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THE MORTGAGE FORGIVENESS DEBT RELIEF ACT OF 2007

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As 2007 wound to a close, Congress passed three bills that the President signed into law on 12/20/07:

1. The [Mortgage Forgiveness Debt Relief Act of 2007](#) excludes debt forgiveness income on residence.
2. The [Tax Increase Prevention Act of 2007](#) authorizes a one-year AMT patch Alternative Minimum Tax.
3. The [Energy Independence and Security Act of 2007](#) extends the FUTA surcharge for an additional year.

Let's discuss the [Mortgage Forgiveness Debt Relief Act of 2007](#). Let's all thank Congress and the President for a legislation that alleviates the plight of homeowners **in danger of losing their homes to foreclosures and repossessions**. The centerpiece of this legislation is a three-year gross income **exclusion for qualifying discharges of home mortgage debt**.

[New Income Exclusion for Home Mortgage Debt Discharges](#). As you know, [Debt Discharge Income \(DDI\)](#) is **taxable** unless an exception applies. The Mortgage Relief Act creates a **new exception** for certain discharges of home mortgage debts that occur from January 2007 (retroactive to 1/1/07) through December 31, 2009 (three full years for 2007, 2008, and 2009). The new exception generally allows a homeowner to **exclude up to \$2 million of "qualified principal residence indebtedness" DDI from gross income**.

The new exception only applies to a debt that's used to acquire, construct, or improve a **principal residence**. It **only helps if you borrowed too much to acquire, build, or improve a principal residence**. It does **not** apply to:

1. **Vacation home** mortgages.
2. A taxpayer in **bankruptcy**.
3. Any factor **not directly related** to a decline in the value of a residence or taxpayer's financial condition.

[Liberalized Home Sale Gain Exclusion for Surviving Spouses](#). Internal Revenue Code Section 121 allows tax-free home sale gains of up to \$250,000 (\$500,000 on a joint return). Before the Mortgage Relief Act, the **larger \$500,000 exclusion was only available when the home seller filed a joint return for the year of sale**. However, an unmarried surviving spouse was **not allowed to file a joint return for years after the year in which his or her spouse dies**. Note that an unmarried surviving spouse can file a joint return for the year of his/her spouse's death, but **not for later years** (even though joint rates may be allowed under the qualifying widow or widower provision). Therefore, the larger \$500,000 home sale gain exclusion **was not available** when an unmarried surviving spouse sold a principal residence in a year **after** the year of the spouse's year of death. The new Mortgage Relief Act allows an unmarried surviving spouse to **take advantage of the larger \$500,000 exclusion** if the home sale occurs **within two years after the spouse's death** and all the other requirements for the \$500,000 exclusion were met immediately before that spouse's death. The two-year period starts on the deceased spouse's date of death.

[Mortgage Insurance Premium Deduction Extended for Three Years](#). Premiums for qualified mortgage insurance on acquisition indebtedness on your qualified residence are **treated as qualified residence interest**. Before the Mortgage Relief Act, this favorable rule only applied to premium amounts that: (1) were paid or accrued before 1/1/08. The new law extends the favorable rule for **three more years** to cover premium amounts paid or accrued 1/1/07 through 12/31/10.