

Patrick J. Deo, CPA, Cr.FA
pat@dldcpa.com
Anthony LaManna, CPA
tonyl@dldcpa.com
Michael J. Deo, CPA
miked@dldcpa.com

CLIENT ALERT

LAST MINUTE 2007 YEAR END TAX LAWS

Almost a repeat of last year, Congress finally passed important and significant tax legislation which will save taxpayers across the country billions of dollars of taxes – with the majority of the savings going to the proverbial forgotten “middle class.”

Unfortunately, the delay in passage will cause a delay in processing returns. The Internal Revenue Service anticipates millions of returns not being able to be processed and refunds issued until the middle of February.

ALTERNATIVE MINIMUM (AMT) PATCH

The Tax Increase Prevention Act of 2007 (H.R. 3996) extends the AMT patch – but only for one year – 2007. If this law was not passed, the Internal Revenue Service predicted that for 2007 as many as 25 million taxpayers would have faced, on average, a \$2,000 tax increase.

1. HIGHER AMT EXEMPTION AMOUNTS

The 2007 AMT exemption amounts are:

- \$44,350 for single taxpayers and heads of household;
- \$66,250 for married couples filing jointly; and
- \$33,125 for married filing separately.

2. NONREFUNDABLE PERSONAL CREDITS

For 2007, the new law allows taxpayers to use most nonrefundable personal credits to offset the AMT liability. These include the Dependent Care, Hope and Lifetime Learning Education Credits. The law continues to allow the adoption, child and saver’s credits to the full extent of the individual’s regular tax and AMT.

MORTGAGE FORGIVENESS DEBT RELIEF ACT OF 2007

1. FORCLOSURE RELIEF

When a lender forecloses on property, sells the home for less than the borrower's outstanding mortgage and forgives all or part of the unpaid mortgage debt, the tax code normally would consider the cancelled debt to be taxable income to the homeowner. This new law excludes from taxation up to \$2 million of forgiven indebtedness that is secured by a principal residence, which was incurred in the acquisition, construction or substantial improvement of the principal residence. This special relief is available for three years beginning January 1, 2007, and ending December 31, 2009.

In addition, mortgage renegotiations are also included in the law's new exception to forgiveness of debt income. So, if a lender determines that foreclosure is not in its best interest and offers a mortgage workout under which the terms of the mortgage are changed to a lower monthly payment, this could technically result in forgiveness of indebtedness income that would be taxable to the homeowner if it were not for the new law.

The new law applies to qualified principal residence indebtedness. This generally means mortgages incurred in the acquisition, construction, or substantial improvement of your principal residence. It also includes refinancing of this debt to the extent that refinancing does not exceed the amount of the original indebtedness. Consequently, home equity loans used to pay off credit card debt, tuition, medical expenses, or other expenditures, are not covered by the new law. That forgiveness of indebtedness income is still fully taxable income. The new law also does not apply to vacation homes or other second residences.

If forgiveness of debt is not taxable under the new law, the basis in your residence is reduced by the amount excluded from income. This most likely results in complete tax forgiveness for most taxpayers, since the \$250,000 gain excluded on the sale of a principal residence (\$500,000 for married couples filing jointly) generally covers most gains.

2. PRIVATE MORTGAGE INSURANCE (PMI) DEDUCTION

The Tax Relief and Health Care Act of 2006 (P.L. 109-432) temporarily allowed taxpayers to take an itemized deduction for PMI, similar to mortgage interest. The new law temporarily extends the deduction for PMI for three years, through December 31, 2010 for contracts entered into after December 31, 2006, or prior to January 1, 2011. Note: The deduction is phased out at 10 percent for each \$1,000 by which our income exceeds \$100,000.

3. SURVIVOR SPOUSE HOME SALE EXCLUSION

In an important development for recently widowed spouses, the new law extends the period of time during which a surviving spouse may use the joint return filers' \$500,000 home sale gain exclusion before being treated as a single individual entitled only to a \$250,000 exclusion.

Starting January 1, 2008, the sale of a residence that had been jointly owned and occupied by the surviving and deceased spouse is entitled to the \$500,000 gain exclusion provided the sale occurs no later than two years after the date of death of the individual's spouse.

4. VOLUNTEER EMERGENCY RESPONDERS

The foreclosure relief bill also gives volunteer firefighters and emergency medical responders some tax relief. Individuals who receive a qualified state and local tax benefit, or any reduction or rebate of a tax, and qualified payments of up to \$360 each year, provided on account of their volunteer services, can exclude these benefits from income. This treatment applies to tax years beginning after December 31, 2007.

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