

CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.
(Also Part I, §§ 61, 108, 451, 6041, 6050P; 1.1001-3)

Rev. Proc. 2013-16

SECTION 1. PURPOSE

This revenue procedure provides guidance to mortgage loan holders, loan servicers, and borrowers who are participating in the Department of the Treasury's (Treasury) and Department of Housing and Urban Development's (HUD) Home Affordable Modification Program[®] (HAMP[®]). Under HAMP, a borrower may be eligible for principal reduction of the outstanding balance of a qualifying mortgage pursuant to the program's Principal Reduction AlternativeSM (PRA). In appropriate cases, HAMP has been offering the PRA as part of a HAMP loan modification since the last quarter of 2010. Current plans call for HAMP to continue accepting new borrowers through the end of 2013. The Internal Revenue Service (Service) is providing this guidance to address the tax consequences for borrowers (HAMP-PRA borrowers) who are participating in the PRA and the reporting obligations for participating mortgage loan holders and servicers.

SECTION 2. BACKGROUND—HAMP AND THE HAMP PRINCIPAL REDUCTION ALTERNATIVE

.01 To help distressed borrowers lower their monthly mortgage payments, Treasury and HUD established HAMP for mortgage loans that are not owned or guaranteed by the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac). A description of the program can be found at www.makinghomeaffordable.gov.

.02 Under HAMP, a participating loan servicer, acting on behalf of the mortgage loan holder, must consider a sequence of modification steps for each eligible borrower's mortgage loan until the borrower's monthly payment is reduced to a monthly payment amount determined under the HAMP guidelines. These steps include a reduction in the mortgage loan's interest rate, an extension of the mortgage loan's term, and a reduction in the mortgage loan's principal balance.

.03 In some cases, the unpaid principal balance of the modified mortgage loan is divided into (1) an amount that bears stated interest and that is used to calculate the borrower's new monthly mortgage payment (the "Non-forbearance Portion"), and (2) a forbearance amount, which does not bear stated interest and on which periodic payments of stated principal are not required. The stated principal of the forbearance amount is due upon the earliest of the borrower's transfer of the property, payoff of the balance on the Non-forbearance Portion of the mortgage loan, or maturity of the mortgage loan. However, as noted in section 2.06 of this revenue procedure, a HAMP-PRA borrower sometimes may

not have to pay all or a portion of the forbearance amount. (The forbearance amount associated with a HAMP-PRA principal reduction is called the “PRA Forbearance Amount.”)

.04 If a mortgage loan is being considered for a HAMP modification and the amount owed on the mortgage loan is greater than 115 percent of the value of the property, then the servicer must consider whether principal reduction under PRA should be used as part of the HAMP modification.

.05 The first step toward a HAMP modification is a trial period plan, in which the borrower’s monthly mortgage payment is set at a monthly payment amount determined under the HAMP guidelines. The trial period plan effective date is the due date for the first of the reduced payments that are to be made under the trial period plan. (It is the first day of either the first or the second month after the servicer transmits the trial period notice to the borrower.) In general, the trial period is three months, and, during this period, the borrower must satisfy certain conditions before the changes to the terms of the mortgage loan become permanent (the “Trial Period Conditions”). Specifically, depending on the borrower’s trial period payment history, the borrower’s compliance with HAMP and servicer guidelines, and his or her satisfaction of all other Trial Period Conditions, the borrower will be offered a permanent modification of the terms of the mortgage loan, including monthly mortgage payments that are lower than those under the old mortgage loan. Until the effective date of a permanent modification, the terms of the existing mortgage loan continue to apply.

