

Internal Revenue Bulletin: 2008-31
August 4, 2008

Notice 2008-64

Disclosure of Activity Groupings Under Section 469

PURPOSE

This notice requests comments from the public regarding a proposal to require taxpayers to report to the Internal Revenue Service their groupings and regroupings of activities and the addition and disposition of specific activities within their existing groupings of activities for purposes of § 469 of the Internal Revenue Code and § 1.469-4 of the Income Tax Regulations. To date, the IRS has not prescribed reporting requirements for taxpayer groupings under section 469 other than those provided for in § 1.469-9(g) (relating to the election available to certain real estate professionals). As a result, the IRS and taxpayers have had difficulty verifying taxpayers' historical groupings. The proposal described in this notice would provide a reporting system that seeks to address this issue without unduly burdening taxpayers.

The proposal described in this notice is one possible approach. The IRS is interested in considering other possible approaches. Therefore, any requirement will not become effective until the IRS considers public comments and suggestions received in response to this notice and publishes final guidance announcing any new reporting rules.

BACKGROUND

Section 469 generally provides that deductions from passive trade or business activities, to the extent they exceed income from all such passive activities (exclusive of portfolio income), may not be deducted against other income.

Section 469(g)(1)(A) generally provides that if during the taxable year a taxpayer disposes of his entire interest in any passive activity (or former passive activity), and all gain or loss realized on such disposition is recognized, the excess of (i) any loss from such activity for such taxable year (determined after the application of § 469(b)), over (ii) any net income or gain for such taxable year from all other passive activities (determined after the application of § 469(b)), shall be treated as a loss which is not from a passive activity.

Section 1.469-4 sets forth the rules for grouping a taxpayer's trade or business activities and rental activities for purposes of applying the passive activity loss and credit limitation rules of § 469.

Section 1.469-4(c)(1) provides that one or more trade or business activities or rental activities may be treated as a single activity if the activities constitute an appropriate economic unit for the measurement of gain or loss for purposes of § 469.

Section 1.469-4(c)(2) provides guidelines for determining whether activities constitute an appropriate economic unit and, therefore, may be treated as a single activity. Section 1.469-4(d) describes limitations on grouping certain activities.

Section 1.469-4(e)(1) provides that except as provided in § 1.469-4(e)(2) and § 1.469-11 (providing three periods of time, all of which are now closed, in which a taxpayer could have regrouped its activities without having to establish that the original grouping was clearly inappropriate under § 1.469-

4(e)(2)), once a taxpayer has grouped activities under § 1.469-4, the taxpayer generally may not regroup those activities in subsequent taxable years. Taxpayers must comply with disclosure requirements that the Commissioner may prescribe with respect to both their original groupings and the addition and disposition of specific activities within those existing groupings in subsequent taxable years.

Section 1.469-4(e)(2) provides that if it is determined that a taxpayer's original grouping was clearly inappropriate or a material change in the facts and circumstances has occurred that makes the original grouping clearly inappropriate, the taxpayer must regroup the activities and must comply with the disclosure requirements that the Commissioner may prescribe.

PROPOSAL

The IRS is considering whether to change the reporting requirements for taxpayer groupings under section 469. Although the Service has considered a number of approaches, the proposal described in paragraphs A through F would generally require taxpayers to report to the Service, as part of their regular annual return, changes to a taxpayer's groupings. The proposal would apply to all persons or entities to whom the rules in § 1.469-4 apply. It would not apply to persons or entities who have made the election provided for in § 1.469-9(g) (relating to the election available to certain real estate professionals).

A. Statement Required for New Groupings

The proposal provides that a taxpayer shall file a written statement with its original return for the first taxable year in which one or more trade or business activities or rental activities are originally grouped as a single activity or as separate activities. This statement must identify the names, addresses, and employer identification numbers, if applicable, for the trade or business activities or rental activities that are being grouped as a single activity or as separate activities. In addition, any statement reporting a new grouping of two or more trade or business activities or rental activities as a single activity must contain a declaration that the grouped activities constitute an appropriate economic unit for the measurement of gain or loss for purposes of § 469. Pursuant to § 1.469-4(e)(1) and except as otherwise provided in § 1.469-4(e)(2) and § 1.469-11, once a taxpayer has grouped activities under § 1.469-4, the taxpayer may not regroup those activities in subsequent taxable years.

B. Statement Required for Addition of New Activities to Existing Groupings

The proposal provides that whenever a taxpayer adds a new trade or business activity or a rental activity to an existing grouping within a taxable year, the taxpayer shall file a written statement with the taxpayer's original return for the taxable year in which the new trade or business activity or rental activity is added to the existing grouping. This statement must identify the names, addresses, and employer identification numbers, if applicable, for the new trade or business activity or rental activity that is being added to the existing grouping. The statement reporting an addition to an existing grouping must also identify the names, addresses, and employer identification numbers, if applicable, for the activity or activities within the existing grouping. In addition, the statement reporting an addition to an existing grouping must contain a declaration that the activities constitute an appropriate economic unit for the measurement of gain or loss for purposes of § 469.

