

Ordinarily, the costs of borrowing money (including amounts paid as "points") cannot be deducted in the year they are paid, but instead can only be deducted over the life of the loan to which the costs relate. However, IRS has set forth a "safe harbor," under which you can choose to deduct points in the year they are paid if all of the following requirements are satisfied:

- You must be on the cash method of accounting for tax purposes.
- The points must be paid in connection with the acquisition of your *principal* residence.
- The mortgage loan must be secured by that residence.
- You must have paid the points directly from funds that you did not borrow, or else the seller must have paid the points on your behalf. In other words, no current deduction is available if the amount of the points was withheld from the loan proceeds by the lender.
- There must be an established business practice in your area of charging points on loans of this type, and the amount you paid must not exceed the amount generally charged in your area.
- The points must be clearly designated as such on the Uniform Settlement Statement prepared in connection with the closing.
- The amount of the points must be computed as a percentage of the stated principal amount of the mortgage.

IRS says that you can choose to claim the points either as a current deduction or over the life of the loan. In most cases, the current deduction is preferable, but there may be circumstances where spreading deduction of the points over the life of the loan is more to your advantage. For example, if you purchased your home late in the year and traditionally take the standard deduction, the points you pay may be wasted as a current deduction because, when added to your other available itemized deductions, the total may still be less than the standard deduction amount. Presumably, beginning in the next year, you can itemize your deductions because of the real estate tax payments and the monthly interest paid on the mortgage, as well as the other deductions (charitable contributions, for example) which can be itemized. In this scenario, you would realize a larger overall tax saving by spreading the deduction for the points over the years.