.06 After the mortgage loan is permanently modified under HAMP, if the modified mortgage loan is in good standing on the first, second, or third annual anniversary of the trial period plan effective date (the “Three-year Period”), the servicer must reduce the unpaid principal balance of the mortgage loan on the respective anniversary date by one-third of the initial PRA Forbearance Amount. (The servicer allocates the entire reduction to the remaining PRA Forbearance Amount.) In general, if a HAMP-PRA borrower’s mortgage loan is in good standing and if the HAMP-PRA borrower pays in full the Non-forbearance Portion of the mortgage loan prior to the reduction of the entire PRA Forbearance Amount, the servicer must reduce the remaining outstanding principal balance of the mortgage loan by the remaining PRA Forbearance Amount.

.07 In connection with every HAMP loan modification, the HAMP program administrator (acting on behalf of the federal government) provides incentives to the borrower, the servicer, and the investor (that is, the holder of the mortgage loan). If a HAMP loan modification includes a PRA principal reduction, the HAMP program administrator makes additional incentive payments to the investor. These additional incentives are called “PRA Investor Incentive Payments” and are generally spread over three years. The size of the PRA Investor Incentive Payments depends on the amount of principal reduced, the loan-to-value ratio at the time of the HAMP modification, and the loan’s payment history before the modification. The PRA Investor Incentive Payments range from 18 to 63 percent of the principal amounts reduced. For purposes of this revenue procedure, the excess of the initial PRA Forbearance Amount of a

mortgage loan over the aggregate PRA Investor Incentive Payments scheduled to be paid with respect to that loan is called the “PRA Adjusted Forbearance Amount.”

.08 A PRA Investor Incentive Payment is earned by the investor on each date on which the servicer reduces the unpaid principal balance of the mortgage loan by a portion of the PRA Forbearance Amount (generally, on the first three annual anniversaries of the trial period plan effective date).

.09 If a HAMP-PRA borrower’s early payment in full of the Non-forbearance Portion of the mortgage loan accelerates the reduction of the remaining PRA Forbearance Amount (described above in section 2.06 of this revenue procedure), the remaining PRA Investor Incentive Payments from the HAMP program administrator are also accelerated.

.10 If, prior to completion of the Three-year Period, a mortgage loan ceases to be in good standing because of the HAMP-PRA borrower’s payment history, then the remaining PRA Forbearance Amount is not further reduced and is due when the HAMP-PRA borrower transfers the property, the HAMP-PRA borrower refinances, or otherwise pays off the Non-forbearance Portion of the mortgage loan, or the mortgage loan matures.

SECTION 3. BACKGROUND—APPLICABLE PROVISIONS OF LAW

.01 Under § 61 of the Internal Revenue Code, except as otherwise provided in subtitle A, gross income means all income from whatever source derived, including income from discharge of indebtedness. See § 61(a)(12).

.02 Under § 1.1001-3 of the Income Tax Regulations, if a debt instrument undergoes a significant modification, then the modification results in an exchange of the original debt instrument for the modified debt instrument. In general, an agreement to change a term of a debt instrument is a modification at the time the borrower and holder enter into the agreement, even if the change in term is not immediately effective. However, if the change is conditioned on reasonable closing conditions, a modification occurs on the closing date of the agreement. See § 1.1001-3(c)(6).

.03 Under § 108(e)(10), in the case of a debt-for-debt exchange (including a deemed exchange under § 1.1001-3), the borrower is treated as having satisfied the original debt instrument with an amount of money equal to the issue price of the new debt instrument. If the amount of debt satisfied in this manner exceeds that issue price, the borrower realizes discharge of indebtedness income on the exchange. See also § 1.61-12(c).

.04 The issue price of a non-publicly traded debt instrument issued for non-publicly traded property generally reflects the amount of principal that the borrower is required to pay to the holder of the instrument. If a borrower has the ability to avoid paying certain amounts (including principal) without violating the terms of the instrument, the payment schedule for the instrument is generally determined based on an assumption that the borrower will avoid any requirement to make those payments. See, e.g., §§ 1.1272-1(c)(5) and 1.1274-2(d).

