

**COMMITTEE ON WAYS AND MEANS
MARK-UP OF H.R. 939
(VETERANS' HOUSING AMENDMENTS OF 1991)
ON FEBRUARY 12, 1992**

I. Legislative Background

H.R. 939 (the Veterans' Housing Amendments of 1991) was reported by the House Committee on Veterans' Affairs on November 6, 1991 (H. Rept. 102-292, Part I). Section 5 of the bill as reported by that committee would clarify the tax treatment of certain waivers and settlements of veterans' indebtedness granted by the Department of Veterans Affairs (the "VA"). (In general, veterans' indebtedness is created when: (1) a veteran receives compensation, pension, education, or vocational rehabilitation benefits to which the veteran is not entitled or (2) a veteran defaults on a VA-guaranteed home loan.)

H.R. 939 has been sequentially referred to the Committee on Ways and Means for a period ending February 28, 1992. This document provides a description of the relevant present law, the tax-related provisions included in H.R. 939 as reported by the Committee on Veterans' Affairs, and a possible option for consideration by the Committee on Ways and Means.

**II. Description of Tax-Related Provisions of
H.R. 939, as Reported by the Committee on Veterans' Affairs**

Present Law

In 1986, Internal Revenue Code section 134 was enacted to consolidate and set forth the tax treatment of military benefits.¹ Under this section, qualified military benefits are excludable from gross income. Any benefits for current or former military personnel that are not expressly excluded under section 134, or under another section of the Code (e.g., the fringe benefit exclusions of section 132), are includible in gross income.

The term "qualified military benefit" generally means

¹ P.L. 99-514. See H. Rep. 99-841, Vol. II, September 18, 1986, pp. 548-549 (Conference Report).

any allowance or in-kind benefit that:

(1) is received by any member or former member (or by a dependent) of the uniformed services of the United States by reason of the member's status or service as a member of the uniformed services; and

(2) was excludable from gross income under a non-Internal Revenue Code provision of law, regulation, or administrative practice that was in effect on September 9, 1986.²

Under Title 38 of the United States Code (Veterans Benefits), as in effect on September 9, 1986, the payment of benefits to a beneficiary pursuant to any of the veterans' laws is exempt from taxation. As a result, an allowance or in-kind benefit that could be classified as a "payment of benefits" as of September 9, 1986 is excludable from income under Internal Revenue Code section 134.

Present law is unclear on whether waivers and settlements of veterans' indebtedness are "payment of benefits." If these waivers and settlements are "payment of benefits," they would be "qualified military benefits" excludable from income under Internal Revenue Code section 134. On the other hand, if these waivers and settlements are not "payment of benefits," they would be treated as discharges of indebtedness.

Discharges of indebtedness generally are includible as income under Internal Revenue Code section 61(a)(12), except when the taxpayer is insolvent or in bankruptcy (sec. 108(a)). The IRS, in a private letter ruling, also has held that certain waivers of debt arising from VA-guaranteed home loans that have been assumed are excludable. In the ruling, a veteran with a VA-guaranteed home loan sold his home and the purchaser of the home assumed the mortgage. After the purchaser defaulted on the loan, the VA sustained a loss and held the veteran liable. The VA waived the veteran's liability, which created discharge of indebtedness to the veteran. Under these facts, the IRS held the discharge of indebtedness excludable from income.

The exclusion from discharge of indebtedness income in assumed-loan cases might be justified under several possible legal theories. Present law is unclear on which, if any, of these legal theories is applicable to the assumed-loan cases.

² Thus, "qualified military benefits" generally are excludable only to the extent and scope of the amount authorized on September 9, 1986. See H. Rep. 99-841, Vol. II, September 18, 1986, p. 548 (Conference Report).

Explanation of Provisions

Section 5 of H.R. 939, as reported, amends Title 38 (U.S. Code) to treat as "payment of benefits" the waiver of recovery of a payment or an overpayment of a benefit provided under any of the laws administered by the VA, and the forgoing of collection by the United States in the settlement of a claim with respect to any benefit provided to a veteran or other eligible person under any of the laws administered by the VA.

H.R. 939, as reported, would apply to waivers that were made, and amounts that were forgone, before, on, or after, the date of enactment.

III. Possible Option

Amend the Internal Revenue Code to clarify that waivers and settlements of veterans' indebtedness for certain VA-guaranteed home loans are excludable from income. The exclusion would apply only where a veteran with a VA-guaranteed home loan sold his or her home and the purchaser of the home assumed the mortgage. In these instances, if the purchaser defaulted, and the VA paid off the loan, any waiver or settlement of the liability of the veteran would be excludable from the veteran's income.

This clarification would apply to waivers that are made, and amounts that are forgone, on or after the date of enactment. No inference would be intended with respect to the proper interpretation of present law.