From the desk of
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Mortgage Interest Deduction Allowed for Equitable Owners

Mortgage interest is deductible for tax purposes by the owner of a personal residence, a second home, and rental properties, but also must be the individual or married couple paying that mortgage, not a tenant or other party.

A taxpayer is allowed to deduct most or all of the "qualified residence interest" paid for their principal residence and a second home such as a vacation home.

The deduction is generally limited to the interest paid on the first $1 million of "acquisition debt" used to purchase, build, or substantially renovate a home secured by the qualified residence.

In addition you may deduct the interest on home-equity debt on loans of up to $100,000.

In this recent US Tax Court case an otherwise tenant who lived with the homeowner assisted in the refinancing the home and claimed in the loan process to be a co-owner in order to make certain renovations.

The taxpayer/tenant, John Wainwright, thereafter deducted the mortgage interest allocable to him pursuant to the loan terms which he paid.

In a subsequent audit the IRS disallowed the mortgage interest deduction he claimed.

The Tax Court disagreed, and awarded Mr. Wainwright the deduction.

To meet the tax law requirements the mortgage must be the obligation of the taxpayer claiming the deduction, and not the obligation of another.

However if a taxpayer is found to be an "equitable owner," taking state law into account, he or she may be entitled to a mortgage interest deduction.

A taxpayer becomes the equitable owner of property by assuming the benefits and burdens of ownership.

In making the determination for this particular case, the Tax Court considered several key factors, including whether Wainwright:

• Had the right to possess the property and to enjoy the use, rents, and profits.
• Had the duty to maintain the property.
• Was responsible for insuring the property.
• Bore the risk of loss of the property.
• Was obligated to pay taxes, assessments, and charges against the property.
• Had the right to improve the property.
• Had the right to obtain legal title to the property at any time by paying the balance of the purchase price.

Based on these factors the Tax Court concluded that Wainwright was the equitable owner of the home and therefore was entitled to deduct the mortgage interest paid.

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