.05 Under § 108(a), gross income does not include any amount that but for § 108(a) would be includible in gross income by reason of the discharge (in

whole or in part) of a taxpayer's indebtedness if (1) the indebtedness discharged is qualified principal residence indebtedness that is discharged before January 1, 2014, or (2) the discharge occurs when the taxpayer is insolvent. Section 108(a)(1)(E) and 108(a)(1)(B). (Although § 108 contains other exclusions as well, this revenue procedure focuses on these two exclusions because they are the most likely to apply to the greatest number of HAMP-PRA borrowers.)

.06 Under §§ 108(h) and 163(h)(3)(B), qualified principal residence indebtedness is any indebtedness that is incurred by a borrower to buy, build, or substantially improve the borrower's principal residence and is secured by that residence.

.07 Qualified principal residence indebtedness also includes a loan secured by the borrower's principal residence that refinances qualified principal residence indebtedness, but only to the extent of the amount of the refinanced indebtedness. See §§ 108(h) and 163(h)(3)(B)(i).

.08 The maximum amount of discharged indebtedness that a borrower may exclude from gross income under the qualified principal residence indebtedness exclusion is \$2,000,000 (\$1,000,000 for a married individual filing a separate return). Under § 108(h)(4), if only part of the discharged indebtedness is qualified principal residence indebtedness, then the exclusion applies only to the amount of the discharged indebtedness that exceeds the amount of the loan (determined immediately before the discharge) that is *not* qualified principal residence indebtedness.

.09 Under § 108(a)(3), the insolvency exclusion applies to the lesser of the amount of the debt discharged or the amount by which the taxpayer is insolvent immediately before the discharge.

.10 Section 108(d)(3) provides that, for purposes of the insolvency exclusion, a taxpayer is insolvent to the extent that the taxpayer's total liabilities exceed the fair market value of all of the taxpayer's assets immediately before the discharge of indebtedness. Under § 108(a)(2)(C), the qualified principal residence indebtedness exclusion takes precedence over the insolvency exclusion when both exclusions apply to discharged indebtedness, unless the taxpayer elects to apply the insolvency exclusion.

.11 If an amount is excluded from gross income as a discharge of qualified principal residence indebtedness, the taxpayer must reduce the basis of the taxpayer's principal residence. See § 108(h)(1). If a discharged amount is excluded from gross income because the taxpayer was insolvent when the discharge occurred, the taxpayer must reduce certain tax attributes (possibly including basis). See § 108(b). For further discussion of income from the discharge of indebtedness, the qualified principal residence indebtedness exclusion, the insolvency exclusion, and other exclusions from gross income that may apply, see Publication 4681, *Canceled Debts, Foreclosures, Repossessions, and Abandonments (for Individuals)*.

.12 Taxpayers who exclude any discharged amounts from gross income report both the exclusion and the resulting reduction in basis or other tax attributes on Form 982, *Reduction of Tax Attributes Due to Discharge of*

Indebtedness (and Section 1082 Basis Adjustment). See Form 982 instructions and Publication 4681. This form is to be filed with the tax return for the taxable year in which the amount is discharged but is excluded from gross income.

.13 Governmental payments made to or on behalf of individuals or other persons are included within the broad definition of gross income under § 61 unless an exception applies. See Notice 2003-18, 2003-1 C.B. 699, and Rev. Rul. 79-356, 1979-2 C.B. 28. However, if disbursements are made by a governmental unit to individuals in the interest of the general welfare (that is, are generally based on individual or family need) and the disbursements do not represent compensation for services, then the amounts disbursed are excluded from the income of the recipient (general welfare exclusion). See Rev. Rul. 2005-46, 2005-2 C.B. 120, and Rev. Rul. 75-246, 1975-1 C.B. 24.

.14 Under § 451 and § 1.451-1(a), a taxpayer that uses the cash receipts and disbursements method of accounting includes income in gross income when the taxpayer actually or constructively receives the income.

