

## Notice of Proposed Rulemaking and Notice of Public Hearing

### Basis Reduction Due to Discharge of Indebtedness

REG-208172-91

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations that provide ordering rules for the reduction of bases of property under sections 108 and 1017 of the Internal Revenue Code of 1986. The regulations will affect taxpayers that exclude discharge of indebtedness from gross income under section 108.

DATES: Written comments must be received by April 7, 1997. Outlines of oral comments to be presented at the public hearing scheduled for April 24, 1997, at 10 a.m. must be received by April 3, 1997.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (REG-208172-91), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (REG-208172-91), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may submit comments electronically via the internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS internet site at [http://www.irs.ustreas.gov/prod/tax\\_regs/comments.html](http://www.irs.ustreas.gov/prod/tax_regs/comments.html).

FOR FURTHER INFORMATION CONTACT: Concerning the regulations generally, Sharon L. Hall or Christopher F. Kane of the Office of Assistant Chief Counsel (Income Tax & Accounting) at (202) 622-4930; concerning partnership adjustments under section 1017, Brian M. Blum of the Office of Assistant Chief Counsel (Passthroughs & Special Industries) at (202) 622-3050; concerning submissions and the hearing, Evangelista C. Lee of the Regulations Unit at (202) 622-7190 (not toll-free numbers).

## SUPPLEMENTARY INFORMATION:

### *Paperwork Reduction Act*

The collections of information contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)).

Comments on the collections of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, T:FP, Washington, DC 20224. Comments on the collections of information should be received by March 8, 1997. Comments are specifically requested concerning:

Whether the proposed collections of information are necessary for the proper performance of the functions of the **Internal Revenue Service**, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collections of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collections of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of service to provide information.

The collections of information in this proposed regulation are in §§ 1.108-4(b), 1.1017-1(e)(2), and 1.1017-1(f)(2)(ii) and (iii). This information is required for a taxpayer to elect to reduce the adjusted bases of depreciable property under section 108(b)(5), to elect to treat section 1221(1) real property as either depreciable property or depreciable real property, and to account for a partnership interest as either depreciable property or depreciable real property. This information will be used to determine whether taxpayers have properly reduced the bases of their properties. The collections of information are

required to obtain a benefit. The likely respondents are individuals, farms, businesses or other for-profit institutions, and small businesses or organizations.

Estimated total annual reporting burden: *100,000* hours.

Estimated average annual burden per respondent: *1* hours.

Estimated number of respondents: *100,000*.

Estimated annual frequency of responses: *On occasion*.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

### *Background*

This notice contains proposed amendments to the income tax regulations (26 CFR Parts 1 and 301) under sections 108 and 1017 of the Internal Revenue Code of 1986 (Code). The amendments are proposed to conform the regulations to amendments to sections 108 and 1017 made by the Bankruptcy Tax Act of 1980, Pub. L. 96-589, § 2, 94 Stat. 3389 (1980), 1980-2 C.B. 607 (Bankruptcy Tax Act); the Technical Corrections Act of 1982, Pub. L. 97-448, § 102(h)(1), 96 Stat. 2365, 2372 (1983), 1983-1 C.B. 451; the Deficit Reduction Act of 1984, Pub. L. 98-369, §§ 474(r)(5) and 721(b)(2), 98 Stat. 494, 839, 966 (1984), 1984-3 C.B. (Vol. 1) 1; the Tax Reform Act of 1986, Pub. L. 99-514, §§ 104(b)(2), 231(d)(3)(D), 822, and 1171(b)(4), 100 Stat. 2085, 2105, 2179, 2373, 2513 (1986), 1986-3 C.B. (Vol. 1) 2; and the Omnibus Budget Reconciliation Act of 1993, Pub. L. 103-66, § 13150, 107 Stat. 312, 446 (1993), 1993-3 C.B. 1.

In general, section 108 excludes from gross income discharges of indebtedness if the discharge occurs in a title 11 case or when the taxpayer is insolvent, or if the indebtedness is "qualified farm indebtedness" or "qualified real property business indebtedness." Taxpayers generally must reduce specified tax attributes, including adjusted bases of properties, to the extent income from

discharge of indebtedness is excluded from gross income under section 108. Section 1017 provides rules regarding any basis reductions required by, or elected under, section 108.

