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**Tax Information for First-Time Homeowners**

For use in preparing 2007 Returns

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**What’s New**

Mortgage insurance premiums. You may be able to take an itemized deduction for mortgage insurance premiums paid or accrued during 2007. For more information, see Mortgage Insurance Premiums.

Limit on itemized deductions. Certain itemized deductions (including taxes and home mortgage interest) are limited if your adjusted gross income is more than $156,400 ($78,200 if you are married filing separately). For more information, see the Instructions for Schedule A (Form 1040).

Rules for Cooperatives. If you own a cooperative apartment special rules apply to you, see Special Rules for Cooperatives.

**Reminders**

Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling 1-800-THE-LOST (1-800-843-5678) if you recognize a child.

**Introduction**

This publication provides tax information for first-time homeowners. Your first home may be a house, condominium, cooperative apartment, mobile home, houseboat, or house trailer.

The following topics are explained.
What You Can and Cannot Deduct

To deduct expenses of owning a home, you must file Form 1040 and itemize your deductions on Schedule A (Form 1040). If you itemize, you cannot take the standard deduction.

This section explains what expenses you can deduct as a homeowner. It also points out expenses that you cannot deduct. There are four primary discussions: real estate taxes, home mortgage interest, and mortgage insurance premiums. Generally, your real estate taxes, home mortgage interest, and mortgage insurance premiums are included in your house payment.

Your house payment. If you took out a mortgage (loan) to finance the purchase of your home, you probably have to make monthly house payments. Your house payment may include several costs of owning a home. The only costs you can deduct are real estate taxes actually paid to the taxing authority, interest that qualifies as home mortgage interest, and mortgage insurance premiums. These are discussed in more detail later.

Nondeductible payments. You cannot deduct any of the following items.

- Insurance (other than mortgage insurance premiums), including fire and comprehensive coverage, and title insurance.
- Wages you pay for domestic help.
- Depreciation.
- The cost of utilities, such as gas, electricity, or water.
- Most settlement costs. See Settlement or closing costs under Cost as Basis, later, for more information.
- Forfeited deposits, down payments, or earnest money.

Real Estate Taxes

Most state and local governments charge an annual tax on the value of real property. This is called a real estate tax. You can deduct the tax if it is based on the assessed value of the real property and the taxing authority charges a uniform rate on all property in its jurisdiction. The value of the property and the assessed value are the basis for the deduction. Real estate taxes are not a payment for a special privilege granted or service rendered to you.

Deductible Real Estate Taxes

You can deduct real estate taxes imposed on you. You must have paid them either at settlement or closing, or to a taxing authority (either directly or through an escrow account) during the year. If you own a cooperative apartment, see Special Rules for Cooperatives, later.

Where to deduct real estate taxes. Enter the amount of your deductible real estate taxes on Schedule A (Form 1040), line 6.

Real estate taxes paid at settlement or closing. Real estate taxes are generally divided so that you and the seller each pay taxes for the part of the property tax year you owned the home. Your share of these taxes is fully deductible, if you itemize your deductions.

Division of real estate taxes. Federal income tax purposes, the seller is treated as paying the taxes up to, but not including, the date of sale. You (the buyer) are treated as paying the taxes beginning with the date of sale. This applies regardless of the lien dates under local law. Generally, this information is included on the settlement statement you get at closing.

You and the seller each are considered to have paid your own share of the taxes, even if one or the other paid the entire amount. You each can deduct your own share, if you itemize deductions, for the year the property is sold.

Example. You bought your home on September 1. The property tax year (the period to which the tax relates) in your area is the calendar year. The tax for the year was $730 and was due and paid by the seller on August 15.

You owned your new home during the property tax year for 122 days (September 1 to December 31, including your date of purchase). You figure your deduction for real estate taxes on your home as follows.

1. Enter the total real estate taxes for the real property tax year $730
2. Enter the number of days in the property tax year that you owned the property 122
3. Divide line 2 by 365 $2.01
4. Multiply line 1 by line 3 .80
5. Enter the result on Schedule A (Form 1040), line 6 $244

You can deduct $244 on your return for the year if you itemize your deductions. You are considered to have paid this amount and can deduct it on your return even if, under the contract, you did not have to reimburse the seller.

Delinquent taxes. Delinquent taxes are unpaid taxes that were imposed on the seller for an earlier tax year. If you agree to pay delinquent taxes when you buy your home, you cannot deduct them. You treat them as part of the cost of your home. See Real estate taxes, later, under Basis.

Escrow accounts. Many monthly house payment plans include an amount placed in escrow (put in the care of a third party) for real estate taxes. You may not be able to deduct the total you pay...
You cannot deduct the interest you pay must be (1). This is your share of the corporation’s deductible real estate taxes if it is:

1. At least 80% of the corporation’s gross income for the tax year was paid by the tenant-stockholders. For this purpose, gross income means all income received during the entire tax year, including any received before the corporation changed to cooperative ownership.
2. At least 80% of the total square footage of the corporation’s property must be available for use by the tenant-stockholder during the entire tax year,
3. If at least 90% of the expenditures paid or incurred by the corporation were used for the acquisition, construction, management, maintenance, or care of the property for the benefit of the tenant-stockholder during the entire tax year.
4. If either of these situations applies to you, you must add these amounts to the basis of your property.

Usually, you can deduct the entire part of your payment that is for mortgage interest, if you itemize your deductions on Schedule A (Form 1040). However, your deduction may be limited if:

- Your total mortgage balance is more than $1 million ($500,000 if married filing separately), or
- You took out a mortgage for reasons other than to buy, build, or improve your home.

If either of these situations applies to you, you will need to get Publication 936. You also may need Publication 936 if you later refinance your mortgage or buy a second home.

Refund of home mortgage interest. If you receive a refund of home mortgage interest that you deducted in an earlier year and that reduced your tax, you generally must include the refund in income in the year you receive it. For more information, see Recoveries in Publication 525. The amount of the refund will usually be shown on the mortgage interest statement you receive from your mortgage lender. See Mortgage Interest Statement, later.

