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**3.04.08**

# Some Home Loans not Deductible

**By Stephen J. Kipp, Special to the Star**

Have you refinanced, taken out a second mortgage, or used a home-equity line of credit? If you are subject to the alternative minimum tax (AMT), you may not be able to take a tax deduction for all of the interest on such loans.

All taxpayers must calculate their taxes under two sets of rules, for normal income tax and the AMT. You pay the higher tax. Even if you're not subject to AMT rules now, you could be soon. The number of AMT taxpayers soared from about 3 million in 2004 to over 20 million in 2006, and will likely continue to rise throughout the decade.

One deductive not allowed under AMT rules is for interest paid on home-equity loans. Forget what lenders mean by that term –as far as the Internal Revenue Service is concerned, home-equity debt is any loan secured by your residence but used for something other than buying or improving the home.

Suppose you've been approved for a line of credit based on your equity in the property, and you draw out money to cover tuition at your daughter's private college. Or, you take a second mortgage at today's reasonable interest rates and use the cash to pay down more expensive credit card debt. In both cases, if you pay AMT, you can't deduct the interest, because you didn't use the money to purchase or fix your home. In contrast, regular rules permit writing off the interest charged on up to $100,000 of home-equity debt, assuming the loan was made after October 13, 1987. All interest on older mortgages is fully deductible for both regular and alternative tax purposes.

The waters become muddier when refinancing is involved. Suppose you and your spouse borrowed $200,000 several years ago to buy your home. You still owe $160,000, but the property has appreciated substantially and interest rates have fallen so you decide to refinance $240,000. The first $160,000 of your new loan replaces the remaining debt on your purchase, and interest on the amount is deductible under AMT rules. But what about the other $80,000, which accounts for the third of the refinanced amount? Use it to pay for non-home-related expenses say, a luxury cruise and new automobiles — and a third of your interest won't be deductible in years you pay AMT.

Even if you refinance only what you owe on your original loan, closing costs could pose a problem. Suppose you take a new loan for the $160,000 balance on your old $200,000 mortgage, and the lender charges $5,000 to process the transaction. If you pay the closing costs out of pocket, you can deduct all of the interest on the new loan, even under AMT. But if you finance those costs, and thus borrow $165,000, AMT rules stipulate you can deduct only the interest on $160,000 because the older money did not pay for a home purchase or renovation.

(Stephen J. Kipp is CEO and president of Kipp Brant Financial, a wealth and retirement planning firm in Ventura. For more information, call 805-650-7654 or visit the website at www.kippbrantdrummond.com)