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Reg. Section 1.469-4(d)(1)(ii), Example 1

Definition of Activity.

(d) Limitation on grouping certain activities. The grouping of activities under this section is subject to the following limitations:

(1) Grouping rental activities with other trade or business activities-


(i) Rule. A rental activity may not be grouped with a trade or business activity unless the activities being grouped together constitute an appropriate economic unit under paragraph (c) of this section and—

(A) The rental activity is insubstantial in relation to the trade or business activity;

(B) The trade or business activity is insubstantial in relation to the rental activity; or

(C) Each owner of the trade or business activity has the same proportionate ownership interest in the rental activity, in which case the portion of the rental activity that involves the rental of items of property for use in the trade or business activity may be grouped with the trade or business activity.

(ii) Examples. The following examples illustrate the application of paragraph (d)(1)(i) of this section:



Example 1.

(i) H and W are married and file a joint return. H is the sole shareholder of an S corporation that conducts a grocery store trade or business activity. W is the sole shareholder of an S corporation that owns and rents out a building. Part of the building is rented to H's grocery store trade or business activity (the grocery store rental). The grocery store rental and the grocery store trade or business are not insubstantial in relation to each other.

(ii) Because they file a joint return, H and W are treated as one taxpayer for purposes of section 469. See § 1.469-1T(j). Therefore, the sole owner of the trade or business activity (taxpayer H-W) is also the sole owner of the rental activity. Consequently, each owner of the trade or business activity has the same proportionate ownership interest in the rental activity. Accordingly, the grocery store rental and the grocery store trade or business activity may be grouped together (under paragraph (d)(1)(i) of this section) into a single trade or business activity, if the grouping is appropriate under paragraph (c) of this section.

Example 2. Attorney D is a sole practitioner in town X. D also wholly owns residential real estate in town X that D rents to third parties. D's law practice is a trade or business activity within the meaning of paragraph (b)(1) of this section. The residential real estate is a rental activity within the meaning of § 1.469-1T(e)(3) and is insubstantial in relation to D's law practice. Under the facts and circumstances, the law practice and the residential real estate do not constitute an appropriate economic unit under paragraph (c) of this section. Therefore, D may not treat the law practice and the residential real estate as a single activity.

(2) Grouping real property rentals and personal property rentals prohibited. An activity involving the rental of real property and an activity involving the rental of personal property (other than personal property provided in connection with the real property or real property provided in connection with the personal property) may not be treated as a single activity.

(3) Certain activities of limited partners and limited entrepreneurs-

(i) In general. Except as provided in this paragraph, a taxpayer that owns an interest, as a limited partner or a limited entrepreneur (as defined in section 464(e)(2)), in an activity described in section 465(c)(1), may not group that activity with any other activity. A taxpayer that owns an interest as a limited partner or a limited entrepreneur in an activity described in the preceding sentence may group that activity with another activity in the same type of business if the grouping is appropriate under the provisions of paragraph (c) of this section.

(ii) Example. The following example illustrates the application of this paragraph (d)(3):

Example.

(i) Taxpayer A, an individual, owns and operates a farm. A is also a member of M, a limited liability company that conducts a cattle-feeding business. A does not actively participate in the management of M (within the meaning of section 464(e)(2)(B)). In addition, A is a limited partner in N, a limited partnership engaged in oil and gas production.

(ii) Because A does not actively participate in the management of M, A is a limited entrepreneur in M's activity. M's cattle-feeding business is described in section 465(c)(1)(B) (relating to farming) and may not be grouped with any other activity that does not involve farming. Moreover, A's farm may not be grouped with the cattle-feeding activity unless the grouping constitutes an appropriate economic unit for the measurement of gain or loss for purposes of section 469.

(iii) Because A is a limited partner in N and N's activity is described in section 465(c)(1)(D) (relating to exploring for, or exploiting, oil and gas resources), A may not group N's oil and gas activity with any other activity that does not involve exploring for, or exploiting, oil and gas resources. Thus, N's activity may not be grouped with A's farm or with M's cattle-feeding business.

(4) Other activities identified by the Commissioner. A taxpayer that owns an interest in an activity identified in guidance issued by the Commissioner as an activity covered by this

paragraph (d)(4) may not group that activity with any other activity, except as provided in the guidance issued by the Commissioner.

(5) Activities conducted through section 469 entities –

- (i) In general. A C corporation subject to section 469, an S corporation, or a partnership (a section 469 entity) must group its activities under the rules of this section. Once the section 469 entity groups its activities, a shareholder or partner may group those activities with each other, with activities conducted directly by the shareholder or partner, and with activities conducted through other section 469 entities, in accordance with the rules of this section. A shareholder or partner may not treat activities grouped together by a section 469 entity as separate activities.
- (ii) Cross reference. An activity that a taxpayer conducts through a C corporation subject to section 469 may be grouped with another activity of the taxpayer, but only for purposes of determining whether the taxpayer materially or significantly participates in the other activity. See § 1.469-2T(c)(3)(i)(A) and (c)(4)(i) for the rules regarding dividends on C corporation stock and compensation paid for personal services.