Deductible Mortgage Interest

To be deductible, the interest you pay must be on a loan secured by your main home or a second home. The loan can be a first or second mortgage, a home improvement loan, or a home equity loan.
Prepaid interest. If you pay interest in advance for a period that goes beyond the end of the tax year, you must spread this interest over the tax years to which it applies. Generally, you can deduct in each year only the interest that qualifies as home mortgage interest for that year. An exception applies to points, which are discussed later.

Late payment charge on mortgage payment. You can deduct as home mortgage interest a late payment charge if it was not for a specific service in connection with your mortgage loan.

Mortgage prepayment penalty. If you pay off your home mortgage early, you may have to pay a penalty. You can deduct that penalty as home mortgage interest provided the penalty is not for a specific service performed or cost incurred in connection with your mortgage loan.

Ground rent. In some states (such as Maryland), you may buy your home subject to a ground rent. A ground rent is an obligation you assume to pay a fixed amount per year on the property. Under this arrangement, you are leasing (rather than buying) the land on which your home is located.

Redeemable ground rents. If you make annual or periodic rental payments on a redeemable ground rent, you can deduct the payments as mortgage interest. The ground rent is a redeemable ground rent only if all of the following are true:

• Your lease, including renewal periods, is for more than 15 years.
• You can freely assign the lease.
• You have a present or future right (under state or local law) to end the lease and buy the lessor’s entire interest in the land by paying a specified amount.
• The lessor’s interest in the land is primarily a security interest to protect the rental payments to which he or she is entitled.

Payments made to end the lease and buy the lessor’s entire interest in the land are not redeemable ground rents. You cannot deduct them.

Nonredeemable ground rents. Payments on a nonredeemable ground rent are not mortgage interest. You can deduct them as rent only if they are a business expense or if they are for rental property.

Cooperative apartment. You can usually treat the interest on a loan you took out to buy stock in a cooperative housing corporation as home mortgage interest if you own a cooperative apartment and the cooperative housing corporation meets the conditions described earlier under Special Rules for Cooperatives. In addition, you can treat as home mortgage interest your share of the corporation’s deductible mortgage interest. Figure your share of mortgage interest the same way that is shown for figuring your share of real estate taxes in the Example under Division of real estate taxes, earlier. For more information on cooperatives, see Special Rule for Tenant-Stockholders in Cooperative Housing Corporations in Publication 936.

Refund of cooperative’s mortgage interest. You must reduce your mortgage interest deduction by your share of any cash portion of a patronage dividend that the cooperative receives. The patronage dividend is a partial refund to the cooperative housing corporation of mortgage interest it paid in a prior year. If you receive a Form 1098 from the cooperative housing corporation, the form should show only the amount you can deduct.

Mortgage Interest Paid at Settlement

One item that normally appears on a settlement or closing statement is home mortgage interest. You can deduct the interest that you pay at settlement if you itemize your deductions on Schedule A (Form 1040). This amount should be included in the mortgage interest statement provided by your lender. See the discussion under Mortgage Interest Statement, later. Also, if you pay interest in advance, see Prepaid interest, earlier, and Points, next.

Points

The term “points” is used to describe certain charges paid, or treated as paid, by a borrower to obtain a home mortgage. Points also may be called loan origination fees, maximum loan charges, loan discount, or discount points. A borrower is treated as paying any points that a home seller pays for the borrower’s mortgage. See Points paid by the seller, later.

General rule. You cannot deduct the full amount of points in the year paid. They are prepaid interest, so you generally must deduct them over the life (term) of the mortgage.

Exception. You can deduct the full amount of points in the year paid if you meet all the following tests:

1. Your loan is secured by your main home. (Generally, your main home is the one you live in most of the time.)
2. Paying points is an established business practice in the area where the loan was made.
3. The points paid were not more than the points generally charged in that area.
4. You use the cash method of accounting. This means you report income in the year you receive it and deduct expenses in the year you pay them. Most individuals use this method.
5. The points were not paid in place of amounts that ordinarily are stated separately on the settlement statement, such as appraisal fees, inspection fees, title fees, attorney fees, and property taxes.
6. The funds you provided at or before closing, plus any points the seller paid, were at least as much as the points charged. The funds you provided do not have to have been applied to the points. They can include a down payment, an escrow deposit, earnest money, and other funds you paid at or before closing for any purpose. You cannot have borrowed these funds from your lender or mortgage broker.
7. You use your loan to buy or build your main home.
8. The points were computed as a percentage of the principal amount of the mortgage.
9. The amount is clearly shown on the settlement statement (such as the Uniform Settlement Statement, Form HUD-1) as points charged for the mortgage. These points may be shown as paid from either your funds or the seller’s.

Note. If you meet all of the tests listed above and you itemize your deductions in the year you get the loan, you can either deduct the full amount of points in the year paid or deduct them over the life of the loan, beginning in the year you get the loan. If you do not itemize your deductions in the year you get the loan, you can spread the points over the life of the loan and deduct the appropriate amount in each future year, if any, when you do itemize your deductions.

Home improvement loan. You can also fully deduct in the year paid points paid on a loan to improve your main home, if you meet the first six tests listed earlier.

Refinanced loan. If you use part of the refinanced mortgage proceeds to improve your main home and you meet the first six tests listed earlier, you can fully deduct the part of the points related to the improvement in the year you paid them with your own funds. You can deduct the rest of the points over the life of the loan.

Points not fully deductible in year paid. If you do not qualify under the exception to deduct the full amount of points in the year paid (or choose not to do so), see Points in Publication 936. Home Mortgage Interest Deduction, for the rules on when and how much you can deduct.

Figure A. You can use Figure A as a quick guide to see whether your points are fully deductible in the year paid.

Amounts charged for services. Amounts charged by a borrower for services connected to the loan are not interest. Examples of these charges are:

• Appraisal fees,
• Notary fees, and
• Preparation costs for the mortgage note or deed of trust.

