

# Publication 908

## Bankruptcy Tax Guide

(Rev. February)  
**2023**

Volume 1 of 2



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## Future Developments

For the latest information about developments related to Pub. 908, such as legislation enacted after it was published, go to [IRS.gov/Pub908](https://www.irs.gov/pub908).

## What’s New

**Bankruptcy estate filing threshold.** For tax year 2022, the requirement to file a return for a bankruptcy estate applies only if gross income is at least \$12,950. This amount is equal to the standard deduction for married individuals filing a separate return and is generally adjusted annually. See the Instructions for Form 1041 for updates to the filing threshold amount for future years.

# Reminders

## **Bankruptcy administrative expenses.**

Bankruptcy administrative expenses are reported on Schedule 1 (Form 1040), as allowable in arriving at adjusted gross income. These expenses were previously reported on Schedule A (Form 1040), as miscellaneous itemized deductions. See Internal Revenue Code section 67(e) and [\*Final Regulations - TD9918\*](#). For specific reporting instructions, see *Administrative expenses*, later.

**Automatic 6-month extension of time to file a bankruptcy estate return.** An automatic 6-month extension of time to file a bankruptcy estate income tax return is available for individuals in chapter 7 or chapter 11 bankruptcy proceedings upon filing a required application.

## **Bankruptcy Code tax filing requirements.**

Debtors filing under chapters 7, 11, 12, and 13 of the Bankruptcy Code must file all applicable federal, state, and local tax returns that become due after a case commences.

Failure to file tax returns timely or obtain an extension can cause a bankruptcy case to be converted to another chapter or dismissed.

In chapter 13 cases, the debtor **must** file all required tax returns for tax periods ending within **4 years** of the filing of the bankruptcy petition.

**Photographs of missing children.** The Internal Revenue Service is a proud partner with the [National Center for Missing & Exploited Children® \(NCMEC\)](#). Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling 1-800-THE-LOST

(1-800-843-5678) if you recognize a child.

# Introduction



*This publication isn't intended to cover bankruptcy law in general, or to provide detailed discussions of the tax rules for the more complex corporate bankruptcy reorganizations or other highly technical transactions. Additionally, this publication isn't updated on an annual basis and may not reflect recent developments in bankruptcy or tax law. If you need more guidance on the bankruptcy or tax laws applicable to your case, you should seek professional advice.*

This publication explains the basic federal income tax aspects of bankruptcy.

A fundamental goal of the bankruptcy laws enacted by Congress is to give an honest debtor a financial “fresh start.” This is accomplished through the bankruptcy discharge, which is a permanent injunction (court-ordered prohibition) against the

collection of certain debts as a personal liability of the debtor.

Bankruptcy proceedings begin with the filing of either a voluntary petition in the United States Bankruptcy Court or, in certain cases, an involuntary petition filed by creditors. This filing creates the bankruptcy estate.

- The bankruptcy estate generally consists of all of the assets the individual or entity owns on the date the bankruptcy petition was filed.
- The bankruptcy estate is treated as a separate taxable entity for individuals filing bankruptcy petitions under chapter 7 or 11 of the Bankruptcy Code, discussed later.
- The tax obligations of taxable bankruptcy estates are discussed later under *Individuals in Chapter 7 or 11*.

Generally, when a debt owed to another person or entity is canceled, the amount canceled or forgiven is considered income that is taxed to the person owing the debt. If a debt is canceled under a bankruptcy proceeding, the amount canceled isn't income. However, the canceled debt reduces other tax benefits to which the debtor would otherwise be entitled. See *Debt Cancellation*, later.

## Useful Items

You may want to see:

### Publication

- 225** Farmer's Tax Guide
- 525** Taxable and Nontaxable Income
- 536** Net Operating Losses (NOLs) for Individuals, Estates, and Trusts
- 538** Accounting Periods and Methods

- 544** Sales and Other Dispositions of Assets
- 551** Basis of Assets
- 4681** Canceled Debts, Foreclosures, Repossessions, and Abandonments

## **Form (and Instructions)**

- SS-4** Application for Employer Identification Number
- 982** Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)
- 1040 U.S. Individual Income Tax Return
- Schedule SE (Form 1040)** Self-Employment Tax
- 1040-SR** U.S. Tax Return for Seniors
- 1040-X** Amended U.S. Individual Income Tax Return 1041 U.S. Income Tax Return for Estates and Trusts

- **1041-ES** Estimated Income Tax for Estates and Trusts
- **1041-V** Payment Voucher
- 4506 Request for Copy of Tax Return
- **4506-T** Request for Transcript of Tax Return
- **4852** Substitute for Form W-2, Wage and Tax Statement, or Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
- **4868** Application for Automatic Extension of Time To File U.S. Individual Income Tax Return
- **7004** Application for Automatic Extension of Time To File Certain Business Income Tax, Information, and Other Returns

See *How To Get Tax Help*, later, for information about getting these publications and forms.

## **Bankruptcy Code Tax Compliance Requirements**

### **Tax Returns Due for Periods Ending Before the Bankruptcy Filing in Chapter 13 Cases**

The Bankruptcy Code requires chapter 13 debtors to **file all required tax returns for tax periods ending within 4 years of the debtor's bankruptcy filing**. All such federal tax returns must be filed with the IRS before the date first set for the first meeting of creditors. The debtor may request the trustee to hold the meeting open for an additional 120 days to enable the debtor to file the returns (or until the day the returns are due under an automatic IRS extension, if later). After notice and hearing, the bankruptcy

court may extend the period for another 30 days.



*Failure to timely file the returns can prevent confirmation of a chapter 13 plan and result in either dismissal of the chapter 13 case or conversion to a chapter 7 case.*

**Note.** Individual debtors should use their home address when filing Form 1040 or 1040-SR with the IRS. Returns should **not** be filed “in care of” the trustee's address.

**Ordering tax transcripts and copies of returns.** Trustees may require the debtor to submit copies or transcripts of the debtor's returns as proof of filing. The debtor can request free transcripts of the debtor's income tax returns by filing Form 4506-T, with the IRS or by going to [IRS.gov/Transcripts](https://www.irs.gov/Transcripts). Click on either “Get Transcript Online” or “Get Transcript by Mail” to order a free copy of the transcript. If preferred, the transcript can be ordered by calling 800-908-

9946. If requested through the phone system, the transcript will be mailed to the debtor's most current address according to the IRS's records. Transcripts requested using Form 4506-T may be mailed to any address, including to the attention of the trustee in the debtor's bankruptcy case. Transcripts are normally mailed within 10 to 15 days of receipt of the request by the IRS. A transcript contains most of the information on the debtor's filed return, but it isn't a copy of the return. To request a copy of the debtor's filed return, file Form 4506, Request for Copy of Tax Return, with a \$43 fee for each copy of each return requested. It may take up to 75 days for the IRS to provide the copies after receipt of the debtor's request.

## **Tax Returns Due After the Bankruptcy Filing**

For debtors filing bankruptcy under all chapters (chapters 7, 11, 12, and 13), the

Bankruptcy Code provides that if the debtor does not file a tax return that becomes due after the commencement of the bankruptcy case, or obtain an extension for filing the return before the due date, the taxing authority may request that the bankruptcy court either dismiss the case or convert the case to a case under another chapter of the Bankruptcy Code. If the debtor does not file the required return or obtain an extension within 90 days after the request is made, the bankruptcy court **must** dismiss or convert the case.

