

Part III - Administrative, Procedural, and Miscellaneous

Forthcoming Guidance Regarding Certain Partnership Related-Party Transactions

Notice 2024-54

SECTION 1. PURPOSE

.01 This notice announces that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) intend to publish two sets of forthcoming proposed regulations that would address certain basis-shifting transactions involving partnerships and related parties. These transactions, referred to as “covered transactions” in this notice, (1) involve partners in a partnership and their related parties, (2) result in increases to the basis of property under § 732, § 734(b), or § 743(b) of the Internal Revenue Code (Code),¹ and (3) generate increased cost recovery allowances or reduced gain (or increased loss) upon the sale or other disposition of the basis-adjusted property.

First, the Treasury Department and the IRS intend to propose regulations under §§ 732, 734(b), 743(b) and 755 (forthcoming Proposed Related-Party Basis Adjustment

¹ Unless otherwise noted, all “section” or “§” references are to sections of the Code or the Income Tax Regulations (26 CFR part 1).

Regulations) that would (1) provide the required method of recovering adjustments to the bases of property held by a partnership, property distributed by a partnership, or both, arising from the covered transactions described in section 3 of this notice, (2) provide rules governing the determination of gain or loss on the disposition of such basis-adjusted property, and (3) include similar transactions involving tax-indifferent parties (for example, certain foreign persons, a tax-exempt organization, or a party with tax attributes that make it tax-indifferent) rather than related parties.

Second, the Treasury Department and the IRS intend to propose regulations under § 1502 (forthcoming Proposed Consolidated Return Regulations) to clearly reflect the taxable income and tax liability of a consolidated group (as defined in § 1.1502-1(h)) whose members own interests in a partnership. More specifically, the Treasury Department and the IRS anticipate that the forthcoming Proposed Consolidated Return Regulations would provide for single-entity treatment of members that are partners in a partnership, so that covered transactions cannot shift basis among group members and distort group income.

.02 Section 2 of this notice provides a summary of relevant law. Section 3 of this notice provides an overview of the need for the forthcoming proposed regulations² and a description of the covered transactions. Sections 4 and 5 of this notice describe the forthcoming Proposed Related-Party Basis Adjustment Regulations and the forthcoming Proposed Consolidated Return Regulations, respectively. Section 6 of this notice

² References in this notice to the “forthcoming proposed regulations” are references to the forthcoming Proposed Related-Party Basis Adjustment Regulations and the forthcoming Proposed Consolidated Return Regulations, collectively.

describes the proposed applicability dates of the forthcoming proposed regulations.

Section 7 of this notice contains a request for comments.

SECTION 2. BACKGROUND

.01 Basis adjustments under subchapter K

(1) In general. Under subchapter K of chapter 1 of the Code (subchapter K), a distribution by a partnership of the partnership's property (partnership property) or a transfer of an interest in a partnership (partnership interest) may result in an adjustment to the basis of the distributed property, partnership property, or both.

A distribution of partnership property may result in an adjustment to the basis of the distributed property under § 732(a), (b), or (d). In the case of a distribution of partnership property to a partner by a partnership with an election under § 754 (§ 754 election) in effect, or with respect to which there is a substantial basis reduction as described in § 734(d), the distribution may also result in an adjustment to the basis of the partnership's remaining partnership property under § 734(b).

If a partnership interest is transferred by sale or exchange or on the death of a partner, and the partnership either has a § 754 election in effect or has a substantial built-in loss with respect to the transfer of the partnership interest as described in § 743(d), the transfer may result in an adjustment to the basis of partnership property under § 743(b) with respect to the transferee partner.

Section 754 provides that if a partnership makes an election in accordance with regulations prescribed by the Secretary of the Treasury or her delegate (Secretary), the basis of partnership property shall be adjusted, in the case of a distribution of property,

in the manner provided in § 734, and in the case of a transfer of a partnership interest, in the manner provided in § 743. Unless the election is revoked in accordance with the regulations under § 754, the § 754 election applies with respect to all distributions of property by the partnership and to all transfers of interests in the partnership during the taxable year with respect to which the election was filed and all subsequent taxable years.

(2) Basis adjustments under § 732. Section 732 governs a distributee partner's basis in distributed property other than money. In the case of a current distribution, and except as provided under § 732(a)(2), § 732(a)(1) provides that the distributee partner's basis in distributed property (other than money) is equal to the partnership's adjusted basis in the distributed property immediately before the distribution. Under § 732(a)(2), however, a distributee partner's basis in distributed property is limited to the adjusted basis of the distributee partner's partnership interest reduced by any money distributed to such partner in the same transaction.

