**8769. What liabilities are included in determining a partner’s adjusted basis in a partnership interest?**

A partner’s basis includes the partner’s share of partnership liabilities.[[1]](#footnote-1) An economic risk of loss analysis is used to determine which liabilities are included in a partner’s adjusted basis.

A partnership liability is treated as a recourse liability to the extent that any partner bears the economic risk of loss for that liability.[[2]](#footnote-2) A partner bears the economic risk of loss for a partnership liability to the extent that the partner (or certain related parties) would be obligated to make a payment to any person or make a contribution to the partnership with respect to a partnership liability (and would not be entitled to reimbursement by another partner, certain parties related to another partner, or the partnership) if the partnership were to undergo a “constructive liquidation.”

A “constructive liquidation” would treat:

(1) all of the partnership’s liabilities as due and payable in full;

(2) all of the partnership assets (including money), except those contributed to secure a partnership liability, as worthless;

(3) all of the partnership assets as disposed of in a fully taxable transaction for no consideration (other than relief from certain liabilities);

(4) all items of partnership income, gain, loss, and deduction for the year as allocated among the partners; and

(5) the partner’s interests in the enterprise as liquidated.[[3]](#footnote-3)

If one or more partners (or related persons) guarantee the payment of more than 25 percent of the interest that will accrue on a partnership nonrecourse liability over its remaining term, the loan will be deemed to be recourse with respect to the guarantor to the extent of the present value of the future interest payments if it is reasonable to expect that the guarantor will be required to pay substantially all of the guaranteed interest if the partnership fails to do so.[[4]](#footnote-4)

An obligation will be considered recourse with respect to a partner to the extent of the value of any property that the partner (or related party in the case of a direct pledge) directly or indirectly pledges as security for the partnership liability.[[5]](#footnote-5) Further, if a partner (or related party) makes a nonrecourse loan, or obtains an interest in such a loan to the partnership and the economic risk of loss is not borne by another partner, the obligation will be considered recourse as to that partner.[[6]](#footnote-6)

A recourse liability allocated to a partner under these rules is included in the partner’s basis.

However, a limited partner generally does not bear the economic risk of loss for any partnership recourse liability because limited partners are not typically obligated to make additional contributions and do not typically guarantee interest, pledge property, or make loans to the partnership. Otherwise, a limited partner can include a share of a partnership liability in his basis only if it is nonrecourse liability (see below).

A partnership liability is treated as a *nonrecourse* liability if no partner bears the economic risk of loss (see above) for that liability. Generally, partners share nonrecourse liability in the same proportion as they share profits. However, nonrecourse liabilities are first allocated among partners to reflect each partner’s share of (1) any partnership minimum gain or (2) IRC Section 704(c) minimum gain.

Partnership minimum gain is the amount of gain that would be realized if the partnership were to sell all of its property that is subject to nonrecourse liabilities in full satisfaction of such liabilities and for no other consideration. IRC Section 704(c) minimum gain is the amount of gain that would be allocated under IRC Section 704(c) to a partner who contributed property to the partnership if the partnership were to sell all of its property that is subject to nonrecourse liabilities in full satisfaction of such liabilities and for no other consideration.[[7]](#footnote-7)

These rules apply to any liability incurred on or after December 28, 1991, except for those incurred or assumed pursuant to a written binding contract that was effective before that date and at all times thereafter. A partnership may elect to apply the provisions of the regulations to liabilities incurred or assumed prior to December 28, 1991, as of the beginning of the first taxable year ending on or after that date.[[8]](#footnote-8)

Similar rules apply to liabilities incurred or assumed by a partnership after January 29, 1989, and before December 28, 1991, unless the liability was incurred or assumed pursuant to a written binding contract that was effective prior to December 29, 1988 and at all times thereafter.[[9]](#footnote-9) They also apply to partner loans and to guarantees of partnership liabilities that were incurred or assumed by a partnership after February 29, 1984, and before December 28, 1991, beginning on the later of March 1, 1984, or the first date on which the partner bore the economic risk of loss with respect to a liability because of his status as a creditor or guarantor of such liability.[[10]](#footnote-10) A partnership could elect to extend application of the temporary regulations to all of its liabilities as of the beginning of its first taxable year ending after December 29, 1988, and before December 28, 1991, subject to certain consistency rules.[[11]](#footnote-11)

1. . IRC Secs. 752, 705(a). [↑](#footnote-ref-1)
2. . Treas. Reg. §1.752-1(a)(1). [↑](#footnote-ref-2)
3. . Treas. Reg. §1.752-2(b)(1). [↑](#footnote-ref-3)
4. . Treas. Reg. §1.752-2(e). [↑](#footnote-ref-4)
5. . Treas. Reg. §1.752-2(h). [↑](#footnote-ref-5)
6. . Treas. Reg. §1.752-2(c). [↑](#footnote-ref-6)
7. . Treas. Regs. §§1.752-3(a), 1.704-2(d). [↑](#footnote-ref-7)
8. . Treas. Reg. §1.752-5. [↑](#footnote-ref-8)
9. . Temp. Treas. Reg. §1.752-4T(a), prior to removal by TD 8380. [↑](#footnote-ref-9)
10. . Temp. Treas. Reg. §1.752-4T(b), prior to removal by TD 8380. [↑](#footnote-ref-10)
11. . Temp. Treas. Reg. §1.752-4T(c), prior to removal by TD 8380. [↑](#footnote-ref-11)