You cannot deduct these amounts as points either in the year paid or over the life of the mortgage. For information about the tax treatment of these amounts and other settlement fees, and closing costs, see Basis, later.

Points paid by the seller. The term “points” includes loan placement fees that the seller pays to the lender to arrange financing for the buyer.

Treatment by seller. The seller cannot deduct these fees as interest; but, they are a selling expense that reduces the seller’s amount realized. See Publication 523 for more information.

Treatment by buyer. The buyer treats seller-paid points as if he or she had paid them. If all the tests listed earlier under Exception are met, the buyer can deduct the points in the year paid. If any of those tests are not met, the buyer must deduct the points over the life of the loan.
Figure A. Are My Points Fully Deductible This Year?

Start Here:

1. Is the loan secured by your main home?
   - Yes
   - No

2. Is the payment of points an established business practice in your area?
   - Yes
   - No

3. Were the points paid more than the amount generally charged in your area?
   - Yes
   - No

4. Do you use the cash method of accounting?
   - Yes
   - No

5. Were the points paid in place of amounts that ordinarily are separately stated on the settlement sheet?
   - Yes
   - No

6. Were the funds you provided (other than those you borrowed from your lender or mortgage broker), plus any points the seller paid, at least as much as the points charged?* 
   - Yes
   - No

7. Did you take out the loan to improve your main home?
   - Yes
   - No

8. Did you take out the loan to buy or build your main home?
   - Yes
   - No

9. Were the points computed as a percentage of the principal amount of the mortgage?
   - Yes
   - No

10. Is the amount paid clearly shown as points on the settlement statement?
    - Yes
    - No

You can fully deduct the points this year. You cannot fully deduct the points this year. See the discussion on Points.

* The funds you provided do not have to have been applied to the points. They can include a down payment, an escrow deposit, earnest money, and other funds you paid at or before closing for any purpose.
The buyer must also reduce the basis of the home by the amount of the seller-paid points. To meet all the tests under Exception except that the funds you paid mortgage insurance provided by the Department of Veterans Affairs or Rural Housing Service, generally, will receive a Form 1098, mortgage insurance premiums you paid or accrued for a summary of where to how much of the interest each of you paid, and If you have a second home, use part of your mortgage insurance contract issued before January 1, 2007, are not deducti-

Mortgage Insurance Premiums

Qualified mortgage insurance is mortgage insurance provided by the Veterans Administration, the Federal Housing Administration, or the Rural Housing Administration, and private mortgage insurance (as defined in section 2 of the Homeowners Protection Act of 1998 as in effect on December 20, 2006).

Special rules for prepaid mortgage insur-

ance. If you paid premiums for qualified mort-

gage insurance that are properly allocable to periods after the close of the taxable year, such premiums are treated as paid in the period to which they are allocated. No deduction is allowed for the unamortized balance if the mortgage is satisfied before its term. The two preceding sentences do not apply to qualified mortgage insurance provided by the Department of Veterans Affairs or Rural Housing Service.

Home Acquisition Debt

Home acquisition debt is a mortgage you took out after October 13, 1987, to buy, build, or substantially improve a qualified home. It also must be secured by that home.

If the amount of your mortgage is more than the cost of the home plus the cost of any substantial improvements, only the debt that is not included in the amount of Veterans Affairs or Rural Housing Service.

Qualified Home

This means your main home or your second home. A home includes a house, condominium, cooperative, mobile home, house trailer, boat, or similar property that has sleeping, cooking, and toilet facilities.

Main home. You can have only one main home at any one time. This is the home where you ordinarily live most of the time.

Second home and other special situations. If you have a second home, use part of your home for other than residential living (such as a home office), rent out part of your home, or are

Example 2. The facts are the same as in Example 1, except that the person who sold you the home also paid one point ($1,000) to help you get your mortgage. In the year paid, you could deduct $1,750 ($750 of the amount you were charged plus the $1,000 paid by the seller). You spread the remaining $250 over the life of the mortgage. You must reduce the basis of your home by the $1,000 paid by the seller.

Excess points. If you meet all the tests under Exception except that the points paid were more than are generally charged in your area (test 3), you can deduct in the year paid only the points that are generally charged. You must spread any additional points over the life of the mortgage.

Mortgage ending early. If you spread your deduction for points over the life of the mortgage, you can deduct any remaining points in the year the mortgage ends. A mortgage may end early due to a prepayment, refinancing, foreclosure, or similar event.

Example. Dan paid $3,000 in points in 2000 that he had to spread out over the 15-year life of the mortgage. He had deducted $1,400 of these points through 2006.

Dan prepaid his mortgage in full in 2007. He can deduct the remaining $1,600 of points in 2007.

Example. If you refinance the mortgage with the same lender, you cannot deduct any remaining points for the year. Instead, deduct them over the term of the new loan.

Form 1098. The mortgage interest statement you receive should show not only the total interest paid during the year, but also your deductible points paid during the year. See Mortgage Interest Statement, later.

Where To Deduct Home Mortgage Interest

Enter on Schedule A (Form 1040), line 10, the home mortgage interest and points reported to you on Form 1098 (discussed next). If you did not receive a Form 1098, enter your deductible interest on line 11, and any deductible points on line 12. See Table 2 for a summary of where to deduct home mortgage interest and real estate taxes.

If you paid home mortgage interest to the person from whom you bought your home, show that person's name, address, and social security number (SSN) or employer identification number (EIN) on the dotted lines next to line 11. The seller must give you the seller's SSN. Form W-9, Request for Taxpayer Identification Number and Certification, can be used for this purpose. Failure to meet either of these requirements may result in a $50 penalty for each failure.

Mortgage Interest Statement

If you paid $600 or more of mortgage interest (including certain points and mortgage insurance premiums) during the year to a mortgage holder in the course of that holder's trade or business, you should receive a Form 1098 or similar statement from the mortgage holder. The statement will show the total interest paid on your mortgage during the year. If you bought a main home during the year, it will also show the deductible points you paid and any points you can deduct that were paid by the person who sold you your home. See Points, later.