***Tax returns and payment of taxes in chapter 11 cases.*** The Bankruptcy Code provides that a chapter 11 debtor's failure to timely file tax returns and pay taxes owed after the date of the "order for relief" (the bankruptcy petition date in voluntary cases) is cause for dismissal of the chapter 11 case, conversion to a chapter 7 case, or appointment of a chapter 11 trustee.

**Disclosure of debtor's return information to trustee.** In bankruptcy cases filed under chapter 7 or 11 by individuals, the debtor's income tax returns for the year the bankruptcy case begins and for earlier years are, upon written request, open to inspection by or disclosure to the trustee. If the bankruptcy case was not voluntary, disclosure cannot be made before the bankruptcy court has entered an order for relief, unless the court rules that the disclosure is needed for determining whether relief should be ordered.

In bankruptcy cases other than those of individuals filing under chapter 7 or 11, the debtor's income tax returns for the current and prior years are, upon written request, open to inspection by or disclosure to the trustee, but only if the IRS finds that the trustee has a material interest that will be affected by information on the return.

Material interest is generally defined as a financial or monetary interest. Material

interest isn't limited to the trustee's responsibility to file a return on behalf of the bankruptcy estate.

However, the U.S. Trustee (an officer of the Department of Justice, responsible for maintaining and supervising a panel of private trustees for chapter 7 bankruptcy cases) and the standing chapter 13 trustee (the administrator of chapter 13 cases in a specific geographic region) generally don't have a material interest in the debtor's return or return information.

**Disclosure of bankruptcy estate's return information to debtor.** The bankruptcy estate's tax return(s) are open, upon written request, to inspection by or disclosure to the individual debtor in a chapter 7 or 11 bankruptcy. Disclosure of the estate's return to the debtor may be necessary to enable the debtor to determine the amount and nature of the tax attributes, if any, that the debtor

assumes when the bankruptcy estate terminates.

## **Individuals in Chapter 12 or 13**

Only individuals may file a chapter 13 bankruptcy. Chapter 13 relief isn't available to corporations or partnerships. The bankruptcy estate is **not** treated as a separate entity for tax purposes when an individual files a petition under chapter 12 (Adjustment of Debts of a Family Farmer or Fisherman with Regular Annual Income) or 13 (Adjustment of Debts of an Individual with Regular Income) of the Bankruptcy Code. In these cases, the individual continues to file the same federal income tax returns that were filed prior to the bankruptcy petition, Form 1040 or 1040-SR.

On the debtor's individual tax return, Form 1040 or 1040-SR, report all income received during the entire year and deduct all allowable expenses. Don't include in income

the amount from any debt canceled due to the debtor's bankruptcy. To the extent the debtor has any losses, credits, or basis in property that were previously reduced as a result of canceled debt, these reductions must be included on the debtor's return. See *Debt Cancellation*, later.

**Interest on trust accounts in chapter 13 cases.** In chapter 13 proceedings, do **not** include interest earned on amounts held by the trustee in trust accounts as income on the debtor's return. This interest isn't available to either the debtor or creditors; it is available only to the trustee for use by the U.S. Trustee system. The interest is also not taxable to the trustee as income.

## **Individuals in Chapter 7 or 11**

When an individual debtor files for bankruptcy under chapter 7 or 11 of the Bankruptcy Code, the bankruptcy estate is treated as a

new taxable entity, separate from the individual taxpayer.

The bankruptcy estate in a chapter 7 case is represented by a trustee. The trustee is appointed to administer the estate and liquidate any nonexempt assets. In chapter 11 cases, the debtor often remains in control of the assets as a “debtor-in-possession” and acts as the bankruptcy trustee. However, the bankruptcy court, for cause, may appoint a trustee if such appointment is in the best interests of the creditors and the estate.

During the chapter 7 or 11 bankruptcy, the debtor continues to file an individual tax return on Form 1040 or 1040-SR. The bankruptcy trustee files a Form 1041 for the bankruptcy estate. However, when a debtor in a chapter 11 bankruptcy case remains a debtor-in-possession, the debtor must file both a Form 1040 or 1040-SR individual return and a Form 1041 estate return for the

bankruptcy estate (if return filing requirements are met).

Although spouses may file a joint bankruptcy petition for their jointly administered bankruptcy estates, the estates are treated as two separate entities for tax purposes. Two *separate* bankruptcy estate income tax returns **must** be filed (if each spouse separately meets the filing requirements).

For information about determining the tax due and paying tax for a chapter 7 or 11 bankruptcy estate, see *Bankruptcy Estate Tax Return Filing Requirements and Payment of Tax Due*, later.

## **Debtor's Election To End Tax Year—Form 1040 or 1040-SR**

**Short tax years.** An individual debtor in a chapter 7 or 11 case may elect to close the debtor's tax year for the year in which the bankruptcy petition is filed, as of the day

before the date on which the bankruptcy case commences. If the debtor makes this election, the debtor's tax year is divided into 2 short tax years of less than 12 months each. The first tax year ends on the day *before* the commencement date and the second tax year begins on the commencement date.

If the election is made, the debtor's federal income tax liability for the first short tax year becomes an allowable claim against the bankruptcy estate arising before the bankruptcy filing. Also, the tax liability for the first short tax year isn't subject to discharge under the Bankruptcy Code.

If the debtor does not make an election to end the tax year, the commencement of the bankruptcy case does not affect the debtor's tax year. Also, no part of the debtor's income tax liability for the year in which the bankruptcy case commences can be collected from the bankruptcy estate.

**Note.** The debtor cannot make a short tax year election if no assets, other than exempt property, are in the bankruptcy estate.

## **Making the Election—Filing Requirements**

**First short tax year.** The debtor can elect to end the debtor's tax year by filing a return on Form 1040 or 1040-SR for the first short tax year. The return must be filed on or before the 15th day of the 4th full month after the end of that 1st tax year.

**Second short tax year.** If the debtor elects to end the tax year on the day before filing the bankruptcy case, the debtor must file the return for the first short tax year in the manner discussed above.

If the debtor makes this election, the debtor must also file a separate Form 1040 or 1040-SR for the second short tax year by the regular due date. To avoid delays in processing the return, write "Second Short

Year Return After Section 1398 Election” at the top of the return.

**Example.** Kori Doe, an individual calendar year taxpayer, filed a bankruptcy petition under chapter 7 or 11 on May 8. If Kori elected to close the tax year at the commencement of Kori’s case, the first short year runs from January 1 through May 7. The second short year runs from May 8 through December 31. To have a timely filed election for the first short year, Kori must file Form 1040 or 1040-SR (or an extension of time to file) for the period January 1 through May 7 by September 15.

To avoid delays in processing the return, write “Section 1398 Election” at the top of the return. The debtor may also make the election by attaching a statement to Form 4868, Application for Automatic Extension of Time To File U.S. Individual Income Tax Return. The statement must state that the debtor elects under Internal Revenue Code

section 1398(d)(2) to close the debtor's tax year on the day before filing the bankruptcy case. The debtor must file Form 4868 by the due date of the return for the first short tax year. The debtor's spouse may also elect to close their individual tax year; see *Election by debtor's spouse* below.

