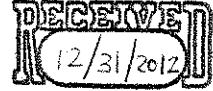




DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224



OFFICE OF THE CHIEF COUNSEL

CC:ITA:B04
GENIN-140142-12

UIL: 108.05-00

Rafael A. Madan, General Counsel
Department of Justice
Office of Justice Programs
Office of the General Counsel
Washington, DC 20531

Attention: Matthew T. Scodellaro

Dear Mr. Madan:

This responds to your letter submitted on behalf of the Bureau of Justice Assistance (BJA) of the Office of Justice Programs, U.S. Department of Justice, at the request of the state administrative agencies (SAA) that administer payments made under the John R. Justice Student Loan Repayment Program (JRJ Program). 42 U.S.C. § 3797cc-21. Specifically, you asked whether a student loan borrower may exclude loan forgiveness under the JRJ Program from gross income and whether the SAA should file information returns with the Internal Revenue Service reporting the loan forgiveness.

John R. Justice Student Loan Repayment Program

In 2008, Congress established the JRJ Program to encourage qualified attorneys to choose careers as state prosecutors and public defenders. In general, a prosecutor is defined as a full-time attorney of a state or unit of local government, and a public defender is defined as a full-time attorney of (i) a state or unit of local government, (ii) a nonprofit organization under a contract with a state or unit of local government, or (iii) a federal defender.

Under the JRJ Program, an eligible student loan borrower with one or more eligible student loans may receive up to \$10,000 in loan repayments in any calendar year, up to an aggregate total of \$60,000. In general, under the JRJ Program, state prosecutors and public defenders who meet certain requirements may have the federal government repay a portion of their student loans after completing qualifying full-time employment for at least three years. The JRJ Program is funded from Congressional appropriations as specified in 42 U.S.C. § 3797cc-21(j) and is carried out by BJA, through SAAs, that assumes the "obligation to repay a student loan by direct payments on behalf of a

borrower to the holder of such loan” for any borrower who meets the service requirements of 42 U.S.C. § 3797cc-21(c).

For purposes of the JRJ Program, the term “student loan” refers generally to three federal student loan programs authorized by the Higher Education Act of 1965 (HEA): (1) the Direct Loan program, (2) the Federal Family Education Loan (FFEL) program, and (3) the Federal Perkins Loan (Perkins Loan) program. Consolidated loans made by private lenders under § 428C of the HEA (20 U.S.C. § 1078-3) or by the Department of Education (DOED) under § 455(g) of the HEA (20 U.S.C. § 1087e(g)) to the extent that the Consolidated Loan is used to repay a FFEL or Direct Loan will also qualify for repayment under the JRJ Program.

HEA Student Loan Programs

For Direct Loans, the federal government makes subsidized and unsubsidized loans directly to students (Federal Direct Stafford/Ford Loans) under Part D of Title IV of the HEA. 20 U.S.C. § 1087a. The Direct Loan program also includes a Federal Direct Consolidation Loan Program under § 455(g) of the HEA. 20 U.S.C. § 1087e(g).

For FFELs, private lenders, non-federal entities such as banks, savings and loan associations, credit unions, schools, and state and private nonprofit agencies, make loans with private funds under Part B of Title IV of the HEA. 20 U.S.C. § 1071 et seq. The FFEL program also includes a Federal Direct Consolidation Loan Program under § 428C of the HEA. 20 U.S.C. § 1078-3. A FFEL is generally insured by a state or nonprofit private organization loan insurance program.¹ When a loan insurance program pays a lender for a loss due to a borrower’s default, the federal government guarantees a percentage of this amount. 20 U.S.C. § 1078(c)(1). This percentage is generally limited to no more than 95 percent for recently issued loans, but it could be as high as 100 percent or as low as 75 percent. 20 U.S.C. § 1078(c)(1).

For Perkins Loans, postsecondary institutions make low-interest loans to financially needy students from a fund capitalized by federal and institutional contributions, in a 3:1 ratio of federal to institutional contributions, under Part E of Title IV of the HEA. 20 U.S.C. § 1087aa. Currently, there is a loan forgiveness provision for Perkins Loans for a full-time attorney employed in a defender organization established in accordance with 18 U.S.C. § 3006A(g)(2).² 20 U.S.C. § 1087ee(a)(2)(F). Title 20 contains a specific exclusion from income for certain loan forgiveness for Perkins Loans. 20 U.S.C. § 1087ee(a)(5).

¹ If the state is not served by a loan insurance program, a FFEL may be insured directly by the federal government. Currently, every state is served by a loan insurance program. However, certain federally insured loans remain outstanding.

² This provision is in addition to loan repayment provided under the JRJ Program.

Tax Consequences of Student Loan Repayment under the JRJ Program

Section 61(a) of the Code provides that, except as otherwise provided in subtitle A, gross income means all income from whatever source derived. Section 61(a)(12) provides that gross income includes income from discharge of indebtedness.

Section 108(f)(1) of the Code provides that gross income does not include any amount that would be includible in gross income by reason of the discharge (in whole or in part) of any student loan if the discharge was pursuant to a provision of a loan under which all or part of the indebtedness of the individual would be discharged if the individual worked for a certain period of time in certain professions for any of a broad class of employers.

