Internal Revenue Service

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Person To Contact:
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November 13, 2013

TY:

Legend

Entity 1	=
Entity 2	=
State X	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Collection Remedy	=

Dear :

This letter responds to the letter dated February 19, 2013, submitted on behalf of Entity 1, requesting a ruling that Entity 1 is not required to file Forms 1099-C with respect to the write-off of balances and charges pursuant to its settlement agreement because the discharge was not the result of an "identifiable event" listed in Treasury Regulation § 1.6050P-1(b)(2), but rather was required by operation of state law. For the reasons set forth below, we conclude that Entity 1 is required to comply with the reporting requirements of I.R.C. § 6050P because the discharge of indebtedness was the result of an identifiable event listed in Treas. Reg. § 1.6050P-1(b)(2).

Facts

Entity 1 is a financial institution chartered by State X engaged in, among other activities, the business of extending credit to consumers for the purchase of certain assets. Entity 1 is the successor by merger to another financial institution that had engaged in similar consumer credit activities as Entity 1 and which, prior to the merger, entered into an agreement with Entity 2 to engage in certain remedies for collection and enforcement of the retail sale installment contracts relating to the consumer loans.

Entity 1 filed a complaint in the Circuit Court of State X on Date 1 to recover a deficiency balance remaining on a consumer credit account after Collection Remedy had been taken. The defendant filed a motion to dismiss the complaint. The court on Date 2 issued an order dismissing the complaint. Also on Date 2, the defendant filed a counterclaim, which she later amended, that became the basis for the continuing litigation. On Date 3, the defendant/counterclaimant filed a Motion for Class Certification. The parties entered into a Settlement and Release Agreement ("Agreement") on Date 4 and, on the same date, filed with the court a Joint Motion for Preliminary Approval of Class Action Settlement Agreement. The following day, the court entered an Order Preliminarily Approving Class Action Settlement ("Preliminary Order"). On Date 5, the court entered an Order Finally Approving Class Action Settlement and Certifying a Class for Settlement Purposes ("Final Order") and also entered its Final Judgment in the case.

The Preliminary Order states that the parties have "executed the Agreement in order to settle and resolve the Litigation as between them and the proposed Settlement Class." The Preliminary Order states that the "Court finds preliminarily…that under [State X] law, [Entity 1] would not accrue any deficiency balance or collect any deficiency judgment…[regarding] 'presale notices' that failed to comply with the [State X] UCC." The Preliminary Order further states that Entity 1 would be permitted to "offset deficiency balances and judgments against damages claimed" by the counterclaimant or class action members, under the law of State X. The Preliminary Order specifies that its findings are "[p]ursuant to the Agreement, and for purposes of the Settlement only." The Final Order incorporates the Preliminary Order and the parties' Agreement. The terms of the Agreement specified the creation of a qualified settlement fund, and the distribution from the fund to the class members and their counsel. The Agreement also specified that Entity 1 would submit a request for a private letter ruling to the IRS requesting a ruling that Entity 1 is not required to file information returns relating to distributions from the settlement fund.

Law and Analysis

Section 6050P of the Internal Revenue Code requires that an applicable entity report any discharges (in whole or in part) of indebtedness of any person in excess

of $600.00. The report is to include the name, address and taxpayer identification number of each person whose indebtedness is discharged, the date of the discharge and the amount of indebtedness discharged. In addition, section 1.6050P-1(b)(2) of the Treasury regulations provides that a discharge of indebtedness occurs if one of eight "identifiable events" that the regulation defines takes place.

Of the identifiable events, only two have a potential bearing on the requested ruling. The first possible event, section 1.6050P-1(b)(2)(F), provides that an identifiable event exists when the applicable financial entity and debtor agree to discharge the indebtedness for less than full consideration. To establish consideration, there must be a performance or a return promised which has been bargained for by the parties. Restatement (Second) Contracts § 71(1) (1981). In this case, Entity 1 and the debtor-class members agreed to the entry of a judgment, approved and supervised by the court, which incorporates the parties' Agreement by which Entity 1 will write off all remaining debt balances as part of the overall settlement of the pending litigation. This appears, on its face, to be the identifiable event described in subsection (F) of the regulations.