**Election by debtor's spouse.** If the debtor is married, the debtor's spouse may join in the election to end the tax year. If the debtor and spouse make a joint election, the debtor **must** file a joint return for the first short tax year. The debtor must elect by the due date for filing the return for the first short tax year. Once the election is made, it cannot be revoked for the first short tax year. However, the election does not prevent the debtor and the spouse from filing separate returns for the second short tax year.

**Later bankruptcy of spouse.** If the debtor's spouse files for bankruptcy later in the same year, that spouse may also choose to end

their own tax year, regardless of whether that spouse joined in the election to end the debtor's tax year.

As each spouse has a separate bankruptcy, one or both of them may have 3 short tax years in the same calendar year. If the debtor's spouse joined the debtor's election or if the debtor had not made the election to end the tax year, the debtor can join in the spouse's election. However, if the debtor made an election and the spouse did not join that election, the debtor cannot then join the spouse's later election. The debtor and the spouse are precluded from this election because they have different tax years. This results because the debtor does not have a tax year ending the day before the spouse's filing for bankruptcy, and the debtor cannot file a joint return for a year ending on the day before the spouse's filing of bankruptcy.

**Example 1.** Chris and Jesse Harris are calendar-year taxpayers. Chris's voluntary chapter 7 bankruptcy case begins on March 4. If Chris does not make an election, Chris's tax year does not end on March 3. If Chris makes an election, the first tax year is January 1–March 3, and the second tax year begins on March 4. Jesse could join in Chris's election as long as they file a joint return for the tax year January 1–March 3. They must make the election by July 15, the due date for filing the joint return.

**Example 2.** Ash and Kyle Barnes are calendar-year taxpayers. Ash's voluntary chapter 7 bankruptcy case begins on May 6, and Kyle's bankruptcy case begins on November 1 of the same year.

Kyle could elect to end the tax year on October 31. If Ash did not elect to end the tax year on May 5, or elected to do so but Kyle had not joined in that election, Kyle would have 2 tax years in the same calendar year if

Kyle closed the tax year. Kyle's first tax year is January 1–October 31, and the second year is November 1–December 31.

If Ash did not end the tax year as of May 5, Ash could join in Kyle's election to close the tax year on October 31, but only if they file a joint return for the tax year January 1–October 31.

If Ash elected to end the tax year on May 5, but Kyle did not join in Ash's election, Ash cannot join in Kyle's election to end the tax year on October 31. Ash and Kyle cannot file a joint return for that short tax year because their tax years preceding October 31 were not the same.

**Example 3.** Reg and Lee Thomas are calendar-year taxpayers. Lee's voluntary chapter 7 bankruptcy case began on April 10, and Reg's voluntary chapter 7 bankruptcy case began on October 3 of the same year. Lee elected to close the tax year on April 9 and Reg joins in Lee's election.

Under these facts, Reg would have 3 tax years for the same calendar year if Reg makes the election relating to Reg's own bankruptcy case. The first tax year would be January 1–April 9; the second, April 10–October 2; and the third, October 3–December 31.

Lee may join in Reg's election if they file a joint return for the second short tax year (April 10–October 2). If Lee does join in, Lee would have the same 3 short tax years as Reg. Also, if Lee joins in Reg's election, they may file a joint return for the third tax year (October 3–December 31), but they aren't required to do so.

**Annualizing taxable income.** If the debtor elects to close the tax year, the debtor must annualize taxable income for each short tax year in the same manner a change in annual accounting period is calculated. See *Short Tax Year* in Pub. 538 for information on how to

annualize the debtor's income and to figure the tax for the short tax year.

**Dismissal of bankruptcy case.** If the bankruptcy court later dismisses an individual chapter 7 or 11 case, the bankruptcy estate is no longer treated as a separate taxable entity. It is as if no bankruptcy estate was created for tax purposes. In this situation, the debtor must file amended tax returns on Form 1040-X to replace all full or short year individual returns (Form 1040 or 1040-SR) and bankruptcy estate returns (Form 1041) filed as a result of the bankruptcy case. Income, deductions, and credits previously reported by the bankruptcy estate must be reported on the debtor's amended returns. Attach a statement to the amended returns explaining why the debtor is filing an amended return.

# Taxes and the Bankruptcy Estate

**Property of the bankruptcy estate.** At the commencement of a bankruptcy case, a bankruptcy estate is created. Bankruptcy law determines which of the debtor's assets become part of a bankruptcy estate. This estate generally includes all of the debtor's legal and equitable interests in property as of the commencement date. However, there are exceptions and certain property is exempted or excluded from the bankruptcy estate.

**Note.** Exempt property and abandoned property are initially part of the bankruptcy estate, but are subsequently removed from the estate. Excluded property is never included in the estate.

**Transfer of assets between debtor and bankruptcy estate.** The transfer (other than by sale or exchange) of an asset from the debtor to the bankruptcy estate isn't treated

as a disposition for income tax purposes. The transfer does not result in gain or loss, acceleration of income or deductions, or recapture of deductions or credits. For example, the transfer of an installment obligation to the estate would not accelerate gain under the rules for reporting installment sales. The estate assumes the same basis, holding period, and character of the transferred assets. Also, the estate generally accounts for the transferred assets in the same manner as the debtor.

When the bankruptcy estate is terminated or dissolved, any resulting transfer (other than by sale or exchange) of the estate's assets back to the debtor is also not treated as a disposition for tax purposes. The transfer does not result in gain or loss, acceleration of income or deductions, or recapture of deductions or credits to the estate.

***Abandoned property.*** The abandonment of property by the estate to the debtor is a nontaxable disposition of property. If the debtor received abandoned property from the bankruptcy estate, the debtor assumes the same basis in the property that the bankruptcy estate had.

**Separate taxable entity.** When an individual files a bankruptcy petition under chapter 7 or 11, the bankruptcy estate is treated as a separate taxable entity from the debtor. The court appointed trustee or the debtor-in-possession is responsible for preparing and filing all of the bankruptcy estate's tax returns, including its income tax return, on Form 1041, and paying its taxes. The debtor remains responsible for filing their own returns on Form 1040 or 1040-SR and paying taxes on income that does not belong to the estate.

## **Employer identification number (EIN).**

The trustee or debtor-in-possession must obtain an EIN for a bankruptcy estate. The trustee or debtor-in-possession uses this EIN on all tax returns filed for the bankruptcy estate with the IRS, including estimated tax returns. See *Employer identification number* under *Bankruptcy Estate Tax Return Filing Requirements and Payment of Tax Due*, later.



*The social security number of the individual debtor cannot be used as the EIN for the bankruptcy estate.*

**Income, deductions, and credits—Form 1040 or 1040-SR.** In an individual chapter 7 or 11 bankruptcy case, don't include the income, deductions, and credits that belong to the bankruptcy estate on the debtor's individual income tax return (Form 1040 or 1040-SR). Also, don't include as income on the debtor's return the amount of any debt canceled by reason of the bankruptcy discharge. The bankruptcy estate must

reduce certain losses, credits, and the basis in property (to the extent of these items) by the amount of canceled debt. See *Debt Cancellation*, later.

