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First Time Buyer

If you're a first time buyer you've probably heard that buying a home may offer important tax advantages. If you've never owned a home, you may not understand what that means.

Actually, tax advantages may be so favorable they're the reason many people decide to buy a home rather than rent. Although many people enjoy the pride and sense of accomplishment that comes with owning a home, it's the tax advantages that often prompt many renters to make the plunge and buy a home.

The tax advantages to owning a home may come in three stages. First, when you own a home, the money you spend on home mortgage interest and on real estate taxes may be deductible from your taxable income, if you itemize deductions. The savings come in income taxes that you don't have to pay.

Just as an example, let's say you buy a home and your mortgage payment is \$1,500 a month, including taxes. In the early years of a mortgage most of the payment is interest, so almost all of that \$1,500 would be deductible when you itemize deductions on your income tax return.

When you multiply \$1,500 a month times 12 months, you get \$18,000 much of which could be deductible from your taxable income. If you are paying income tax at a rate of 28 percent, an \$18,000 deduction means a tax savings of just over \$5,000... or more than \$400 a month. It's easy to see why people decide to buy. In this example, not only do you get a place to live, you get a taxbreak of \$5,000, and all of the appreciation as your home grows in value.

Second, home ownership may offer some very important long term tax advantages. Generally, when you invest in something and then sell it, you are required to pay taxes on the profit you reaped from your investment. That's true of houses too. You are responsible for paying taxes on any profit you gain by selling a home. But under the current tax code you may defer those taxes as long as you buy a home of equal or greater value. People can and do buy and sell home after home, making a profit on each one and deferring the taxes each time.

When the time comes to buy a smaller home, or not buy a home at all, there may be a third tax break. Since that change usually comes when a homeowner is a senior citizen, the federal government has established a tax exemption to make things easier for older homeowners. Senior citizens who meet certain criteria may receive an exemption on the profits on the sale of their home of up to \$125,000. That's a big savings in taxes that don't have to be paid...and makes a nice nest egg for retirement.

These three tax features, the deduction from taxable income, the deferral of tax on profits when you sell a home, and the exemption for senior citizens, are tax advantages that make home ownership such an important part of your financial planning. When you buy a home you not only save on taxes today, you may save on taxes far into your future.

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