

tradeable on an established securities market.

(i) *Treatment of recourse liabilities in tiered partnerships.* If a partnership (the "upper-tier partnership") owns (directly or indirectly through one or more partnerships) an interest in another partnership (the "lower-tier partnership"), the liabilities of the lower-tier partnership are allocated to the upper-tier partnership in an amount equal to the sum of the following—

(1) The amount of the economic risk of loss that the upper-tier partnership bears with respect to the liabilities; and

(2) Any other amount of the liabilities with respect to which partners of the upper-tier partnership bear the economic risk of loss.

(j) *Anti-abuse rules*—(1) *In general.* An obligation of a partner or related person to make a payment may be disregarded or treated as an obligation of another person for purposes of this section if facts and circumstances indicate that a principal purpose of the arrangement between the parties is to eliminate the partner's economic risk of loss with respect to that obligation or create the appearance of the partner or related person bearing the economic risk of loss when, in fact, the substance of the arrangement is otherwise. Circumstances with respect to which a payment obligation may be disregarded include, but are not limited to, the situations described in paragraphs (j)(2) and (j)(3) of this section.

(2) *Arrangements tantamount to a guarantee.* Irrespective of the form of a contractual obligation, a partner is considered to bear the economic risk of loss with respect to a partnership liability, or a portion thereof, to the extent that:

(i) The partner or related person undertakes one or more contractual obligations so that the partnership may obtain a loan;

(ii) The contractual obligations of the partner or related person eliminate substantially all the risk to the lender that the partnership will not satisfy its obligations under the loan; and

(iii) One of the principal purposes of using the contractual obligations is to attempt to permit partners (other than those who are directly or indirectly liable for the obligation) to include a por-

tion of the loan in the basis of their partnership interests.

The partners are considered to bear the economic risk of loss for the liability in accordance with their relative economic burdens for the liability pursuant to the contractual obligations. For example, a lease between a partner and a partnership which is not on commercially reasonable terms may be tantamount to a guarantee by the partner of a partnership liability.

(3) *Plan to circumvent or avoid the obligation.* An obligation of a partner to make a payment is not recognized if the facts and circumstances evidence a plan to circumvent or avoid the obligation.

(4) *Example.* The following example illustrates the principle of paragraph (j)(3) of this section.

Example. Plan to circumvent or avoid obligation. A and B form a general partnership. A, a corporation, contributes \$20,000 and B contributes \$80,000 to the partnership. A is obligated to restore any deficit in its partnership capital account. The partnership agreement allocates losses 20% to A and 80% to B until B's capital account is reduced to zero, after which all losses are allocated to A. The partnership purchases depreciable property for \$250,000 using its \$100,000 cash and a \$150,000 recourse loan from a bank. B guarantees payment of the \$150,000 loan to the extent the loan remains unpaid after the bank has exhausted its remedies against the partnership. A is a subsidiary, formed by a parent of a consolidated group, with capital limited to \$20,000 to allow the consolidated group to enjoy the tax losses generated by the property while at the same time limiting its monetary exposure for such losses. These facts, when considered together with B's guarantee, indicate a plan to circumvent or avoid A's obligation to contribute to the partnership. The rules of section 752 must be applied as if A's obligation to contribute did not exist. Accordingly, the \$150,000 liability is a recourse liability that is allocated entirely to B.

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§ 1.752-3 Partner's share of non-recourse liabilities.

(a) *In general.* A partner's share of the nonrecourse liabilities of a partnership equals the sum of paragraphs (a)(1) through (a)(3) of this section as follows—

(1) The partner's share of partnership minimum gain determined in accordance with the rules of section 704(b) and the regulations thereunder;

(2) The amount of any taxable gain that would be allocated to the partner under section 704(c) (or in the same manner as section 704(c) in connection with a revaluation of partnership property) if the partnership disposed of (in a taxable transaction) all partnership property subject to one or more nonrecourse liabilities of the partnership in full satisfaction of the liabilities and for no other consideration; and

(3) The partner's share of the excess nonrecourse liabilities (those not allocated under paragraphs (a)(1) and (a)(2) of this section) of the partnership as determined in accordance with the partner's share of partnership profits. The partner's interest in partnership profits is determined by taking into account all facts and circumstances relating to the economic arrangement of the partners. The partnership agreement may specify the partners' interests in partnership profits for purposes of allocating excess nonrecourse liabilities provided the interests so specified are reasonably consistent with allocations (that have substantial economic effect under the section 704(b) regulations) of some other significant item of partnership income or gain. Alternatively, excess nonrecourse liabilities may be allocated among the partners in accordance with the manner in which it is reasonably expected that the deductions attributable to those nonrecourse liabilities will be allocated. Additionally, the partnership may first allocate an excess nonrecourse liability to a partner up to the amount of built-in gain that is allocable to the partner on section 704(c) property (as defined under §1.704-3(a)(3)(ii)) or property for which reverse section 704(c) allocations are applicable (as described in §1.704-3(a)(6)(i)) where such property is subject to the nonrecourse liability to the extent that such built-in gain exceeds the gain described in paragraph (a)(2) of this section with respect to such property. This additional method does not apply for purposes of §1.707-5(a)(2)(ii). To the extent that a partnership uses this additional method and the entire amount

of the excess nonrecourse liability is not allocated to the contributing partner, the partnership must allocate the remaining amount of the excess nonrecourse liability under one of the other methods in this paragraph (a)(3). Excess nonrecourse liabilities are not required to be allocated under the same method each year.