The interest you paid at settlement should be included on the statement. If it is not, add the interest from the settlement sheet that qualifies as home mortgage interest to the total shown on Form 1098 or similar statement. Put the total on Schedule A (Form 1040), line 10, and attach a statement to your return explaining the difference. Write "See attached" to the right of that line.

When you took out a $100,000 mortgage loan to buy your home in December, you were charged one point ($1,000). You meet all the tests for deducting points in the year paid (see Exception, earlier), except the only funds you provided were a $750 down payment. Of the $1,000 you were charged for points, you can deduct $700 in the year paid. You spread the remaining $250 over the life of the mortgage.

Example 1. When you took out a $100,000 mortgage loan to buy your home in December, you were charged one point ($1,000). You meet all the tests for deducting points in the year paid (see Exception, earlier), except the only funds you provided were a $750 down payment. Of the $1,000 you were charged for points, you can deduct $700 in the year paid. You spread the remaining $250 over the life of the mortgage.

Second home and other special situations. If you use part of your home as your main home or your second home, see

Mortgage Insurance

You can have only one main home mortgage interest and points reported to you on Form 1098 (discussed next). If you did not receive a Form 1098, enter your deductible interest on line 11, and any deductible points on line 12. See Table 2 for a summary of where to deduct home mortgage interest and real estate taxes.
The fraction will not change as long as you are entitled to take the mortgage interest credit. The amount of the mortgage interest credit shown on your home mortgage interest deduction by the amount that you can deduct. If your AGI is more than $109,000 ($54,500 if married filing separately), you cannot deduct your mortgage insurance premiums.

**Form 1098.** The amount of mortgage insurance premiums you paid during 2007 should be reported in box 4; see Form 1098. Mortgage Interest Statement in Publication 936.

**Mortgage Interest Credit**

The mortgage interest credit is intended to help lower-income individuals afford home ownership. You qualify if you can claim the credit each year for part of the home mortgage interest you pay.

Who qualifies. You may be eligible for the credit if you were issued a mortgage credit certificate (MCC) from your state or local government. Generally, an MCC is issued only in connection with a new mortgage for the purchase of your main home. The MCC will show the certificate credit rate you will use to figure your credit. It also will show the certified indebtedness amount. Only the interest on that amount qualifies for the credit. See Figuring the Credit, later.

You must contact the appropriate government agency about getting an MCC before you get a mortgage and buy your home. Contact your state or local housing finance agency for information about the availability of MCCs in your area.

How to claim the credit. To claim the credit, complete Form 8396 and attach it to your Form 1040. Include the credit in your total for Form 1040, line 54; be sure to check box a on that line.

**Reducing your home mortgage interest deduction.** If you itemize your deductions on Schedule A (Form 1040), you must reduce your home mortgage interest deduction by the amount of the mortgage interest credit shown on Form 8396, line 3. You must do this even if part of that amount is to be carried forward to 2008.

**Selling your home.** If you purchase a home after 1990 using an MCC, and you sell that home within 9 years, you may have to recapture (payback) all or part of the benefit you received from the MCC program. For additional information, see Recapturing (Paying Back) a Federal Mortgage Subsidy, in Publication 523.

**Figuring the Credit**

Figure your credit on Form 8396. Mortgage not more than certified indebtedness. If your mortgage loan amount is equal to (or smaller than) the certified indebtedness amount shown on your MCC, enter on Form 8396, line 1, all the interest you paid on your mortgage during the year. Mortgage more than certified indebtedness. If your mortgage loan amount is larger than the certified indebtedness amount shown on your MCC, you can figure the credit on only part of the interest you paid. To find the amount to enter on line 1, multiply the total interest you paid during the year on your mortgage by the following fraction.

### Table 1. Where To Deduct Interest and Taxes Paid on Your Home

<table>
<thead>
<tr>
<th>IF you are eligible to deduct . . .</th>
<th>THEN report the amount on Schedule A (Form 1040) . . .</th>
</tr>
</thead>
<tbody>
<tr>
<td>real estate taxes</td>
<td>line 6.</td>
</tr>
<tr>
<td>home mortgage interest and points reported on Form 1098</td>
<td>line 10.</td>
</tr>
<tr>
<td>home mortgage interest not reported on Form 1098</td>
<td>line 11.</td>
</tr>
<tr>
<td>points not reported on Form 1098</td>
<td>line 12.</td>
</tr>
<tr>
<td>qualified mortgage insurance premiums</td>
<td>line 13.</td>
</tr>
</tbody>
</table>

**Example.** Emily bought a home this year. Her mortgage loan is $125,000. The certified indebtedness amount on her MCC is $100,000. She paid $7,500 interest this year. Emily figures the interest to enter on Form 8396, line 1, as follows:

\[
\frac{100,000}{725,000} = 80\% (.80)
\]

Emily enters $6,000 on Form 8396, line 1. In each later year, she will figure her credit using only 80% of the interest she pays for that year.

**Limits**

Two limits may apply to your credit.
- A limit based on the credit rate, and
- A limit based on your tax.

**Example.** John and his brother, George, were issued an MCC. They used it to get a mortgage on their main home. John has a 60% ownership interest in the home, and George has a 40% ownership interest in the home. John paid $5,400 mortgage interest this year and George paid $3,800.

**Dividing the Credit**

If two or more persons (other than a married couple filing a joint return) hold an interest in the home to which the MCC relates, the credit must be divided based on the interest held by each person.

**Example.** John and his brother, George, were issued an MCC. They used it to get a mortgage on their main home. John has a 60% ownership interest in the home, and George has a 40% ownership interest in the home. John paid $5,400 mortgage interest this year and George paid $3,800.
The type and rule above prints on all proofs including departmental reproduction proofs. MUST be removed before printing.

Table 3. Adjusted Basis
This table lists examples of some items that generally will increase or decrease your basis in your home. It is not intended to be all-inclusive.

