



Topic no. 431, Canceled debt – Is it taxable or not?

If you borrow money and are legally obligated to repay a fixed or determinable amount at a future date, you have a debt. You may be personally liable for a debt or may own a property that secures a debt for which you may or may not also be personally liable.

If your debt is forgiven or discharged for less than the full amount owed, the debt is considered canceled for the forgiven or discharged amount that you no longer need to pay. Cancellation of a debt may occur if the creditor can't collect, or gives up on collecting, the amount you're obligated to pay. If you own property securing a debt, cancellation of the debt may occur due to foreclosure, repossession, voluntary transfer of the property to the lender, abandonment of the property, or a mortgage modification.

In general, if your debt is canceled, forgiven, or discharged for less than the amount owed, the amount of the canceled debt is taxable. If taxable, you must report the canceled debt on your tax return for the year in which the cancellation occurred.

However, the law provides several exceptions in which the discharged amount is not considered canceled debt. These exceptions will be discussed later.

After a debt is canceled, the creditor may send you a [Form 1099-C, Cancellation of Debt](#) showing the amount canceled and date of cancellation. Contact the creditor if you receive a 1099-C reflecting incorrect information. If a creditor continues to attempt to collect the debt after you receive a 1099-C, the debt may not have been canceled and you may not have income from a canceled debt. Verify your specific situation with the creditor. Your responsibility to report the correct taxable amount of canceled debt as income on your tax return for the year in which the cancellation occurred remains, regardless of the accuracy of the Form 1099-C you received.

In general, you must report any taxable amount of a canceled debt as ordinary income on [Form 1040, U.S. Individual Income Tax Return](#), [Form 1040-SR, U.S. Tax Return for Seniors](#) or [Form 1040-NR, U.S. Nonresident Alien Income Tax Return](#) (attach [Schedule 1 \(Form 1040\), Additional Income and Adjustments to Income](#) [PDF](#) or [Schedule NEC \(Form 1040-NR\), Tax on Income Not Effectively Connected With a U.S. Trade or Business](#) [PDF](#)) if the debt is a nonbusiness debt, or on an applicable schedule if the debt is a business debt. See [Publication 4681, Canceled Debts, Foreclosures, Repossessions, and Abandonments \(for Individuals\)](#).

Caution: If your debt is secured by property, and the creditor takes that property in full or partial satisfaction of your debt, you are treated as having sold that property to the creditor. The tax treatment of the deemed sale depends on whether you were personally liable for the debt (recourse debt) or not personally liable for the debt (nonrecourse debt).

For recourse debt, your amount realized on the sale is the fair market value (FMV) of the property. The difference between FMV and your adjusted basis (usually your cost) will be a gain or loss on the disposition of the property. Your ordinary income from the cancellation of the debt is the amount by which the discharged debt exceeds the FMV of the property. Include this cancellation of debt in gross income unless an exception or exclusion, discussed below, applies.

For nonrecourse debt, your amount realized is the entire amount of the nonrecourse debt, plus the amount of cash and the FMV of any non-cash property you received. You will not have ordinary income resulting from debt cancellation.

The examples below show the difference between how recourse and nonrecourse debt is treated.

1. You bought a boat for business use for \$20,000, paying \$2,000 down and signing a recourse note for \$18,000. After paying down \$4,000 on the note, you are no longer able to make payments. The boat dealer repossesses the boat, which is now worth \$11,000, and cancels the remaining balance (\$3,000). Your adjusted basis in the boat is now \$10,000 due to allowable depreciation deductions of \$10,000. You will have ordinary income from cancellation of debt of \$3,000 (\$14,000 remaining debt owed minus \$11,000 FMV of boat). You will have \$1,000 of gain on disposition of the boat, the excess of the boat's FMV of \$11,000 (the amount you realized on repossession) over your \$10,000 adjusted basis in the boat.
2. The facts are the same except that you signed a nonrecourse note when buying the boat. When the dealer repossesses the boat, you will have gain of \$4,000, the difference between the \$14,000 realized (the face amount of the remaining debt) and your \$10,000 adjusted basis in the boat. You have no ordinary income from cancellation of the debt.

See [Publication 4681](#) for detailed information on canceled debt and on reporting a gain or loss from repossession, foreclosure, or abandonment of property. See also [Publication 544, Sales and Other Dispositions of Assets](#) and [Publication 523, Selling Your Home](#).

There are several exceptions to the requirement that you include canceled debt in income. These exceptions apply before the exclusion (discussed later) and do not require you to reduce your tax attributes.

Exceptions to taxability of cancellation of debt income:

1. Amounts canceled as gifts, bequests, devises, or inheritances
2. Certain qualified student loans containing loan provisions for cancellation based on length of employment in certain professions for a broad class of employers
3. Certain student loan discharges after December 31, 2020, and before January 1, 2026
4. Cancellation due to death or total and permanent disability of the student
5. Amounts received or forgiven under certain student loan repayment assistance programs
6. Amounts of canceled debt that would be deductible if you, as a cash basis taxpayer, had paid it
7. A qualified purchase price reduction given by the seller of property to the buyer

Amounts that meet the requirements for any of the following exclusions aren't included in income, even though they're cancellation of debt income.

Exclusions of cancelation of debt income from gross income:

1. Debt canceled in a Title 11 bankruptcy case
2. Debt canceled to the extent insolvent
3. Cancellation of qualified farm indebtedness
4. Cancellation of qualified real property business indebtedness
5. Cancellation of qualified principal residence indebtedness that is discharged before January 1, 2026, or discharged subject to an arrangement that is entered into and evidenced in writing before January 1, 2026

Generally, if you exclude canceled debt from income under one of the exclusions listed above, you must reduce certain tax attributes (certain credits and carryovers, losses and carryovers, basis of assets, etc.) (but not below zero) by the amount excluded. You must report the amount qualifying for exclusion, and any corresponding reduction of those tax attributes on [Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness \(and Section 1082 Basis Adjustment\)](#) and attach to your tax return. For cancellation of qualified principal residence indebtedness that's excluded from income, you must only reduce your basis in your principal residence. For cancellation of qualified real property business indebtedness, you must only reduce your basis in your depreciable real property.

Additional information

Refer to [Publication 4681](#) for more detailed information regarding taxability of canceled debt, how to report it, and related exceptions and exclusions. [Publication 525, Taxable and Nontaxable Income](#) contains additional information. If you received a [Form 1099-A, Acquisition or Abandonment of Secured Property](#), review [Topic no. 432](#) for more information. Refer to [How do I report the debt forgiven on my residence due to foreclosure, repossession, abandonment, or because of a loan modification or short sale?](#) to determine if any canceled debt on your principal residence is required to be included as income on your federal tax return.

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