**Q 8043. When is a debt deemed to be discharged and what is the significance of the issuance of a Form 1099-C to the taxpayer?**

 Obviously, the actual forgiveness of a debt by a creditor triggers income from discharge of indebtedness to the debtor. So, in that case, the income from discharge of indebtedness must be reported in the tax year of discharge. However, under many circumstances, due to the lack of communication between the creditor and the debtor, it is not clear when a debt is forgiven. Therefore, in the absence of direct communication, it is possible that a creditor’s actions or inactions may result in a de facto discharge. Moreover, absent some reporting requirement by the discharging creditor, debtors may be unlikely to voluntarily report a discharge of debt that could create a substantial tax liability.

Perhaps to address the uncertainty as to when a discharge of debt occurs, IRC Section 6050P generally requires financial institutions such as banks, credit unions and credit card companies to issue a Form 1099C (a copy to the IRS and a copy to the debtor/taxpayer). To this point, the regulations require the filing of Form 1099-C (for discharges of at least $600 during the calendar year) upon the occurrence of an “identifiable event” whether or not an actual discharge has occurred on or before the date of an “identifiable event.”[[1]](#endnote-1) The list of the identifiable events includes:

* Discharge in bankruptcy;
* Cancellation that renders debt unenforceable in receivership, foreclosure or similar proceeding;
* Unenforceability due to the expiration of the statute of limitations for collection or expiration of statutory period for commencing deficiency judgment proceedings;
* Cancellation pursuant to a lender’s election to foreclose that statutorily extinguishes the lender’s right to pursue collection of the indebtedness;
* Cancellation or extinguishment of debt that renders it unenforceable pursuant to a probate or similar proceeding;
* Discharge pursuant to an agreement between a lender and debtor to discharge the debt for less than full consideration;
* Discharge pursuant to a lender’s decision or the application of defined policy of the lender to discontinue collection activity and discharge the debt; and
* In the case of certain creditor entities, the expiration of the non-payment testing period

**Q 8044. . Does the issuance of a Form 1099-C definitively establish the discharged amount as being income from discharge of indebtedness and/or the tax year in which it must be reported?**

No. As to whether the issuance of a Form 1099-C definitively establishes discharge of debt income, the regulations state that the occurrence of an identifiable event is solely for the purpose of triggering the creditor’s reporting requirement.[[2]](#endnote-2) Additionally, the regulations make it clear that the discharged debt must be reported without regard to whether it is actually included in gross income.[[3]](#endnote-3) Therefore, in spite of receiving a Form 1099-C, the taxpayer may challenge whether the discharged debt is subject to tax.

*Example*: In 2015, Asher receives a Form 1099-C from a credit card company listing $100,000 of discharged debt. However, before and after the discharge, Asher is insolvent. Because of the insolvency exception to the inclusion of discharge of debt income (see Q 8056) none of the discharged debt would be includible in gross income.

 As to whether the issuance of Form 1099-C definitively establishes the year of discharge, case law indicates that the taxpayer may take the position that the relevant identifiable event did not occur in the year in which the Form 1099-C was issued.[[4]](#endnote-4)

*Example*: In 2000, Asher who was in default on credit card debt ceased making any payments. However, the applicable statute of limitations for collection expired in 2004. Subsequently, in 2015, the credit card company issued a Form 1099-C to Asher reporting the outstanding credit card balance. Since the identifiable event occurred in 2004 (at the time the credit card company was legally barred from pursuing a legal collection action), the Form 1099-C issued in 2015 was in error. Thus, Asher may take the position on his 2015 Form 1040 that the amount reported on the Form 1099-C is not properly included in gross income.[[5]](#footnote-1)

**Q. 8045 . Does the issuance of a Form 1099-B by a creditor bar it from pursuing subsequent collection against the debtor?**