<table>
<thead>
<tr>
<th>Increases to Basis</th>
<th>Decreases to Basis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improvements:</td>
<td></td>
</tr>
<tr>
<td>• Putting an addition on your home</td>
<td>• Insurance or other reimbursement for casualty losses</td>
</tr>
<tr>
<td>• Replacing an entire roof</td>
<td>• Deductible casualty loss not covered by insurance</td>
</tr>
<tr>
<td>• Paving your driveway</td>
<td>• Payments received for easement or right-of-way granted</td>
</tr>
<tr>
<td>• Installing central air conditioning</td>
<td>• Depreciation allowed or allowable if used for business or rental purposes</td>
</tr>
<tr>
<td>• Rewiring your home</td>
<td>• Value of subsidy for energy conservation measure excluded from income</td>
</tr>
<tr>
<td>Assessments for local improvements (see Assessments for local benefits, under What You Can and Cannot Deduct)</td>
<td></td>
</tr>
<tr>
<td>Amounts spent to restore damaged property</td>
<td></td>
</tr>
</tbody>
</table>

The MCC shows a credit rate of 25% and a certified indebtedness amount of $130,000. The loan amount (mortgage) on their home is $120,000. The credit is limited to $2,000 because the credit rate is more than 20%. If you refinance your original mortgage loan on maturity date of the old mortgage, the interest rate you would have paid on the old loan is $3,600. If you did not get a new MCC, you may want to contact the state or local housing finance agency that issued your original MCC for information about whether you can get a reissued MCC.

Year of refinancing. In the year of refinancing, add the applicable amount of interest paid on the old mortgage and the applicable amount of interest paid on the new mortgage, and enter the total on Form 8396, line 1. If your new MCC has a credit rate different from the rate on the old MCC, you must attach a statement to Form 8396. The statement must show the calculation for lines 1, 2, and 3 for the part of the year when the old MCC was in effect. It must show a separate calculation for the part of the year when the new MCC was in effect. Combining amounts from both calculations for line 3, enter the total on line 3 of the form, and write “See attached” on the dotted line.

New MCC cannot increase your credit. The credit that you claim with your new MCC cannot be more than the credit that you could have claimed with your old MCC. In most cases, the agency that issues your new MCC will make sure that it does not increase your credit. However, if either your old loan or your new loan has a variable (adjustable) interest rate, you will need to check this yourself. In that case, you will need to know the amount of the credit you could have claimed using the old MCC.

There are two methods for figuring the credit you could have claimed. Under one method, you figure the actual credit that would have been allowed. This means you use the credit rate on the old MCC and the interest you would have paid on the old loan. If your old loan was a variable rate mortgage, you can use another method to determine the credit that you could have claimed. Under this method, you figure the credit using a payment schedule of a hypothetical self-amortizing mortgage with level payments projected to the final maturity date of the old mortgage. The interest rate of the hypothetical mortgage is the annual percentage rate (APR) of the new mortgage for purposes of the Federal Truth in Lending Act. The principal of the hypothetical mortgage is the remaining outstanding balance of the certified mortgage indebtedness shown on the old MCC.

You must choose one method and use it consistently beginning with the first tax year for which you claim the credit based on the new MCC.

As part of your tax records, you should keep your old MCC and the schedule of payments for your old mortgage.

District of Columbia First-Time Homebuyer Credit
You may be able to claim a one-time tax credit of up to $5,000 ($2,500 if married filing separately) if you buy a main home in the District of Columbia. You must reduce the basis of your home by the amount of the tentative credit.

The credit is not allowed if you acquired your home from certain related persons or by gift or inheritance.

You qualify for the credit if (and your spouse if you are married) did not have an ownership interest in a main home in the District of Columbia for at least 1 year before buying the new home. Individuals with modified adjusted gross income of $90,000 or more ($130,000 or more in the case of a joint return) cannot claim the credit. Individuals with modified adjusted gross income between $70,000 and $90,000 (between $110,000 and $130,000 in the case of a joint return) can claim only a reduced credit.

Use Form 8859, District of Columbia First-Time Homebuyer Credit, to figure your credit. See the form and its instructions for more information.

Basis
Basis is your starting point for figuring a gain or loss if you later sell your home, or for figuring depreciation if you later use part of your home for business purposes or for rent.

While you own your home, you may add certain items to your basis. You may subtract certain other items from your basis. These items are called adjustments to basis and are explained later under Adjusted Basis.

It is important that you understand these terms when you first acquire your home because you must keep track of your basis and adjusted basis during the period you own your home. You also must keep records of the events that affect basis or adjusted basis. See Keeping Records, later.

Figuring Your Basis
How you figure your basis depends on how you acquire your home. If you buy or build your home, your cost is your basis. If you receive your home as a gift, your basis is usually the same as the adjusted basis of the person who gave you the property. If you inherit your home from a decedent, the fair market value at the date of the
Cost as Basis

The cost of your home, whether you purchased it or constructed it, is the amount you paid for it, including any debt you assumed.

The cost of your home includes most settlement or closing costs you are paid when you bought the home. If you built your home, your cost includes most closing costs paid when you bought the land or settled on your mortgage.

If you elect to deduct the sales taxes on the purchase or construction of your home as an itemized deduction on Schedule A (Form 1040), you cannot include the sales taxes as part of your cost basis in the home.

Purchase. The basis of a home you bought is the amount you paid for it. This usually includes your down payment and any debt you assumed. The basis of a cooperative apartment is the amount you paid for your shares in the corporation that owns or controls the property. This amount includes any purchase commissions or other costs of acquiring the shares.

Construction. If you contracted to have your home built on land that you own, your basis in the home is your basis in the land plus the amount you paid to have the home built. This includes the cost of labor and materials, the amount you paid the contractor, any architect’s fees, building permit charges, utility meter and connection charges, and legal fees that are directly connected with building your home. If you built all or part of your home yourself, your basis is the total amount it cost you to build it. You cannot include the value of your own labor or any other labor for which you did not pay.