**Note.** The debtor may not be able to claim certain deductions available to the bankruptcy estate, such as administrative expenses. Additionally, the bankruptcy exclusion cannot be used to exclude income from a cancelled debt if the discharge of indebtedness was not within the bankruptcy case, even though the debtor was under the bankruptcy court's protection at the time. However, other exclusions, such as the insolvency exclusion, may apply.

## **Bankruptcy Estate—Income, Deductions, and Credits**

### **Bankruptcy Estate Income**

**Income of the estate in individual chapter 7 cases.** The gross income of the

bankruptcy estate includes gross income of the debtor to which the estate is entitled under the Bankruptcy Code. Gross income also includes income generated by the bankruptcy estate from property of the estate after the commencement of the case.

Gross income of the bankruptcy estate does not include amounts received or accrued by the debtor *before* the commencement of the case. Additionally, in chapter 7 cases, gross income of the bankruptcy estate does not include any income that the debtor earns *after* the date of the bankruptcy petition.

### **Income of the estate in individual chapter 11 cases.**

In chapter 11 cases, under Internal Revenue Code section 1398(e)(1), gross income of the bankruptcy estate includes income that the debtor earns for services performed after the bankruptcy petition date. Also, earnings from services performed by an individual debtor

after the commencement of the chapter 11 case are property of the bankruptcy estate under section 1115 of the Bankruptcy Code (11 U.S.C. section 1115).

**Note.** A debtor-in-possession may be compensated by the estate for managing or operating a trade or business that the debtor conducted before the commencement of the bankruptcy case. Such payments should be reported by the debtor as miscellaneous income on their individual income tax return (Form 1040 or 1040-SR).

Amounts paid by the estate to the debtor-in-possession for managing or operating the trade or business may qualify as administrative expenses of the estate. See *Administrative expenses*, later.

***Conversion or dismissal of chapter 11 cases.*** If a chapter 11 case is converted to a chapter 13 case, the chapter 13 estate isn't a separate taxable entity and earnings from post-conversion services and income from

property of the estate realized after the conversion to chapter 13 are taxed to the debtor. If the chapter 11 case is converted to a chapter 7 case, 11 U.S.C. section 1115 does not apply after conversion and:

- Earnings from post-conversion services will be taxed to the debtor, rather than the estate; and
- The property of the chapter 11 estate will become property of the chapter 7 estate.

Any income on this property will be taxed to the estate even if the income is realized after the conversion to chapter 7. If a chapter 11 case is dismissed, the debtor is treated as if the bankruptcy case had never been filed and as if no bankruptcy estate had been created.

## **Bankruptcy Estate Deductions and Credits**

A bankruptcy estate deducts expenses incurred in a trade, business, or activity, and uses credits in the same way the debtor would have deducted or credited them had they continued operations.

**Note.** Expenses may be disallowed under other provisions of the Internal Revenue Code (such as the disallowance of certain capital expenditures or expenses relating to tax-exempt interest).

**Administrative expenses.** Allowable expenses include administrative expenses.



*Administrative expenses can only be deducted by the estate, never by the debtor.*

The bankruptcy estate is allowed deductions for bankruptcy administrative expenses and fees, including accounting fees, attorney fees,

and court costs. These expenses are deductible on Schedule 1 (Form 1040), as allowable in arriving at adjusted gross income because they would not have been incurred if property had not been held by the bankruptcy estate. See Internal Revenue Code section 67(e) and [Final Regulations - TD9918](#).

**Note.** Report this amount as a write-in on Schedule 1 (Form 1040), Part II, line 24z.

Administrative expenses of the bankruptcy estate attributable to conducting a trade or business or for the production of estate rents or royalties are deductible in arriving at adjusted gross income on Form 1040 or 1040-SR, Schedules C, E, and F.

**Note.** The bankruptcy estate uses Form 1041 as a transmittal for the tax return prepared using Form 1040 or 1040-SR and its schedules. See *Transmittal for Form 1040 or 1040-SR* under *Bankruptcy Estate Tax Return Filing Requirements and Payment of Tax*, later.

***Administrative expense loss.*** If the administrative expenses of the bankruptcy estate are more than its gross income for a tax year, the excess amount is an administrative expense loss (AEL). An AEL may be carried back 3 years and forward 7 years. The AEL amounts can only be carried to a tax year of the estate and never to a debtor's tax year. An AEL must first be carried back to the earliest year possible. However, NOL carrybacks (see *Carrybacks from the bankruptcy estate*, later, regarding farm losses) and carryovers must be applied against income of the estate (and are reduced) before administrative loss carrybacks and carryovers. See Internal Revenue Code section 1398(h)(2)(C).

***Attribute carryovers.*** The bankruptcy estate may use its tax attributes the same way that the debtor would have used them. These items are determined as of the first day of the debtor's tax year in which the bankruptcy

case begins. The bankruptcy estate assumes the following tax attributes from the debtor:

1. NOL carryovers.
2. Carryovers of excess charitable contributions.
3. Recovery of tax benefit items.
4. Credit carryovers.
5. Capital loss carryovers.
6. Basis, holding period, and character of assets.
7. Method of accounting.
8. Passive activity loss and credit carryovers.
9. Unused at-risk deductions.
10. Other tax attributes provided in the regulations.

Certain tax attributes of the bankruptcy estate must be reduced by the amount of income that was previously excluded as a result of cancellation of debt during the bankruptcy proceeding. See *Debt Cancellation*, later.

When the bankruptcy estate is terminated (for example, when the case ends), the debtor assumes any remaining tax attributes previously taken over by the bankruptcy estate. The debtor also generally assumes any of the tax attributes, listed above, that arose during the administration of the bankruptcy estate.

**Note.** The debtor does not assume the bankruptcy estate's administrative expense losses because they cannot be used by an individual taxpayer filing Form 1040 or 1040-SR. See *Administrative expense loss*, earlier.

***Passive and at-risk activities.*** For bankruptcy cases beginning after November 8, 1992, passive activity carryover losses and

credits and unused at-risk deductions are treated as tax attributes passing from the debtor to the bankruptcy estate, which the estate then passes back to the debtor when the bankruptcy estate terminates.

Additionally, transfers to the debtor (other than by sale or exchange) of interests in passive or at-risk activities are treated as nontaxable exchanges. These transfers include the return of exempt property and abandonment of estate property to the debtor.

### **Carrybacks from the debtor's activities.**

The debtor cannot carry back any NOL or credit carryback from a tax year ending after the bankruptcy case has begun to any tax year ending before the case began.

### **Carrybacks from the bankruptcy estate.**

The estate may carry back excess credits, such as the general business credit, to the pre-bankruptcy tax years.

Generally, an NOL arising in a tax year beginning in 2021 or later may not be carried back and instead must be carried forward indefinitely. However, farming losses arising in tax years beginning in 2021 or later may be carried back 2 years and carried forward indefinitely. See Pubs. 536 and 225 for more information.