.15 Section 6041 requires every person engaged in a trade or business (including the United States and its agencies) to (1) file an information return (Form 1099-MISC, *Miscellaneous Income*, is used for this purpose) for each calendar year in which the person makes, in the course of its trade or business, payments to another person of fixed or determinable income aggregating \$600 or more, and (2) furnish a copy of the information return to that other person. See § 6041(a) and (d) and § 1.6041-1(a)(1) and (b).

.16 Section 6050P requires applicable entities (including the United States and its agencies, financial entities, and any organization a significant trade or business of which is the lending of money) to (1) file an information return (Form 1099–C, *Cancellation of Debt*, is used for this purpose) for each calendar year in which it discharges indebtedness of another person of \$600 or more, and (2) furnish a copy of the information return to that other person. See § 6050P(a)-(c) and §§ 1.6050P-1(a) and 1.6050P-2(a) and (d).

.17 Section 6721 imposes penalties with respect to information returns required to be filed with the Service. These penalties apply in the case of a failure to timely file an information return, a failure to include all required information on the return, or the inclusion of incorrect information on the return. Section 6724(d)(1) includes Forms 1099–MISC and 1099–C in the term “information return.”

.18 Section 6722 imposes penalties with respect to payee statements required to be furnished to payees. These penalties apply in the case of a failure to timely furnish a payee statement, a failure to include all required information on the statement, or the inclusion of incorrect information on the payee statement. Section 6724(d)(2) includes in the term “payee statement” copies of Forms 1099–MISC and 1099–C that are required to be furnished to taxpayers.

SECTION 4. FEDERAL INCOME TAX TREATMENT

.01 Because a HAMP modification with a PRA principal reduction is a significant modification, it results in a deemed debt-for-debt exchange in which the HAMP-PRA borrower satisfies the old mortgage loan by issuing a new one.

See § 1.1001-3. At the time of the modification, therefore, under § 108 and this revenue procedure, the HAMP-PRA borrower realizes discharge of indebtedness income equal to any excess of the adjusted issue price of the old mortgage loan (which was satisfied in the deemed exchange) over the issue price of the new (post-modification) mortgage loan. See *also* § 61(a)(12) and § 1.61-12(c).

.02 A HAMP-PRA borrower has the ability to avoid payment of the PRA Adjusted Forbearance Amount. Because the HAMP-PRA borrower has this ability, that amount should not be taken into account in determining the issue price of the new mortgage loan. Because the issue price of the new mortgage loan does not include the PRA Adjusted Forbearance Amount, the PRA Adjusted Forbearance Amount contributes to the excess of the adjusted issue price of the old mortgage loan (which was satisfied in the deemed exchange) over the issue price of the new mortgage loan.

.03 On the other hand, the investor has not given up its right to receive the remainder of the PRA Forbearance Amount, because the HAMP program administrator is expected to make those payments on the HAMP-PRA borrower's behalf by making the PRA Investor Incentive Payments. Because the remainder of the PRA Forbearance Amount is payable in this manner, that remainder is included in the issue price of the new mortgage loan.

.04 The Trial Period Conditions are reasonable closing conditions that must be satisfied before the changes to the terms of the mortgage loan become permanent. Therefore, for purposes of § 1.1001-3, the date of the modification is the date of the permanent modification.

.05 Unless an exclusion applies, the HAMP-PRA borrower includes in gross income the discharge of indebtedness income described in section 4.01 of this revenue procedure for the taxable year in which the permanent modification occurs. Under certain conditions, however, section 6 of this revenue procedure permits a borrower to report the discharge of indebtedness under HAMP-PRA over the Three-year Period. The qualified principal residence indebtedness exclusion under § 108(a)(1)(E) and the insolvency exclusion under § 108(a)(1)(B) are two exclusions that may apply to the discharge.

.06 The PRA Investor Incentive Payment is treated as a payment on the mortgage loan by the HAMP program administrator on behalf of the HAMP-PRA borrower.