Real estate taxes. Real estate taxes are usually divided so that you and the seller each pay taxes for the part of the property tax year that each owned the home. See the earlier discussion of Real Estate taxes paid at settlement or closing, under Real Estate Taxes, to figure the real estate taxes you paid or are considered to have paid.

If you pay any part of the seller’s share of the real estate taxes (the taxes beginning with the date of sale), you can still deduct those taxes. Do not include those taxes in your basis. If you did not reimburse the seller, you must reduce your basis by the amount of those taxes.

Example 1. You bought your home on Sep- tember 1. The property tax year in your area is the calendar year, and the tax is due on August 15. The real estate taxes on the home you bought were $1,275 for the year and had been paid by the seller on August 15. You did not pay the seller for the real estate taxes from September 1 through Decem- ber 31. You must reduce the basis of your home by $1,275 ($1,275 − $1,275 × $1,275 = $1,275) the seller paid for you. You can deduct your $426 share of real estate taxes on your return for the year you purchased your home.

Example 2. You bought your home on May 5, 2007. The property tax year in your area is the calendar year. The taxes for the previous year are assessed on January 2 and are due on May 31 and November 30. Under state law, the taxes become a lien on May 31. You agreed to pay all taxes due after the date of sale. The taxes due in 2007 for 2006 were $1,375. The taxes due in 2008 for 2007 will be $1,425.

You cannot deduct any of the taxes paid in 2007 because they relate to the 2006 property tax year and you did not own the home until 2007. Instead, you add the $1,375 to the cost basis of your home.

You owned the home in 2007 for 243 days (May 3 to December 31), so you can take a tax deduction on your 2008 return of $949 [(243 ÷ 365) × $1,425] paid in 2008 for 2007. You added the remaining $476 ($1,425 – $949) of taxes paid in 2008 to the cost basis of your home.

Settlement or closing costs. If you bought your home, you probably paid settlement or closing costs in addition to the contract price. These costs are divided between you and the seller according to the sales contract, local custom, or understanding of the parties. If you built your home, you probably paid these costs when you bought the land or settled on your mortgage.

The only settlement or closing costs you can deduct are home mortgage interest and certain real estate taxes. You deduct them in the year you buy your home if you itemize your deductions. You can add certain other settlement or closing costs to the basis of your home.

Items added to basis. You can include in your basis the settlement fees and closing costs that you can include in the original basis of your home.

- Abstract fees (abstract of title fees).
- Charges for installing utility services.
- Legal fees (including fees for the title search and preparation of the sales contract and deed).
- Recording fees.
- Surveys.
- Transfer taxes.
- Owner’s title insurance.

• Any amount the seller owes that you agree to pay, such as back taxes or interest, recording or mortgage fees, cost for improvements or repairs, and sales com- missions.

If the seller actually paid for any item for which you are liable and for which you can take a deduction (such as your share of the real estate taxes for the year of sale), you must reduce your basis by that amount unless you are charged for it in the settlement.

Items not added to basis and not deducti- ble. Here are some settlement and closing costs that you cannot deduct or add to your basis.

If you bought your home after April 3, 1994, you must reduce your basis by any points paid for your mortgage by the person who sold you your home.

Points paid by seller. If you bought your home after April 3, 1994, you must reduce your basis by seller-paid points only if you deducted them. See Points, earlier, for the rules on deducting points.

Gift

To figure the basis of property you receive as a gift, you must know its adjusted basis (defined later) to the donor just before it was given to you, its FMV at the time it was given to you, and any gift tax paid on it.

Donor’s adjusted basis is more than FMV. If someone gave you your home and the donor’s adjusted basis, when it was given to you, was more than the fair market value, your basis at the time of receipt is the same as the donor’s adjusted basis.

Disposition basis. If the donor’s adjusted basis at the time of the gift is more than the FMV, your basis when you dispose of the property will depend on whether you have a gain or a loss.

- If using the donor’s adjusted basis results in a loss when you sell the home, you must use the fair market value of the home at the time of the gift as your basis.
- If using the fair market value results in a gain, you have neither a gain nor a loss.

Donor’s adjusted basis equal to or less than the FMV. If someone gave you your home after 1976 and the donor’s adjusted basis, when it was given to you, was equal to or less than the fair market value, your basis at the time of receipt is the same as the donor’s adjusted basis, plus the part of any federal gift tax paid that is due to the net increase in value of the home.
Part of federal gift tax due to net increase in value. Figure the part of the federal gift tax paid that is due to the net increase in value of your home by multiplying the total federal gift tax paid by a fraction. The numerator (top part) of the fraction is the net increase in the value of the home, and the denominator (bottom part) is the value of the home for gift tax purposes after reduction for any annual exclusion and marital or charitable deduction that applies to the gift. The net increase in the value of the home is its fair market value minus the adjusted basis of the donor.

Publication 551 gives more information, including examples, on figuring your basis when you receive property as a gift.

Inheritance
Your basis in a home you inherited is generally the fair market value of the home on the date of the decedent’s death or on the alternate valuation date if the personal representative for the estate chooses to use alternative valuation. If an estate tax return was filed, your basis is generally the value of the home listed on the estate tax return. If an estate tax return was not filed, your basis is the appraised value of the home at the decedent’s date of death for state inheritance or transmission taxes. Publication 551 and Publication 559, Survivors, Executors, and Administrators, have more information on the basis of inherited property.

Adjusted Basis
While you own your home, various events may take place that can change the original basis of your home. These events can increase or decrease your original basis. The result is called an adjusted basis. See Table 3, earlier, for a list of some of the items that can adjust your basis.

Improvements. An improvement materially adds to the value of your home, considerably prolongs its useful life, or adapts it to new uses. You must add the cost of any improvements to the basis of your home. You cannot deduct these costs.

Improvements include putting a recreation room in your unfinished basement, adding another bathroom or bedroom, putting up a fence, putting in new plumbing or wiring, installing a new roof, and paving your driveway.

