6 Home Deduction Traps and How to Avoid Them

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Get an "A" on your Schedule A Form: Dodge these tax deduction pitfalls to save time, money, and an IRS investigation.

Trap #1: Line 6 - real estate taxes

Your monthly mortgage payment often includes money for a tax escrow, from which the lender pays your local real estate taxes.

The money you send the bank may be more than what the bank pays for your taxes, says Julian Block, a tax attorney and author of *Julian Block's Home Seller's Guide to Tax Savings*. That will lead you to putting the wrong number on Schedule A.

Example:

- Your monthly payment to the lender: $2,000 for mortgage + $500 escrow for taxes
- Your annual property tax bill: $5,500

Now do the math:

- Your bank received $6,000 for real estate taxes, but only paid $5,500. It may keep the extra $500 to apply to the next tax bill or refund it to you at some point, but meanwhile, you're making a mistake if you enter $6,000 on Schedule A.
- Instead, take the number from Form 1098—which your bank sends you each year—that shows the actual taxes paid.

Trap #2: Line 6 - tax calculations for recent buyers and sellers

If you bought or sold a home in the middle of 2012, figuring out what to put on line 6 of your Schedule A Form is tricky.

Don’t simply enter the number from your property tax bill on line 6 as you would if you owned the house the whole year. If you bought or sold a house in midyear, you should instead use the property tax amount listed on your HUD-1 closing statement, says Phil Marti, a retired IRS official.

Here’s why: Generally, depending on the local tax cycle, either the seller gives the buyer money to pay the taxes when they come due or, if the seller has already paid taxes, the buyer reimburses the seller at closing. Those taxes are deductible that year, but won’t be reflected on your property tax bill.

Trap #3: Line 10 - properly deducting points

You can deduct points paid on a refinance, but not all at once, says David Sands, a CPA with Buchbinder Tunick & Co LLP. Rather, you deduct them over the life of your loan. So if you paid $1,000 in points for a 10-year refinance, you’re entitled to deduct only $100 per year on your Schedule A Form.

Trap #4: Line 10 - HELOC limits

If you took out a home equity line of credit (HELOC), you can generally deduct the interest on it only up to $100,000 of debt each year, says Matthew Lender, a CPA with EisnerLubin LLP.

For example, if you have a HELOC for $200,000, the bank will send you Form 1098 for interest paid on $200,000. But you can deduct only the interest paid on $100,000. If you just pull the number off Form 1098, you’ll deduct more than you’re entitled to.

Trap #5: line 13 - Private mortgage insurance

You can deduct PMI on your Schedule A Form, as long as you started paying the insurance after Dec. 31, 2006. Congress renewed the PMI deduction for 2012 and 2013 for people making less than $110,000.

Since you're thinking about it, this is also a good time to review your PMI: You might be able to cancel your PMI altogether because you've had a change in loan-to-value status.

Trap #6: line 20 - casualty and theft losses

You can deduct part or all of losses caused by theft, vandalism, fire, or similar causes, as well as corrosive drywall, but the process isn't always obvious or simple:

- Only deduct losses that are greater than 10% of your adjusted gross income (line 38 of Form 1040).
- Fill out Form 4684, which involves complex calculations for the cost basis and fair market value. This form gives you the number you need for line 20.

Bottom line on line 20: If you've got extensive losses, it's best to consult a tax pro. "I wouldn't do it myself, and I've been dealing with taxes for 40 years," says former IRS official Marti.

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