## **Tax Reporting—Chapter 11 Cases**

**Allocation of income and credits on information returns and required statement for returns for individual chapter 11 cases.** In chapter 11 cases, when an employer issues a Form W-2 reporting all of the debtor's wages, salary, or other compensation for a calendar year, and a portion of the earnings represent post-petition services includible in the estate's gross income, the Form W-2 amounts **must** be allocated between the estate and the

debtor. The debtor-in-possession or trustee must allocate the income amount reported in box 1 and the income tax withheld reported in box 2 between the debtor and the estate. These allocations must reflect that the debtor's gross earnings from post-petition services and gross income from post-petition property are, generally, includible in the estate's gross income and not the debtor's gross income. The debtor and trustee may use a simple percentage method to allocate income and income tax withheld. The same method must be used to allocate the income and the withheld tax.

**Example.** If 20% of the wages reported on Form W-2 for a calendar year were earned after the commencement of the case and are included in the estate's gross income, 20% of the withheld income tax reported on Form W-2 must also be claimed as a credit on the estate's income tax return. Likewise, 80% of wages must be reported by the debtor and

80% of the income tax withheld must be claimed as a credit on the debtor's income tax return. See Internal Revenue Code section 31(a).

If information returns are issued to the debtor for gross income, gross proceeds, or other reportable payments that should have been reported to the bankruptcy estate, the debtor-in-possession or trustee must allocate the improperly reported income in a reasonable manner between the debtor and the estate. In general, the allocation must ensure that any income and income tax withheld attributable to the post-petition period is reported on the estate's return, and any income and income tax withheld attributable to the pre-petition period is reported on the debtor's return.

IRS Notice 2006-83 requires the debtor to attach a statement to his or her individual income tax return (Form 1040 or 1040-SR) stating that the return is filed subject to a

chapter 11 bankruptcy case. The statement must also:

- Show the allocations of income and income tax withheld;
- Describe the method used to allocate income and income tax withheld; and
- List the filing date of the bankruptcy case, the bankruptcy court in which the case is pending, the bankruptcy court case number, and the bankruptcy estate's EIN.

**Note.** The debtor-in-possession or trustee must attach a similar statement to the bankruptcy estate's income tax return (Form 1041).

The model Notice 2006-83 Statement, shown later, may be used by debtors, debtors-in-possession, and trustees to satisfy the reporting requirement.

**Self-employment taxes in individual chapter 11 cases.** Internal Revenue Code section 1401 imposes a tax upon the self-employment income, that is, the net earnings from self-employment of an individual. Net earnings from self-employment are equal to the gross income derived by an individual from any trade or business carried on by such individual, less deductions attributable to the business.

Neither section 1115 of the Bankruptcy Code nor Internal Revenue Code section 1398 addresses the application of self-employment tax to the post-petition earnings of the individual debtor. Therefore, if the debtor continues to derive gross income from the performance of services as a self-employed individual after the commencement of the bankruptcy case, the debtor must continue to report the debtor's self-employment income on Schedule SE (Form 1040) of the debtor's income tax return. This schedule includes

self-employment income earned post-petition and the attributable deductions. The debtor must pay any self-employment tax imposed by Internal Revenue Code section 1401.

**Employment taxes and employer's obligation to file Form W-2 in individual chapter 11 cases.**

In chapter 11 cases, post-petition wages earned by a debtor are generally treated as gross income of the estate. However, section 1115 of the Bankruptcy Code does not affect the determination of what are deemed wages for Federal Insurance Contributions Act (FICA) tax, Federal Unemployment Tax Act (FUTA) tax, or federal income tax withholding purposes. See Notice 2006-83.

The reporting and withholding obligations of a debtor's employer also don't change. An employer should continue to report the wages and tax withholding on a Form W-2 issued under the debtor's name and social security number.

**Notice to persons required to file information returns (other than Form W-2, Wage and Tax Statement) in individual chapter 11 cases.** Within a reasonable time after the commencement of a chapter 11 bankruptcy case, the trustee or debtor-in-possession should provide notification of the bankruptcy estate's EIN to all persons (or entities) that are required to file information returns for the bankruptcy estate's gross income, gross proceeds, or other types of reportable payments. See Internal Revenue Code section 6109(a)(2). As these payments are the property of the estate under section 1115 of the Bankruptcy Code, the payors should report the gross income, gross proceeds, or other reportable payments on the appropriate information return using the estate's name and EIN, as required under the Internal Revenue Code and regulations (see Internal Revenue Code sections 6041 through 6049).

The trustee or debtor-in-possession should not, however, provide the EIN to a person (or entity) filing Form W-2 reporting the debtor's wages or other compensation, as section 1115 of the Bankruptcy Code does not affect the determination of what constitutes wages for purposes of federal income tax withholding or FICA. See Notice 2006-83. An employer should continue to report all wage income and tax withholding, both pre-petition and post-petition, on a Form W-2 to the debtor under the debtor's social security number.

The debtor in a chapter 11 case isn't required to file a new Form W-4 with an employer solely because the debtor filed a chapter 11 case and the post-petition wages are includible in the estate's income and not the debtor's income. However, a new Form W-4 may be necessary if the debtor is no longer entitled to claim the same number of allowances previously claimed because certain

deductions or credits now belong to the estate. See Employment Tax Regulations section 31.3402(f)(2)-1. Additionally, the debtor may wish to file a new Form W-4 to increase the income tax withheld from post-petition wages allocated to the estate to avoid having to make estimated tax payments for the estate. See Internal Revenue Code section 6654(a).

***Notice required in converted and dismissed cases.*** When a chapter 11 bankruptcy case is closed, dismissed, or converted to a chapter 12 or 13 case, the bankruptcy estate ends as a separate taxable entity. The debtor should, within a reasonable time, send notice of such event to the persons (or entities) previously notified of the bankruptcy case. This helps to ensure that gross income, proceeds, and other reportable payments realized after the event are reported to the debtor under the correct

taxpayer identification number (TIN) rather than to the estate.

When a chapter 11 case is converted to a chapter 7 case, the bankruptcy estate will continue to exist as a separate taxable entity. Gross income (other than post-conversion income from the debtor's services), gross proceeds, or other reportable payments should continue to be reported to the estate if they are property of the chapter 7 estate. However, income from services performed by the debtor after conversion of the case to chapter 7 isn't property of the chapter 7 estate. After the conversion, the debtor should notify payors required to report the debtor's nonemployee compensation that compensation earned after the conversion should be reported using the debtor's name and TIN, not the estate's name and EIN.

**Employment taxes.** The trustee or debtor-in-possession must withhold income and social security taxes and file employment tax

returns for any wages paid by the trustee or debtor, including wage claims paid as administrative expenses. See Pub. 15, (Circular E), *Employer's Tax Guide*, for details on employer tax responsibilities.

The trustee also has the duty to prepare and file Forms W-2 for wage claims paid by the trustee, regardless of whether the claims accrued before or during bankruptcy. For a further discussion of employment taxes, see *Employment Taxes*, later.

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## Notice 2006-83

### Notice 2006-83 Statement

#### *Pending Bankruptcy Case*

The taxpayer, \_\_\_\_\_, filed a bankruptcy petition under chapter 11 of the Bankruptcy Code in the bankruptcy court for the District of \_\_\_\_\_. The bankruptcy court case number is \_\_\_\_\_. Gross income, and withheld federal income tax, reported on Form W-2, Forms 1099, Schedule K-1, and other information returns received under the taxpayer's name and social security number (or other taxpayer identification number) are allocated between the taxpayer's TIN and the bankruptcy estate's EIN as follows, using [describe allocation method]: \_\_\_\_\_.