Amount added to basis. The amount you add to your basis for improvements is your actual cost. This includes all costs for material and labor, except your own labor, and all expenses related to the improvement. For example, if you had your lot surveyed to put up a fence, the cost of the survey is a part of the cost of the fence. You also must add to your basis state and local assessments for improvements such as streets and sidewalks if they increase the value of the property. These assessments are discussed earlier under Real Estate Taxes.

Repairs versus improvements. A repair keeps your home in an ordinary, efficient operating condition. It does not add to the value of your home or prolong its life. Repairs include repainting your home inside or outside, fixing your gutters or floors, fixing leaks or plastering, and replacing broken window panes. You cannot deduct repair costs and generally cannot add them to the basis of your home.

However, repairs that are done as part of an extensive remodeling or restoration of your home are considered improvements. You add them to the basis of your home.

Records to keep. You can use Table 4 (at the end of the publication) as a guide to help you keep track of improvements to your home. Also see Keeping Records, later.

Energy conservation subsidy. If a public utility gives you (directly or indirectly) a subsidy for the purchase or installation of an energy conservation measure for your home, do not include the value of that subsidy in your income.

You must reduce the basis of your home by that value.

An energy conservation measure is an installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand.

Keeping Records
Keeping full and accurate records is vital to properly report your income and expenses, to support your deductions and credits, and to know the basis or adjusted basis of your home. These records include your purchase contract and settlement papers if you bought the property, or other objective evidence if you acquired it by gift, inheritance, or similar means. You should keep any receipts, canceled checks, and similar evidence for improvements or other additions to the basis. In addition, you should keep track of any decreases to the basis such as those listed in Table 3.

How to keep records. How you keep records keeps your home in an ordinary, efficient operating condition. It does not add to the value of your home or prolong its life. Repairs include repainting your home inside or outside, fixing your gutters or floors, fixing leaks or plastering, and replacing broken window panes. You cannot deduct repair costs and generally cannot add them to the basis of your home.

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You must reduce the basis of your home by that value.

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The type and rule above prints on all proofs including departmental reproduction proofs. MUST be removed before printing.

Table 4. Record of Home Improvements

Keep this for your records. Also, keep receipts or other proof of improvements.

<table>
<thead>
<tr>
<th>(a)</th>
<th>(b) Date</th>
<th>(c) Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Additions:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bedroom</td>
<td></td>
<td></td>
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<tr>
<td>Bathroom</td>
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<tr>
<td>Deck</td>
<td></td>
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<tr>
<td>Garage</td>
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<tr>
<td>Porch</td>
<td></td>
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<tr>
<td>Patio</td>
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<tr>
<td>Storage shed</td>
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<tr>
<td>Fireplace</td>
<td></td>
<td></td>
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<tr>
<td>Other</td>
<td></td>
<td></td>
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<tr>
<td>Lawn &amp; Grounds:</td>
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<td></td>
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<tr>
<td>Landscaping</td>
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<tr>
<td>Driveway</td>
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<tr>
<td>Walkway</td>
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<tr>
<td>Fences</td>
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<tr>
<td>Retaining wall</td>
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<tr>
<td>Sprinkler system</td>
<td></td>
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<tr>
<td>Swimming pool</td>
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<tr>
<td>Exterior lighting</td>
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<td>Satellite dish</td>
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<td>Intercom</td>
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<tr>
<td>Security system</td>
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<td>Other</td>
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<td>Miscellaneous:</td>
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<td>Storm windows and doors</td>
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<tr>
<td>Roof</td>
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<tr>
<td>Central vacuum</td>
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<td>Other</td>
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<tr>
<td>Heating &amp; Air Conditioning:</td>
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<td>Heating system</td>
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<td>Central air conditioning</td>
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<tr>
<td>Furnace</td>
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<tr>
<td>Duct work</td>
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<td>Central humidifier</td>
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<tr>
<td>Filtration system</td>
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<td>Lighting fixtures</td>
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<td>Wiring upgrades</td>
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<tr>
<td>Soft water system</td>
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<tr>
<td>Filtration system</td>
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<td>Other</td>
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<tr>
<td>Insulation:</td>
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<td>Attic</td>
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<td>Walls</td>
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<td>Floors</td>
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<td>Pipes and duct work</td>
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<tr>
<td>Other</td>
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<tr>
<td>Interior Improvements:</td>
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<td></td>
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<tr>
<td>Built-in appliances</td>
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<tr>
<td>Kitchen modernization</td>
<td></td>
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<tr>
<td>Bathroom modernization</td>
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<tr>
<td>Flooring</td>
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<tr>
<td>Wall-to-wall carpeting</td>
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<td>Other</td>
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</table>
How To Get Tax Help

You can get help with unresolved tax issues, order free publications and forms, ask tax questions, and get information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Contacting your Taxpayer Advocate. The Taxpayer Advocate Service (TAS) is an independent organization within the IRS whose employees assist taxpayers who are experiencing economic harm, who are seeking help in resolving tax problems that have not been resolved through normal channels, or who believe that an IRS system or procedure is not working as it should.

You can contact the TAS by calling the TAS toll-free case intake line at 1-877-777-4778 or TTY/TDD 1-800-829-4059 to see if you are eligible for assistance. You can also call or write to your local taxpayer advocate, whose phone number and address are listed in their local telephone directory and in Publication 1546, Taxpayer Advocate Service - Your Voice at the IRS. You can file Form 911, Request for Taxpayer Advocate Service Assistance (And Application for Taxpayer Assistance Order), or ask an IRS employee to complete it on your behalf. For more information, go to www.irs.gov/advocate.

Taxpayer Advocacy Panel (TAP). The TAP listens to taxpayers, identifies taxpayer issues, and makes suggestions for improving IRS services and customer satisfaction. If you have suggestions for improvements, contact the TAP, toll free at 1-888-912-1227 or go to www.improvers.org.

