

MVFG ADVISOR

M A R T H A ' S V I N E Y A R D F I N A N C I A L G R O U P

W W W . M V B A N K . C O M

Greetings! May 11th marks my 1st year anniversary at Martha's Vineyard Financial Group. It has been an exciting year of meeting existing customers and welcoming new customers into the bank. I am especially grateful for the warm welcome I received and look forward to my 2nd year. As spring weather is upon us and we turn our thoughts to summer vacations I am reminded of the many vacation homes on the island. Whether you currently own or are considering the purchase of a second home for personal use or rental be aware of the unique tax rules. To assist you our article this month outlines some general tax tips that we trust you will find helpful. As always, you should speak with a tax professional about your particular circumstances.

We also believe it pays to invest in a team to help manage your various financial affairs. At MVSB our team of estate planning and investment professionals, together with local estate planning lawyers, all understand the value of trust. Since 1991 Martha's Vineyard Financial Group has been helping individuals protect and preserve their assets by offering sound investment advice and estate planning guidance. With decades of experience the Martha's Vineyard Financial Group has a proven track record of providing effective estate planning strategies.

As the largest money manager on Martha's Vineyard we stand ready to assist you with protecting your assets and planning for your retirement. When you entrust your family and financial assets to us we never forget that we are in business to serve you and take that charge very seriously. Our team of experienced professionals is always available to meet with you to review your account and to discuss how our products and services can help you meet your objectives.

If you are an existing client - thank you for your business. If not, we welcome the opportunity to speak with you about our many investment products and services.

Bob Ripley, Executive Vice President



**Martha's
Vineyard**

FINANCIAL GROUP

For more information on our investment services or to schedule a confidential visit, please contact the Financial Group at 508-693-8850.

MARTHA'S VINEYARD FINANCIAL GROUP - SINCE 1991

Buying a Second Home - Tax Tips for Homeowners

Mortgage interest - If you use the property as a second home rather than renting it out interest on the mortgage is deductible within the same limits as the interest on the mortgage on your first home.

Property taxes - You can deduct property taxes on your second home, too. In fact, unlike the mortgage interest rule, you can deduct property taxes paid on any number of homes you own.

If you rent out the property - Lots of second-home buyers rent out the property part of the year to get others to help pay the bills. Very different tax rules apply depending on the breakdown between personal and rental use.

If you rent the property out for 14 or fewer days during the year, you can pocket the rental income tax-free. Even if you're charging \$5,000 a week, the IRS doesn't want to hear about it. The house is considered a personal residence, so you deduct mortgage interest and property taxes under the standard rules for a second home. **Longer rentals mean different rules**

Rent for more than 14 days and you must report all rental income. You also get to deduct rental expenses, and that gets complicated because you need to allocate costs between the time the property is used for personal purposes, and the time it is rented.

Consider this example - If you and your family use a beach house for 30 days during the year and it's rented for 120 days, 80 percent (120 divided by 150) of your mortgage interest and property taxes, insurance premiums, utilities and other costs would be rental expenses. The entire amount you pay a property manager would be deductible, too. And you could claim depreciation deductions based on 80 percent of the value of the house. If a house is worth \$200,000 (not counting the value of the land) and you're depreciating 80 percent, a full year's depreciation deduction would be about \$5,800. You can always deduct expenses up to the level of rental income you report. But what if costs exceed what you take in? Whether a loss can shelter other income depends on two things: how much you use the property yourself and how high your income is.

If you use the property more than 14 days, or more than 10 percent of the number of days it is rented whichever is more it is considered a personal residence and the rental loss can't be deducted. (But because it is a personal residence, the interest that doesn't count as a rental expense 20 percent in our example can be deducted as a personal expense.)

If you limit personal use to 14 days or 10 percent, the vacation home is considered a rental property and up to \$25,000 in losses might be deductible each year. That's why lots of vacation homeowners hold down leisure use and spend lots of time "maintaining" the property. Fix-up days don't count as personal use. The tax savings from the loss (up to \$7,000 a year if you're in the 28 percent tax bracket) helps pay for the vacation home. Unfortunately, holding down personal use means you have to forfeit the write-off for the portion of mortgage interest that does not qualify as either a rental or personal-residence expense.

Passive losses - We say such losses *might* be deductible because real estate losses are considered "passive losses" by the tax law. And passive losses are generally not deductible. But there's an exception that might protect you. If your Adjusted Gross Income (AGI) is less than \$100,000, up to \$25,000 of such losses can be deducted each year to offset income such as your salary. (AGI is basically income before subtracting your exemptions and deductions.) As income rises between \$100,000 and \$150,000, however, that \$25,000 allowance disappears. Passive losses you can't deduct can be stored up and used to offset taxable profit when you ultimately sell the vacation house.

Tax-free profits - Although the rule that allows home sellers to take up to \$500,000 of profit tax-free (up to \$250,000 if you're unmarried) applies only to a sale of your principal residence, there is a way to extend the break to your second home: make it your principal residence before you sell. That's not as strange as it might sound. Some retirees, for example, are selling the big family home and moving full-time into what had been their vacation home.

Once you live in that home for two years, up to \$500,000 (or \$250,000) of profit can be tax-free. Any profit attributable to depreciation while you rented the place, though, would be taxable. Depreciation reduces your tax basis in the property and, therefore, increases profit dollar-for-dollar. Also, due to a recent change in the law, if you use the property after 2008 for purposes other than your principal residence, part of the eventual gain on sale won't be eligible for the \$500,000/\$250,000 exclusion.

As always, we recommend you speak with a tax professional as to your specific situation. If you do not have one we would be happy to assist you. Please do not hesitate to call us at 508-693-8850.