

Credit for first-time homebuyers in the 2008 Housing Act

Dear Client and Friends:

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. Designed to help reduce the existing stock of unoccupied housing, the tax credit allows qualified homebuyers to subtract the credit amount from their federal income tax when they buy a home. 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:

- Individuals may credit the lesser of \$7,500 or 10% of the price paid for the home against tax owed in the year of purchase. 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 phases out for individual taxpayers with modified adjusted gross income between \$75,000 and \$95,000 (\$150,000-\$170,000 for joint filers) for the year of purchase.
- In the second year after purchase, taxpayers who took the credit must start adding the credit amount back into taxes paid incrementally over 15 years with no interest charge. This would work as follows. Suppose a first-time homebuyer purchases a home this coming December. He could claim a tax credit equal to 10 percent of the purchase price of the home or \$75,000, whichever is smaller, on his 2008 tax return. Assuming for purposes of this example that the amount of his credit is \$7,500, he then would be required to pay \$500 (one-fifteenth of the credit) back on his 2010 tax return and on his return for each of the following 14 years.
- If the taxpayer sells the home (or the home ceases to be used as the principal residence of the taxpayer or the taxpayer's spouse) prior to complete repayment of the credit, any remaining credit repayment amount is due on the tax return for the year in which the home is sold (or ceases to be used as the principal residence). However, the credit repayment amount may not exceed the amount of gain from the sale of the residence to an unrelated person. For this purpose, gain is determined by reducing the basis of the residence by the amount of the credit to the extent not previously recaptured. No amount is recaptured after the death of a taxpayer. In the case of an involuntary conversion of the home, recapture is not accelerated if a new principal residence is acquired within a two-year period. In the case of a transfer of the residence to a spouse or to a former spouse incident to divorce, the transferee spouse (and not the transferor spouse) will be responsible for any future recapture.

- The tax credit is refundable, meaning that households with incomes too low to owe income taxes could benefit from it.
- The credit applies to homes purchased on or after April 9, 2008 and on or before July 1, 2009. A special rule allows those who purchase a principal residence after Dec. 31, 2008, and before July 1, 2009, to treat the purchase as made on Dec. 31, 2008 (effectively allowing them to claim the credit on their 2008 returns rather than on their 2009 returns).
- A taxpayer is considered a first-time homebuyer if the individual (and the individual's spouse if married) had no ownership interest in a principal residence in the U.S. during the 3-year period prior to the purchase of the home to which the credit applies.
- No credit is allowed if the D.C. homebuyer credit is allowable for the taxable year the residence is purchased or a prior tax year, the taxpayer's financing is from tax-exempt mortgage revenue bonds, the taxpayer is a nonresident alien, the taxpayer disposes of the residence (or it ceases to be a principal residence) before the close of the tax year for which the credit otherwise would be allowable, or the home is acquired from certain related persons or by gift or inheritance.

I hope this information is helpful. If you would like more details about this provision or any other aspect of the new law, please do not hesitate to call.

Very truly yours,

Paresky Flitt & Company, LLP