	Year	Taxpayer	Estate
1.	Form W-2, Payor: _____ Withheld income tax shown on Form W-2	\$ _____	\$ _____
2.	Form 1099-INT Payor: _____ Withheld income tax (if any) shown on Form 1099-INT	\$ _____	\$ _____
3.	Form 1099-DIV Payor: _____ Withheld income tax (if any) shown on Form 1099-DIV	\$ _____	\$ _____
4.	Form 1099-MISC Payor: _____ Withheld income tax (if any) shown on Form 1099-MISC	\$ _____	\$ _____

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# Bankruptcy Estate Tax Return Filing Requirements and Payment of Tax Due

## Filing Requirements

**Filing threshold.** If the bankruptcy estate has gross income that meets or exceeds the minimum amount required for filing, the trustee or debtor-in-possession must file an income tax return on Form 1041. This amount is equal to the basic standard deduction for a *married individual filing separately*.

For 2022, the threshold filing amount for a bankruptcy estate is \$12,950 (this amount is equal to the \$12,950 standard deduction for married individuals filing separately).

This amount is generally adjusted annually. See the Form 1041 instructions at [IRS.gov/Form1041](https://www.irs.gov/Form1041) for the current threshold amount for future years.

**Accounting period.** A bankruptcy estate may have a fiscal year. However, this period cannot be longer than 12 months.

***Change of accounting period.*** The bankruptcy estate may change its accounting period (tax year) once without IRS approval. This rule allows the bankruptcy trustee to close the estate's tax year early, before the expected termination of the bankruptcy estate. The trustee can then file a return for the first short tax year to get a quick determination of the estate's tax liability.

**Employer identification number (EIN).** The trustee or debtor-in-possession must obtain an EIN for a bankruptcy estate. The trustee or debtor-in-possession uses this EIN on all tax returns filed for the bankruptcy estate with the IRS, including estimated tax returns.



*The social security number of the individual debtor cannot be used as the EIN for the bankruptcy estate.*

Obtain an EIN for a bankruptcy estate by applying in one of the following ways.

- Apply for an EIN online. Go to the IRS website at [IRS.gov/EIN](https://www.irs.gov/ein) and click on *Apply for an EIN Online*. The EIN is issued immediately once the application information is validated.
- By mailing or faxing Form SS-4, Application for Employer Identification Number.

If the trustee or debtor-in-possession hasn't received the bankruptcy estate's EIN by the time the return is due, write "Applied for" and the date you applied in the space for the EIN. For more details, see Pub. 583, *Starting a Business and Keeping Records*.

Trustees representing 10 or more bankruptcy estates (other than estates that will be filing employment or excise tax returns) may request a series or block of EINs.

**Figuring tax due.** The bankruptcy estate figures its taxable income the same way an individual figures taxable income. However, the estate uses the tax rates for a *married individual filing separately* to calculate the tax on its taxable income. The estate may either itemize deductions or take the basic standard deduction for a married individual filing a separate return. The estate cannot take the higher standard deduction allowed for married persons filing separately who are 65 or older or blind.



***Tax rate schedule.*** *The tax on income for bankruptcy estates is calculated using the tax rate schedule for Married Individuals Filing Separately, **not** the Estates and Trusts tax rate schedule.*

**When to file.** Calendar year bankruptcy estates must file Form 1041 by April 15. Fiscal year bankruptcy estates must file on or before the 15th day of the 4th month following the close of its tax year. For example, an estate that has a tax year that ends on June 30 must file Form 1041 by October 15 of the tax year. If the due date falls on a Saturday, Sunday, or legal holiday, file on the next business day.

**Note.** The bankruptcy estate is allowed an automatic 6-month extension of time to file the bankruptcy estate tax return upon filing the required application, Form 7004, Application for Automatic Extension of Time To File Certain Business Income Tax, Information, and Other Returns.

An estate (other than a bankruptcy estate) and a trust filing Form 1041 are eligible for an automatic 5<sup>1</sup>/<sub>2</sub>-month extension of time to file, which is due September 30. Bankruptcy estate income tax returns are due October 15

(unless a fiscal year) and are eligible for a 6-month extension. See Form 7004.

### **Transmittal for Form 1040 or 1040-SR.**

Form 1041 is used as a *transmittal* for Form 1040 or 1040-SR. If a return is required, the trustee or debtor-in-possession must complete the identification area at the top of Form 1041 and indicate the chapter under which the bankruptcy estate filed, either chapter 7 or chapter 11.

Prepare the bankruptcy estate's return by completing Form 1040 or 1040-SR. In the top margin of Form 1040 or

1040-SR, write "Attachment to Form 1041—**DO NOT DETACH.**" Then, attach Form 1040 or 1040-SR to the Form 1041 transmittal. Enter the tax and payment amounts on lines 24 through 30 of Form 1041, then sign and date the return. An example of a bankruptcy estate's tax return is shown later.

**Note.** The filing of the bankruptcy estate's tax return does not relieve a debtor from the requirement to file their individual tax return on Form 1040 or 1040-SR.

## **Payment of Tax Due**

**Payment methods.** Payment of tax due may be made by check or money order or by credit or debit card. For information on how to make payments electronically by credit or debit card, go to [IRS.gov/PayByCard](https://www.irs.gov/PayByCard).

Payments may also be made electronically using the Electronic Federal Tax Payment System (EFTPS), a free tax payment system that allows you to make payments online or by phone. To get more information about EFTPS or to enroll in EFTPS, visit [EFTPS.gov](https://www.eftps.gov) or call 800-555-4477. To contact EFTPS using the Telecommunications Relay Services (TRS), for people who are deaf, hard of hearing, or have a speech disability, dial 711 and provide the TRS assistant the 800-555-

4477 number above or 800-733-4829. For more information, see Pub. 966, Electronic Federal Tax Payment System: A Guide to Getting Started.

**Payment voucher—Form 1041-V.** Form 1041-V accompanies payments made by check or money order for Form 1041. The voucher includes information about the bankruptcy estate, including the name of the bankruptcy estate, trustee, EIN, and amount due. Using Form 1041-V assists the IRS in processing the payment more accurately and efficiently. We recommend the use of Form 1041-V; however, there is no penalty if the voucher isn't used.

**Estimated tax—Form 1041-ES.** In most cases, the trustee or debtor-in-possession **must** pay any required estimated tax due for the bankruptcy estate. See the Form 1041-ES instructions for information on the minimum threshold amount required for filing Form

1041-ES, paying the estimated tax, and exceptions to filing.

## **Employment Taxes**

The trustee or debtor-in-possession must withhold income and social security taxes and file employment tax returns for any wages paid by the trustee or debtor, including wage claims paid as administrative expenses. Until these employment taxes are deposited, as required by the Internal Revenue Code, they should be set aside in a separate bank account to ensure that funds are available to satisfy the liability. If the employment taxes aren't paid as required, the trustee may be held personally liable for payment of the taxes. See Pub. 15, (Circular E), *Employer's Tax Guide*, for details on employer tax responsibilities. Also see Notice 931, *Deposit Requirements for Employment Taxes*, for details on the deposit rules, including the requirement that federal employment tax

deposits be made by electronic funds transfer.

