

Purchasing a Home

When considering purchasing a home, the first step is to closely review your current financial picture. About six months before you plan to buy, obtain copies of your credit report with credit scores from all three credit reporting agencies. If you find errors, be sure to correct them. Your credit history is extremely important when it comes to buying a home. To get best interest rates, you need a high credit score.

Next, decide the type home and neighborhood you want to live in. By visiting websites, such as www.realtor.com, you will learn about the price of homes you are interested in, as well as estimate the amount you need to borrow.

After determining how much you will borrow, visit www.bankrate.com to get information about the current mortgage rates and an estimate of your monthly payment. When estimating your monthly payment, add 30 percent to your payment for expenses such as homeowner's insurance, property taxes, and home maintenance.

After you have the estimate of your monthly payment, determine how your payment fits into your budget. Be prepared to revise your goals for the type home and neighborhood you want if the monthly payment is too high.

There are tax advantages for home ownership, which include the following tax breaks:

- Mortgage interest and real estate taxes are tax-deductible on federal and many state income tax returns, including Alabama. These amounts are usually more than the IRS's standard deduction. By itemizing your return, you are able to take advantage of more deductions.
- The profits made by selling a home can be tax-free. If you sell a home for more than what you paid for it, you have a capital gain. Capital gains are normally taxed, but you can avoid paying taxes if you qualify. In order to qualify, you must have used the home as your principal residence for two of the last five years. Current tax laws allow tax-free capital gains of up to \$500,000 if married and filing jointly and up to \$250,000 if you are single.
- Most lenders require a down payment of at least 20 percent. To accumulate the funds for the down payment, consider saving using a tax-sheltered account, such as a Roth IRA. If you are a first time home buyer, up to \$10,000 may be withdrawn tax- and penalty-free for contributions held for at least 5 years. Parents and grandparents may also make withdrawals from Roth IRAs to help family members when purchasing their first home.

Source: Garman, E. Thomas, and Raymond E. Forgue. *Personal Finance*. Boston and New York: Houghton Mifflin Company: 2006.

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