In the case of a liquidating distribution, § 732(b) provides that the distributee partner's basis in distributed property (other than money) is equal to the adjusted basis of the distributee partner's partnership interest reduced by any money distributed to such partner in the same transaction.

In the case of a distribution of more than one property from a partnership, the basis of the distributed properties to which § 732(a)(2) and (b) apply must be allocated among the distributed properties under the rules of § 732(c) and the regulations thereunder.

(3) Basis adjustments under § 734. In the case of a distribution of property by a partnership with a § 754 election in effect, and for which either the distributee partner recognizes gain or loss on the distribution, or for which the basis of the distributed property in the distributee partner's hands, as determined under § 732, differs from the partnership's adjusted basis in the distributed property immediately before the distribution, § 734(b) requires the partnership to increase or decrease (as applicable) the basis of its remaining partnership property. Also, in the case of a distribution of property by a partnership that results in a substantial basis reduction under § 734(d), the basis of remaining partnership property must be adjusted under § 734(b), even if the partnership does not have a § 754 election in effect.

Section 734(b)(1) requires a partnership to increase the basis of its remaining property if a distribution of property by the partnership results in the distributee partner recognizing gain under § 731(a)(1), or if property (other than money) to which § 732(a)(2) or (b) applies is distributed to the distributee partner and the property's adjusted basis to the partnership immediately before the distribution is greater than the distributee partner's basis in the distributed property as determined under § 732.

Section 731(a)(1) requires a distributee partner to recognize gain in a current or liquidating distribution to the extent that any money distributed to that partner in the distribution exceeds the adjusted basis of that partner's partnership interest immediately before the distribution. The amount of the basis increase to the partnership's remaining property under § 734(b)(1) following a distribution of partnership property to a partner is equal to the amount of gain recognized by the distributee partner in the distribution

under § 731(a)(1) and the excess of the partnership's adjusted basis in the distributed property immediately before the distribution over the distributee partner's basis in the distributed property as determined under § 732.

Section 734(b)(2) requires a partnership to decrease the basis of its remaining property if a distribution of property by the partnership results in the distributee partner recognizing loss under § 731(a)(2), or if property (other than money) to which § 732(b) applies is distributed to the distributee partner in a distribution and the property's adjusted basis to the partnership immediately before the distribution is less than the distributee partner's basis in the distributed property as determined under § 732. Under § 731(a)(2), a distributee partner may recognize a loss in a liquidating distribution of that partner's interest in the partnership to the extent that such partner received only money, unrealized receivables described in § 751(c), or inventory items described in § 751(d) in the distribution. In such a case, the distributee partner is required to recognize a loss to the extent that such partner's adjusted basis in the partnership interest exceeds the sum of any money distributed to that partner in the distribution and the basis to the distributee partner (determined under § 732) of any unrealized receivables or inventory received by that partner in the distribution. The amount of the basis decrease to the partnership's remaining property under § 734(b)(2) following a distribution of partnership property to a partner is equal to the amount of loss recognized by the distributee partner in the distribution under § 731(a)(2) and the excess of the distributee partner's basis in the distributed property as determined under § 732 over the partnership's adjusted basis in the distributed property immediately before the distribution.

A partnership without a § 754 election in effect is subject to a mandatory basis adjustment under § 734(b)(2) if there is a substantial basis reduction with respect to a distribution of partnership property. Under § 734(d), a substantial basis reduction with respect to a distribution of partnership property occurs if the sum of the amount of loss recognized to the distributee partner on the distribution, plus any increase in basis in the distributed property to the distributee partner under § 732(b), exceeds \$250,000.

(4) Basis adjustments under § 743(b). Generally, if a partnership interest is transferred in a sale or exchange or on the death of a partner, the transferee partner's basis in the transferred partnership interest is determined under § 742 and the basis of partnership property is determined under § 743(a). Section 742 provides that the transferee partner's basis in a partnership interest acquired other than by contribution is determined under part II of subchapter O of chapter 1 of the Code, beginning at § 1011 and following. Thus, for example, a transferee partner's basis in a partnership interest acquired by purchase generally is cost basis under § 1012.

Section 743(a) provides that, in the case of a transfer of a partnership interest by sale or exchange or on the death of a partner, the basis of partnership property is not adjusted unless either the partnership has a § 754 election in effect or the partnership has a substantial built-in loss with respect to the transfer of the partnership interest.

Under § 743(b), in the case of a transfer of a partnership interest by sale or exchange or on the death of a partner, a partnership with a § 754 election in effect or that has a substantial built-in loss with respect to the transfer of the partnership interest must increase or decrease (as applicable) the adjusted basis of partnership property

with respect to the transferee partner.