The trustee also has a duty to prepare and file Forms W-2, for wage claims paid by the trustee, regardless of whether the claims accrued before or during bankruptcy. If the debtor fails to prepare and file Forms W-2 for wages paid before bankruptcy, the trustee should instruct the employees to file a Form 4852, Substitute for Form W-2, Wage and Tax Statement, or Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., with their individual income tax returns.

## **Example—Tax Due**



*This publication isn't revised annually. Future changes to the forms and their instructions may not be reflected in this example.*

**Note.** The following information was prepared for tax year 2022. In 2022, the threshold filing amount for a bankruptcy estate was \$12,950 (this amount is equal to the \$12,950 standard deduction for married individuals filing separately).

**Facts and circumstances.** On December 15, 2021, Dylan Smith filed a bankruptcy petition under chapter 7. Riley Black was appointed trustee to administer the bankruptcy estate and to distribute the assets.

The estate received the following assets from Dylan Smith.

1. A \$100,000 certificate of deposit.
2. Commercial rental real estate with a fair market value (FMV) of \$280,000.
3. A personal residence with an FMV of \$200,000.

Also, the estate received a \$251,500 capital loss carryover.

Dylan Smith's bankruptcy case was closed on December 31, 2022. During 2022, Dylan Smith was relieved of \$70,000 of debt by the bankruptcy court. The estate chose a calendar year as its tax year. Riley Black, the trustee, reviews the estate's transactions and reports the taxable events on the estate's final return.

**Schedule B (Form 1040).** The certificate of deposit earned \$5,500 of interest during 2022. Riley reports this interest on Schedule B. Riley completes this schedule, then enters the result on Form 1040 or 1040-SR.

**Form 4797.** The commercial real estate was sold on July 1, 2022, for \$280,000. The property was purchased in 2003 at a cost of \$250,000. Additionally, \$25,000 of selling expenses were incurred. Assume the total depreciation allowable as of the date of sale was \$125,000. Riley reports the gain of \$130,000 from the sale on Form 4797 and

then enters the gain on Schedule D (Form 1040).

Dylan Smith's former residence was sold on September 30, 2022. The sale price was \$200,000, the selling expenses were \$20,000, and Dylan Smith's adjusted basis was \$140,000. This sale is excluded from gross income under Internal Revenue Code section 121.

**Note.** Gains from the sale of personal residences are excluded from gross income up to \$250,000 under Internal Revenue Code section 121 (\$500,000 for married couples filing a joint return). Bankruptcy estates succeed to this exclusion at the commencement of the case. See Regulations section 1.1398-3.

**Schedule E (Form 1040).** The commercial real estate was rented through the date of sale. Riley reports the income and expenses on Schedule E. In 2022, there was net rental income of \$40,000. Riley completes this

schedule, then enters the net income on Schedule 1 (Form 1040), Part I, line 5.

**Schedule D (Form 1040).** Riley completes Schedule D, taking into account the \$251,500 capital loss carryover from 2021. Riley then enters the 2022 allowable capital loss of \$1,500 from Schedule D on Form 1040 or 1040-SR.

**Schedule 1 (Form 1040).** Riley reports the net rental income of \$40,000 from Schedule E on Schedule 1 (Form 1040), Part I, line 5. Riley also reports the bankruptcy estate's administrative expenses of \$10,000 as an adjustment to income on Schedule 1 (Form 1040), Part II, line 24z. Riley completes this schedule, then enters the result on Form 1040 or 1040-SR.

**Schedule A (Form 1040).** During 2022, the bankruptcy estate paid mortgage interest of \$10,000 and real property tax of \$4,000 on Dylan Smith's former residence. It also paid income tax of \$1,000 to the state. Riley

enters the mortgage interest, real estate tax, and income tax on Schedule A. Riley completes Schedule A, then enters the total itemized deductions of \$15,000 on Form 1040 or 1040-SR.

**Form 982.** Riley completes the Schedule D Tax Worksheet to figure the capital loss carryover. Because \$70,000 of debt was canceled, Riley must reduce the tax attributes of the estate by the amount of the canceled debt. See *Debt Cancellation*, later. After the bankruptcy case ends, Dylan Smith will assume the estate's tax attributes. Dylan Smith will assume a capital loss carryover of \$50,000 (\$120,000 carryover minus the \$70,000 attribute reduction) for use in preparation of Dylan's individual tax return (Form 1040 or 1040-SR).

**Note.** If the bankruptcy estate had continued, the capital loss carryover would be available to the bankruptcy estate for the 2023 tax year.

**Tax computation.** The bankruptcy estate's 2022 tax due is computed as follows:

Income:

Interest income.....	\$ 5,500
Capital loss.....	(1,500)
Net rental income.....	<u>40,000</u>
Total income.....	\$44,000
Minus: Adjustments to income.....	<u>10,000</u>
Adjusted gross income...	\$34,000
Minus: Itemized deductions	<u>15,000</u>
Taxable income .....	<u>\$19,000</u>
<b>Tax due.....</b>	<b>\$2,078</b>

**Form 1040 or 1040-SR.** Riley determines the bankruptcy estate's taxable income and figures its tax using the tax rate schedule for Married Individuals Filing Separately.

**Form 1041.** Riley enters the total tax, any estimated tax payments, and tax due from Form 1040 or 1040-SR on Form 1041. Riley completes the identification area at the top of Form 1041, then signs and dates the return as the trustee on behalf of the bankruptcy estate.

## **Partnerships and Corporations**

### **Filing Requirements**

A separate taxable estate isn't created when a partnership or corporation files a bankruptcy petition and their tax return filing requirements don't change. The debtor-in-possession, or court-appointed trustee, must

file the entity's income tax returns on Form 1065, Form 1120, or Form 1120-S.

In cases where a trustee isn't appointed, the debtor-in-possession continues business operations and remains in possession of the business' property during the bankruptcy proceeding. The debtor-in-possession, rather than the general partner of a partnership or corporate officer of a corporation, assumes the fiduciary responsibility to file the business' tax returns.

## **Partnerships**

The filing requirements for a partnership in a bankruptcy proceeding don't change. However, the responsibility to file the required returns becomes that of the trustee, or debtor-in-possession.

A partnership's debt that is canceled as a result of the bankruptcy proceeding isn't included in the partnership's income. However, it may or may not be included in

the individual partner's income. See *Partnerships*, later, under *Debt Cancellation*.

## **Corporations**

The filing requirements for a corporation in a bankruptcy proceeding also don't change. A bankruptcy trustee, or debtor-in-possession, having possession of or holding title to substantially all of the property or business operations of the debtor corporation, must file the debtor's corporate income tax return for the tax year.



*The following discussion only highlights bankruptcy tax rules applying to corporations. The complex details of corporate bankruptcy reorganizations are beyond the scope of this publication. Therefore, you may wish to seek the help of a professional tax advisor. See Corporations under Debt Cancellation, later, for information about a corporation's debt canceled in a bankruptcy proceeding.*

## **Tax-Free Reorganizations**

The tax-free reorganization provisions of the Internal Revenue Code allow a corporation to transfer all or part of its assets to another corporation in a bankruptcy under title 11 of the United States Code. However, under the reorganization plan, the stock or securities of the corporation to which the assets are transferred must be distributed in a transaction that qualifies under Internal Revenue Code section 354, 355, or 356.

