

Mortgage Insurance Deduction Extended for Three Years in Mortgage Forgiveness Debt Relief Act of 2007



Mortgage insurance will continue to be deductible after 2007, thanks to a key provision in the recently enacted Mortgage Forgiveness Debt Relief Act of 2007. The new law extends the mortgage interest deduction, which was set to expire at the end of 2007, for three years (through 2010). Here is a brief overview of this potentially valuable deduction.

Financing a home with a small down payment. When you buy a house, lenders consider you a riskier borrower if you make a down payment of less than 20%. There are two main ways to make you pay for that risk: mortgage insurance and piggyback loans. Mortgage insurance is insurance that is paid for by the borrower, but the lender is the beneficiary. If the borrower falls behind on the loan payments and the lender has to foreclose, the mortgage insurance policy reimburses the lender for legal costs and lost income. The premiums depend on the size of the loan, the percentage of the down payment, the borrower's credit score and the type of mortgage insurance the borrower gets.

Alternatively, a borrower with less than the 20% down payment needed to avoid a mortgage insurance requirement might be able to make use of a second mortgage (sometimes referred to as a piggyback loan) to make up the difference. One advantage of using a piggy-back arrangement was that under prior (pre-2007) law, mortgage interest payments were deductible on the borrower's income taxes, whereas mortgage insurance premiums were not.

How the mortgage interest deduction works. Under the deduction that was originated in 2007 and has now been extended for three years (through 2010), taxpayers can treat amounts paid during the year for qualified mortgage insurance as home mortgage interest and thus deductible. The insurance must be in connection with home acquisition debt, the insurance contract must have been issued after 2006, and the taxpayer must have paid the premiums for coverage in effect during the year. Qualified mortgage insurance is mortgage insurance provided by the Department of Veterans

Affairs, the Federal Housing Administration, or the Rural Housing Service, and private mortgage insurance (as defined in section 2 of the Homeowners Protection Act of 1998 as in effect on December 20, 2006).

Mortgage insurance provided by the Department of Veterans Affairs is commonly known as a funding fee. If provided by the Rural Housing Service, it is commonly known as a guarantee fee. The funding fee and guarantee fee can either be included in the amount of the loan or paid in full at the time of closing. These fees can be deducted fully in the year the mortgage insurance contract was issued.

Premiums for qualified mortgage insurance that are properly allocable to periods after the close of the tax year are treated as paid in the period to which they are allocated. No deduction is allowed for the unamortized balance if the mortgage is satisfied before its term (except in the case of qualified mortgage insurance provided by the Department of Veterans Affairs or Rural Housing Service).

There are income limits on the deduction. You can get the full deduction if your adjusted gross income is \$100,000 or less (\$50,000 if your filing status is married filing separately). The amount you can deduct phases out rapidly after that, and no mortgage insurance deduction is available if you make more than \$109,000 (\$54,500 if married filing separately).

We hope this information is helpful. Please keep in mind that this is only a summary of the mortgage insurance deduction portion of the Mortgage Forgiveness Debt Relief Act of 2007. If you would like more details about this change, or any other aspect of the new law, please do not hesitate to call and schedule an appointment with us.

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555 South Renton Village Place, Suite 700 Renton, WA 98057; Phone: (425) 271-3550