

# Reverse Mortgage Conference 2009 Tax and Medicaid Implications for Seniors

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# Are the Mortgage Proceeds Subject to Income Taxes?

- No
- Not subject to Income Taxation
- Loan proceeds
  - Constitute nontaxable income to the borrower
  - Treated as a Loan Advance
- *See IRS Publication 936*

# What happens if Reverse Mortgage Proceeds are used to payoff an existing traditional mortgage?

- Senior deducts interest on mortgage that is paid off
- Schedule A (1040 Income Tax Return)
  - \$1,000,000 limit for acquisition indebtedness
  - Plus \$100,000 for Home Equity loans
  - Deduct any remaining unamortized points
  - Itemized Deduction limitations apply

# What happens if Reverse Mortgage Proceeds are used to payoff an existing traditional mortgage?

- Proceeds are subject to Home Equity Debt rules
- Home Equity Debt
  - Subject to Alternative Minimum Tax Limitations
  - If proceeds were not used for improvements

# Is Reverse Mortgage Interest Deductible by the Senior as the Interest Accrues?

- No
- Interest that is added monthly to the loan balance is not deductible
  - IRS Rev. Rul. 80-248, 1980-2 CB 164.
- IRS Publication 936
  - Any interest (including OID) accrued on a reverse mortgage is not deductible until the loan is paid in full.

## **Is the Mortgage Interest Deductible by the Senior if the Loan is Paid Off during Senior's lifetime?**

- Yes
- When would this typically happen?
  - Senior Moves Out Permanently
    - One Year Rule
  - House Sold during Senior's Lifetime
- Accumulated Interest is deducted in the year the mortgage is repaid, subject to limits.

## Is the Mortgage Interest Deductible by the Senior if the Loan is Paid Off during Senior's lifetime?

- Maybe
- IRS Publication 936:
- Interest Deduction may be limited
- Reverse mortgage loan generally is subject to the limit on Home Equity Debt.
  - Limited to the smaller of:
    - \$100,000 (\$50,000 if married filing separately);  
or
    - Fair Market Value (FMV) of the home.

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- When would this typically happen?
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  - House Sold during Senior's Lifetime
- Accumulated Interest is deducted in the year the mortgage is repaid.

# What Happens if Reverse Mortgage Proceeds are invested in an Annuity?

- A tax-deferred annuity has no tax due on asset accumulation until withdrawals are taken.
- Withdrawals are considered to come first from interest, which is fully taxable.
- Each annuitized payment consists of interest and principal.
  - Interest portion is taxable; return of principal is not.
  - Annuity payouts may impact the taxation of Social Security benefits.

# What Impact will the Reverse Mortgage have on the Senior's Medicaid benefits?

- Generally, Reverse Mortgages are exempt under the Medicaid rules but...
- Payments may affect eligibility for government benefits, including Medicaid.
- Generally, payments are *not* counted as income under Medicaid
- Senior should spend the payment within the same month received.
- Any funds not spent could push resources over the allowable limits for Medicaid or SSI eligibility.

# What Impact will the Reverse Mortgage have on the Senior's Medicaid benefits?

- Payments from *reverse annuity mortgages* may be counted as income for purposes of Medicaid and SSI *whether or not* they are spent within the month they are received.
- This shouldn't be treated as income, since it simply involves withdrawing equity from one's home, but some states may view it differently since the funds come in a regular monthly check.
- Consult with an elder lawyer in your state if you have any concern about how a reverse mortgage will affect eligibility for federal benefits such as Medicaid.

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**Tax and Medicaid**  
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**Have A Great Day!**

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