Section 743(b)(1) provides that the adjusted basis of partnership property is increased by the excess of the transferee partner's basis in the transferred partnership interest over the transferee partner's proportionate share of the adjusted basis of partnership property.

Section 743(b)(2) provides that the adjusted basis of partnership property is decreased by the excess of the transferee partner's proportionate share of the adjusted basis of partnership property over the transferee partner's basis in the transferred partnership interest.

A partnership without a § 754 election is subject to a mandatory basis adjustment under § 743(b) with respect to a transfer of a partnership interest if the partnership has a substantial built-in loss with respect to the transfer of the partnership interest. Under § 743(d)(1), a partnership has a substantial built-in loss with respect to a transfer of an interest in the partnership if either the partnership's adjusted basis in its property exceeds the fair market value of such property by more than \$250,000, or the transferee partner would be allocated a loss of more than \$250,000 if the partnership assets were sold for cash equal to their fair market value immediately after the transfer.

Under regulations prescribed by the Secretary, a basis adjustment under § 743(b) is an adjustment to the basis of partnership property with respect to the transferee partner only. The transferee partner's proportionate share of the partnership's adjusted basis in its property generally is determined in accordance with the transferee partner's interest in the partnership's previously taxed capital (including

the transferee partner's share of partnership liabilities) under regulations prescribed by the Secretary.

(5) Allocation of § 734(b) or § 743(b) basis adjustments. Section 734(c) states that a basis adjustment under § 734(b) is allocated among partnership properties under the rules of § 755. Section 743(c) states that a basis adjustment under § 743(b) is allocated among partnership properties under the rules of § 755.

Section 755(a) generally requires basis adjustments under § 734(b) or § 743(b) to be allocated in a manner that has the effect of reducing the difference between the fair market value and the adjusted basis of partnership properties or in any other manner permitted by regulations. In addition, § 755(b) requires these basis adjustments to be allocated to partnership property of a like character or to subsequently acquired partnership property of a like character if such property is not available or has insufficient basis at the time of the basis adjustment (because a decrease in the adjusted basis of the property would reduce the basis of such property below zero). Section 755(c) provides a special rule that prohibits allocating a basis decrease under § 734(b) to the stock of a corporation that is a partner of the partnership (or that is related to a partner of the partnership within the meaning of § 267(b) or § 707(b)(1)).

(6) Common terminology for bases with respect to a partnership interest. A partner's adjusted basis in its partnership interest commonly is referred to as the partner's "outside basis" in its partnership interest. A partnership's adjusted basis in its property commonly is referred to as the "inside basis" of the partnership's property. Each partner has a share of inside basis. For ease of explanation, this terminology is

used in section 3 of this notice.

.02 Affiliated group of corporations filing a consolidated return. Section 1501 grants an affiliated group of corporations the privilege of making a consolidated return, in lieu of separate returns, for Federal income tax purposes. Section 1502 authorizes the Secretary to prescribe consolidated return regulations for an affiliated group of corporations that join in filing (or that are required to join in filing) a consolidated return (that is, a consolidated group as defined in § 1.1502-1(h)) to clearly reflect the Federal income tax liability of the consolidated group and to prevent avoidance of such tax liability (§ 1502 regulations). For purposes of carrying out those objectives, § 1502 also permits the Secretary to prescribe rules that may be different from the provisions of chapter 1 of the Code that would apply if the corporations composing the consolidated group filed separate returns. Terms used in the § 1502 regulations generally are defined in § 1.1502-1.

The § 1502 regulations provide rules to clearly reflect the Federal income tax liability of both the consolidated group and each of its members. Therefore, these regulations reflect a mix of single- and separate-entity treatment. For example, the intercompany-transaction rules in § 1.1502-13(c) generally respect the existence of intercompany transactions between the separate members but recompute and redetermine the members' tax items from the transaction to produce the same effect on the group as if the transacting members were divisions of a single corporation.

.03 Basis-adjustment reporting for consolidated groups

Form 1120, *U.S. Corporation Income Tax Return*, includes a new question on

Schedule K, Question 31, applicable to certain large, consolidated groups for any taxable year ending on or after December 31, 2023. This question asks consolidated groups with gross receipts or sales of \$1 billion or more to report certain subchapter K basis adjustments, as described in the Instructions to the 2023 Form 1120 (released for public comment on December 20, 2023). The intent of this question is for taxpayers to identify certain related-party basis adjustment transactions that were entered into by members of the consolidated group in consolidated years ending on or after December 31, 2023.

SECTION 3. COVERED TRANSACTIONS

.01 Overview of the need for the forthcoming proposed regulations.