### *Explanation of Provisions*

#### *Overview*

The legislative history of the Bankruptcy Tax Act states that the exclusion of discharge of indebtedness (COD income) from gross income under section 108 is intended to promote a debtor's fresh start. S. Rep. No. 1035, 96th Cong., 2d Sess. 10 (1980), 1980-2 C.B. 620, 624; H.R. Rep. No. 833, 96th Cong., 2d Sess. 11 (1980). The exclusion provided by the statute generally operates, however, to defer, rather than eliminate, income from discharge of indebtedness.

The deferral of income provided by statute is generally achieved by requiring a taxpayer to reduce specified tax attributes (including adjusted bases of property) under section 108(b) by an amount equal to the COD income excluded from gross income under section 108(a). Section 108(b)(2) requires a taxpayer to reduce tax attributes in the following order: (A) net operating loss; (B) general business credit; (C) minimum tax credit; (D) capital loss carryovers; (E) adjusted bases of property; (F) passive activity loss and credit carryovers; and (G) foreign tax credit carryovers. If the excluded COD income exceeds the sum of the taxpayer's tax attributes, the excess is permanently excluded from the taxpayer's gross income.

When basis reductions are necessary, section 1017(a) requires the taxpayer to reduce the adjusted bases of property held on the first day of the following tax year. Section 1017(b)(1) provides that the amount of the basis reduction required under section 1017(a), and the particular properties the bases of which are to be reduced, shall be determined under regulations.

#### *General Rules for Basis Reduction*

Consistent with the legislative history of the Bankruptcy Tax Act, the proposed regulations generally retain the "tracing" approach of the existing regulations issued under prior law. Thus, the proposed regulations require a taxpayer to reduce the adjusted basis of the property that secured the discharged indebtedness before reducing the adjusted bases of other property.

In addition, the proposed regulations modify the categories in the existing regulations to simplify the process of basis reduction. First, the distinction between purchase-money indebtedness and other secured indebtedness is eliminated. Second, the order of basis reduction for property that secured discharged indebtedness is changed. Thus, the first category of the general ordering rule is real property used in the taxpayer's trade or business or held for the production of income (other than section 1221(1) real property) that secured the discharged indebtedness, and the second category is personal property used in the taxpayer's trade or business or held for the production of income (other than inventory, accounts receivable, and notes receivable) that secured the discharged indebtedness. Therefore, if an indebtedness secured by a building, a parcel of land used in the taxpayer's trade or business, office equipment, and office furniture is discharged, the taxpayer proportionately reduces the adjusted bases of the building and the parcel of land, based upon their relative adjusted bases, to the full extent of the excluded COD income before reducing the adjusted bases of the office equipment and the office furniture. The IRS and Treasury Department believe that this modification of the current regulations will simplify the process of basis reduction for many taxpayers.

#### *Special Rules for Depreciable Properties*

Instead of reducing tax attributes in the order specified by section 108(b)(2), a taxpayer may elect under section 108(b)(5) first to reduce the adjusted bases of depreciable property (real and personal) to the extent of the excluded COD income. If the adjusted bases of depreciable property are insufficient to offset the entire amount of excluded COD income, the taxpayer must reduce any remaining tax attributes in the order specified in section 108(b)(2). Section 108(c) requires that excluded COD income from the cancellation of qualified real property business indebtedness must be applied against depreciable real property.

Section 1017(b)(3)(C) provides that a taxpayer must treat a partnership interest as depreciable property when reducing adjusted bases under section 108(b)(5), and as depreciable real property when reducing adjusted bases under section 108(c), to the extent the partnership correspondingly reduces the partner's

proportionate interest in the adjusted bases of depreciable property (or depreciable real property) held by the partnership (inside basis).

The proposed regulations generally provide that a taxpayer may freely choose whether or not to request that a partnership reduce the partner's share of depreciable basis in partnership property and thereby permit the taxpayer to treat the partnership interest as depreciable property (or depreciable real property). In addition, the proposed regulations generally provide that the partnership is free to grant or deny its consent. In order to prevent avoidance of the general ordering rules of the proposed regulations through the use of partnerships, however, a partner is required to request consent if the partner owns (directly or indirectly) more than 50 percent of the capital and profits interests of the partnership, or if the partner receives a distributive share of COD income from the partnership. In addition, the partnership is required to grant consent if requests are made by partners owning (directly or indirectly) an aggregate of more than 50 percent of the capital and profits interests of the partnership.

