

Newsletter

**RIOLO
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CERTIFIED PUBLIC
ACCOUNTANTS

AUGUST 2009

MORTGAGE DEBT RELIEF ~ ANSWERS TO FREQUENTLY ASKED QUESTIONS

To compound the financial woes resulting from a foreclosure or other mortgage restructuring for your home, the IRS generally imposes tax when debt is cancelled. In other words, you're taxed on the amount forgiven by the lender as if you actually received it as income. However, Congress provided some relief to homeowners under the Mortgage Forgiveness Debt Relief Act of 2007.

Here are the answers to several common questions in this area ~

- ◆ What relief does the new law provide? Generally, it excludes tax on cancellation-of-debt income realized from a foreclosure, short sale, or other mortgage restructuring. This tax break only applies to debt used to buy, build, or improve your principal residence. It isn't available for vacation homes or investment property.
- ◆ Is there a limit? Yes. The exclusion can cover the tax due on up to \$2 million of forgiven debt (\$1 million if you're married and file separate tax returns). Any excess is taxable under the general rules.
- ◆ How does the exclusion affect your basis in the home? You must reduce your basis (the amount used to determine taxable gain or loss from a home sale) by the amount of cancelled debt excluded from taxable income. For example, if a loan restructuring results in cancellation of \$50,000 of debt on a home with a basis of \$450,000, your basis is reduced to \$400,000. This could increase your taxable gain when you sell the home, although the first \$250,000 of gain (\$500,000 for joint filers) may still be sheltered by the home sale exclusion.
- ◆ How do I know how much debt is excluded? Your lender will send you Form 1099-C (Cancellation of Debt) showing the amount of debt forgiven and the fair market value of property given up through foreclosure. A copy of the form is also sent to the IRS. The IRS encourages homeowners to check this information carefully.
- ◆ What is a short sale? Instead of foreclosing on a home, a lender may allow you to sell it for less than the mortgage amount and take the proceeds in full satisfaction of the debt. For instance, let's say you still have a mortgage of \$250,000 on your home, but the home's value has dropped to \$225,000. Assuming the bank agrees to a short sale and you incur \$15,000 in selling expenses, you turn over the remaining \$210,000 to the bank. The \$40,000 difference, which will be reported on Form 1099-C, qualifies for the new tax exclusion on cancellation-of-debt income.
- ◆ Is the new tax relief permanent? No. Initially, the tax exclusion only applied to debt forgiven in 2007, 2008, or 2009. However, the economic stimulus law passed last year – the Emergency Economic Stabilization Act of 2008 – extended this tax break for three years through 2012.

This is just a brief overview of the new mortgage debt relief available to homeowners. Please call us if you have questions pertaining to your situation.

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A NEW VEHICLE COULD BRING TAX SAVINGS

If you're thinking of buying a new car, truck, motorcycle, or motor home this year, you might benefit from a tax break included in the Recovery Act of 2009.

Here are the details ~

- ◆ You can deduct state and local sales taxes paid on up to \$49,500 of the purchase price of a qualifying vehicle.
- ◆ Qualifying vehicles generally include new (not used) cars, light trucks, motorcycles, and motor homes purchased after February 16, 2009, and before January 1, 2010.
- ◆ The deduction can be claimed on your 2009 tax return regardless of whether or not you itemize other deductions.
- ◆ The deduction phases out for single taxpayers with income between \$125,000 and \$135,000. For joint filers, the phase out range is \$250,000 to \$260,000.

For more information or planning assistance, please give us a call.

This newsletter provides business, financial, and tax information to clients and friends of our firm. This general information should not be acted upon without first determining its application to your specific situation.

For further details on any article, please contact us.