The Treasury Department and the IRS are aware of related persons using partnerships to engage in transactions that inappropriately exploit the basis-adjustment provisions of subchapter K applicable to distributions of partnership property or transfers of partnership interests discussed in section 2 of this notice. This awareness results from the IRS's review of various partnership transactions involving related parties in which basis adjustments were created to artificially generate or regenerate Federal income tax benefits that resulted in significant tax savings without a corresponding economic outlay. These transactions were carefully structured to exploit the mechanical basis-adjustment provisions of subchapter K to produce significant tax benefits with little or no economic impact on the related parties, and in a manner that would not be a likely arrangement between partners negotiating at arm's-length.

Generally, in a covered transaction, partnership property is distributed to a

partner who is related to one or more other partners, and that distribution results in a person related to the distributee partner, the distributee partner, or both, receiving all or a share of a basis increase in the distributed property or remaining partnership property under § 732 or § 734(b) (as applicable); alternatively, a partnership interest is transferred between related persons or to a transferee partner who is related to an existing partner in the partnership, and that transfer results in an increase to the inside basis in partnership property with respect to the transferee partner under § 743(b).

The covered transactions generally are structured so that, under the applicable allocation rules (§§ 732(c), 734(c), 743(c), and 755), the basis increase is allocated to property that is eligible for cost recovery allowances (or eligible for a shorter cost recovery period) or that the partnership or the distributee partner disposes of in a taxable sale or exchange. Accordingly, the basis increase results in related partners decreasing their overall taxable income through additional or accelerated cost recovery allowances or decreasing their taxable gain or increasing their taxable loss on the subsequent taxable disposition of the property subject to the basis increase.

The related partners receive these tax benefits directly in the case of a distribution of property in which the basis of the distributed property is increased in the distributee partner's hands under § 732(b) or § 732(d). They receive these benefits indirectly in the case of a transfer of a partnership interest in which the inside basis of partnership property is increased for the transferee partner under § 743(b) or in the case of a distribution of property that results in an increase to the common basis of partnership property under § 734(b). Whether the tax benefits are received directly or

indirectly, the resulting decrease in taxable income or gain (or increase in taxable loss) benefits the related-party group as a whole. Further, because the partners are related, the distributions or transfers may have little or no effect on the overall economic ownership of the property yet produce significant tax benefits shared by the related partners.

A related partner's partnership interest must have certain characteristics to create the opportunity for a covered transaction. In general, these characteristics are (1) a partner's outside basis in its partnership interest that is low compared to the partnership's basis in property it distributes to such partner, (2) a partner's outside basis in its partnership interest that is high compared to such partner's share of the partnership's basis in the partnership property (that is, the partner's share of inside basis), or (3) a partner's outside basis in its partnership interest that is high compared to the partnership's basis in property it distributes to such partner in liquidation of the partner's interest. Partnerships with related parties can create these characteristics through orchestrated contributions and distributions, as well as allocations under § 704(b) and (c). In most commercial transactions involving unrelated parties, the opportunity for abuse is limited because each party has separate, and often competing, economic and tax interests, and the parties transact at arm's length. In contrast, for related parties, basis can be manipulated to provide a material net tax benefit to the related parties. Such basis shifting is contrary to congressional intent in enacting subchapter K. Congress intended that the provisions of subchapter K apply to transactions between partnerships and their partners to preserve parity between inside

and outside basis “so as to prevent any unintended tax benefit or detriment to the partners.” H.R. Rep. No. 1337, 83d Cong., 2d Sess. A225 (1954); S. Rep. No. 1622, 83d Cong., 2d Sess. 384 (1954). Congress also expressed its desire to prevent related parties from exploiting the rules of subchapter K to avoid tax “through the realization of fictitious losses or increasing the basis of property for purposes of depreciation.” H.R. Rep. No. 1337, at A226; S. Rep. No. 1622, at 386-87.

.02 Covered transactions under § 734(b).

In a covered transaction under § 734(b), a partnership with a § 754 election in effect and two or more partners that are related to each other makes a current or liquidating distribution of property to one or more of the related partners. Immediately before the distribution, the partnership’s basis in the distributed partnership property exceeds the distributee partner’s basis in its partnership interest (that is, the partnership distributes property with a relatively high inside basis to a distributee partner with a relatively low outside basis). Under § 732(a)(2) or (b), the low-outside basis partner takes a basis in the distributed property that is lower than the inside basis of the property immediately before the distribution.