The proposed regulations provide that a partner requesting a reduction in inside basis must make the request before the due date (including extensions) for filing the partner's Federal income tax return for the taxable year in which the partner has COD income. A partnership that consents to a basis reduction must include a consent statement with its Form 1065, U.S. Partnership Return of Income, and must also provide a copy of that statement to the affected partner on or before the date the Form 1065 is filed. The IRS and Treasury Department recognize that under current law a partner may not always have sufficient information with which to decide to request a basis reduction until on, or shortly before, the due date (including extensions) for filing the partner's tax return. For example, for calendar year taxpayers, a partner's tax return and a partnership's Form 1065 are generally due on the same day. *See* sections 6031 and 6072. Comments are requested as to whether additional rules (such as requiring a partnership to inform partners of COD income prior to the date the Form 1065 is filed) are necessary to ensure that information is exchanged between the partnership and its partners in a timely fashion.

The proposed regulations remove § 301.9100-13T, which governs elec-

tions under section 108(b)(5), and add new proposed § 1.108-4. Under the temporary regulations, a taxpayer is required to make the election with the taxpayer's Federal income tax return for the taxable year in which the discharge occurs, but is permitted to file an election with an amended return, or claim for credit or refund, if the taxpayer establishes reasonable cause for failing to file the election with the original return. New proposed § 1.108-4 requires the taxpayer to make the election on the timely filed (including extensions) Federal income tax return for the taxable year the taxpayer has COD income that is excluded under section 108(a). Therefore, a taxpayer that fails to make the election on that return must request the Commissioner's consent to file a late election under § 301.9100-3T or any regulations that supersede § 301.9100-3T.

### *Special Analyses*

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required.

Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

### *Initial Regulatory Flexibility Act Analysis*

This initial analysis is required under the Regulatory Flexibility Act (5 U.S.C. chapter 6). In certain circumstances, the proposed regulations will require a partnership to include a statement with its Form 1065, U.S. Partnership Return of Income, and provide a copy of that statement with the taxpayer's Schedule K-1 (Form 1065), Partner's Share of Income, Credits, Deductions, etc., for the taxable year in which the COD income is excluded under section 108(a), stating the amount of the partner's share of the reduction in the partnership's adjusted bases of depreciable real or personal property (inside basis). This requirement will ensure that the partner knows it is entitled to reduce the adjusted basis of the partnership interest and that the affected partnership knows it must reduce the partner's interest in inside basis. The legal basis for

this requirement is contained in sections 1017(b), 6001, and 7805(a).

Though the proposed regulations might affect any partnership owning depreciable property, the IRS and Treasury Department believe that partnerships owning depreciable real property are the most likely to be affected. Approximately 1,560,000 partnership returns were filed for 1993. Approximately 620,000 of these were for partnerships owning real property. It is unlikely, however, that many of these partnerships will be affected by the proposed regulations in any given year.

After a partner conveys information concerning the amount of COD income excluded from gross income under section 108(a) to the affected partnership, the partnership must reduce the partner's interest in inside basis. Accordingly, the partnership must prepare and maintain special entries on its books because this basis reduction will reduce the partner's share of the partnership's depreciation deductions, and ultimate gain or loss on the sale of the property, in subsequent years. In many cases, partnership returns are prepared using computer software that can prepare and maintain these special entries after the initial year.

The IRS and Treasury Department are not aware of any federal rules that may duplicate, overlap, or conflict with the proposed rule.

As an alternative to the disclosure described above, the IRS and Treasury Department considered, but rejected as too burdensome, a rule that would have required an affected partnership to disclose the reductions of adjusted basis on a property-by-property basis. There are no known alternative rules that are less burdensome to small entities but that accomplish the purpose of the statute. The IRS and Treasury Department request comments from small entities concerning possible alternatives.

### *Comments and Public Hearing*

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying.

A public hearing has been scheduled for April 29, 1997, at 10 a.m. in IRS Auditorium, 7th Floor, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC. Because of access restrictions, visitors will not be

admitted beyond the Internal Revenue Building lobby more than 15 minutes before the hearing starts.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons that wish to present oral comments at the hearing must submit written comments by April 7, 1997 and submit an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by April 3, 1997.

