

# SHORT-SALES, MORTGAGE DEBT RELIEF and INSOLVENT TAXPAYER EXCLUSIONS

Confused about where to report these transactions on your Tax Return? We can help!

If the decline in the real estate market or the nation's economic downturn has caused you to lose your home by foreclosure or short sale, or you voluntarily signed the deed over to the lienholder, you will probably be faced with debt relief income. You can also have debt relief income if you had a credit card, an automobile loan, or other debt forgiven in a settlement with a credit card company or other lender.

Normally debt forgiveness results in taxable income. But, there are several provisions of the tax code that allow individuals to exclude debt relief income and thereby avoid taxes on the forgiven income. The two exclusions that will most often apply this year are:

**Insolvent Taxpayer Exclusion** - An insolvent taxpayer is one whose debts (liabilities) exceed his assets. Tax law generally allows taxpayers to exclude debt relief income to the extent their liabilities exceed their assets. In addition, when adding up the assets, a taxpayer does not need to include assets excluded under state bankruptcy law. Although the concept is rather simple, inventorying and appraising assets and liabilities can be a tedious and time-consuming job. Yet, should be accomplished as soon as possible since valuations are based upon the assets' values and the amount of the liabilities immediately before the debt is relieved.

**Home Mortgage Debt Relief** - Under a special rule that applies to years 2007 through 2012, taxpayers can exclude from taxation up to \$2 million (\$1 million for an unmarried person filing separately) of home "acquisition" debt forgiven on their principal residence. Debt forgiven on second homes, rental property, business property, credit cards, or car loans do not qualify for this special tax-relief provision.

Whenever your debt is reduced or eliminated, you will receive a year-end statement (Form 1099-C) from your lender. By law this form must show the amount of debt forgiven, and if the debt relief involves a foreclosure or repossession, Form 1099-C will generally include the fair market value of the property taken back by the lender.

The information included on the 1099-C is not always correct, and it may be necessary to notify the lender immediately if any of the information shown is in error.

If you have had debt or mortgage relief during the year, you are encouraged to contact this office right away to determine the impact on your tax liability and explore your options.

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