As a result of the basis decrease to the distributed property in the hands of the distributee partner under § 732(a)(2) or (b), the partnership increases the basis of its remaining properties under § 734(b) by an amount equal to the excess of the partnership’s basis in the distributed property immediately before the distribution over the basis of the distributed property in the hands of the distributee partner immediately after the distribution. Under §§ 734(c) and 755, the partnership allocates this basis

increase among remaining partnership properties.

.03 Covered transactions under § 743(b).

In a covered transaction under § 743(b), (1) a partner transfers an interest in a partnership that has a § 754 election in effect or a substantial built-in loss immediately after such transfer (2) to a related transferee or a transferee that is related to one or more of the partners (3) in a nonrecognition transaction within the meaning of § 7701(a)(45) in which the gain recognized, if any, and for which tax imposed by subtitle A of the Code (subtitle A) is required to be paid, is less than the aggregate amount of the increase(s) in the basis of partnership property with respect to the transferee partner under §§ 743(b) and 755.

In order for the transfer to give rise to a basis adjustment under § 743(b), the transferee partner must have an inside-outside basis disparity with respect to its partnership interest so that the transferee partner's outside basis does not equal the transferee partner's share of inside basis. Because a § 754 election is in effect for the taxable year of the transfer or the partnership or a substantial built-in loss immediately after such transfer, a basis adjustment is made under § 743(b) or (d) to partnership property with respect to the transferee partner to eliminate the inside-outside basis disparity of the transferee partner. As a result of the transfer, the partnership allocates one or more basis increases to partnership property with respect to the transferee partner under §§ 743(c) and 755.

.04 Covered transactions under § 732.

In a covered transaction under § 732, a partner (distributee partner) receives a

liquidating distribution of property resulting in a basis increase in the distributed property under § 732(b) and (c), and either—

(1) The partnership liquidates and distributes the partnership's remaining partnership property to one or more parties related to the distributee partner (related distributee partner) resulting in a basis adjustment that reduces the basis (basis decrease) of such property to the related distributee partners under § 732(b) and (c), or

(2) The partnership continues, and a related party to the distributee partner is a continuing partner (related continuing partner) that has a share of the partnership's basis decrease under § 734(b) or (d) resulting from the liquidating distribution or would have had a share of the partnership's basis decrease under § 734(b) if the partnership had a § 754 election in effect.

SECTION 4. FORTHCOMING PROPOSED RELATED-PARTY BASIS ADJUSTMENT REGULATIONS

.01. In general. The forthcoming Proposed Related-Party Basis Adjustment Regulations would provide special rules that would apply to the cost recovery of basis adjustments arising from the covered transactions described in section 3 of this notice, as well as rules that would govern whether and how a basis adjustment arising from a covered transaction would be taken into account upon the disposition of such basis-adjusted property. These proposed regulations would be mechanical rules applicable to all covered transactions without regard to the taxpayer's intent and without regard to whether the transactions could be abusive or lacking in economic substance. Additionally, these proposed regulations would apply only if, and to the extent that,

property has been allocated a basis increase. If, and to the extent, property has been allocated a basis decrease, the proposed rules would not apply.

.02 Related persons; cost recovery. In general, for purposes of the forthcoming Proposed Related-Party Basis Adjustment Regulations, partners and other persons would be considered as related if they have a relationship described in § 267(b) (without regard to § 267(c)(3)) or § 707(b)(1) immediately before or immediately after a transaction. For purposes of the forthcoming Proposed Related-Party Basis Adjustment Regulations, the term “cost recovery” means an allowance for depreciation, amortization, or depletion under subtitle A.

.03 Related-party basis adjustments; cost recovery and disposition rules. Based on the authority provided in §§ 482, 732, 734(b), 743(b), 755, and 7805, as well as the provisions of the Code that otherwise permit cost recovery allowances with respect to basis increases under subchapter K, the forthcoming Proposed Related-Party Basis Adjustment Regulations would provide that a basis increase allocated to property retained or distributed by a partnership following a covered transaction (related-party basis adjustment, or RPBA) would be subject to specific rules providing the required method of recovering the basis adjustment and the treatment of the basis adjustment upon the disposition of the property to which the adjustment applies.

.04 Treatment of basis adjustments resulting from covered transactions under § 734(b).