A period of 10 minutes will be allotted to each person for making comments.

An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

### *Drafting Information*

The principal author of these regulations is Leo F. Nolan II, Office of Assistant Chief Counsel (Income Tax and Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

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### *Proposed Amendments to the Regulations*

Accordingly, 26 CFR parts 1 and 301 are proposed to be amended as follows:

#### **PART 1—INCOME TAXES**

Paragraph 1. The authority citation for 26 CFR part 1 is amended by adding entries in numerical order to read as follows:

Authority: 26 U.S.C. 7805 \* \* \*

Section 1.108-4 also issued under 26 U.S.C. 108.

Section 1.108-5 also issued under 26 U.S.C. 108.

Section 1.1017-1 also issued under 26 U.S.C. 1017.

#### **§ 1.108(a)-1 [Removed]**

Par. 2. Section 1.108(a)-1 is removed.

#### **§ 1.108(a)-2 [Removed]**

Par. 3. Section 1.108(a)-2 is removed.

#### **§ 1.108(b)-1 [Removed]**

Par. 4. Section 1.108(b)-1 is removed.

## § 1.1016-7 [Removed]

Par. 5. Section 1.1016-7 is removed.

## § 1.1016-8 [Removed]

Par. 6-7. Section 1.1016-8 is removed.

## § 1.1017-2 [Removed]

Par. 8. Section 1.1017-2 is removed.

Par. 9. Section 1.108-4 is added to read as follows:

### § 1.108-4 Election to reduce basis of depreciable property under section 108(b)(5).

(a) *Description.* An election under section 108(b)(5) is available whenever a taxpayer excludes discharge of indebtedness (COD income) from gross income under sections 108(a)(1)(A), (B), or (C) (concerning title 11 cases, insolvency, and qualified farm indebtedness, respectively). See sections 108(d)(2) and (3) for the definitions of *title 11 case* and *insolvent*. See section 108(g)(2) for the definition of *qualified farm indebtedness*.

(b) *Time and manner.* To make an election under section 108(b)(5), a taxpayer must enter the appropriate information on Form 982, *Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)*, and attach the form to the timely filed (including extensions) Federal income tax return for the taxable year in which the taxpayer has COD income that is excluded from gross income under section 108(a). An election under this section may be revoked only with the consent of the Commissioner.

(c) *Effective date.* This section is effective for elections concerning discharges of indebtedness occurring on or after the date these regulations are published as final regulations in the **Federal Register**.

Par. 10. Section 1.108-5 is added to read as follows:

#### § 1.108-5 Limitations on the exclusion of income from the discharge of qualified real property business indebtedness

(a) *Indebtedness in excess of value.* The amount excluded from gross income under section 108(a)(1)(D) (concerning discharges of qualified real property business indebtedness) shall not exceed the excess, if any, of the out-

standing principal amount of that indebtedness immediately before the discharge over the net fair market value of the qualifying real property, as defined in § 1.1017-1(c)(1), immediately before the discharge. For purposes of this section, *net fair market value* means the fair market value of the qualifying real property (notwithstanding section 7701(g)) reduced by the outstanding principal amount of any other qualified real property business indebtedness secured by that property immediately before and after the discharge.

(b) *Overall limitation.* The amount excluded from gross income under section 108(a)(1)(D) shall not exceed the aggregate adjusted bases of all depreciable real property held by the taxpayer immediately before the discharge (other than depreciable real property acquired in contemplation of the discharge) reduced by the sum of any—

(1) Depreciation claimed for the taxable year the taxpayer excluded discharge of indebtedness from gross income under section 108(a)(1)(D); and

(2) Reductions to the adjusted bases of depreciable real property required under section 108(b) or section 108(g) for the same taxable year.

(c) *Effective date.* This section is effective for discharges of qualified real property business indebtedness occurring on or after the date these regulations are published as final regulations in the **Federal Register**.

