



[CLICK HERE](#) to return to the home page

PLR 8920019

February 14, 1989

This is in reply to your letter of March 8, 1988, submitted on behalf of

***, requesting a ruling as to whether a spouse's separate assets will be used to determine insolvency of a taxpayer under section 108(a)(1)(B) of the Internal Revenue Code if a joint federal income tax return is filed.

The information you submitted indicates that during the 1986 tax year the taxpayer was discharged from indebtedness in the amount of \$

*** and, at the time of the discharge of indebtedness, the taxpayer was insolvent in the amount of approximately \$

***. For the 1986 tax year, the taxpayer filed Form 1040 claiming the status of married filing a separate return and excluded from gross income the amount of the discharge of indebtedness up to the extent of his insolvency.

The taxpayer's spouse, who was not insolvent when the taxpayer was discharged from indebtedness, also filed Form 1040 claiming the status of married filing a separate return for the 1986 tax year. The taxpayer's spouse held assets immediately before the discharge of indebtedness that were not subject to the claims of his creditors. The taxpayer and his spouse now propose to file a joint return, as provided by section 6013(b)(1) of the Code, for the 1986 tax year.

Under section 61(a)(12) of the Code, except as otherwise provided, gross income means all income including income from discharge of indebtedness.

Section 108(a)(1)(B) of the Code provides that discharge of indebtedness income is excluded from gross income if the discharge occurs when the taxpayer is insolvent. Section 108(a)(3) provides that the amount excluded by section 108(a)(1)(B) does not exceed the amount by which the taxpayer is insolvent.

Section 108(d)(3) of the Code defines "insolvent" to mean the excess of liabilities over fair market value of assets and states that the amount of a taxpayer's insolvency is determined on the basis of the taxpayer's assets and liabilities immediately before the discharge.

Section 6013(b) of the Code provides that if an individual has filed a separate return for a taxable year for which a joint return could have been filed, and the time prescribed by law for filing the return for such taxable year has expired, the individual and his spouse may nevertheless file a joint return for the taxable year.

Section 1.6013-4(b) of the Income Tax Regulations states that if a joint return is filed, the gross income of husband and wife on the joint return are computed in an aggregate amount and the deductions allowed and the taxable income are likewise computed on an aggregate basis.

Although there are two taxpayers on a joint return, there is only one taxable income. The tax on

the joint return is computed on the aggregate income and the liability with respect to the tax is joint and several.

The Bankruptcy Tax Act of 1980, Pub. L. No. 96-589, added sections 108(a)(1)(B) and 108(d)(3) to the Internal Revenue Code. The Bankruptcy Tax Act codified the judicially developed "insolvency exception" to the general rule that income is realized upon discharge of indebtedness. See H.R. Rep. No. 833, 96th Cong., 2d Sess. 7 (1980); S. Rep. No. 1035, 96th Cong., 2d Sess. 8 (1980).

The insolvency exception evolved from a line of cases beginning with *United States v. Kirby Lumber Co.*, 284 U.S. 1 (1931). In that case, the Supreme Court held that income was realized when a debt was discharged for less than the full amount. In *Dallas Transfer & Terminal Warehouse Co. v. Commissioner*, 70 F.2d 95 (5th Cir. 1934), the Court of Appeals held that no income was realized from discharge of indebtedness where the debtor was insolvent both before and after the discharge. The Dallas Transfer court reasoned that since no assets had been freed from the claims of creditors, the taxpayer did not realize any income. Similarly, in *Marcus Estate v. Commissioner*, T.C.M. 1975-9, the Tax Court held that assets exempt from the claims of creditors should not be included in the determination of a taxpayer's insolvency immediately following the cancellation of a debt. Since the rationale for the insolvency exception is that where no assets are freed from claims of creditors no income is realized, only assets that are subject to the claims of a taxpayer's creditors should be used to determine the taxpayer's insolvency under section 108(a)(1)(B) of the Code.

According to the Tax Court, a joint return under section 6013 of the Code "does not create a new tax personality which would be entitled, in its own right, to deductions not otherwise available to the individual spouses under the pertinent sections of the statute." *Coerver v. Commissioner*, 36 T.C. 252, 254 (1961) *aff'd per curiam* 297 F.2d 837 (3d Cir. 1962). In *Coerver*, a husband and wife claimed a section 162 deduction on their joint return for the wife's expenses of working and maintaining an apartment in New York City and travel expenses between New York City and Wilmington, Delaware, where her husband worked and resided. The taxpayers claimed the "home" of the "taxable unit" was Wilmington, Delaware and took the position that the wife's expenses incurred in maintaining the New York apartment and traveling to Delaware were incurred "away from home" within the meaning of section 162. The Tax Court held that although the concept of a "taxable unit" under the joint return provision, section 6013, permits aggregation of deductions, each spouse must first be entitled to a particular deduction before it can be aggregated. The Tax Court denied the taxpayers' section 162 deduction.

Although the court in *Coerver* addressed the question of whether the filing of a joint return effects the allowability of a deduction, and here we address the question of whether the filing of a joint return effects entitlement to an exclusion, the reasoning of the court in *Coerver* is instructive in the present case. While section 6013 requires the aggregation of income and deductions, the determination of a taxpayer's entitlement to the insolvency exclusion under section 108(a)(1)(B) is based on all the assets reachable by the individual taxpayer's creditors. The filing of a joint return, pursuant to section 6013(b) of the Code, does not affect whether a spouse's separate assets will be used to determine the insolvency of the taxpayer.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) of the Code provides that this letter may not be used or cited as precedent.

If the taxpayer chooses to file a joint return under section 6013 of the Code for the 1986 tax year, he should attach a copy of this letter to the return. A copy is enclosed for this purpose.