C. Statement Required for Disposition of Activities from Existing Groupings

The proposal provides that whenever a taxpayer disposes of a specific activity from an existing grouping within a taxable year, the taxpayer shall file a written statement with the taxpayer's original return for the taxable year in which the disposition of the specific trade or business activity or rental activity within the existing grouping occurs. This statement must identify the names, addresses, and employer identification numbers, if applicable, for the specific trade or business activity or rental activity that is disposed of, as well as the names, addresses, and employer identification numbers, if

applicable, for the activity or activities that remain in the existing grouping. The statement reporting a disposition of a specific activity within an existing grouping must contain a declaration that the remaining activities (if more than one) within the existing grouping constitute an appropriate economic unit for the measurement of gain or loss for purposes of § 469. Except as otherwise provided in § 1.469-4(g) (providing for the treatment of partial dispositions where there is a disposition of substantially all of an activity), the rules provided for in § 469(g) will not apply to the disposition of a specific activity from an existing grouping. For example, assume A, an individual, owns and operates four bakeries which A has treated as one activity under § 1.469-4. If, within a taxable year, A sells A's entire interest in one of those bakeries, the rules provided for in § 469(g) will generally not apply to the sale, and any losses or credits attributable to the disposed of bakery will be treated as a deduction or credit allocable to the continuing bakery activity. If a taxpayer believes § 1.469-4(g) applies to the disposition of a specific activity within an existing grouping, the statement reporting the disposition must contain a declaration that the disposition satisfies the requirements of § 1.469-4(g).

D. Statement Required for Regroupings

The proposal provides that, under § 1.469-4(e)(2), if it is determined that the taxpayer's original grouping was clearly inappropriate or a material change in the facts and circumstances has occurred that makes the original grouping clearly inappropriate, the taxpayer must regroup the activities. If such a determination and regrouping is made, the taxpayer shall file a written statement with the taxpayer's original return for the taxable year in which the trade or business activities or rental activities are regrouped. This statement must identify the names, addresses, and employer identification numbers, if applicable, for the trade or business or rental activities that are being regrouped. If two or more activities are regrouped into a single activity, the statement reporting a regrouping must also contain a declaration that the regrouped activities constitute an appropriate economic unit for the measurement of gain or loss for purposes of § 469. Furthermore, the statement reporting a regrouping must contain an explanation of why the taxpayer's original grouping was determined to be clearly inappropriate or the nature of the material change in the facts and circumstances that makes the original grouping clearly inappropriate.

E. Reporting of Pre-Existing Groupings Required only upon Change

The proposal clarifies that no written statement is required to be filed reporting the grouping of the trade or business activities and rental activities that have been made as of the effective date of any published final guidance until the taxpayer makes a change to the grouping as described in paragraphs A, B, C, or D of this notice.

F. Effect of Failure to Report

Under the proposal, except as provided in § 1.469-4(d)(5), if a taxpayer is engaged in two or more trade or business activities or rental activities and fails to report whether the activities have been grouped as a single activity or as separate activities in accordance with this proposal, then each trade or business activity or rental activity will be treated as having been grouped as a separate activity for purposes of applying the passive activity loss and credit limitation rules of § 469.

EFFECTIVE DATE

The proposal would be effective on the date that final guidance is published by the Internal Revenue Service.

REQUEST FOR COMMENTS

The proposal contained in this notice is one way, but not the only way, to implement a reporting system for taxpayer groupings under section 469. The IRS requests public comments on this proposal and, specifically, whether it sufficiently balances the need for reporting with the burden of compliance.

Comments regarding other possible approaches are also requested. All comments will be available for public inspection and copying. Therefore, submissions received by the IRS should not include taxpayer-specific information of a confidential nature. Submissions should include the name and telephone number of a person to contact. Comments must be submitted by November 4, 2008. Comments should be addressed to:

Internal Revenue Service
Office of the Associate Chief Counsel
(Passthroughs and Special Industries),
CC:PSI
Attn: Jonathan Cornwell, Room 5004
1111 Constitution Avenue, NW
Washington, DC 20224

In addition, comments may be submitted electronically via the Internet by sending them in an email to notice.comments@irscounsel.treas.gov and specifying that the comments concern Notice 2008-64.

DRAFTING INFORMATION

The principal author of this notice is Jonathan E. Cornwell of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this notice, contact Mr. Cornwell at (202) 622-3050 (not a toll-free call).