Par. 11. Section 1.1017-1 is revised to read as follows:

#### § 1.1017-1 Basis reductions following a discharge of indebtedness

(a) *General rule for section 108(b)(2)(E).* This paragraph (a) applies to basis reductions under section 108(b)(2)(E) that are required by section 108(a)(1)(A) or (B) because the taxpayer excluded discharge of indebtedness (COD income) from gross income. A taxpayer must reduce in the following order, to the extent of the excluded COD income but not below zero, the adjusted bases of property held on the first day of the taxable year following the taxable year that the taxpayer excluded COD income from gross income (in proportion to adjusted basis):

(1) Real property used in a trade or business or held for investment, other than real property described in section 1221(1), that secured the discharged indebtedness immediately before the discharge (see paragraph (f)(1) of this

section for the treatment of partnership indebtedness as indebtedness secured by the taxpayer's interest in the partnership);

(2) Personal property used in a trade or business or held for investment, other than inventory, accounts receivable, and notes receivable, that secured the indebtedness immediately before the discharge (see paragraph (f)(1) of this section for the treatment of partnership indebtedness as indebtedness secured by the taxpayer's interest in the partnership);

(3) Remaining property used in a trade or business or held for investment, other than inventory, accounts receivable, notes receivable, and real property described in section 1221(1);

(4) Inventory, accounts receivable, notes receivable, and real property described in section 1221(1); and

(5) Property not used in a trade or business nor held for investment.

(b) *Operating rules—(1) Prior tax-attribute reduction.* The amount of excluded COD income applied to reduce basis does not include any COD income applied to reduce tax attributes under sections 108(b)(2)(A) through (D) and, if applicable, section 108(b)(5). For example, if a taxpayer excludes \$100 of COD income from gross income under section 108(a) and reduces tax attributes by \$40 under sections 108(b)(2)(A) through (D), the taxpayer is required to reduce the adjusted bases of property by \$60 (\$100 - \$40) under section 108(b)(2)(E).

(2) *Multiple discharged indebtednesses.* If a taxpayer has COD income attributable to more than one discharged indebtedness resulting in the reduction of tax attributes under sections 108(b)(2)(A) through (D) and, if applicable, section 108(b)(5), paragraph (b)(1) of this section must be applied by allocating the tax-attribute reductions among the indebtednesses in proportion to the amount of COD income attributable to each discharged indebtedness. For example, if a taxpayer excludes \$20 of COD income attributable to secured indebtedness A and excludes \$80 of COD income attributable to unsecured indebtedness B (a total exclusion of \$100), and if the taxpayer reduces tax attributes by \$40 under sections 108(b)(2)(A) through (D), the taxpayer must reduce the amount of COD income attributable to secured indebtedness A to \$12 (\$20 - (\$20 ÷ \$100 x \$40)) and must reduce the amount of COD income attributable to unsecured indebtedness B to \$48 (\$80 - (\$80 ÷ \$100 x \$40)).

(3) *Limitation on basis reductions under section 108(b)(2)(E) in bankruptcy or insolvency.* If COD income arises from a discharge of indebtedness in a title 11 case or while the taxpayer is insolvent, the amount of any basis reduction under section 108(b)(2)(E) shall not exceed the excess of—

(i) The aggregate of the adjusted bases of property and the amount of money held by the taxpayer immediately after the discharge; over

(ii) The aggregate of the liabilities of the taxpayer immediately after the discharge.

(c) *Modification of ordering rules for basis reductions under sections 108(b)(5) and 108(c)*—(1) *In general.* The ordering rules prescribed in paragraph (a) of this section apply, with appropriate modifications, to basis reductions under sections 108(b)(5) and (c). Thus, a taxpayer may reduce only the adjusted bases of depreciable property under section 108(b)(5) and may reduce only the adjusted bases of depreciable real property under section 108(c). Furthermore, for basis reductions under section 108(c), a taxpayer must reduce the adjusted basis of the qualifying real property to the extent of the discharged qualified real property business indebtedness before reducing the adjusted bases of other depreciable real property. The term *qualifying real property* means real property with respect to which the indebtedness is qualified real property business indebtedness within the meaning of section 108(c)(3). See paragraphs (e) and (f) of this section for elections relating to section 1221(1) property and partnership interests.