.07 To the extent that the HAMP-PRA borrower uses the property as the HAMP-PRA borrower's principal residence or the property is occupied by the HAMP-PRA borrower's legal dependent, parent, or grandparent without rent being charged or collected, the HAMP-PRA borrower excludes from his or her gross income under the general welfare exclusion the PRA Investor Incentive Payments that the HAMP program administrator makes to the investor in the mortgage loan. This is consistent with Rev. Rul. 2009-19, 2009-28 I.R.B. 111, which addressed the treatment of Pay-for-Performance Success Payments.

.08 To the extent that the HAMP-PRA borrower uses the property as a rental property or holds the property vacant and available for rent, the HAMP-PRA borrower includes PRA Investor Incentive Payments in gross income. If the HAMP-PRA borrower uses the cash receipts and disbursements method of

accounting, then the HAMP-PRA borrower includes a PRA Investor Incentive Payment in gross income in the taxable year in which it is applied as a payment on the HAMP-PRA borrower's mortgage loan.

.09 As described in section 2.09 of this revenue procedure, if a HAMP-PRA borrower pays in full the Non-forbearance Portion of the mortgage loan while the loan is in good standing and prior to completion of the Three-year Period, that payment accelerates both the reduction in the remaining PRA Forbearance Amount and the PRA Investor Incentive Payments from the HAMP program administrator. To the extent that the HAMP-PRA borrower is described in section 4.07 of this revenue procedure, the HAMP-PRA borrower excludes from his or her gross income under the general welfare exclusion the accelerated PRA Investor Incentive Payments. To the extent that the HAMP-PRA borrower is described in section 4.08 of this revenue procedure, the HAMP-PRA borrower includes in income in the year of the acceleration the remaining amount of the PRA Investor Incentive Payment.

SECTION 5. INFORMATION-REPORTING OBLIGATIONS

.01 Under § 6050P, the investor is required to file a Form 1099-C with respect to a borrower who realizes discharge of indebtedness of \$600 or more. A copy of this form is required to be furnished to the borrower.

.02 As stated in sections 4.01 and 4.04 of this revenue procedure, the HAMP-PRA discharge of indebtedness is realized at the time of the permanent modification of the mortgage loan.

.03 An investor is an applicable entity that is required under § 1.6050P-1 and this revenue procedure to issue a Form 1099-C for discharge of indebtedness. Under § 1.6050P-1(b)(2)(F), the permanent modification of a mortgage loan is an identifiable event. Identifiable events determine when Forms 1099-C have to be issued. Thus, the Form 1099-C is issued for the calendar year in which the permanent mortgage loan modification occurs. This rule under § 1.6050P-1(b)(2)(F) applies even if, under section 6 of this revenue procedure, the HAMP-PRA borrower chooses to treat the HAMP-PRA discharge as being realized at the times when the unpaid principal balance of the new mortgage loan is reduced.

.04 The investor (or the loan servicer acting on behalf of the investor) reports the full amount of the discharge on the Form 1099-C regardless of whether some or all of the amount is excludible from income under the qualified principal residence indebtedness exclusion, the insolvency exclusion, or any other exclusion that may apply. That discharged amount will generally be the PRA Adjusted Forbearance Amount (which does not include the amounts expected to be satisfied by PRA Investor Incentive Payments).

.05 To the extent that PRA Investor Incentive Payments are made on behalf of a HAMP-PRA borrower who is described in section 4.07 of this revenue procedure, the PRA Investor Incentive Payments are excluded from the gross income of the HAMP-PRA borrower, and thus they are not fixed or determinable income to the HAMP-PRA borrower. Under § 6041, these payments are not subject to information reporting. See Notice 2011-14, 2011-11 I.R.B. 544, 546.

.06 To the extent that PRA Investor Incentive Payments are made on behalf of a HAMP-PRA borrower who is described in section 4.08 of this revenue procedure, the PRA Investor Incentive Payments are includible in gross income as fixed or determinable income in the taxable year required by the HAMP-PRA borrower's method of accounting. The payment is subject to the information reporting requirements of § 6041, as described in section 3.15 of this revenue procedure. Accordingly, the HAMP program administrator is required to issue a Form 1099-MISC reporting the PRA Investor Incentive Payment.

