

# ST20-01 Cancellation of Debt – Credit Card

See Screening Sheet on page D-60 of Pub 4012 to determine if COD is in scope.

Taxpayer receives a 1099-C from a credit card company or bank. The amount of the debt canceled is shown in Box 2 of 1099C.

- Canceled debt is generally considered income and is reported on the 1040, Schedule 1 line 8, other income, UNLESS the taxpayer was in bankruptcy or insolvent (i.e., the taxpayer’s liabilities exceeded assets) immediately before the debt was canceled.
- If the taxpayer was in bankruptcy or insolvent immediately before the debt was canceled, all or part of the canceled debt may be excludable from income.
  - **Cases involving bankruptcy or insolvency are OUT OF SCOPE...**
- The preparer needs to ask taxpayer if they were in bankruptcy or might have been insolvent immediately before the debt was canceled; if “yes” or “not sure,” we must refer the client to a paid preparer. (OUT OF SCOPE)
- The debt must be personal (i.e. NOT related to a business)
  - **Cases involving business related debt are OUT OF SCOPE...**
- Credit card cancellation of debt is reported on a 1099-C if the amount is over \$600. Any amounts less than \$600 not reported on a 1099-C are still taxable.
- The amount of interest shown in box 3 can be ignored since it is included in box 2 and is taxable.
- All other types of forgiven debt including Qualified Principal Residence Indebtedness is **OUT OF SCOPE**.
- Cancellation of debt amounts are not taxable in NJ.

## Example

Fred runs up \$15,000 in credit card debt and can’t pay. He works out a deal with the credit card company to settle for \$10,000 and the rest of the debt is canceled. Fred was solvent immediately before the debt was canceled. Fred receives a 1099-C from the creditor shown below:

CORRECTED (if checked)

CREDITOR'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.  <b>Big Bank</b> <b>1 Big Plaza</b> <b>Gotham DE</b>		1 Date of identifiable event	OMB No. 1545-1424	2020	Cancellation of Debt
		2 Amount of debt discharged			
		3 Interest, if included in box 2	Form <b>1099-C</b>		
CREDITOR'S TIN <b>23-4567890</b>		DEBTOR'S TIN <b>123-00-4567</b>		Copy B For Debtor	
DEBTOR'S name  <b>Fred Doe</b> Street address (including apt. no.) <b>123 Elm St</b> City or town, state or province, country, and ZIP or foreign postal code <b>Anytown, NJ 12345</b>		4 Debt description  <b>Credit Card</b>			
Account number (see instructions)		5 If checked, the debtor was personally liable for repayment of the debt . . . . . ▶ <input checked="" type="checkbox"/>		6 Identifiable event code	
7 Fair market value of property \$		7 Fair market value of property \$			

Form **1099-C** (keep for your records) [www.irs.gov/Form1099C](http://www.irs.gov/Form1099C) Department of the Treasury - Internal Revenue Service

The consequence is \$5,000 of taxable income which is reported on the 1040, Schedule 1, line 8, other income, as CANCELLED DEBT.

- Step 1:** In TSO, enter 1099-C in the search box.
- Step 2:** Go to 4012 Pages D-62 and follow the screen entries on this page
- Step 3:** The amount entered on 1040, Schedule 1, line 8 of the Federal return should **not** go to line 26 (Other Income) of the NJ return. TSO seems to be doing this correctly. **Check the NJ return to be sure.**