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## Highlights of the 2008 Housing Act

H.R. 3221, the "American Housing Rescue and Foreclosure Prevention Act of 2008" was signed into law by the President on July 30, 2008. This sweeping measure is designed to shore up the ailing housing market as well as tighten lending practices and reform financial institutions associated with that market. It also contains a number of tax changes in Division C of H.R. 3221, the "Housing Assistance Tax Act of 2008,"—the 2008 Housing Act—including tax breaks for homebuyers and homeowners, relaxed requirements for tax-exempt bonds, eased AMT rules, tax changes for businesses, as well as highly specialized changes affecting low-income housing and special investment vehicles called Real Estate Investment Trusts (REITs).

### **A tax credit—with a twist— for first-time homebuyers.**

The new law gives first-time homebuyers a \$7,500 tax credit (or, in the unlikely event the home costs less than \$75,000, a credit equal to 10% of the home's purchase price). The top credit amount is \$3,750 for married persons filing separate returns. The new credit, like other tax credits, reduces a person's tax liability on a dollar-for-dollar basis (and if the credit is more than the tax you owe, the difference is paid to you as a tax refund). However, unlike other Federal tax credits (for example, the child credit), the new credit must be paid back to the Government ratably over a period of 15 years. So, as a practical matter, the new credit for first-time homebuyers is the equivalent of an interest-free loan from the Government.

A number of terms and conditions must be met for the credit to apply. The two key rules are that:

- (1) you (and if married, your spouse) didn't own a principal residence during the 3-year period before you make the credit-eligible home purchase; and
- (2) you must buy a new principal residence after April 8, 2008, and before July 1, 2009.

The credit for new homebuyers is available in full only if AGI (adjusted gross income, with some modifications for highly specialized income) doesn't exceed \$150,000 if you file a joint return (\$75,000 for all other filers). The credit phases out over the \$150,000 to \$170,000 AGI range for joint filers (\$75,000 to \$95,000 for all other filers).

In general, you claim the credit on the tax return you file for the year you buy the principal residence. However, if you buy the home after Dec. 31, 2008, and before July 1, 2009, you have the option of claiming the credit on your 2008 tax return instead of your 2009 tax return.

You'll have to start paying back the credit over 15 years as an extra tax amount on your Federal returns beginning with the tax return for the second year after the year in which you buy the new home. First-time homebuyers who buy principal residences in 2008, and claim a \$7,500 credit, will pay it back (1) starting with the 2010 tax return they file in 2011, and (2) ending with the 2024 tax return they file in 2025, at the rate of \$500 per year.

In general, the payback of the credit is accelerated if you sell the principal residence (or stop using the home as your principal residence) before the end of the pay-back period.

Property tax deduction for non-itemizers. For 2008 only, those who take the standard deduction instead of itemizing deductions may claim an additional standard deduction for State and local property taxes paid (but taxes written off as business deductions don't count). The deduction is \$1,000 for joint return

and \$500 for all other filers (or actual property tax paid, if that's less).

### **Reduced homesale exclusion for some sellers.**

After 2008, some homesellers who don't use their properties as principal residences for their entire ownership period may wind up paying more of a tax bill than they would under current rules (or pay tax when none would be owed currently). The tax break affected is the homesale exclusion, which generally allows up to \$250,000 of homesale profit to be tax-free if a home was owned and used by the seller as a principal residence (i.e., main home) for at least 2 of the 5 years before the sale. In general, the tax-free break can only be used once every 2 years. The tax-free profit amount is up to \$500,000 for married taxpayers filing jointly for the year of sale if several conditions are met. A reduced maximum exclusion may apply to taxpayers who must sell their principal residence because of health or employment changes (or certain unforeseen circumstances) and as a result (1) fail the 2-out-of-5-year ownership and use rule, or (2) previously used the homesale exclusion within two years.

For sales after 2008, the homesale exclusion will be reduced proportionately for the period of time a home wasn't used as a principal residence. The prime example is a vacation home that is turned into a principal residence by its owners, but the new rule also can hit individuals who use a property as a main home for a while, rent it out for a period of time, and then move back in. There are, however, a number of exceptions. For starters, pre-2009 periods of non-principal-residence use don't count, and neither do periods of temporary absence totaling no more than 2 years due to health or employment changes (or certain unforeseen circumstances), or up to 10 years of absence for qualifying members of the military or certain government employees. Finally, non-principal-residence use doesn't count if it occurs (1) in the five years preceding the sale, but (2) after you permanently stop using the home as a main home.

As you can see, the new rule is quite complex and down the road will cause big headaches for some homesellers unless they're careful and get an expert's advice.

### **Specialized AMT relief provisions.**

The AMT (alternative minimum tax) means a higher tax bill only if the "tentative minimum tax" (the tax found by applying the AMT rules) exceeds the regular tax bill. The AMT is a hazard because many tax breaks ("preferences") allowed for purposes of calculating regular taxes are disallowed for AMT purposes, and some types of income exempt from regular tax are added back to arrive at tentative minimum tax.

The new law includes the followed specialized relief measures for individuals and businesses:

- The tax rules provide an income tax credit for putting up low-income housing, and another income tax credit for rehabilitating older buildings. Under current rules, these tax credits are allowed in full against regular income taxes, but can't be used to offset the AMT. Under the new law, the low-income housing credit claimed for buildings put in service after 2007, and the rehabilitation credit for post-2007 expenses, can both be used to offset the AMT.
- Interest on certain tax-exempt private activity bonds is taxed for AMT purposes even though it's tax-free for regular tax purposes. The new law exempts from the AMT three special classes of bonds issued after July 30, 2008: (1) certain exempt facility bonds used at least 95% for qualifying residential rental projects; (2) qualifying mortgage bonds; and (3) qualifying veterans' mortgage bonds.

### **New writeoff choices for corporations.**

To stimulate a sagging economy, the Economic Stimulus Act of 2008 (signed into law in February of this year) allowed businesses to claim a bonus first-year depreciation deduction of 50% for most personal property and software acquired and placed in service after 2007 and before 2009. However, many corporations are struggling and can't make good use of the enhanced depreciation writeoff. The Housing Act gives such corporations an alternative tax break. For tax years ending after Mar. 31, 2008,

corporations otherwise eligible for bonus depreciation may instead elect to claim additional research tax credits or certain minimum tax credits. This alternative choice is highly specialized and will require detailed analysis of a corporation's tax situation.

**Information reporting of merchants' credit card transactions.**

After 2010, banks will be required to file an information return with the IRS reporting the total dollar amount of credit and debit card payments a merchant receives during the year, along with the merchant's name, address, and taxpayer identification number (TIN). Similar reporting also will be required for third party network transactions (e.g., those facilitating online sales), with exceptions for certain small merchants. The new information reporting requirement is designed to boost the tax compliance rate of merchants.

Please keep in mind that we've described only the highlights of the tax changes in the new Housing Act. If you would like more details, please call our offices at your earliest convenience.