



Tax Deductions for Refinance Loan Points

Refinancing is a very popular loan option these days for homeowners. It is often a great way to get into a lower interest rate on a mortgage, pull out of a resetting adjustable rate loan, or tap into valuable home equity for various financial projects. The down side is that getting into the refinance loan will likely cost you several hundred or thousands in closing costs, fees, and points. Fortunately, in an effort to encourage homeownership, the government has created tax deductions for interest paid on that refinance. What many people do not realize is that there are also available deductions for points paid on a refinance mortgage.

Mortgage points are fees that borrowers can pay to the lender in exchange for a lower interest rate. One point is equal to 1% of the loan, meaning for an average home loan, one point could equal several thousand dollars. Points may or may not be required by the mortgage lender. If you do end up paying points, the good news is that for basically any type of refinance or home equity loan, the government allows you to deduct those points. In most cases the deductions will be spread out over the entire course of the loan. You can figure out just how much you can deduct each year by dividing the amount you paid in points by the number of years it will take to repay your loan. For example, if you paid \$2000 in points on a 30-year refinance loan, you will be able to deduct about \$67 dollars during each year of the loan.

You may qualify to deduct more during the first year if you plan to use some or all of your refinance proceeds towards improvement of your home. Whatever amount you dedicate to home improvement that year, the same percentage of your mortgage points can be deducted on that year's tax forms. The balance of points will be amortized and be deducted over the remaining length of the refinance loan.

And here is more good tax news: Even if you refinance again into another loan, you will not lose out on the benefits of deducting your mortgage points. You may have had to deduct your points monthly during the time you held your first refinance loan. When you pay off that loan with a new refinance loan, the government stipulates that you can deduct the total remaining point balance that year. Consider this example. You took out a 30-year fixed loan and paid \$2000 points. Each year you have deducted \$67 dollars on your taxes. After five years you have deducted a total of \$335, but you decide to move into a loan with a better interest rate. When you pay off your first refinance loan with the second, you can deduct the remaining \$1665 in mortgage points that same year.

Be aware though, that one exception to this rule is if you obtain your next refinance loan from the same lender that financed your earlier loan. In this situation, the IRS will require that the remaining point balance be added to your new loan points and that amount will be amortized over the length of the new refinance.

If you are looking into a refinance loan with points, make sure you find out the rules that apply to your situation so that you can make the most of the great tax deductions!