Low Income Taxpayer Clinics (LITCs). LITCs are independent organizations that provide low-income taxpayers with representation in federal tax controversies with the IRS for free or for a nominal charge. The clinics also provide tax education and outreach for taxpayers with limited English proficiency or who speak English as a second language. Publication 4134, Low Income Taxpayer Clinic List, provides information on clinics in your area. It is available at www.irs.gov or at your local IRS office.

Free tax services. To find out what services are available, get Publication 910, IRS Guide to Free Tax Services. It contains a list of free tax publications and describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics. Accessible versions of IRS published products are available on request in a variety of alternative formats for people with disabilities.

Internet. You can access the IRS website at www.irs.gov 24 hours a day, 7 days a week.

- E-file your return. Find out about commercial tax preparation and e-file services available free to eligible taxpayers.
- Check the status of your 2007 refund. Click on Where’s My Refund. Wait at least 6 weeks from the date you filed your return (3 weeks if you filed electronically). Have your 2007 tax return available because you will need to know your social security number, your filing status, and the exact whole dollar amount of your refund.
- Download forms, instructions, and publications.
- Order IRS products online.
- Research your tax questions online.
- Search publications online by topic or keyword.
- View Internal Revenue Bulletins (IRBs) published in the last few years.
- Figure your withholding allowances using the withholding calculator online at www.irs.gov/individuals.
- Determine if Form 6251 must be filed using our Alternative Minimum Tax (AMT) Assistant.
- Sign up to receive local and national tax alerts by email.
- Get information on starting and operating a small business.

Phone. Many services are available by phone.

- Ordering forms, instructions, and publications. Call 1-800-829-3676 to order current-year forms, instructions, and publications, and prior-year forms and instructions. You should receive your order within 10 days.
- Asking tax questions. Call the IRS with your tax questions at 1-800-829-1040.
- Solving problems. You can get face-to-face help solving tax problems every business day in IRS Taxpayer Assistance Centers. An employee can explain IRS letters, request adjustments to your account, or help you set up a payment plan. Call your local Taxpayer Assis-
tance Center for an appointment. To find the number, go to www.irs.gov/localcontacts or look in the phone book under United States Government, Internal Revenue Service.
- TTY/TDD equipment. If you have access to TTY/TDD equipment, call 1-800-829-4059 to ask tax questions or to order forms and publications.
- TeleTax topics. Call 1-800-829-4477 to listen to pre-recorded messages covering various tax topics.
- Refund information. To check the status of your 2007 refund, call 1-800-829-4477 and press 1 for automated refund information or call 1-800-829-1954. Be sure to wait at least 6 weeks from the date you filed your return (3 weeks if you filed electronically). Have your 2007 tax return available because you will need to know your social security number, your filing status, and the exact whole dollar amount of your refund.

Evaluating the quality of our telephone services. To ensure IRS representatives give accurate, courteous, and professional answers, we use several methods to evaluate the quality of our telephone services. One method is for a second IRS representative to listen in on or record random telephone calls. Another is to ask some callers to complete a short survey at the end of the call.

Walk-in. Many products and services are available on a walk-in basis.

- Products. You can walk in to many post offices, libraries, and IRS offices to pick up certain forms, instructions, and publications. Some IRS offices, libraries, grocery stores, copy centers, city and county government offices, credit unions, and office supply stores have a collection of products available to print from a CD or photocopy from reproducible proofs. Also, some IRS offices and libraries have the Internal Revenue Code, regulations, Internal Revenue Bulletin, and Cumulative Bulletin available for research purposes.
- Services. You can walk in to your local Taxpayer Assistance Center every business day for personal, face-to-face tax help. An employee can explain IRS letters, request adjustments to your tax account, or help you set up a payment plan. If you need to resolve a tax problem, have questions about how the tax law applies to your individual tax return, or you’re more comfortable talking with someone in person, visit your local Taxpayer Assistance Center where you can spread out your records and talk with an IRS representative face-to-face. No appointment is necessary, but if you prefer, you can call your local Center and leave a message requesting an appointment to resolve a tax account issue. A representative will call you back within 2 business days to schedule an in-person appointment at your convenience. To find the number, go to www.irs.gov/localcontacts or look in the phone book under United States Government, Internal Revenue Service.

Mail. You can send your order for forms, instructions, and publications to the address below. You should receive a response within 10 days after your request is received.

National Distribution Center P.O. Box 8903 Bloomington, IL 61702-8903

CD/DVD for tax products. You can order Publication 1796, IRS Tax Products CD/DVD, and obtain:

- Current-year forms, instructions, and publications.
- Prior-year forms, instructions, and publications.
- Bonus: Historical Tax Products DVD - Ships with the final release.
- Tax Map: an electronic research tool and finding aid.
- Tax law frequently asked questions.
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- Tax Topics from the IRS telephone response system.
- Fill-in, print, and save features for most tax forms.
- Internal Revenue Bulletins.
- Toll-free and email technical support.
- The CD which is released twice during the year.
  - The final release will ship the beginning of March 2008.
- Purchase the CD/DVD from National Technical Information Service (NTIS) at www.irs.gov/coloriers for $35 (no handling fee) or call 1-877-CDFORMS (1-877-233-6767) toll free to buy the CD/DVD for $35 (plus a $5 handling fee). Price is subject to change.
- Web links to various government agencies, business associations, and IRS organizations.
- “Rate the Product” survey—your opportunity to suggest changes for future editions.
- A site map of the CD to help you navigate the pages of the CD with ease.
- An interactive “Teens in Biz” module that gives practical tips for teens about starting their own business, creating a business plan, and filing taxes.

An updated version of this CD is available each year in early April. You can get a free copy by calling 1-800-829-3676 or by visiting www.irs.gov/smallbiz.

To help us develop a more useful index, please let us know if you have ideas for index entries. See “Comments and Suggestions” in the “Introduction” for the ways you can reach us.

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See How To Get Tax Help for a variety of ways to get publications, including by computer, phone, and mail.

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Commonly Used Tax Forms

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