KPMG

cutting through complexity

Section 199
Domestic Production Activities Deduction

OVERVIEW

Internal Revenue Code (I.R.C.) Section 199, the Domestic Production Activities Deduction (DPAD), was created as part of the American Jobs Creation Act of 2004 to incentivize companies engaging in certain activities to keep and/or create jobs in the United States.

Section 199 allows the taxpayer to take a permanent deduction that is equal to 9 percent of the lesser of *Qualified Production Activities Income* (QPAI) or *Taxable Income*. The deduction, however, may not exceed 50 percent of qualifying W-2 wages paid by the taxpayer in the applicable tax year. The deduction can be equivalent to a 3 percent tax rate reduction on qualified income.

Amended returns may be filed for prior tax years to claim the benefit.

HELPFUL DEFINITIONS:

QPAI: Qualified Production Activities Income is the net income generated from a taxpayer's qualifying activities. For the computation of QPAI, see the formula on the following page.

DPGR: Domestic Production Gross Receipts are qualifying gross receipts of the taxpayer. For the various ways a taxpayer can generate DPGR, see chart below.

MPGE: Manufactured, Produced, Grown, or Extracted – relevant to the discussion of how Qualifying Production Property is created by the taxpayer.

QPP: Qualifying Production Property is the item/good generating revenue for the taxpayer that may potentially be considered DPGR.

COMPUTING DPGR

Determining domestic production gross receipts (DPGR) is the first step in computing the DPAD. A taxpayer must consider qualifying property and qualifying activities.

Domestic Production Gross Receipts "DPGR"

Gross receipts derived from

Qualifying Activity

- **Lease, rental, license, sale, exchange, or other disposition**
- **Construction of real property performed in the U.S.**
- **Engineering or architectural services performed in the U.S. with respect to construction of real property in the U.S.**

Qualifying Property

- **QPP MPGE by the taxpayer in whole or in significant part within the U.S.**
  - **Tangible personal property**
  - **Computer software**
  - **Sound recordings**
- **Qualified film produced by the taxpayer**
- **Electricity, natural gas, or potable water produced by the taxpayer in the U.S.**

COMPUTING THE DEDUCTION

DPGR

(CGS)

(Other expenses allocable to DPGR)

QPAI

X 9%

DPAD

* Subject to the Taxable Income and W-2 Wage limitations described above.

HOW KPMG CAN HELP

KPMG LLP's (KPMG) Section 199 practice

KPMG offers dedicated local and national resources with extensive experience serving companies across a spectrum of industries. Some of the key ways KPMG can help your company include assistance with:

- Determining eligibility for the DPAD deduction by helping to identify both common and unique qualifying production activities;
- Analyzing the computation of the deduction, including required allocations, on an annual and/or quarterly basis;
- Assessing the potential impact to other tax positions, including tax accounting methods (e.g., income recognition, inventories, I.R.C. section 263A/UNICAP, etc.), foreign tax credit utilization, research and development credit, state and local taxes;
- Preparing qualitative documentation to support a company's technical position under I.R.C. section 199;
- Assisting with controversy-related issues pertaining to I.R.C. section 199, including responding to information document requests and assisting clients with respect to Internal Revenue Service examinations; and
- Enhancing the information-gathering process to support the annual deduction calculation.

Customized, scalable studies

KPMG's approach to assisting clients with I.R.C. section 199 calculations can be tailored to fit your company's specific needs. For example:

- For clients that are currently claiming I.R.C. section 199 benefits, KPMG can perform a review of the most recent calculations to identify potential opportunities and/or exposures;
- For clients that desire a more thorough approach, our team has extensive experience performing fully integrated studies with a focus on delivering audit-ready qualitative and quantitative documentation;
- With an emphasis on lessening the intrusion to our clients, our team's ability to understand clients' data collection and analysis resources has allowed us to develop several tools and techniques (including statistical sampling) that have helped us to more efficiently gather data and information.
- KPMG's cross-functional approach can provide clients with wide-ranging support by incorporating resources from our Washington National Tax, Economic and Valuation Services, Data Analytics, International Tax Services, State and Local Taxes, and Tax Dispute Resolution practices.

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