

## Big News from Congress...Mortgage Insurance now Tax Deductible!

Provided to you by: Susan Davis – Mortgage Planner



As you probably know, Private Mortgage Insurance (PMI) is required any time a loan is taken out with a higher "loan to value" ratio of 80%, as the loan is riskier to the lender. Mortgage Insurance allows a consumer to purchase a home with little or no down payment, or refinance at higher loan to values than 80%...but the beneficiary of the Mortgage Insurance is the lender, as it only provides coverage to the lender to protect against financial loss should the homeowner default on the loan.

And historically, these Mortgage Insurance premiums have never been tax deductible, so many consumers turned to the "piggyback" loan strategy. A "piggyback" means the first mortgage is placed at 80% of the value of the home - therefore not requiring mortgage insurance - and the additional funds needed to finance the home were placed on a second home loan, "piggybacked" behind the first mortgage...and providing more tax-deductible interest.

But these second home loan rates have risen dramatically higher in recent years, since most are tied to the Fed Funds Rate...and the Fed has made seventeen .25% rate hikes since June 2004 - a total increase of 4.25%! And although the Fed is currently in a "paused" mode...there is debate as to whether or not the Fed is done hiking rates just yet.

**But in the final session hours of 2006 - Congress passed a law with a change to the tax code which will allow Mortgage Insurance Premiums to be claimed as tax deductions for households earning less than \$100k annually.**

### **What does this mean?**

Primarily, it means that mortgage options that include standard Private Mortgage Insurance will now become much more competitive and attractive, especially as the Mortgage Insurance premium payment can often be later removed with sufficient property appreciation or declining loan balance, assuming timely payments. In fact, hundreds of thousands of 2007 homebuyers or home refinancees will save an estimated total of \$91,000,000 when they file their tax returns in 2008.

### **A few important notes:**

The current legislation applies to new loans closed in 2007 only, and as such, will

require another act of Congress to be extended to 2008 and beyond.

The full deduction can only be taken if your Adjusted Gross Income is \$100,000 or less. There is a rapidly declining proration table for incomes up to \$110,000, with no deductibility if your Adjusted Gross Income exceeds that level.

The deduction is only available if you itemize your deductions on your tax return, rather than taking the standard deduction. For most homeowners, itemizing generally makes more financial sense anyways, due to the large amount of home loan interest and real estate taxes paid, but a small mortgage may not generate enough interest charges to itemize. As a rule of thumb, the mortgage normally needs to be around \$130,000 for itemizing to make good financial sense.

And although the initial payment with a Mortgage Insurance premium might be slightly higher when compared to a "piggyback" option - remember that Mortgage Insurance can often be removed in time, with property appreciation or a declining loan balance, assuming payments are being made in a timely manner.

***And of course, whenever the IRS is concerned...it always makes sense to review specifics with a tax professional. We'd be happy to make a recommendation to you or your clients if you like. As always, please call with any questions - we'd be happy to get answers about these changes for you, or anyone who might be looking into a mortgage in the New Year!***

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