



# Tax Reduction Letter

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## Office of Chief Counsel Internal Revenue Service Memorandum

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date: December 17, 2014

to: Kelly H. Myers  
(Small Business/Self-Employed)

from: Associate Chief Counsel  
(Passthroughs & Special Industries)

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subject: Meaning of "brokerage" within §469(c)(7)(C)

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

### **ISSUES**

1. Whether a real estate agent is engaged in a real property brokerage trade or business within the meaning of § 469(c)(7)(C)?
2. Whether a mortgage broker is engaged in a real property brokerage trade or business within the meaning of § 469(c)(7)(C)?

### **CONCLUSIONS**

1. A real estate agent who brings together buyers and sellers of real property may be engaged in a real property brokerage trade or business under § 469(c)(7)(C).
2. A mortgage broker who is a broker of financial instruments is not in a real property brokerage trade or business within the meaning of § 469(c)(7)(C).

### **FACTS**

X is a state licensed real estate agent and works full-time as an independent contractor for a real estate brokerage firm. Under state law, X is not licensed as a real estate

broker. X brings together buyers and sellers of real property and negotiates contracts of sale and other agreements between buyers and sellers of real property.

Y is a state licensed mortgage broker. As a mortgage broker, Y markets mortgage loans and brings together lenders and borrowers. Under state law, Y's mortgage brokerage business is considered to be a real property brokerage business.

## **LAW AND ANALYSIS**

Section 469(c)(7)(C) defines the term "real property trade or business" as "any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental operation, management, leasing, or brokerage trade or business." These terms are not defined in § 469 or the regulations. Absent further guidance, legislative history and principles of statutory construction apply to determine the meaning of "real property brokerage" for purposes of § 469.

It has long been held that Federal law governs the construction of terms for Federal tax purposes. See Julius M. Israel Lodge of B'nai B'rith No. 2113 v. Comm'r, 98 F.3d 190 (5th Cir. 1996) (citing United States v. Irvine, 511 U.S. 242 (1994)); Hoover v. C.I.R., 102 F.3d 842, 845 (6th Cir. 1996) (stating "federal law governs the federal income tax treatment of [§ 71] property."). Thus, state law definitions of the terms "real estate agent" and "mortgage broker" are not determinative of whether a taxpayer is engaged in a real property brokerage trade or business within the meaning of § 469(c)(7)(C).

Although Congress initially included "finance operations" in the list of qualifying real property trade or business activities in an earlier, unenacted version of what would become § 469(c)(7)(C), (H.R. 3732, 101st Cong. (2d Sess. 1989), S. 2384, 101st Cong. (1989-90)), "finance operations" was removed from the final bill. H.R. 2264, 103d Cong. (1993) (enacted). It is therefore reasonable to infer that Congress did not intend for financing activities to constitute a real property trade or business and that financing activities should not be included in the definition of "real property brokerage."

Moreover, principles of statutory construction indicate that a mortgage broker is not engaged in real property brokerage. "Statutory words are uniformly presumed, unless the contrary appears, to be used in their ordinary and usual sense, and with the meaning commonly attributed to them." Caminetti v. United States, 242 U.S. 470, 485-86 (1917); Smith v. United States, 508 U.S. 223, 228-29 (1993). Courts often resort to standard reference dictionaries to determine the ordinary or common meaning of a word. See, e.g. Smith, 508 U.S. at 228; Crane v. Comm'r, 331 U.S. 1, 6 (1947).

Webster's Dictionary defines "real estate" as "property consisting of buildings and land; the business of selling land and buildings," and defines "brokerage" as "the business of

a broker” or the “broker’s fee or commission.”<sup>1</sup> Webster’s defines a “broker” as “a person who helps other people... to buy and sell property.”<sup>2</sup> Accordingly, the common and ordinary construction of “real property brokerage” for purposes of § 469(c)(7)(C) involves bringing together buyers and sellers of real property. This definition of “real property brokerage” does not include the brokerage of financial instruments.

Therefore the “financing” of real property such as by bringing together lenders and borrowers is not a real property brokerage trade or business within the meaning of §469(c)(7)(C). Thus, consistent with the legislative history of § 469(c)(7)(C), and under the common and ordinary construction of “real property brokerage,” X is engaged in a real property trade or business within the meaning of § 469(c)(7)(C), and Y is not.

### **CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS**

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call (202) 317-6850 if you have any further questions.

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Curt Wilson  
Associate Chief Counsel  
(Passthroughs and Special Industries)

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<sup>1</sup> *Merriam-Webster Online Dictionary*, “Real Estate” (Apr. 30, 2014), <http://www.merriam-webster.com/dictionary/real%20estate>; *Merriam-Webster Online Dictionary*, “Brokerage” (Apr. 30, 2014), <http://www.merriam-webster.com/dictionary/brokerage>.

<sup>2</sup> *Merriam-Webster Online Dictionary*, “Broker” (Apr. 30, 2014), <http://www.merriam-webster.com/dictionary/broker>.