

considered § 1.752-7 liabilities under the proposed regulations) to the master partnership. Because a contribution by a mutual fund to a master partnership is not the type of abusive loss duplication transaction that section 309(c) of the Act was designed to address, the proposed regulations treat this type of contribution as a contribution of a trade or business. Treasury and the IRS request comments on additional types of activities that should be treated as trades or businesses for purposes of these regulations.

The proposed regulations do not include the section 358(h) exception for situations in which substantially all of the assets with which the liability is associated are transferred to the partnership assuming the liability. Treasury and the IRS are concerned that taxpayers would rely on that exception to facilitate transactions of the type that section 309(c) of the Act was designed to prevent.

An additional *de minimis* exception, not present in section 358(h), is included in the proposed regulations. Under this exception, the proposed regulations do not apply where, immediately before the disposition of the partnership interest by the § 1.752-7 liability partner, the liquidation of the § 1.752-7 liability partner's partnership interest, or the assumption of the § 1.752-7 liability by another partner, the amount of the remaining built-in loss with respect to all § 1.752-7 liabilities assumed by the partnership (other than § 1.752-7 liabilities that are assumed by the partnership with an associated trade or business) is less than the lesser of 10% of the gross value of the partnership's assets or \$1,000,000. This exception was added in recognition of the fact that loss acceleration and duplication strategies typically are engaged in only if the accelerated or duplicated loss is substantial.

4. Advanced Notice of Proposed Rulemaking Under Section 358(h)(2)

Treasury and the IRS are considering exercising their regulatory authority under section 358(h)(2) to limit the exceptions to section 358(h)(1) to follow the exceptions set forth in these proposed regulations (other than the *de minimis* exception). Treasury and the IRS request comments on the scope and substance of such regulations, which will be retroactive to the extent necessary to prevent abuse.

5. Rules Applicable to Tiered Structures

Proposed § 1.752-7(e) and (i) provide rules to address a contribution of a partnership interest to another

partnership. First, under § 1.752-7(e)(3), a transfer by a partner of an interest in a partnership (lower-tier partnership) to another partnership (upper-tier partnership) is not treated as a transfer of a partnership interest for purposes of applying these rules. Therefore, the partner does not have to reduce the basis of the partnership interest before such a transfer. However, look-through rules in § 1.752-7(i) apply to treat the transfer of the partnership interest as a transfer of the partner's share of the assets and § 1.752-7 liabilities of the partnership. Therefore, a transfer of a partnership interest to another partnership may be treated as an assumption of a § 1.752-7 liability by a partnership under these proposed regulations. Under proposed § 1.358-7(a), similar rules apply to a contribution of a partnership interest to a corporation.

Also, § 1.752-7(i)(2) provides a limitation on the trade or business exception where a partnership (upper-tier partnership) assumes a § 1.752-7 liability from a partner, and then another partnership (lower-tier partnership) assumes the § 1.752-7 liability from the upper-tier partnership. In such a case, the trade or business exception does not apply on the assumption of the § 1.752-7 liability by the lower-tier partnership from the upper-tier partnership unless it applied on the assumption of the § 1.752-7 liability by the upper-tier partnership from the § 1.752-7 liability partner. Section 1.358-7(c) of these proposed regulations provide for similar rules where a corporation assumes an obligation described in section 358(h)(3) from a partnership that the partnership had previously assumed from a partner. In addition, § 1.358-7(b) of these proposed regulations provide special rules for adjusting the partners' bases in a partnership when a corporation assumes a § 1.752-7 liability from the partnership.

Additional rules are provided for look-through treatment where a partnership is a § 1.752-7 liability partner in another partnership. The proposed regulations also provide special rules for situations in which the § 1.752-7 liability partner disposes of the partner's interest in the partnership and then another partnership (or a corporation) assumes the § 1.752-7 liability from the partnership.

Effective Date

The regulations described above are proposed to apply to assumptions of § 1.752-7 liabilities occurring on or after June 24, 2003. In the Rules and Regulations section of this issue of the

Federal Register, the IRS is issuing temporary regulations (§ 1.752-6T) that apply to liabilities assumed by a partnership after October 18, 1999, and before June 24, 2003. The text of those temporary regulations published in the Rules and Regulation section of this issue of the **Federal Register** serves as the text of § 1.752-6 of these regulations. In lieu of applying § 1.752-6T of the temporary Income Tax Regulations, partnerships may elect to be subject to the proposed rules of § 1.358-7 and 1.752-7 and the proposed revisions of § 1.704-1(b)(2)(iv)(b), 1.704-2(b)(3), 1.705-1(a)(7), and 1.752-1, published as part of this Notice of Proposed Rulemaking, with respect to all liabilities (including § 1.752-7 liabilities) assumed by the partnership after October 18, 1999 and before June 24, 2003. The election must be filed with the first Federal income tax return filed by the partnership on or after September 22, 2003. The election will be valid only if the partnership and its partners promptly amend any returns for open taxable years that would be affected by the election.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that few partnerships engage in the type of transactions that are subject to these regulations (assumptions of liabilities not described in section 752(a) and (b) from a partner). In addition, available data indicates that most partnerships that engage in the type of transactions that are subject to these regulations are large partnerships. Certain broad exceptions to the application of these regulations (including a *de minimis* exception) further limit the economic impact of these regulations on small entities. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business. Comments are sought as to the number of legitimate business transactions that will be affected by the proposed regulations.