Internal Revenue Service

Number: **201240001**
Release Date: 10/5/2012

Index Number: 6050P.00-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PA:02
PLR-100404-12
Date:
July 05, 2012

Legend

Entity 1 =
Entity 2 =
Asset =
State X =
State Y =
Date 1 =
Date 2 =
Date 3 =
Date 4 =
Collection Remedy =

Dear :

This letter responds to the letter dated December 15, 2011, submitted on behalf of Entity 1, requesting a ruling that Entity 1 is not required to file Forms 1099-C with respect to the write-off of balances and charges pursuant to its settlement agreement because the discharge was not the result of an "identifiable event" listed in Treasury Regulation § 1.6050P-1(b)(2), but rather was required by operation of state law. For the reasons set forth below, we conclude that Entity 1 is required to comply with the reporting requirements of I.R.C. § 6050P because the discharge of indebtedness was the result of an identifiable event listed in Treas. Reg. § 1.6050P-1(b)(2).

Facts

Entity 1 is a financial institution chartered in State X that provides its members with thrift services such as checking and savings accounts, and other financial services. Entity 2 was a service company that offered retail sale installment contracts from Asset dealers

to financial institutions for the financing of the Assets and serviced those contracts including, when necessary, initiating default proceedings on behalf of the financial institution that held a security interest in the Asset. Entity 1 acquired various Asset loan installment contracts and retained Entity 2 for servicing, collection and enforcement of those contracts.

On Date 1, consumers in State Y filed a class action lawsuit against Entity 1 in the Circuit Court of State Y alleging violations of State Y law, including that the notices related to the Collection Remedy did not meet the statutory notice requirements. On Date 2, the case was removed to U.S. District Court, Western District of State Y. On Date 3, Entity 1 and the class plaintiffs signed a Settlement and Release Agreement (Agreement) settling the entire class action lawsuit. The Agreement provides, among other things, that Entity 1 shall close all accounts and write off any balances owed or claimed remaining as any deficiency on the loans, including judgment balances, that were the subject of the litigation.

The Agreement further provides for payments from Entity 1 to the class members out of a "Net Distributable Settlement Fund" provided by Entity 1. The Agreement states that all class members shall be responsible for paying any and all federal taxes due on payments made to them pursuant to the settlement. The Agreement provides that Entity 1 will request a Private Letter Ruling from the IRS supporting the parties' position that Entity 1 is not required to file information returns relating to the terms of the Agreement. The Notice of Proposed Class Action Settlement that Entity 1 sent to the class members states that the request for Private Letter Ruling would be made by Entity 1 in support of the parties' position that the class members are not obligated to report the amount of the deficiency write-off or judgment write-off received as part of the settlement.

Law & Analysis

Section 6050P of the Internal Revenue Code requires that an applicable entity report any discharges (in whole or in part) of indebtedness of any person in excess of $600.00. The report is to include the name, address and taxpayer identification number of each person whose indebtedness is discharged, the date of the discharge and the amount of indebtedness discharged. In addition, section 1.6050P-1(b)(2) of the Treasury Regulations provides that a discharge of indebtedness occurs if one of the following "identifiable events" takes place:

> (A) A discharge of indebtedness under title 11 of the United States Code (bankruptcy);
> (B) A cancellation or extinguishment of an indebtedness that renders a debt unenforceable in a receivership, foreclosure, or similar proceeding in a federal or state court, as described in section 368(a)(3)(A)(ii) (other than a discharge described in paragraph (b)(2)(i)(A) of this section);

> (C) A cancellation or extinguishment of an indebtedness upon the expiration of the statute of limitations for collection of an indebtedness, subject to the limitations described in paragraph (b)(2)(ii) of this section, or upon the expiration of a statutory period for filing a claim or commencing a deficiency judgment proceeding;
> (D) A cancellation or extinguishment of an indebtedness pursuant to an election of foreclosure remedies by a creditor that statutorily extinguishes or bars the creditor's right to pursue collection of the indebtedness;
> (E) A cancellation or extinguishment of an indebtedness that renders a debt unenforceable pursuant to a probate or similar proceeding;
> (F) A discharge of indebtedness pursuant to an agreement between an applicable financial entity and a debtor to discharge indebtedness at less than full consideration;
> (G) A discharge of indebtedness pursuant a decision by the creditor, or the application of a defined policy of the creditor, to discontinue collection activity and discharge debt; or
> (H) The expiration of the non-payment testing period, as described in paragraph (b)(2)(iv) of this section.

