



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

U.I.L.# 108.01-02

CC:DOM:IT&A:3CFKane
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This is in reference to your letter of May 2, 2000, in which you inquired about the insolvency exclusion available under section 108(a)(1)(B) of the Internal Revenue Code, and the requirement that tax attributes be reduced pursuant to section 108(b).

A taxpayer who claims the insolvency exclusion is required to reduce attributes under section 108(b), but only to the extent of those attributes. If the income arising from the discharge of indebtedness exceeds the amount of the taxpayer's attributes listed in section 108(b), the excess amount may still be eligible to be excluded from gross income. The exclusion applies up to the amount of the taxpayer's insolvency, not to the amount of the taxpayer's attributes.

Section 108(d)(3) states that insolvency means the excess of the liabilities over the fair market value of assets immediately before the discharge.

Generally then, a taxpayer who receives a Form 1099-C reporting cancellation of indebtedness income and who was insolvent at the time of the discharge, may exclude the reported amount up to the amount of the taxpayer's insolvency. The taxpayer must then reduce attributes. The fact that the taxpayer does not have enough attributes to absorb all of the excluded amount has no bearing on the amount the taxpayer may exclude.

COR-109758-00

Thank you for your inquiry regarding this matter.

Sincerely,

Assistant Chief Counsel,
Income Tax & accounting

By _____
Christopher F. Kane
Assistant to the Branch Chief,
Branch 3