(b) *Allocation of a single nonrecourse liability among multiple properties*—(1) *In general.* For purposes of determining the amount of taxable gain under paragraph (a)(2) of this section, if a partnership holds multiple properties subject to a single nonrecourse liability, the partnership may allocate the liability among the multiple properties under any reasonable method. A method is not reasonable if it allocates to any item of property an amount of the liability that, when combined with any other liabilities allocated to the property, is in excess of the fair market value of the property at the time the liability is incurred. The portion of the nonrecourse liability allocated to each item of partnership property is then treated as a separate loan under paragraph (a)(2) of this section. In general, a partnership may not change the method of allocating a single nonrecourse liability under this paragraph (b) while any portion of the liability is outstanding. However, if one or more of the multiple properties subject to the liability is no longer subject to the liability, the portion of the liability allocated to that property must be reallocated among the properties still subject to the liability so that the amount of the liability allocated to any property does not exceed the fair market value of such property at the time of reallocation.

(2) *Reductions in principal.* For purposes of this paragraph (b), when the outstanding principal of a partnership liability is reduced, the reduction of outstanding principal is allocated among the multiple properties in the same proportion that the partnership liability originally was allocated to the properties under paragraph (b)(1) of this section.

(c) *Examples.* The following examples illustrate the principles of this section:

Example 1. Partner's share of nonrecourse liabilities. The AB partnership purchases depreciable property for a \$1,000 purchase money note that is nonrecourse liability under the rules of this section. Assume that this is the only nonrecourse liability of the partnership, and that no principal payments are due on the purchase money note for a year. The partnership agreement provides that all items of income, gain, loss, and deduction are allocated equally. Immediately after purchasing the depreciable property, the partners share the nonrecourse liability equally because they have equal interests in partnership profits. A and B are each treated as if they contributed \$500 to the partnership to reflect each partner's increase in his or her share of partnership liabilities (from \$0 to \$500). The minimum gain with respect to an item of partnership property subject to a nonrecourse liability equals the amount of gain that would be recognized if the partnership disposed of the property in full satisfaction of the nonrecourse liability and for no other consideration. Therefore, if the partnership claims a depreciation deduction of \$200 for the depreciable property for the year it acquires that property, partnership minimum gain for the year will increase by \$200 (the excess of the \$1,000 nonrecourse liability over the \$800 adjusted tax basis of the property). See section 704(b) and the regulations thereunder. A and B each have a \$100 share of partnership minimum gain at the end of that year because the depreciation deduction is treated as a nonrecourse deduction. See section 704(b) and the regulation thereunder. Accordingly, at the end of that year, A and B are allocated \$100 each of the nonrecourse liability to match their shares of partnership minimum gain. The remaining \$800 of the nonrecourse liability will be allocated equally between A and B (\$400 each).

Example 2. Excess nonrecourse liabilities allocated consistently with reasonably expected deductions. The facts are the same as in *Example 1* except that the partnership agreement provides that depreciation deductions will be allocated to A. The partners agree to allocate excess nonrecourse liabilities in accordance with the manner in which it is reasonably expected that the deductions attributable to those nonrecourse liabilities will be allocated. Assuming that the allocation of all of the depreciation deductions to A is valid under section 704(b), immediately after purchasing the depreciable property, A's share of the nonrecourse liability is \$1,000. Accordingly, A is treated as if A contributed \$1,000 to the partnership.

Example 3. Allocation of liability among multiple properties. (i) A and B are equal partners in a partnership (PRS). A contributes \$70 of cash in exchange for a 50-percent interest in PRS. B contributes two items of property, X and Y, in exchange for a 50-percent interest in PRS. Property X has a fair market value (and book value) of \$70 and an adjusted basis

of \$40, and is subject to a nonrecourse liability of \$50. Property Y has a fair market value (and book value) of \$120, an adjusted basis of \$40, and is subject to a nonrecourse liability of \$70. Immediately after the initial contributions, PRS refinances the two separate liabilities with a single \$120 nonrecourse liability. All of the built-in gain attributable to Property X (\$30) and Property Y (\$80) is section 704(c) gain allocable to B.

(ii) The amount of the nonrecourse liability (\$120) is less than the total book value of all of the properties that are subject to such liability (\$70 + \$120 = \$190), so there is no partnership minimum gain. § 1.704-2(d). Accordingly, no portion of the liability is allocated pursuant to paragraph (a)(1) of this section.

(iii) Pursuant to paragraph (b)(1) of this section, PRS decides to allocate the nonrecourse liability evenly between the Properties X and Y. Accordingly, each of Properties X and Y are treated as being subject to a separate \$60 nonrecourse liability for purposes of applying paragraph (a)(2) of this section. Under paragraph (a)(2) of this section, B will be allocated \$20 of the liability for each of Properties X and Y (in each case, \$60 liability minus \$40 adjusted basis). As a result, a portion of the liability is allocated pursuant to paragraph (a)(2) of this section as follows:

Partner	Property	Tier 1	Tier 2
A	X	\$0	\$0
	Y	0	0
B	X	0	20
	Y	0	20

(iv) PRS has \$80 of excess nonrecourse liability that it may allocate in any manner consistent with paragraph (a)(3) of this section. PRS determines to allocate the \$80 of excess nonrecourse liabilities to the partners up to their share of the remaining section 704(c) gain on the properties, with any remaining amount of liabilities being allocated equally to A and B consistent with their equal interests in partnership profits. B has \$70 of remaining section 704(c) gain (\$10 on Property X and \$60 on Property Y), and thus will be allocated \$70 of the liability in accordance with this gain.

The remaining \$10 is divided equally between A and B. Accordingly, the overall allocation of the \$120 nonrecourse liability is as follows:

Partner	Tier 1	Tier 2	Tier 3	Total
A	\$0	\$0	\$5	\$5
B	0	40	75	115

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