An Airbnb can qualify as an active ‘trade-or-business’ if the owner provides **substantial services** to their guests, much like a running a motel or B&B. Thus, the owner’s activity is treated as self-employment and is reported on Schedule C to the owner’s income tax return. Examples of these substantial services include activities like daily cleaning, providing fresh linens, meals, having an average guest stay of 7 days or less, and managing bookings, guest communications, and general property upkeep, e.g., lawn care and pool cleaning.

**Safe Harbor:** The IRS Regulations provide what is informally called a ‘safe harbor’ for rental real estate. Even if the operation of an Airbnb does not rise to the level of a trade-or-business as defined in IRC 162, the owner can still *elect* to be treated as a trade-or-business by meeting the requirements of the ‘safe harbor’ provision explained in IRS Notice 2019-07. Each of the following requirements must be fulfilled to fall within the IRS’s ‘safe harbor’:

1. The Airbnb owner must keep detailed logs, time reports, or other documentation that shows who performed the rental services, the date and hours spent, and a description of the work or services provided. Accordingly, accurate record-keeping is critical to substantiate eligibility for the Airbnb owner to elect to file under this ‘safe harbor.’
2. There must be at least 250 hours devoted Airbnb rental services per year. These hours can be provided by the owner, employees, or other independent contractors. Again, recordkeeping is critical to document the required 250 hours.
3. The owner must maintain separate books and records for each rental property or enterprise.

4. A formal statement must be attached to the Airbnb owner's income tax return that expressly states that the owner is relying on the IRS's 'safe harbor,' i.e., the owner must *elect* to be treated under the 'safe harbor.'

**Mixed Use:** This 'safe harbor' generally will not apply if the Airbnb owner uses their property for personal use during the year for more than 14 days or 10% of the total rental days in the year, whichever is greater.

**Reporting Airbnb Activity:** How Airbnb income is reported on the tax return is very important. If the Airbnb is classified as a 'trade-or-business' due to the substantial services that are provided by the owner, the income is subject to both income tax and self-employment tax, e.g., Social Security and Medicare taxes. This is probably the easiest path to qualify for the QBI income tax deduction.

If the Airbnb rental activity is more limited or passive, such as minimal services provided by the owner, or there are much longer guest stays at the property, the Airbnb owner will report his/her income on Schedule E, which is not subject to self-employment tax, but it will *generally* not be eligible for the QBI deduction unless the owner elects to qualify for the IRS 'safe harbor' described above.

**Conclusion:** More small business owners are expected to qualify for the qualified business income (QBI) tax deduction if they itemize their income taxes with the OBBBA changes. This includes Airbnb owners. The challenge will be either for the Airbnb owner to qualify as a 'trade-or-business' but then he/she must expect to pay Social Security and Medicare taxes as a trade-off to claiming the QBI deduction, or the owner must elect to fall within the IRS's safe harbor, which entails detailed record-keeping, logs, and documenting at least 250 hours a year devoted to the Airbnb activity.

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