The forthcoming Proposed Related-Party Basis Adjustment Regulations would provide that an RPBA arising from a covered transaction described in section 3.02 of

this notice (§ 734(b) RPBA) would be recovered using the cost recovery method and remaining recovery period, if any, of the corresponding distributed property that gave rise to such § 734(b) RPBA. In addition, the partnership would not be eligible to take the § 734(b) RPBA into account upon the sale or other disposition of partnership property to which a § 734(b) RPBA applies, subject to the rules described below. After a qualifying disposition of a corresponding distributed property, the basis adjustment would cease to be a § 734(b) RPBA. A qualifying disposition would mean a disposition of a corresponding distributed property to an unrelated person in an arm's-length transaction in which taxable gain or loss is fully recognized. Except as otherwise provided, if a basis adjustment ceases to be a § 734(b) RPBA, the remaining basis attributable to the former RPBA would be treated as giving rise to newly placed in service property that is subject to the cost recovery period and method of the property to which it was allocated, to the extent the property is eligible for cost recovery allowances, and the basis adjustment would be taken into account in computing gain or loss upon the sale or other disposition of the property. These rules would not apply to the share of any § 734(b) basis adjustment of a partner that is unrelated to the distributee partner. For purposes of this rule, a partner's share of a basis adjustment under § 734(b) would be determined under principles similar to those in § 1.197-2(h)(12)(iv)(D).

If a partnership distributes to a partner property with respect to which there is a § 734(b) RPBA in place, the partner would take into account the § 734(b) RPBA in determining the basis of the property in the partner's hands and the partner's outside basis in the partnership, and the basis adjustment would remain a § 734(b) RPBA until

the basis adjustment ceases to be a § 734(b) RPBA, as described above.

If a partnership disposes of property to which a § 734(b) RPBA applies (other than in a distribution to a partner) or a partner disposes of property to which a § 734(b) RPBA applies, the amount of the § 734(b) RPBA would be reallocated to other property of the partnership or the partner (under rules similar to the rules of § 1.755-1(c)) and would remain a § 734(b) RPBA. If the partnership or partner cannot reallocate a § 734(b) RPBA to any asset under the preceding sentence because the partnership or partner does not own property of a like character, the reallocation would be made when property of a like character is subsequently acquired.

.05 Treatment of basis adjustments resulting from covered transactions under § 743(b).

The forthcoming Proposed Related-Party Basis Adjustment Regulations would provide that an RPBA arising from a covered transaction described in section 3.03 of this notice (§ 743(b) RPBA) would be ineligible for cost recovery until the transferee partner becomes unrelated to both the transferor partner and to all existing partners as described below. In addition, the transferee partner would not be eligible to take the § 743(b) RPBA into account upon the sale or other disposition of partnership property to which a § 743(b) RPBA applies, subject to the rules described below. If a transferee partner that has a § 743(b) RPBA in place ceases to be related to both the transferor and all persons who were partners immediately before or immediately after the covered transaction, then the basis adjustment would cease to be a § 743(b) RPBA. Except as otherwise provided, if a basis adjustment ceases to be a § 743(b) RPBA, the basis

attributable to the former RPBA would be treated as giving rise to newly placed in service property that is subject to the cost recovery period and method of the property to which it was allocated, to the extent the property is eligible for cost recovery allowances, and the basis adjustment would be taken into account in computing gain or loss upon the sale or other disposition of the property.

If a partnership distributes to a transferee partner property with respect to which there is a § 743(b) RPBA in place, the transferee partner would take into account the § 743(b) RPBA in determining the basis of the property in the partner's hands as well as in determining the partner's outside basis in the partnership, and the basis adjustment would remain a § 743(b) RPBA until the basis adjustment ceases to be a § 743(b) RPBA, as described above. That is, the § 743(b) RPBA would be taken into account for purposes of applying § 732 but would remain ineligible for cost recovery and would not be used in computing gain or loss on the sale or disposition of the distributed property by the transferee partner.

If a partnership disposes of property to which a § 743(b) RPBA applies (other than in a distribution to the transferee partner) or a transferee partner disposes of property to which a § 743(b) RPBA applies, then the amount of the § 743(b) RPBA would be reallocated to other property (under rules similar to the rules of § 1.755-1(c)) and would remain a § 743(b) RPBA. If the partnership or transferee partner cannot reallocate a § 743(b) RPBA to any asset under the preceding sentence because the partnership or transferee partner does not own property of a like character, the reallocation would be made when property of a like character is subsequently acquired.

If any gain is recognized in a covered transaction described in section 3.03 of this notice, and tax imposed by subtitle A is required to be paid on such gain, the portion of each basis increase attributable to the gain would not be treated as a § 743(b) RPBA.

.06 Treatment of basis adjustments resulting from covered transactions under § 732.