(2) *Partial basis reductions under section 108(b)(5).* If the amount of basis reductions under section 108(b)(5) is less than the amount of the COD income excluded from gross income under section 108(a), the taxpayer must reduce the balance of its tax attributes, including any remaining adjusted bases of depreciable property, under section 108(b)(2). For example, if a taxpayer excludes \$100 of COD income from gross income under section 108(a) and elects to reduce the adjusted bases of depreciable property by \$10 under section 108(b)(5), the taxpayer must reduce its remaining tax attributes by \$90 under section 108(b)(2).

(3) *Modification of fresh start rule for prior basis reductions under section 108(b)(5).* After reducing the adjusted bases of depreciable property under section 108(b)(5), a taxpayer must compute

the limitation on basis reductions under section 1017(b)(2) using the aggregate of the remaining adjusted bases of property. For example, if, immediately after the discharge of indebtedness in a title 11 case, a taxpayer's adjusted bases of property is \$100 and its undischarged indebtedness is \$70, and if the taxpayer elects to reduce the adjusted bases of depreciable property by \$10 under section 108(b)(5), section 1017(b)(2) limits any further basis reductions under section 108(b)(2)(E) to \$20 ( $[\$100 - \$10] - \$70$ ).

(d) *Changes in security.* Any change in the property securing an indebtedness during the one-year period preceding the discharge of that indebtedness shall be disregarded if a principal purpose of that change is to affect the taxpayer's basis reductions under section 1017.

(e) *Election to treat section 1221(1) real property as depreciable*—(1) *In general.* For basis reductions under sections 108(b)(5) and (g), a taxpayer may elect under sections 1017(b)(3)(E) and (4)(C), respectively, to treat real property described in section 1221(1) as depreciable property. This election is not available, however, for basis reductions under section 108(c).

(2) *Time and manner.* To make an election under section 1017(b)(3)(E) or (4)(C), a taxpayer must enter the appropriate information on Form 982, *Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)*, and attach the form to a timely filed (including extensions) Federal income tax return for the taxable year in which the taxpayer has COD income that is excluded from gross income under section 108(a). An election under this paragraph (e) may be revoked only with the consent of the Commissioner.

(f) *Partnerships*—(1) *Partnership COD income.* For purposes of paragraph (a) of this section, a taxpayer must treat a distributive share of a partnership's COD income as attributable to a discharged indebtedness secured by the taxpayer's interest in that partnership.

(2) *Partnership interest treated as depreciable property*—(i) *In general.* For purposes of making basis reductions, if a taxpayer makes an election under section 108(b)(5) or (c) the taxpayer must treat a partnership interest as depreciable property (or depreciable real property) to the extent of the partner's proportionate share of the partnership's basis in depreciable property (or depreciable real property), provided the part-

nership consents to a corresponding reduction in the partnership's basis (inside basis) in depreciable property (or depreciable real property) with respect to such partner.

(ii) *Request by partner and consent of partnership*—(A) *In general.* Except as otherwise provided in this paragraph (f)(2)(ii), a taxpayer may choose whether or not to request that a partnership reduce the inside basis of its depreciable property (or depreciable real property) with respect to the taxpayer, and the partnership may grant or withhold such consent, in its sole discretion. A request by the taxpayer must be made before the due date (including extensions) for filing the taxpayer's Federal income tax return for the taxable year in which the taxpayer has COD income that is excluded from gross income under section 108(a).

(B) *Request for consent required.* A taxpayer must request a partnership's consent to reduce inside basis if the taxpayer owns (directly or indirectly) a greater than 50 percent interest in the capital and profits of the partnership, or if reductions to the basis of the taxpayer's depreciable property (or depreciable real property) are being made with respect to the taxpayer's distributive share of COD income of the partnership.

(C) *Granting of request required.* A partnership must consent to reduce its partners' shares of inside basis if consent is requested by partners owning (directly or indirectly) an aggregate of more than 50 percent of the capital and profits interests of the partnership. For example, if there is a cancellation of partnership indebtedness securing real property used in a partnership's trade or business, and if partners owning (in the aggregate) 60 percent of the capital and profits interests of the partnership elect to exclude the COD income under section 108(c), the partnership must make the appropriate reductions in those partners' shares of inside basis.