SECTION 6. HAMP-PRA BORROWERS' REPORTING OF DISCHARGES OF INDEBTEDNESS UNDER HAMP-PRA

.01 In general. The HAMP-PRA program began in the last quarter of 2010, and since that time there has been uncertainty about whether the amount of the discharge of indebtedness should be reported in the year of the permanent modification or over the Three-year Period (when the unpaid principal balance on the new mortgage loan is reduced). As a result, some HAMP-PRA borrowers have been reporting the discharge of indebtedness under HAMP-PRA over the Three-year Period. Given the temporary nature of the program and the issuance of this guidance after participation in the program has begun, in the interests of equitable and sound tax administration, HAMP-PRA borrowers may report discharges of indebtedness under HAMP-PRA under the rules in this section 6. A HAMP-PRA borrower may choose to report discharges of indebtedness under HAMP-PRA pursuant to the rules in this section 6 only if the borrower applies the same borrower option under section 6.02 of this revenue procedure consistently

to the taxable year of the permanent modification and to all subsequent taxable years. Thus, a HAMP-PRA borrower may not choose a borrower option under section 6.02 of this revenue procedure if a statute of limitations has expired for any of the taxable years that are necessary for consistent application of that option.

.02 HAMP-PRA borrower options. A HAMP-PRA borrower may treat the HAMP-PRA discharge as being realized in either of the following ways—

(1) One hundred percent of the PRA Adjusted Forbearance Amount at the time of the permanent modification; or

(2) One third of the PRA Adjusted Forbearance Amount on each of the first three annual anniversaries of the trial period plan effective date (described in section 2.06 of this revenue procedure), when, as required by the terms of the new mortgage loan, the servicer reduces the unpaid principal balance of the new mortgage loan. If some or all of the reduction in the unpaid principal balance is accelerated (as described in section 2.06 of this revenue procedure) because the HAMP-PRA borrower prepays the Non-forbearance Portion of the mortgage loan, then the HAMP-PRA discharge represented by the amount of the reduction that was accelerated is treated as being realized at the time of the accelerated reduction.

.03 HAMP-PRA borrowers who choose to realize the HAMP-PRA discharge at the time of the permanent modification.

(1) If a HAMP-PRA borrower chooses to treat the HAMP-PRA discharge as being realized at the time of the permanent modification, then for the taxable

year in which the permanent modification occurs, the HAMP-PRA borrower reports on Form 982 the amount, if any, of the discharge that is excluded from gross income and includes in gross income any remaining discharge.

(2) If a HAMP-PRA borrower's mortgage loan was permanently modified under HAMP in 2010 or 2011, and if the borrower was reporting the discharge of indebtedness using the method described in section 6.02(2) of this revenue procedure, then the borrower may change to reporting the discharge of indebtedness using the method described in section 6.02(1) of this revenue procedure by filing a 2012 Form 982 with the borrower's timely filed (with extensions) 2012 income tax return. This section 6.03(2) applies only if the change to reporting the discharge using the method described in section 6.02(1) of this revenue procedure does not change the borrower's federal income tax liability (including any change in federal income tax liability due to a change in basis or tax attributes (under § 108(h)(1) or § 108(b))) for any taxable year prior to the borrower's 2012 taxable year. To make this change, the borrower must—

(i) Compute the amount of discharge of indebtedness that would be included in income under § 61(a)(12) or excluded from gross income under § 108, basing the computation of the discharge on the facts as of the year of the permanent modification; and

(ii) Report on a 2012 Form 982 the reduction in basis or tax attributes (under § 108(h)(1) or § 108(b)) due to the permanent modification that the borrower would have reported on the Form 982 for the taxable year of the

permanent modification, minus any reductions due to the permanent modification that the borrower actually reported on Forms 982 for taxable years prior to 2012.