The forthcoming Proposed Related-Party Basis Adjustment Regulations would generally require that a basis increase to distributed property under § 732(b) and (c) be treated as a § 732 RPBA to the extent such increase corresponds to a basis decrease of a related partner (or the basis decrease a related partner would have had if the partnership had a § 754 election in effect). In the case of a covered transaction described in section 3.04(1) of this notice (complete liquidation of the partnership), if a partnership makes liquidating distributions to all partners, a basis increase under § 732(b) and (c) to property distributed to the distributee partner would be treated as one or more § 732 RPBA's to the extent of a basis decrease under § 732(b) and (c) to property distributed to a related distributee partner. In the case of a covered transaction described in section 3.04(2) of this notice (continuation of the partnership), if a partnership makes a liquidating distribution to one partner and there is a resulting basis decrease under § 734(b), including a basis decrease that is suspended under § 1.755-1(c)(4) (or there would have been if the partnership had a § 754 election in effect), a basis increase under § 732(b) and (c) to property distributed to the distributee partner would be treated as one or more § 732 RPBA's to the extent of a related continuing partner's share of a resulting basis decrease under § 734(b) (or the basis decrease

under § 734(b) that would have resulted if the partnership had a § 754 election in effect).

The forthcoming Proposed Related-Party Basis Adjustment Regulations would require that a § 732 RPBA arising from a covered transaction described in section 3.04(1) of this notice resulting in a basis increase under § 732(b) and (c) to the property of the distributee partner would be recovered using the cost recovery method and remaining recovery period, if any, of the corresponding property the basis of which a related distributee partner reduced. In addition, the distributee partner would not be eligible to take the § 732 RPBA into account upon the sale or other disposition of the property to which the § 732 RPBA applies, subject to the rules described below. These rules would not apply to any portion of the basis increase that corresponds to a basis decrease to property distributed to an unrelated partner.

The forthcoming Proposed Related-Party Basis Adjustment Regulations would require that a § 732 RPBA arising from a covered transaction described in section 3.04(2) of this notice and resulting in a basis increase under § 732(b) and (c) to the property of the distributee partner would be recovered using the cost recovery method and remaining recovery period, if any, of the corresponding property the basis of which the partnership reduced under § 734(b), or would have reduced under § 734(b) if the partnership had a § 754 election in effect. In addition, the distributee partner would not be eligible to take the § 732 RPBA into account upon the sale or other disposition of the property to which the § 732 RPBA applies, subject to the rules described below. These rules would not apply to any portion of the basis increase that

corresponds to the share of any basis decrease under § 734(b) of a partner unrelated to the distributee partner (or the unrelated partner's share of a basis decrease under § 734(b) if the partnership had a § 754 election in effect). For purposes of this rule, a partner's share of a basis decrease under § 734(b) would be determined under principles similar to those in § 1.197-2(h)(12)(iv)(D).

For purposes of all covered transactions described in section 3.04 of this notice, in the case of multiple distributed properties, the proposed regulations would treat each distributed property as having a separate § 732 RPBA with respect to each basis decrease to corresponding property. The amount of a § 732 RPBA would be proportional to the share of the basis decrease to that § 732 RPBA's corresponding property out of the aggregate basis decrease to all corresponding property. A § 732 RPBA would be recovered using the cost recovery method and remaining recovery period, if any, of that § 732 RPBA's corresponding property. For purposes of this section 4.06, "corresponding property" would mean, in the case of a covered transaction described in section 3.04(1) of this notice, property distributed to a related distributee partner and allocated a basis decrease under § 732(b) and (c) and, in the case of a covered transaction described in section 3.04(2) of this notice, property allocated a basis decrease under § 734(b) of which a related continuing partner has a share (or would have a share if the partnership had a § 754 election in effect). In addition, the partner would not be eligible to take the § 732 RPBA into account upon the sale or other disposition of property to which a § 732 RPBA applies, subject to the rules described below.

For purposes of all covered transactions described in section 3.04 of this notice, upon a qualifying disposition of a corresponding property, any § 732 RPBA to which that property corresponds would cease to be a § 732 RPBA. If a basis adjustment ceases to be a § 732 RPBA, the remaining basis attributable to the former RPBA would be treated as giving rise to newly placed in service property that is subject to the cost recovery period and method of the distributed property, to the extent the property is eligible for cost recovery allowances, and the basis adjustment would be taken into account in computing gain or loss upon the sale or other disposition of the property. A qualifying disposition would mean a disposition of property to an unrelated person in a fully taxable, arm's-length transaction.

