

Home Ownership Offers Lucrative Tax Benefits

By J. Lennox Scott

More than 75 years ago, the U.S. government decided to award homeowners a lucrative tax break, permitting them to deduct home loan interest from their personal taxable income. Although Washington State does not have an income tax, residents are still allowed to take this deduction from their annual federal tax return.

This benefit is particularly useful to first time homebuyers because during the early years of their home loan, most of the monthly payment goes to pay deductible interest rather than the principal. For example, at the end of the first year of a thirty-year fixed rate mortgage at six percent, less than one percent of the principal is repaid. However, the benefit to the new homeowner is that they can deduct the amount that they paid toward interest on their loan, from their federal tax return.

The longer the term of the mortgage, the higher the tax savings will be for the homeowner. This is because there is more interest paid on a thirty year mortgage than there is on a fifteen year equivalent. However, keep in mind, even when the tax savings is taken into account, a fifteen-year mortgage will probably cost less in the long run because the loan is paid off in half the time.

To take advantage of tax deductions homeowners must switch from standard deductions to itemized deductions. The three main deductions that homeowners can take are mortgage interest, property taxes, and loan points. Loan points are fully deductible from federal tax returns in the same year that they are paid.

Property taxes are also deductible with the exception of certain government fees, such as water and sewer assessments. Tax levies vary from one district to the next, however every homeowner is taxed based upon the assessed value of their property. In Washington State, the constitution requires property to be revalued every four years. Homeowners are entitled to contest reassessments that are made on their home. Over half of the people who protest their tax assessment get them reduced, saving themselves hundreds of dollars in property tax payments. Homeowners who have questions about their assessment can contact the local tax assessor for more information.

When a buyer closes on their new home, the lender prorates interest owed and property taxes, collecting enough to cover their fees until the next payment period. Homeowners need to keep a record of this amount. The lender sends out a 1099 form at the end of the year for tax filing purposes that lists interest paid for the year. Homeowners who have kept accurate records can verify this amount and new home owners should make sure that the prorated tax that they paid at closing is also included.

The U.S. government offers a variety of tax breaks for homeowners, but tax guidelines can be complicated, so if you have questions contact a tax specialist.

REALTOR® J. Lennox Scott is the Chairman and CEO of John L. Scott Real Estate. You can visit his Web site at www.johnlscott.com

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Shelley Rossi
Director of Public Relations
John L. Scott Real Estate
(206) 230-7627
shelleyro@johnlscott.com