(3) Example. The following example illustrates the application of section 6.03(2) of this revenue procedure.

In 2010, B's basis in B's principal residence was \$330,000. In 2010, B's mortgage loan on the principal residence is permanently modified under HAMP-PRA. B realized \$30,000 of cancellation of indebtedness from the permanent modification, all of which qualifies for the exclusion from income for qualified principal residence indebtedness under § 108(a)(1)(E). The trial period plan effective date also fell in 2010.

B's federal income tax return for 2010 was consistent with B's reporting this discharge of indebtedness using the method described in section 6.02(2) of this revenue procedure. That is, B's 2010 return did not include income from discharge of indebtedness under HAMP-PRA, nor did the return contain a Form 982 reporting exclusion of any such discharge of indebtedness. The next year, B reported on line 10(b) of the 2011 Form 982 that B filed with B's 2011 federal income tax return a \$10,000 reduction in basis in the principal residence.

For 2012, B chooses to change to reporting the discharge of indebtedness using the method described in section 6.02(1) of this revenue procedure. Thus, B files a 2012 Form 982 with B's timely filed (including extensions) 2012 federal income tax return, and on line 10(b) of that form, B reports a \$20,000 basis reduction in the principal residence (\$30,000 basis reduction that B would have excluded from income in 2010 using the method described in section 6.02(1) of this revenue procedure, minus the \$10,000 basis reduction that B reported on B's 2011 Form 982).

(4) If a HAMP-PRA borrower reports the entire HAMP-PRA discharge using the method described in section 6.02(1) of this revenue procedure, and if that HAMP-PRA borrower's mortgage loan ceases to be in good standing during the Three-year Period as described in section 2.10 of this revenue procedure, then some or all of the anticipated reductions in the PRA Adjusted Forbearance Amount will not take place. Because the amount of these anticipated reductions was not included in determining the issue price of the new mortgage loan that,

pursuant to § 1.1001-3, the HAMP-PRA borrower is deemed to issue in satisfaction of the old mortgage loan, the issue price of the new mortgage loan was understated. Under these circumstances, the discharge of indebtedness income determined as of the date of the permanent modification will have been overstated.

(5) The Service will not challenge a HAMP-PRA borrower who is described in section 6.03(4) of this revenue procedure and who takes the following corrective measures:

(i) If a HAMP-PRA borrower included any of the discharge of indebtedness in gross income, the HAMP-PRA borrower may file an amended return that does not include the amount of the discharge of indebtedness that was previously reported as gross income but that, because of the HAMP-PRA borrower's failure to keep the new mortgage loan in good standing, was not ultimately discharged. The amended return should be for the taxable year in which the income was included (that is, the year of the permanent modification), provided the applicable statute of limitations remains open for that taxable year.

(ii) If the HAMP-PRA borrower did not include any of the discharge of indebtedness in gross income (that is, if the HAMP-PRA borrower excluded all of it), the HAMP-PRA borrower may file a new Form 982 that the Service will treat as superseding the earlier Form 982. The new Form 982 will reflect the revised reduction in basis or in tax attributes (under § 108(h)(1) or § 108(b)). The new Form 982 should be the

Form 982 for the year of the permanent modification and should be filed with the return for the taxable year in which the HAMP-PRA borrower's mortgage loan ceased to be in good standing.

.04 HAMP-PRA borrowers who choose to treat the HAMP-PRA discharge as being realized on the dates on which the unpaid principal balance of the mortgage loan is reduced.

(1) If a HAMP-PRA borrower chooses to realize the HAMP-PRA discharge at the times that the unpaid principal balance on the new mortgage loan is reduced, instead of at the time of the permanent modification, then the HAMP-PRA borrower's federal income tax returns for the taxable year that contains the permanent modification and for the subsequent taxable years must not treat any of the discharge as being realized at the time of the permanent modification and must treat the entire HAMP-PRA discharge as being realized in the amounts—and at the times—of the reductions in the unpaid principal balance. Except as described in the last sentence of this paragraph, therefore, the income tax return for the year of the permanent modification must include no gross income from—nor report on Form 982 an exclusion of—any amount of the HAMP-PRA discharge. Instead, the HAMP-PRA discharge is included in gross income (or is reported on Form 982 as excluded from gross income) in the subsequent years in which the unpaid principal balance is reduced. If the first such reduction occurs in the year of the permanent modification, however, then the amount of any such reduction is reflected as an inclusion or exclusion on the federal income tax return for that year.