(iii) *Partnership consent statement*—(A) *Partnership requirement.* A consenting partnership must include with the Form 1065, U.S. Partnership Return of Income, for the taxable year of the partnership that ends with or within the taxable year the taxpayer excludes COD income from gross income under section 108(a), and must provide to the taxpayer on or before the date the Form 1065 is filed, a statement that—

(1) Contains the name, address, and taxpayer identification number of the partnership; and

(2) States the amount of the reduction of the partner's proportionate interest in the adjusted bases of the partnership's depreciable property or depreciable real property, whichever is applicable.

(B) *Taxpayer's requirement.* Statements described in paragraph (f)(2)(iii)(A) of this section must be attached to a taxpayer's timely filed (including extensions) Federal income tax return for the taxable year in which the taxpayer has COD income that is excluded from gross income under section 108(a).

(iv) *Partner's share of partnership's adjusted basis.* [Reserved.]

(3) *Partnership basis reduction.* The rules of this section (including this paragraph (f)), apply in determining the properties to which the partnership's basis reductions must be made.

(g) *Special allocation rule for cases to which section 1398 applies.* If a bankruptcy estate and a taxpayer to whom section 1398 applies (concerning only individuals under Chapter 7 or 11 of title 11 of the United States Code) hold property subject to basis reduction under section 108(b)(2)(E) or (5) on the first day of the taxable year following

the taxable year of discharge, the bankruptcy estate must reduce all of the adjusted bases of its property before the taxpayer is required to reduce any adjusted bases of property.

(h) *Effective date.* This section is effective for discharges of indebtedness occurring on or after the date these regulations are published as final regulations in the **Federal Register**.

**PART 301—PROCEDURE AND ADMINISTRATION**

Par. 12. The authority citation for part 301 continues to read as follows:  
Authority: 26 U.S.C. 7805 \* \* \*

**§ 301.9100-13T [Removed]**

Par. 13. Section 301.9100-13T is removed.

Margaret Milner Richardson,  
*Commissioner of Internal Revenue.*

(Filed by the Office of the Federal Register on January 6, 1997, 8:45 a.m., and published in the issue of the Federal Register for January 7, 1997, 62 F.R. 955)

**Announcement 97-10**

The Health Insurance Portability and Accountability Act of 1996 added section 220 to the Internal Revenue Code to permit eligible individuals to establish medical savings accounts (MSAs). The Act also added Code section 6050Q, which requires any person paying long-term care or accelerated death benefits to report the aggregate benefits paid and certain other information. In addition, the Small Business Job Protection Act of 1996 added section 408(p), which allows individuals to establish Savings Incentive Match Plans for Employees of Small Employers (SIMPLE) retirement accounts.

To carry out the MSA provisions, the IRS developed three new forms: **Form 1099-MSA**, Distributions From Medical Savings Accounts, for trustees to report distributions from an MSA; **Form 5498-MSA**, Medical Savings Account Information, for trustees to report contributions to an MSA; and **Form 8851**, Summary of Medical Savings Accounts, for trustees to report the number of MSAs established.

For insurance companies and other payers to report the aggregate benefits paid and other information required under section 6050Q, the IRS developed **Form 1099-LTC**, Long-Term Care and Accelerated Death Benefits.

The filing requirements for trustees and other payers are as follows:

If the Form Is	Then File With or Furnish to	By This Date
1099-MSA (Copy A)	IRS	March 2, 1998
1099-MSA (Copy B)	Recipient	February 2, 1998
Form 5498-MSA (Copy A)	IRS	June 1, 1998
Form 5498-MSA (Copy B)	Participant	June 1, 1998
Form 8851	IRS	June 2, 1997 (For MSAs established from Jan. 1—Apr. 30, 1997)
Form 8851	IRS	August 1, 1997 (For MSAs established from May 1—June 30, 1997)
Form 1099-LTC (Copy A)	IRS	March 2, 1998
Form 1099-LTC (Copy B)	Policyholder	February 2, 1998
Form 1099-LTC (Copy C)	Insured	February 2, 1998

Copy A of Forms 1099-MSA, 5498-MSA, and 1099-LTC are provided for your information. Form 8851 is also included. Printed forms are expected to be available in late February.

No new forms are required for trustees to report distributions from and

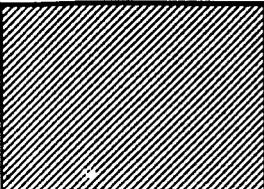
contributions to a SIMPLE. Trustees must report distributions from a SIMPLE on Form 1099-R and report contributions to a SIMPLE on Form 5498. The filing dates for Form 1099-R and Form 5498 will remain the same as in prior years. The 1997 versions of

these forms have been revised for reporting SIMPLEs. Printed copies of Forms 1099-R and 5498 can be obtained by calling 1-800-829-3676.