Section 108(f)(2) of the Code defines "student loan" as any loan to an individual to assist the individual in attending an educational organization described in § 170(b)(1)(A)(ii) made by

- (A) the United States, or an instrumentality or agency thereof,
- (B) a State, territory, or possession of the United States, or the District of Columbia, or any political subdivision thereof, or
- (C) a public benefit corporation
 - (i) which is exempt from taxation under § 501(c)(3),
 - (ii) which has assumed control over a State, county, or municipal hospital,
- and
- (iii) whose employees have been deemed to be public employees under State law, or
- (D) any educational organization described in § 170(b)(1)(A)(ii) if such loan is made
 - (i) pursuant to an agreement with any entity described in subparagraphs (A), (B), or (C) under which the funds from which the loan was made were provided to such educational organization, or
 - (ii) pursuant to a program of such educational organization which is designed to encourage its students to serve in occupations with unmet needs or in areas with unmet needs and under which the services provided by the students (or former students) are for or under the direction of a governmental unit or an organization described in § 501(c)(3) and exempt from tax under § 501(a).

In the case of a Direct Loan, the federal government is the lender, and the loans qualify as "student loans" for purposes of § 108(f)(2)(A) of the Code. Additionally, the federal government is the source of the funds for reducing the Direct Loans conditioned by statute on the borrower working for a certain period of time in qualifying public service positions. Therefore, loan repayment under the JRJ Program that discharges a portion of the borrower's Direct Loan satisfies the requirements of § 108(f)(1), and a Direct

Loan borrower may exclude loan forgiveness under the JRJ Program from gross income under § 108(f)(1).

In the case of a FFEL, the federal government is not the holder of the loan at the time the debt is discharged or forgiven. The nominal private financial institution may not be a lender described in § 108(f)(2)(A) of the Code. However, by statute, the federal government is the source of funds for debt forgiveness through its obligation to guarantee substantially all of the forgiven amount. As guarantor, the federal government pays the borrower's debt to the private lender and then, in turn, discharges the borrower's debt. In this regard, the federal government reasonably can be viewed as the lender for purposes of § 108(f)(2)(A). Additionally, as with the Direct Loans, the JRJ Program loan repayment under FFEL is conditioned by statute on the borrower working for a certain period of time in qualifying public service positions. Therefore, loan repayment under the JRJ Program that discharges a portion of the borrower's FFEL satisfies the requirements of § 108(f)(1), and a FFEL borrower may exclude loan forgiveness under the JRJ Program from gross income under § 108(f)(1).

In the case of a Perkins Loan, the federal government is the source of 75 percent of the loan funds. Thus, the educational organization reasonably can be viewed as a lender described in § 108(f)(2)(D)(i).³ Additionally, as for Direct Loans and FFELs, the federal government is the source of the funds for reducing the Perkins Loan conditioned by statute on the borrower working for a certain period of time in qualifying public service positions. Therefore, loan repayment under the JRJ Program that discharges a portion of the borrower's Perkins Loan satisfies the requirements of § 108(f)(1), and a Perkins Loan borrower may exclude loan forgiveness under the JRJ Program from gross income under § 108(f)(1).

Information Reporting under § 6050P of the Code

Section 6050P of the Code provides that an applicable entity must file an information return (Form 1099-C) if it discharges an indebtedness of any person (in whole or in part) that is greater than \$600. Section 1.6050P-1(a)(3) of the Income Tax Regulations (regulations) provides that the discharged indebtedness must be reported regardless of whether the debtor is subject to tax on the discharged debt under §§ 61 and 108. The term "applicable entity" is defined under § 6050P(c).

Section 1.6050P-1(a)(1) of the regulations provides that for purposes of this reporting requirement, a discharge of indebtedness is deemed to have occurred if and only if one

³ Only "educational organizations" as defined in § 170(b)(1)(A)(ii) of the Code qualify to make a "student loan" under § 108(f)(2). However, loan forgiveness of student loans made by non-qualifying educational organizations may qualify for an exclusion from gross income under the Perkins Loan program for a full-time attorney employed in a defender organization established in accordance with 18 U.S.C. § 3006A(g)(2). 20 U.S.C. § 1087ee(a)(2)(F).

of eight identifiable events takes place. Section 1.6050P-1(b)(2) lists the eight identifiable events as:

- (1) a discharge of indebtedness in bankruptcy;
- (2) a cancellation or extinguishment of indebtedness that renders a debt unenforceable in a receivership, foreclosure, or similar federal or state court proceeding;
- (3) a cancellation or extinguishment of indebtedness upon the expiration of a statute of limitation for collection or upon the expiration of a statutory period for filing a claim or commencing a deficiency judgment proceeding;
- (4) a cancellation or extinguishment of indebtedness pursuant to a foreclosure election that bars the applicable entity's right to pursue collection;
- (5) a cancellation or extinguishment of indebtedness in a probate or similar proceeding that renders a debt unenforceable;
- (6) a discharge of indebtedness pursuant to an agreement between the debtor and applicable entity that discharges the debt for less than full consideration;
- (7) a discharge of indebtedness pursuant to the applicable entity's defined policy to discontinue collection and discharge the debt; or
- (8) the expiration of the non-payment testing period described in § 1.6694-1(b)(2)(iv) of the regulations.

The cancellation of student loan debt under the JRJ Program is a discharge by operation of law. The debt is cancelled, as described above, in certain circumstances relating to the performance of public service by the student. 42 U.S.C. § 3797cc-21. These discharges do not fall into one of the eight identifiable events listed above that require reporting of the cancelled debt. Since no identifiable event has occurred when a loan is forgiven under the JRJ Program, there is no requirement for the lender to file an information return under IRC § 6050P.

This letter calls your attention to certain general principles of the law. It is intended for informational purposes only and does not constitute a ruling. See Rev. Proc. 2012-1, 2012-1 I.R.B. 7, § 2.04. If you have any additional questions about the exclusion from gross income please contact Craig Wojay at (202) 622-4920 and if you have any additional questions about the information reporting requirements please contact Janet Engel Kidd at (202) 622-4940.

Sincerely,



Donna J. Welsh
Senior Technician Reviewer, Branch 4
(Income Tax & Accounting)