 There is a split of authority as to whether a creditor who issues a Form 1099-C should be barred from collection. Although it may seem counterintuitive, according to the majority view, the issuance of a Form 1099-C does not bar the creditor from pursuing a legal collection action against the debtor.[[6]](#endnote-5) Conversely, according to the minority view, based on equitable principles, the issuance of a Form 1099-C bars the issuing creditor from pursuing collection against the debtor.[[7]](#endnote-6)

*Example*: In 2014, Asher who was in default on credit card debt ceased making any payments. According to the applicable statute of limitations for collection, the limitations period would not expire until 2017. In 2015, with no communication with Asher regarding the discharge of the credit card debt, the credit card company issues a Form 1099-C. On Asher’s 2015 Form 1040, Asher reports the discharged credit card debt as income and pays the corresponding tax. Subsequently, in 2016, prior to the expiration of the limitation period, the credit card company pursues a legal action against Asher.

**Q. 8046. What should a taxpayer do who receives a Form 1099-C?**

Based on the discussion in Q 8044 and Q 8045, above, a taxpayer who receives a Form 1099-C has two concerns: (1) Has the debt been formally discharged by the creditor, and, if so, when did the creditor actually discharge the debt; and, (2) Is the taxpayer required to report and pay tax on the discharge of debt income?

As to the first concern, based on the majority view discussed in Q 8045, the taxpayer should contact the creditor to request formal confirmation of its discharge of the debt as well as the year in which the creditor determined to be the year of discharge. By securing a formal confirmation, the creditor would be barred from pursuing legal action against the taxpayer. If the creditor fails to provide the taxpayer with formal confirmation, the taxpayer should attempt to pinpoint the identifiable event the creditor likely relied upon in issuing the Form 1099-C.[[8]](#footnote-2)

*Example*: In 2015, Asher received a Form 1099-C from a credit card company. Although Asher requested a formal confirmation of his discharge as well as the year in which it was forgiven, the credit card company failed to respond. However, the credit card debt was incurred in 2004 and the applicable statute of limitations for collection expired in 2007. Based on this information, Asher can challenge the inclusion of the discharged debt as income in 2015 as well as defend any subsequent collection action initiated by the credit card company.

As to whether the amount reported on Form 1099-C is taxable, the receipt of a Form 1099-C reporting a substantial amount of discharged debt can be a daunting experience to many taxpayers. As discussed in Q 8045, however, a Form 1099-C is simply a reporting requirement of the creditor and does not establish whether the amount reported is taxable to the debtor. For that reason, the taxpayer should consider the various exceptions (discussed in Q9) that may apply to render all or part of the discharged debt non-taxable.

*Example*: In 2015, Asher received a Form 1099-C from a credit card company reporting a substantial amount of discharged debt. However, the debt reported on the Form 1099-C was discharged in bankruptcy. Because debt discharged in bankruptcy is excluded from gross income, Asher would not be taxed on such income.

1. 1.Treas. Reg. § 1.6050P-1(a)(1). [↑](#endnote-ref-1)
2. Treas. Reg. § 1.6050P-1(a)(1). [↑](#endnote-ref-2)
3. Treas. Reg. § 1.6050-1(a)(3) [↑](#endnote-ref-3)
4. See *Bacon v. Commissioner,* T.C. Summary Opinion 2015-15 (March 2, 2015). [↑](#endnote-ref-4)
5. *Bacon v. Commissioner,* T.C. Summary Opinion 2015-15 (March 2, 2015). [↑](#footnote-ref-1)
6. *Mennes v. Capital One, NA*, (W.D. Wisc. 2015); *FDIC v. Cashion*, 720 F. 3d 169 (4th Cir. 2013). [↑](#endnote-ref-5)
7. *In Re Reed*, 492 B.R. 261 (Barkr. E.D. Tenn. 2013); *In Re Crosby*, 261 B.R. 470 (Bankr, Kan. 2001). [↑](#endnote-ref-6)
8. Unfortunately, the Form 1099-C does not require the creditor to specifically state the identifiable event. [↑](#footnote-ref-2)