

## CLIENT ALERT

# Housing and Economic Recovery Act of 2008 contains major tax incentives

August 2008

On July 30, 2008, President George W. Bush signed the Housing and Economic Recovery Act of 2008 (H.R. 3221) into law. The new law is intended to support homeowners and the housing industry, and it includes more than \$15 billion in tax incentives. Below, we have summarized some of the major incentives – and revenue raisers – in the Housing Act. As always, we encourage you to contact your Williams-Keepers LLC tax advisor if you have any questions.

### Tax Incentives

**First-time homebuyer tax credit.** One tax incentive in the new law, the first-time homebuyer tax credit, has been getting a lot of attention in the news, but be careful. The credit, while generous, is essentially an interest-free loan from the government. Taxpayers who take the credit, which equals 10 percent of the purchase price (up to \$7,500 for single individuals and married couples filing jointly; \$3,750 for married individuals filing separate returns) must repay the credit. They will have 15 years to repay the credit in equal amounts. If a taxpayer sells his or her home before the end of the 15-year period, he or she will likely have to immediately repay any outstanding balance. Important income thresholds also apply. Additionally, the credit is temporary and applies to homes purchased on or after April 9, 2008, and before July 1, 2009. There are also complex rules about who can take it, when they can claim it and so on. Please contact us if you have any questions about this potentially valuable but complicated new credit.

**Property deduction for non-itemizers.** Significantly less complicated is a new standard property deduction for taxpayers who do not itemize deductions. Before the new law, only itemizers could deduct state and local property taxes. The Housing Act gives non-itemizers a limited deduction for state and local property taxes by increasing the amount of their standard deduction by the lesser of the amount of property taxes they paid or \$500 (\$1,000 for a married couple filing jointly). If you have paid off your mortgage and no longer itemize, you might benefit from this new deduction. As now written, however, this is a one-year shot in the arm, available only for taxes paid in 2008.

**Borrowers.** Many homeowners are trying to refinance mortgages that initially offered low teaser rates but have skyrocketed. The new law authorizes states to issue \$11 billion more in mortgage revenue bonds for 2008 and allows qualifying subprime borrowers to use their state's mortgage revenue bond program to refinance into a loan with a more favorable rate. The Housing Act also creates a new program

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called “HOPE for Homeowners” to help homeowners refinance their mortgages. Both provisions are temporary.

**Businesses.** The Economic Stimulus Act of 2008 included bonus depreciation to encourage businesses to increase investment. However, companies in a loss position cannot take advantage of bonus depreciation because they do not have any taxable income against which to take the deductions. The Housing Act allows taxpayers (corporations) to use accumulated alternative minimum tax (AMT) credits as well as research and development (R and D) tax credits to make investments that would qualify for bonus depreciation, if the taxpayers were profitable. The new law also dramatically changes the information reporting requirements of banks and other processors of merchant payment card transactions. Starting in 2011, they will be required to report a merchant’s annual gross payment card receipts to the IRS and the merchant. Congress believes that enhanced information reporting will help close the \$300 billion tax gap, the difference between what taxpayers owe and what they actually pay.

**Home sale exclusion.** The home sale exclusion is one of the most popular tax breaks in the Tax Code. A married couple filing jointly can generally exclude up to \$500,000 in gain (single individuals up to \$250,000). Before the new law, if a second home becomes a principal residence, after two years the owner could sell it and exclude up to \$250,000 in gain from their income or up to \$500,000 for couples filing jointly. The Housing Act closes what some call a “loop hole.” The new law pro-rates the exclusion between the time that a home is used as a principal residence and the total length of ownership, which includes any “non-qualifying” use as a rental or vacation property. As good news to those who have already owned property for a while and have seen it appreciate, non-qualifying use before the January 1, 2009 effective date of the provision is not used in the calculation; neither are periods after a qualified use of the property or temporary absences of less than two years.

**Real estate investment trusts.** A real estate investment trust (REIT) holds passive investments in real property equity and mortgages. Like the rules for tax-exempt bonds and the LIHTC, the rules for REITs are complex. If a REIT violates these rules, the tax consequences can be severe. The Housing Act clarifies some of the rules, such as allowing REITs to treat certain foreign currency gains as qualified income for purposes of income tests. Congress also clarified other aspects of the income tests and authorized the IRS to determine if other items should be treated as qualified income for purposes of the income tests, among other changes.

**Down payment assistance.** Seller-funded down-payment-assistance programs provide cash assistance to homebuyers who cannot afford to make the minimum down payment or pay the closing costs involved in obtaining a mortgage. Despite their popularity, these programs have been criticized for helping to inflate home prices.

In 2006, the IRS ruled that organizations that provide seller-funded down-payment assistance to home buyers do not qualify as tax-exempt charities. The new law bans seller-funded down payment assistance programs.

**Military personnel.** The Housing Act includes many provisions to help military personnel on active duty and veterans avoid foreclosure. Under the new law, service members and veterans are protected from foreclosure for nine months following a period of military service (rather than the current 90 days). Congress also made the VA home loan program more attractive and provided funding for disabled veterans to make accommodations in their homes for their disabilities.

**Affordable housing.** Tax-exempt housing bonds and the low-income housing tax credit (LIHTC) help to fund the construction of affordable housing units. The rules for tax-exempt housing bonds and the LIHTC are extremely technical. The Housing Act simplifies these rules and makes other changes, such as excluding tax-exempt interest on certain housing bonds from being a preference item for AMT purposes. The Housing Act also allows taxpayers to use the LIHTC and the rehabilitation tax credit to offset AMT liability. Congress also enhanced the rehabilitation tax credit and some special tax breaks for taxpayers in the Gulf Opportunity Zone.

## **More provisions**

The Housing Act completely overhauls government regulation of Fannie Mae and Freddie Mac, creating a new regulator for these entities, which own or guarantee nearly half of all U.S. mortgages. Congress also authorized the U.S. Treasury to help fund Fannie Mae and Freddie Mac if needed. Additionally, the new law sets minimum standards for mortgage brokers, strengthens the Truth in Lending Act and funds foreclosure prevention counseling.

## **Contact us**

For more information on the tax implications of the Housing and Economic Recovery Act of 2008, contact us at (573) 442-6171 or (573) 635-6196, or visit our Web site at [www.williamskeepers.com](http://www.williamskeepers.com).

Sincerely,



Williams-Keepers LLC