

liability partner, the partnership must reduce the basis of partnership assets by the remaining built-in loss associated with the § 1.752-7 liability. The reduction in the basis of partnership assets must be allocated among partnership assets as if that adjustment were a basis adjustment under section 734(b).

(4) *Consequences to assuming partner.* No deduction or capital expense is allowed to an assuming partner (other than the § 1.752-7 liability partner) on the economic performance of a § 1.752-7 liability assumed from a partnership to the extent of the remaining built-in loss associated with the § 1.752-7 liability. Instead, on economic performance of the § 1.752-7 liability, the assuming partner must adjust the basis of the partnership interest, any assets (other than cash, accounts receivable, or inventory) distributed by the partnership to the partner, or gain or loss on the disposition of the partnership interest, as the case may be. These adjustments are determined as if the assuming partner's basis in the partnership interest at the time of the assumption were increased by the lesser of the amount paid to satisfy the § 1.752-7 liability or the remaining built-in loss associated with the § 1.752-7 liability. However, the assuming partner cannot take into account any adjustments to depreciable basis, reduction in gain, or increase in loss until economic performance of the § 1.752-7 liability. Any adjustment to the basis of an asset under this provision is taken into account over the recovery period of that asset.

(5) *Example.* The following example illustrates the provisions of this paragraph (g):

Example —(i) Facts. In 2004, A, B, and C form partnership PRS. A contributes Property 1, a nondepreciable capital asset with a fair market value and basis of \$5,000,000, in exchange for a 25% interest in PRS and assumption by PRS of a § 1.752-7 liability of \$2,000,000. B contributes \$3,000,000 cash for a 25% interest in PRS, and C contributes \$6,000,000 cash for a 50% interest in PRS. PRS uses the cash contributed to purchase Property 2. In 2007, PRS distributes Property 1, subject to the § 1.752-7 liability to B in liquidation of B's interest in PRS. At the time of the distribution, A's interest in PRS has a value of \$3,000,000 and a basis of \$5,000,000, and B's interest in PRS has a value and basis of \$3,000,000. Also at that time, Property 1 has a value and basis of \$5,000,000, Property 2 has a value and basis of \$9,000,000, and the remaining built-in loss associated with the § 1.752-7 liability is \$2,000,000. Assume that none of the exceptions of paragraph (d)(2)(i) of this section apply to the assumption of the § 1.752-7 liability by B and that economic performance of the § 1.752-7 liability would

have given rise to a deductible expense to A. In 2010, B pays \$1,000,000 to satisfy the entire § 1.752-7 liability. At that time, B still owns Property 1, which has a basis of \$3,000,000.

(ii) *Assumption of § 1.752-7 liability by B.* Section 704(c)(1)(B) does not apply to the assumption of the § 1.752-7 liability by B. Instead, A's basis in the PRS interest is reduced (to \$3,000,000) by the § 1.752-7 liability reduction, i.e., the lesser of the excess of A's basis in the PRS interest over the adjusted value of that interest (\$2,000,000), or the remaining built-in loss associated with the § 1.752-7 liability as of the time of the assumption (\$2,000,000). PRS's basis in Property 2 is reduced (to \$7,000,000) by the \$2,000,000 remaining built-in loss associated with the § 1.752-7 liability. B's basis in Property 1 under section 732(b) is \$3,000,000 (B's basis in the PRS interest). This is \$2,000,000 less than PRS's basis in Property 1 before the distribution of Property 1 to B. If PRS has a section 754 election in effect for 2007, PRS may increase the basis of Property 2 under section 734(b) by \$2,000,000.

(iii) *Satisfaction of § 1.752-7 liability.* B is not entitled to a deduction for the economic performance of the § 1.752-7 liability in 2010 to the extent of the remaining built-in loss associated with the § 1.752-7 liability as of the time of the assumption (\$2,000,000). As this amount exceeds the amount paid by B to satisfy the § 1.752-7 liability, B is not entitled to any deduction for the § 1.752-7 liability in 2010. B may, however, increase the basis of Property 1 by the lesser of the remaining built-in loss associated with the § 1.752-7 liability (\$2,000,000) or the amount paid to satisfy the § 1.752-7 liability (\$1,000,000). Therefore, B's basis in Property 1 is increased to \$4,000,000. If B notifies A of the economic performance of the § 1.752-7 liability, then A is entitled to an ordinary deduction in 2010 of \$1,000,000 (the amount paid in satisfaction of the § 1.752-7 liability) and a capital loss of \$1,000,000 (the remaining § 1.752-7 liability reduction).

(h) *Notification by the partnership (or successor) of the economic performance of the § 1.752-7 liability.* For purposes of paragraphs (e), (f), and (g) of this section, notification by the partnership (or successor) of the economic performance of the § 1.752-7 liability must be attached to the § 1.752-7 liability partner's return for the year in which the loss is being claimed and must include—

(1) The amount paid in satisfaction of the § 1.752-7 liability, and whether the amounts paid were in partial or complete satisfaction of the § 1.752-7 liability;

(2) The name and address of the person satisfying the § 1.752-7 liability;

(3) The date of the payment on the § 1.752-7 liability; and

(4) The character of the loss with respect to the § 1.752-7 liability.

(i) *Tiered partnerships—(1) Look-through treatment.* For purposes of this

section, a contribution by a partner of an interest in a partnership (lower-tier partnership) to another partnership (upper-tier partnership) is treated as a contribution of the partner's share of each of the lower-tier partnership's assets and an assumption by the upper-tier partnership of the partner's share of the lower-tier partnership's liabilities (including § 1.752-7 liabilities). See paragraph (e)(3)(ii), *Example 1* of this section. In addition, a partnership is treated as having its share of any § 1.752-7 liabilities of the partnerships in which it has an interest.

(2) *Trade or business exception.* If a partnership (upper-tier partnership) assumes a § 1.752-7 liability of a partner, and, subsequently, another partnership (lower-tier partnership) assumes that § 1.752-7 liability from the upper-tier partnership, then the § 1.752-7 liability is treated as associated only with any trade or business contributed to the upper-tier partnership by the § 1.752-7 liability partner. The same rule applies where a partnership assumes a § 1.752-7 liability of a partner, and, subsequently, the § 1.752-7 liability partner transfers that partnership interest to another partnership. See paragraph (e)(3)(ii), *Example 1* of this section.

(3) *Partnership as a § 1.752-7 liability partner.* If a transaction described in paragraph (e), (f), or (g) of this section occurs with respect to a partnership (upper-tier partnership) that is a § 1.752-7 liability partner of another partnership (lower-tier partnership), then such transaction will also be treated as a transaction described in paragraph (e), (f), or (g) of this section, as appropriate, with respect to the partners of the upper-tier partnership, regardless of whether the upper-tier partnership assumed the § 1.752-7 liability from those partners. (See paragraph (b)(3) of this section for rules relating to the treatment of transactions by the partners of the upper-tier partnership.) In such a case, the § 1.752-7 liability reduction with respect to each partner in the upper-tier partnership is equal to that partner's share of the § 1.752-7 liability. The partners of the upper-tier partnership at the time of the transaction described in paragraph (e), (f), or (g) of this section, and not the upper-tier partnership, are entitled to the loss or deduction on the economic performance of the § 1.752-7 liability. Similar principles apply where the upper-tier partnership is itself owned by one or a series of partnerships. This paragraph does not apply to the extent that § 1.752-7(i)(4) applies to the assumption of the § 1.752-7 liability by the lower-tier partnership.