

INCENTIVES FOR HOMEBUYERS

In recent months, Congress has passed two major tax bills in hopes of spurring a rebound in the housing market. Below is a summary of the provisions of the 2008 legislation immediately followed by changes and updates in the 2009 law.

HOUSING ASSISTANCE ACT OF 2008

(Note: This section contains the original provisions of the 2008 tax legislation. See the changes made by the 2009 legislation below.)

The single largest provision in the \$15.1 billion package of housing tax incentives in the recently enacted Housing Assistance Tax Act of 2008 (the "Housing Act") is a measure allowing individuals buying their first home to take a tax credit of up to \$7,500 of the purchase price. Qualified homebuyers can subtract the credit amount from their federal income tax when they buy a home and even get a refund if the credit exceeds the tax. However, they are then required to pay the credit back over 15 years. The result is that the credit resembles an interest free loan that must be repaid to the government. Here are the details of the new credit:

- The home must be located in the U.S. and must be the taxpayer's principal residence (main home). The taxpayer (and the taxpayer's spouse if married) must not have owned another principal residence in the U.S. in the three-year period before purchasing the new home. Thus, the home doesn't literally have to be the taxpayer's first home.
- The home must have been purchased from April 9, 2008 through June 30, 2009, inclusive. Purchases from certain related persons and acquisitions by gift or inheritance don't qualify. A home constructed by the taxpayer does qualify if the taxpayer moves in from April 9, 2008 through June 30, 2009.
- A special rule allows taxpayers who purchase a principal residence in the first six months of 2009 to treat the purchase as if made on Dec. 31, 2008. This allows the taxpayer to claim the credit for 2008 rather than 2009.
- The credit is equal to 10% of the price paid for the home, up to a maximum of \$7,500. The \$7,500 maximum credit applies both to individuals and married couples filing a joint return. A married individual filing separately can claim a maximum credit of \$3,750.
- The credit is phased out for individual taxpayers with modified adjusted gross income (AGI) between \$75,000 and \$95,000 (\$150,000 and \$170,000 for joint filers) for the year of purchase. Taxpayers with modified AGI over \$95,000 (\$170,000 for joint filers) can't claim the credit.

- The credit is refundable, meaning that households with incomes too low to owe income tax can benefit from it.
- In the second year after purchase, taxpayers who took the credit must start paying back the credit in equal installments over 15 years, with no interest charge. This works as follows. Suppose a first-time homebuyer purchases a home for \$100,000 this coming December and claims the maximum credit of \$7,500 on his 2008 tax return. He would then be required to pay back \$500 (one-fifteenth of the credit) on his tax return for 2010 and for each of the following 14 years, through 2024.
- If the taxpayer sells the home (or the home ceases to be the principal residence of the taxpayer or the taxpayer's spouse) before complete repayment of the credit, any remaining credit is due on the tax return for the year in which the home is sold (or ceases to be the principal residence). If the home was sold at a loss to an unrelated person, repayment of the remaining credit is forgiven to the extent of the loss.

No credit is allowed if: the taxpayer was ever entitled to a D.C. homebuyer credit; the home purchase was financed through tax-exempt mortgage revenue bonds; the taxpayer is a nonresident alien; or the taxpayer disposes of the residence (or it ceases to be a principal residence) in the year of purchase.

AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009

The Housing Assistance Act of 2008 did not produce the desired results quickly enough. In hopes of spurring the housing industry, the recently enacted "American Recovery and Reinvestment Act of 2009" includes an enhanced tax credit for first-time homebuyers. Here are the details.

The 2008 Housing Act included a tax credit giving first-time homebuyers up to a \$7,500 (actually, \$7,500 or 10% of the purchase price, whichever is less) credit for buying a home between April 8, 2008, and July 1, 2009, with single taxpayers with incomes up to \$75,000 and married couples with incomes up to \$150,000 qualifying for the full tax credit. However, despite high hopes that the credit would be effective in getting people to buy homes and thereby reduce the excessive inventory on the market, the credit is widely acknowledged to have failed in its objective. The problem, according to realtors and industry officials, was that buyers were turned off by the odd way the credit worked.

While the credit functioned initially like other tax credits, reducing a person's tax liability on a dollar-for-dollar basis, it was unusual in that, unlike other federal tax credits (for example, the child credit), the credit for first-time homebuyers had to be paid back to the government ratably over a period of 15 years (or earlier if the house is sold). So, as a practical matter, the credit was the equivalent of an interest-free loan from the government. It was the payback requirement that many in the industry felt kept potential buyers on the sidelines. Now, Congress has beefed up the credit in renewed optimism of enticing more first-time homebuyers to take the plunge. First and foremost, the new legislation scuttles the repayment requirement for homes purchased on or after January 1, 2009. The new law also extends the credit through the end of November 2009, and bumps up the maximum credit amount from \$7,500 to \$8,000. However, the new law retains the recapture provisions if the house is sold within three years of purchase.

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