Out of the above events, only two have a potential bearing on the requested ruling. The first possible event, section 1.6050P-1(b)(2)(F), provides that an identifiable event exists when the applicable financial entity and debtor agree to discharge the indebtedness for less than full consideration. To establish consideration, there must be a performance or a return promised which has been bargained for by the parties. Restatement (Second) Contracts § 71(1) (1981). In this case, Entity 1 and the debtor-class members agreed to the entry of a judgment, approved and supervised by the court, that incorporates the parties' Agreement by which Entity 1 will write off all remaining debt balances as part of the overall settlement of the pending litigation. This appears, on its face, to be the identifiable event described in subsection (F) of the regulations.

The request for the PLR submitted on behalf of Entity 1 argues that the Agreement does not reflect a mere agreement of the parties. Entity 1 argues instead that the Agreement reflects the operation of the law of State Y. The law of State Y provides that, in a case where the Collection Remedy did not strictly comply with notice requirements, there is an absolute bar on collecting any remaining deficiency balances. The class members alleged that Entity 1 violated various aspects of the notice requirements in the presale notices sent to the class members as part of its Collection Remedy. The Agreement acknowledges that plaintiffs' claims are "premised on state law," which provides that collection of the deficiency balances may be barred without proper notice having been given to the debtors. The "Representations and Stipulations" section of the Agreement refers to a potential "Court's finding that there was a failure to send a pre-sale notice to each of the Class Members and/or that the pre-sale notices…failed to comply with [state law]." That language also is contained draft Preliminary Approval Order attached to the

Agreement as Exhibit B. The Agreement otherwise contains no admission or concession by Entity 1 with respect to the claims or defenses alleged in the litigation, including any alleged violation of federal, state or local law. The Agreement contains a specific denial of liability, "no admissions" paragraph, which states that the settlement is being entered into for the purpose of "avoiding the burdens, expense, and risk of further litigation."

Entity 1 contends that the application of state law and, specifically, the bar on collection of the deficiency balances, was "triggered by the judicial rulings which certified the matter as a class action and thereby made the deficiency bar available to all Class members." Entity 1, however, continued to pursue the litigation and assert its defenses to the complaint well after the certification of the class, including filing a motion for partial summary judgment. It was only by reaching a settlement agreement with the plaintiffs that Entity 1 gave up its disputed claims to the deficiency amounts.

The court order issued on Date 4 contains a finding that "there was a failure to send a pre-sale notice to each of the Class Members and/or that the pre-sale notices…failed to comply with [state law] such that [Entity 1] cannot collect any deficiency balances from the Class Members." This language is identical to the language referenced above that was contained in the draft Preliminary Approval Order attached to the Agreement as Exhibit B. Thus, the court finding of the bar on collection of remaining deficiency balances was at the behest of the parties, and was a component of the overall settlement of the litigation, as reflected in the Agreement. The fact that the terms of the settlement were reflected in the order does not serve to convert the forgiveness of the debt from being entered into voluntarily to one forced by operation of state law. The Agreement should be taken on its face, as an agreement between Entity 1 and the debtors to discharge the indebtedness at less than full consideration. Therefore, section 1.6050P-1(b)(2)(F) applies.

The second possible event, section 1.6050P-1(b)(2)(G), provides that a discharge of indebtedness exists where a creditor discontinues collection activity pursuant to a decision by the creditor or a defined policy of the creditor. According to section 1.6050P-1(b)(2)(iii), a creditor's defined policy includes both a written policy and the creditor's established business practice. In this case, the cancellation of indebtedness does not appear to have been as a result of any defined policy or business practice of Entity 1, but rather by its decision to discontinue collection action as part of settling the litigation. This decision appears to fall within subsection (G). In any event, regardless of whether subsection (G) of the regulation applies, the event set forth in regulation subsection (F), as set forth above, does apply and the section 6050P reporting requirements must be met.

Conclusion

Based solely on the information provided and the representations made, we conclude that Entity 1 is required to file Forms 1099-C with respect to the write-off of balances and charges pursuant to its settlement agreement because the discharge was the result of an identifiable event listed in section 1.6050P-1(b)(2) and not by operation of state law.[1]

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Ashton P. Trice
Chief, Branch 2
(Procedure & Administration)

Enclosures:
Copy of letter
Copy for section 6110 purposes

cc:

[1] The letter requesting the PLR by Entity 1 refers to the year 2011 as the relevant tax period; however, because the Agreement did not become final until 2012, the reporting requirement is for the year 2012.