The request for PLR submitted on behalf of Entity 1 argues that the Agreement does not reflect a mere agreement of the parties, or any other identifiable event, but rather is simply a recognition that the write-off of the deficiency balances was required under the law of State X. The law of State X provides that, in a case where the Collection Remedy did not strictly comply with notice requirements, there is an absolute bar on collecting any remaining deficiency balances. The defendant's motion to dismiss filed in response to Entity 1's complaint, and the defendant's counterclaim, alleged that Entity 1 violated various aspects of the notice requirements in the presale notices sent to the class members as part of the Collection Remedy. The settlement Agreement acknowledges that the "claims are premised on state law which bars the recovery of deficiency balances in certain circumstances" and "[t]he settlement consideration provided in the Agreement is determined by application of state law." The Agreement contains no admission or concession by Entity 1 with respect to the claims or defenses alleged in the class action counterclaim. The Agreement contains a specific denial of liability in paragraph 1, which denial of liability was incorporated into the Preliminary Order and Final Order. The Final Order recites that by entering into the settlement Agreement, the parties shall not be deemed to have admitted or conceded liability with respect to any of the pending claims or defenses alleged.

Entity 1 contends that the order granting the defendant's motion to dismiss, coupled with the Preliminary and Final Orders approving the settlement, constitutes a substantive ruling that the presale notices were defective and the deficiencies, therefore, were not legally accrued or collectible. The original order dismissing the defendant from the case, however, was a one-sentence order with no substantive findings or memorandum opinion, issued simultaneously with the filing of the defendant's counterclaim. The Preliminary Order approving the class action settlement

specifically states that the findings are “Pursuant to the Agreement, and for the purposes of the Settlement only.” The Preliminary Order was drafted by the parties and submitted to the court for signature, rather than an order that resulted from an independent judicial investigation into the allegations and defenses of the parties. Entity 1 has never made any admission regarding the alleged inadequacy of the presale notices. It vigorously pursued the litigation, including filing a Motion for Summary Judgment, throughout the pendency of the case. It was only by entering into a settlement agreement with the class members that Entity 1 gave up its disputed claims to deficiency amounts.

Although the application of the law of State X regarding the adequacy of the presale notices may have been a factor in the parties’ decision to settle the litigation, such considerations are typical of parties’ assessment of litigation hazards in arriving at a negotiated settlement. As the Preliminary Order states, the parties entered into the Agreement “which memorializes the Parties’ negotiations and agreed-upon settlement” of the litigation. The Agreement states that Entity 1 entered into the Agreement because Entity 1 “desires to settle the claims being asserted against it in the Litigation…for the purpose of avoiding the burden, expense, and uncertainty of continuing litigation.” The fact that the terms of the Agreement were approved and incorporated into the Circuit Court’s Preliminary Order or Final Order does not serve to covert the discharge of the debt from being entered into voluntarily to one forced by operation of state law. The Settlement and Release Agreement should be taken on its face, as an agreement between Entity 1 and the debtors to discharge the indebtedness at less than full consideration for the purpose of resolving the pending litigation. Therefore, section 1.6050P-1(b)(2)(F) applies.

The second possible event, section 1.6050P-1(b)(2)(G), provides that a discharge of indebtedness exists where a creditor discontinues collection activity pursuant to a decision by the creditor or a defined policy of the creditor. According to section 1.6050P-1(b)(2)(iii), a creditor’s defined policy includes both a written policy and the creditor’s established business practice. In this case, the cancellation of indebtedness is not a result of any defined policy or business practice of Entity 1, but rather by its decision to discontinue collection action as part of settling the litigation. This decision therefore may fall within subsection (G). In any event, even if subsection (G) of the regulation did not apply, the event set forth in regulation subsection (F), as set forth above, does apply and the section 6050P reporting requirements must be met.

Conclusion

Based solely on the information provided and the representations made, Entity 1 is required to file Forms 1099-C with respect to the write-off of balances and charges pursuant to its settlement agreement because the discharge was the result of an identifiable event listed in section 1.6050P-1(b)(2).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Ashton P. Trice
Chief, Branch 2
(Procedure & Administration)

Enclosures: (1) Copy of letter for section 6110 purposes
(2) Notice of Intention to Disclose, Notice 437

cc: