**Q 8028. If more than one discharge of debt exclusion applies, which one takes precedence?**

Clearly, it is possible for more than one discharge of debt exclusion to apply. Depending on the taxpayer’s situation, however, there is an order of precedence that must be followed. In other words, the exclusion with the highest precedence applies.[[1]](#endnote-1)

So, if a taxpayer is in bankruptcy, that exclusion applies regardless of whether any of the other exclusions apply. If the taxpayer is insolvent (but not in bankruptcy) that exclusion applies regardless of whether the qualified farm indebtedness or qualified real property business indebtedness exclusions apply. If, the qualified principal residence exclusion also applies, however, that exclusion would apply unless the taxpayer elects to apply the insolvency exclusion.[[2]](#endnote-2)

***Example***: In 2015, the fair market value of Asher’s assets is $200,000 and the aggregate amount of his liabilities is $250,000. Thus, Asher is insolvent to the extent of $50,000 ($250,000 minus $200,000). In a bankruptcy proceeding, Asher receives a discharge of $150,000 of his debt. As a result, Asher becomes solvent to the extent of $100,000 ($200,000 minus $100,000). Under these circumstances, the bankruptcy exclusion and the insolvency exclusion both apply. Applying the insolvency exclusion, because the discharge made Asher solvent to the extent of $100,000, only $50,000 (the extent of Asher’s insolvency) of the $150,000 discharged debt would be excluded from gross income. The balance, $100,000 of discharged debt would be included in gross income. However, the bankruptcy exclusion takes precedence over the insolvency exclusion so Asher would exclude the entire $150,000 of discharged debt (rather than $50,000) from gross income.

1. IRC Section 108(a)(2), [↑](#endnote-ref-1)
2. IRC Section 108(a)(2)(C). [↑](#endnote-ref-2)