.07 Special rules and tax-indifferent parties. Special rules in the forthcoming Proposed Related-Party Basis Adjustment Regulations would apply to covered transactions that involve other related subchapter K provisions, such as § 732(d) and (f), and additional steps, as well as to tiered-partnership structures. The forthcoming Proposed Related-Party Basis Adjustment Regulations would also treat as a covered transaction certain partnership arrangements involving taxable and tax-indifferent parties that would otherwise be a covered transaction if the relatedness requirement of section 3.02, 3.03, or 3.04 of this notice were satisfied. For example, if a partnership, in which no partners are related, makes a distribution to an organization exempt from tax imposed by subtitle A by reason of § 501(a) of property that results in a basis increase to remaining partnership property under § 734(b)(1), this transaction would be treated as a covered transaction described in section 3.02 of this notice. For purposes of the

forthcoming Proposed Related-Party Basis Adjustment Regulations, a tax-indifferent party would be defined as a person that is either not liable for Federal income tax because of its tax-exempt or, in certain cases, foreign status or, also in certain cases, to which gain from the transaction would not result in Federal income tax liability for the person's taxable year within which such gain is recognized.

SECTION 5. FORTHCOMING PROPOSED CONSOLIDATED RETURN REGULATIONS

.01 In general. As a result of the interplay between the § 1502 regulations and the rules of subchapter K, a consolidated group's income from investments in partnerships often is not clearly reflected in the group's consolidated taxable income (as determined under § 1.1502-11 and other applicable § 1502 regulations) and consolidated tax liability (as determined under § 1.1502-2 and other applicable § 1502 regulations). In particular, anomalous results arise in certain situations in which the group's ownership interest in a partnership is split among members of the group, or in which a partnership interest is transferred from one member to another.

The Treasury Department and the IRS are concerned that some consolidated groups have attempted to alter consolidated taxable income or consolidated tax liability through basis adjustments to the property of partnerships owned by a group's members simply by: (i) transferring partnership interests from one member to another; or (ii) separating the group's ownership interest in a partnership between different members and causing the partnership to distribute property to one or more of the member partners. Such an alteration of consolidated taxable income or consolidated

tax liability does not clearly reflect the income of the group, which files a single tax return for each taxable year and generally reports its income and tax liability as if it were a single corporation. See §§ 1501 and 1502.

To prevent distortion of a consolidated group's income from investments in partnerships, the forthcoming Proposed Consolidated Return Regulations would apply a single-entity approach with respect to interests in a partnership held by members of a consolidated group. It is intended that the forthcoming Proposed Consolidated Return Regulations would prevent direct or indirect basis shifts among the members of the group resulting from the covered transactions described in section 3 of this notice. This approach would avoid many of the anomalous results that arise from split ownership of partnership interests among members of the group or from intercompany transfers of partnership interests.

SECTION 6. PROPOSED APPLICABILITY DATES

.01 The Treasury Department and the IRS intend to propose that the Treasury decision that adopts the Proposed Related-Party Basis Adjustment Regulations described in section 4 of this notice as final regulations would apply to taxable years ending on or after June 17, 2024. That is, once finalized, the regulations would govern the availability and amount of cost recovery deductions and gain or loss calculations for taxable years ending on or after June 17, 2024 even if the relevant covered transaction was completed in a prior taxable year.

.02 The applicability date for the Treasury decision that adopts the forthcoming Proposed Consolidated Return Regulations described in section 5 of this notice will not

relate to the issuance of this notice but will be proposed in the notice of proposed rulemaking containing the forthcoming Proposed Consolidated Return Regulations.

SECTION 7. REQUEST FOR COMMENTS AND SUBMISSION INFORMATION

.01 Request for comments. The Treasury Department and the IRS request comments on the approaches to addressing distortions of income from partnership related-party basis shifting transactions described in sections 4 and 5 of this notice.

.02 Procedures for submitting comments.

(1) Deadline. Written comments should be submitted by July 17, 2024.

However, consideration will be given to any written comments submitted after July 17, 2024, if such consideration will not delay the issuance of the proposed regulations.

(2) Form and manner. The subject line for the comments should include a reference to Notice 2024-54. All commenters are strongly encouraged to submit comments electronically. However, comments may be submitted in one of two ways:

(a) Electronically via the Federal eRulemaking Portal at

<https://www.regulations.gov> (type IRS-2024-XXXX in the search field on the [regulations.gov](https://www.regulations.gov) homepage to find this notice and submit comments); or

(b) By mail to: Internal Revenue Service, CC:PA:01:PR (Notice 2024-54), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, D.C., 20044.

(3) Publication of comments. The Treasury Department and the IRS will publish for public availability any comment submitted electronically and on paper to its public docket on <https://www.regulations.gov>.

SECTION 8. DRAFTING INFORMATION

The principal authors of this notice are Kevin I. Babitz and Anthony P. Sacco of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, contact Elizabeth V. Zanet at (202) 317-6007 or Anthony P. Sacco at (202) 317-5805. Regarding the forthcoming Proposed Consolidated Return Regulations, contact Jeremy Aron-Dine at (202) 317-6847.