All the forms discussed above can be downloaded from the IRS's Internet Web Site at <http://www.irs.ustreas.gov>.

0594

 VOID  CORRECTED

PAYER'S name, street address, city, state, and ZIP code				OMB No. 1545-1517	<b>1997</b> Form 1099-MSA	<b>Distributions From          Medical Savings          Accounts</b>  <b>Copy A</b> <b>For          Internal Revenue          Service Center</b>  <b>File with Form 1096.</b>  For Paperwork Reduction Act Notice and instructions for completing this form, see the 1997 <b>Instructions for          Forms 1099, 1098,          5498, and W-2G.</b>
PAYER'S Federal identification number	RECIPIENT'S identification number			1 Gross distribution		
RECIPIENT'S name		3 Distribution code				
Street address (including apt. no.)						
City, state, and ZIP code						
Account number (optional)						

Form 1099-MSA

Cat. No. 23114L

Department of the Treasury - Internal Revenue Service

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0527

 VOID  CORRECTED

TRUSTEE'S name, street address, city, state, and ZIP code		1 Employee MSA contributions made in 1997 and 1998 for 1997		OMB No. 1545-1518	<b>1997</b> Form 5498-MSA	<b>Medical          Savings          Account          Information</b>  <b>Copy A</b> <b>For          Internal Revenue          Service Center</b>  <b>File with Form 1096.</b>  For Paperwork Reduction Act Notice and instructions for completing this form, see the 1997 <b>Instructions for          Forms 1099, 1098,          5498, and W-2G.</b>
		2 Total MSA contributions made in 1997				
TRUSTEE'S Federal identification number	PARTICIPANT'S social security number	3 Total MSA contributions made in 1998 for 1997				
PARTICIPANT'S name		4 MSA rollover contributions (not included in boxes 1, 2, or 3)		5 Fair market value of account		
Street address (including apt. no.)						
City, state, and ZIP code						
Account number (optional)						

Form 5498-MSA

Cat. No. 23097L

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**Summary of Medical Savings Accounts**

**1997**

Department of the Treasury  
Internal Revenue Service

► For Paperwork Reduction Act Notice, see back of form.

Trustee's name	Employer identification no.
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Number, street, and room/suite no.

City, state, and ZIP code	Telephone number (    )
---------------------------	----------------------------

a This report is for the period:     January 1 through April 30, 1997     May 1 through June 30, 1997

b Total number of medical savings accounts (see instructions) . . . ►	c Total number of previously uninsured account holders (see instructions). . . ►	d Total number of excludable account holders (see instructions) . . . . ►
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	Name of Account Holder (Last name, first name, and middle initial)	Social Security Number	Check if Previously Uninsured	Check if Excludable
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
17				
18				
19				
20				

0593

 VOID CORRECTED

PAYER'S name, street address, city, state, and ZIP code		1 Gross long-term care benefits paid	OMB No. 1545-1519  <b>1997</b>  Form <b>1099-LTC</b>	<b>Long-Term Care and Accelerated Death Benefits</b>
		\$		
PAYER'S Federal identification number		2 Accelerated death benefits paid	INSURED'S social security no.	
		\$		
POLICYHOLDER'S identification number		3 Check one: <input type="checkbox"/> Per diem <input type="checkbox"/> Reimbursed amount	<b>Copy A</b> <b>For Internal Revenue Service Center</b> <b>File with Form 1096.</b>  For Paperwork Reduction Act Notice and instructions for completing this form, see the <b>1997 Instructions for Forms 1099, 1098, 5498, and W-2G.</b>	
POLICYHOLDER'S name		INSURED'S name		
Street address (including apt. no.)		Street address (including apt. no.)		
City, state, and ZIP code		City, state, and ZIP code		
Account number (optional)		4 (optional) <input type="checkbox"/> Chronically ill <input type="checkbox"/> Terminally ill		
		Date certified		

Form **1099-LTC**

Cat. No. 23021Z

Department of the Treasury - Internal Revenue Service

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