Generally, Internal Revenue Code section 354 provides that no gain or loss is recognized if a corporation's stock is exchanged solely for stock or securities in a corporation that is a party to the reorganization under a qualifying reorganization plan. In this case, shareholders in the bankrupt corporation would recognize no gain or loss if they exchange their stock solely for stock or securities of the corporation acquiring the bankrupt corporation's assets.

Internal Revenue Code section 355 generally provides that no gain or loss is recognized by a shareholder if a corporation distributes solely stock or securities of another corporation that the distributing corporation controls immediately before the distribution.

Internal Revenue Code section 356 allows tax-free exchanges in situations that would qualify under Internal Revenue Code section 354 or 355, except that other property or money, in addition to the permitted stock or securities, is received by the shareholder. In this situation, gain is recognized by the shareholder, but only to the extent of the money and the FMV of the other property received. No loss is recognized in this situation.

## **Exemption From Tax Return Filing**

A trustee in a corporate bankruptcy case may apply to the IRS for relief from filing federal income tax returns for the corporation. To

qualify, the corporation must have ceased business operations and have no assets or income for the tax year. The exemption request must be submitted to the local IRS Insolvency Office handling the case.

The request to the IRS must include the name, address, and EIN of the corporation and a statement of the facts (with any supporting documents) showing why the debtor needs relief from the filing requirements. The request must also include the following statement:

"I hereby request relief from filing federal income tax returns for tax years ending \_\_\_\_\_ for the above-named corporation and declare under penalties of perjury that to the best of my knowledge and belief the information contained herein is correct."

The statement must be signed by the trustee. The IRS will act on your request within 90 days.

**Disclosure of return information to trustee.** Upon written request, current and earlier returns of the debtor are open to inspection by or disclosure to the trustee. However, in bankruptcy cases other than those of individuals filing under chapter 7 or 11, such as a corporate bankruptcy, the IRS must find that the trustee has a material interest that will be affected by information on the return. Material interest is generally defined as a financial or monetary interest. Material interest isn't limited to the trustee's responsibility to file a return on behalf of the bankruptcy estate.

## **Receiverships**

Court-established receiverships sometimes arise in connection with bankruptcies. Certain court-established receiverships should be treated as qualified settlement funds (QSFs) for purposes of Internal Revenue Code section 468B and the underlying Treasury regulations. QSFs are required to file an

annual income tax return, Form 1120-SF, U.S. Income Tax Return for Settlement Funds. More information about QSFs may be found in Treasury Regulations sections 1.468B-1 through -5.

## **Determination of Tax**

The determination of the proper amount of tax due for a tax year begins with the bankruptcy estate's filing of Form 1041, and the individual debtor's filing of Form 1040 or 1040-SR, or for bankrupt entities filing Forms 1065, 1120, or 1120-S. After a return is filed, the IRS will either accept the return as filed or select the return for examination. Under examination, the IRS may redetermine the tax liability shown on the return. If the bankruptcy estate or debtor disagrees with the redetermined tax due, the tax as redetermined by the IRS may be contested in the bankruptcy court, or Tax Court, as applicable. See *Court Jurisdiction Over Tax Matters*, later.

# Prompt Determination Requests

Pursuant to Revenue Procedure 2006-24, 2006-22 I.R.B. 943, available at [IRS.gov/irb/2006-22\\_IRB/ar12](https://www.irs.gov/irb/2006-22_IRB/ar12), as modified by Announcement 2011-77, available at [IRS.gov/irb/2011-51\\_IRB/ar13](https://www.irs.gov/irb/2011-51_IRB/ar13), the bankruptcy trustee may request a determination of any unpaid tax liability incurred by the bankruptcy estate during the administration of the case, by filing a tax return and a request for such determination with the IRS. Unless the return is fraudulent or contains a material misrepresentation, the estate, trustee, debtor, and any successor to the debtor are discharged from liability upon payment of the tax:

1. As determined by the IRS;
2. As determined by the bankruptcy court, after completion of the IRS examination; or

3. As shown on the return, if the IRS does not:
  - a. Notify the trustee within 60 days after the request for determination that the return has been selected for examination, or
  - b. Complete the examination and notify the trustee of any tax due within 180 days after the request (or any additional time permitted by the bankruptcy court).

**Making the request for determination.** As detailed in Revenue Procedure 2006-24, as modified by Announcement 2011-77, to request a prompt determination of any unpaid tax liability of the estate, the trustee must file a signed written request, in duplicate, with the IRS. **The trustee should send the request using the preferred method by fax to: 844-250-2035.** This fax number is **only** for prompt packages. No other items should be faxed to this number. The trustee

can also mail the request to the following address, marked "Request for Prompt Determination".

Internal Revenue Service  
Centralized Insolvency Operation  
P.O. Box 7346  
Philadelphia, PA 19101-7346

The request must be submitted in duplicate and must be executed under penalties of perjury. In addition, the trustee must submit along with the request an exact copy of the return(s) filed by the trustee with the IRS for each completed tax period. The request must contain the following information.

- A statement indicating that it is a Request for Prompt Determination of Tax Liability, specifying the type of return and tax period for each return being filed.
- The name and location of the office where the return was filed.

- The name of the debtor.
- Debtor's social security number, TIN, or EIN.
- Type of bankruptcy estate.
- Bankruptcy case number.
- Court where the bankruptcy case is pending.

The copy of the return(s) submitted with the request **must** be an exact copy of a valid return. A request for prompt determination will be considered incomplete and returned to the trustee if it is filed with a copy of a document that does not qualify as a valid return.



*To qualify as valid, a return must meet certain criteria, including a signature under penalties of perjury. A document filed by the trustee with the jurat stricken, deleted, or modified doesn't qualify as a valid return.*

**Examination of return.** The IRS will notify the trustee within 60 days from receipt of the request whether the return filed by the trustee has been selected for examination or has been accepted as filed. If the return is selected for examination, it will be examined as soon as possible. The IRS will notify the trustee of any tax due within 180 days from receipt of the application or within any additional time permitted by the bankruptcy court.

If a prompt determination request is incomplete, all the documents received by the IRS will be returned to the trustee by the assigned Field Insolvency Office with an explanation identifying the missing item(s) and instructions to re-file the request once corrected.

Once corrected, the request **must** be filed with the IRS at the Field Insolvency Office address specified in the correspondence

accompanying the returned incomplete request.

In the case of an incomplete request submitted with a copy of an invalid return document, the trustee must file a valid original return with the appropriate IRS office and submit a copy of that return with the corrected request when the request is re-filed.

**Note.** An incomplete request includes those submitted with a copy of a return form, the original of which does not qualify as a valid return.

The 60-day period to notify the trustee whether the return is accepted as filed or has been selected for examination does not begin to run until a complete request package is received by the IRS. The complete request package must be filed with the Field Insolvency Office specified by the IRS in its correspondence returning the incomplete request for the 60-day period to begin to run.