(2) A HAMP-PRA borrower who has been using the method described in section 6.02(1) of this revenue procedure may change to the method described in section 6.02(2) but must comply with the consistency and open-year requirements described in section 6.01 of this revenue procedure.

SECTION 7. PENALTY RELIEF FOR 2012

.01 The Service will not assert penalties under § 6721 or § 6722 against an investor for failing to timely file and furnish a 2012 Form 1099-C as required by section 5.03 through 5.04 and section 8.02 of this revenue procedure with respect to discharge of indebtedness resulting from HAMP-PRA permanent modifications that take place during calendar year 2012 if the following requirements are satisfied:

(1) Not later than February 28, 2013, a statement is sent to the HAMP-PRA borrower containing the following:

(a) The HAMP-PRA borrower's name, address, and taxpayer identification number; and

(b) The date and amount of the discharge of indebtedness (as described in sections 4.01 through 4.04 of this revenue procedure) that is required to be reported for 2012.

(2) Not later than March 28, 2013, a statement is sent to the Service. It must be in the form of a single statement that separately lists for each HAMP-PRA borrower the information specified in section 7.01(1) of this revenue procedure. The statement should be sent to the Service at the following address:

Internal Revenue Service Center
Stop 6728AUSC
Austin, TX 73301

.02 The Service will not assert penalties under § 6721 or § 6722 with respect to any Forms 1099-MISC for 2012 that sections 5.06 and 8.02 of this revenue procedure require to be filed with the Service and furnished to taxpayers.

.03 Section 8.03 and 8.04 of this revenue procedure, below, describes penalty relief regarding Forms 1099-C and 1099-MISC for 2010 and 2011.

SECTION 8. SCOPE AND EFFECTIVE DATE

.01 This revenue procedure applies to all borrowers, investors, and servicers who participate, or have participated, in the HAMP-PRA, regardless of when the permanent modification occurs.

.02 Section 5 of this revenue procedure is effective for Forms 1099-C and 1099-MISC due or filed after January 24, 2013.

.03 Because of the effective date in section 8.02 of this revenue procedure, an investor is not subject to penalties under § 6721 or § 6722 on the grounds that the investor failed to timely file and furnish a 2010 or 2011 Form 1099-C as described in section 5.03 through 5.04 of this revenue procedure (or on the grounds that the investor filed or furnished a 2010 or 2011 Form 1099-C that is inconsistent with section 5.03 through 5.04 of this revenue procedure), provided that the investor demonstrates a good faith attempt to comply with the requirements of § 6050P and that the failure was not due to willful neglect.

.04 Because of the effective date in section 8.02 of this revenue procedure, the Service will not assert penalties under § 6721 or § 6722 on the grounds of a failure to timely file and furnish a 2010 or 2011 Form 1099-MISC, as described in section 5.06 of this revenue procedure.

SECTION 9. DRAFTING INFORMATION

The principal authors of this revenue procedure are Ronald J. Goldstein of the Office of Chief Counsel (Procedure and Administration); Shareen S. Pflanz and Sheldon A. Iskow of the Office of Chief Counsel (Income Tax and Accounting); and Andrea M. Hoffenson of the Office of Chief Counsel (Financial Institutions and Products). For further information regarding this revenue procedure contact Procedure and Administration branch 1 at (202) 622-4910, Income Tax and Accounting branch 4 at (202) 622-4920, or Financial Institutions and Products branch 1 at (202) 622-3920 (not toll free calls).