ABOUT RECAPTURE TAX

When you receive a first-time homebuyer Mortgage Loan, you are receiving the benefit of a lower mortgage interest rate and/or down payment/closing cost assistance that is not customarily available on other mortgage loans. The tax-exempt mortgage revenue bond program used to fund your Mortgage Loan is governed by federal law. The law mandates a "recapture" of some of the benefit of the program if buyers meet all three of the following criteria – there is disposition of the residence in the first full nine years of ownership; there is a profit on the disposition of the residence **AND** the household income of the buyer increases significantly (generally over the program limits in the first year and an additional 5% over the previous year every year thereafter). "Disposition" of a residence includes non-sale transfers such as exchanges and involuntary conversions, but is referred to generally as a "sale" for purposes of this notice.

If "Recapture Tax" is owed, it's computed and paid to the IRS for the tax year in which the residence is sold. For the average buyer in these programs, it's very unlikely that they'll be required to pay because their income is lower than that allowed. But if Recapture Tax must be paid, it will **never exceed the <u>lesser</u>** of 6.25% of the highest principal amount of the Mortgage Loan or one half of the gain on the sale of the residence.

The most that you will ever be required to pay when you sell your residence in the first nine years is 6.25% of the highest principal amount of the mortgage loan during the life of the loan (i.e. if the highest principal amount of the Mortgage Loan amount during the course of the loan was $50,000 and you sold within 49-60 months of ownership, then multiply $50,000 x .0625 and the maximum Recapture Tax would be $3,125.) This amount is considered to be the federally subsidized amount.

When you sell your residence is as important as the amount you receive for the sale of your residence and your income at the time you sell.

The actual recapture tax, if any, can only be determined when you sell your residence.
Remember

- if you sell your residence after nine years, there is no Recapture Tax due;
- if your don't receive a gain (net profit) on the sale of your residence, there is no Recapture Tax due, **or**
- if your adjusted gross income does not increase significantly over the nine years(usually that means more than 5% per year), there is no Recapture Tax due.

To owe any Recapture Tax, you must sell your residence within nine years, make a net profit on the sale of your residence AND have a significant increase in income. All three criteria must be met in order for Recapture Tax to be due.

You May Not Have to Pay Recapture Tax if

- your residence is destroyed by fire, storm, flood or other casualty. There is generally no recapture tax if within two years you build or rehab for use as your principal residence on the site of the residence financed with your original subsidized mortgage loan.

You Are Not Subject to Recapture Tax if

- you sell or give away or dispose of your residence later than 9 full years after you close your mortgage loan.
- your residence is disposed of as a result of your death.
- you transfer your residence to your spouse or your former spouse as an agreement of your divorce and you have no gain or loss included in your income as a result of the transfer.

INFORMATION YOU'LL NEED IN THE FUTURE

After you close your loan, you will receive a detailed letter from the Servicer or one that will be provided by your lender at closing. This letter should be kept with your other mortgage documents. It contains extremely important information that you will need to determine if you must pay recapture tax.

The letter contains information that you'll need in order to complete Form 8828 such as

- The loan amount (the highest principal amount of the loan),
- Closing Date,
- Name of the issuer of the bonds,
- Name of the original lender that made the loan, and

- Chart that details data necessary to complete Form 8828.

What about refinancing my residence?
If you refinance your residence and stay in it for a full nine years, you won't pay Recapture Tax. However, if you dispose of your residence before nine years of ownership, then you may owe Recapture Tax. If you refinance in the first full four years and you dispose of the residence before the full nine years, there is a special calculation worksheet that must be used if you must pay Recapture Tax. See "For More Information" on the next page and instructions for Form 8828 for more detail.

What does "net profit" on the sale of your residence mean?
Consult your tax advisor, but generally you will be considering the amount you received for the sale of your residence and deducting the expenses of selling your residence (i.e. commission paid to a real estate agent, advertising, legal fees, etc.). This is the "Amount Realized" from the sale of the residence. From the "Amount Realized" you will subtract your "Adjusted Basis" of your interest in the residence. The "Adjusted Basis" will be increased by any sales commission you paid when you bought the residence and decreased by depreciation. Your tax advisor will be helpful in determining the exact amount. If the total of the "Amount Realized" minus the "Adjusted Basis" is "0" or lower, you did not realize a gain (make a profit) when you sold the residence and you **DO NOT** owe Recapture Tax. You will still need to complete a form 8828 and send it to the IRS with your federal income tax return in the year you sell or otherwise dispose of the residence.

What about my income?
If you did make a profit, then you may have to pay Recapture Tax. Now you must consider your income. There will be a chart on the letter you receive after closing that shows the maximum income allowable for each 12-month period following closing. The income limits are the **program limits for the first 12 months** and then 5% more than the preceding year for each year thereafter. Example: If your income at the time you bought the residence was $40,000 and the income limit is $50,000, the limit for the first 12 months after closing is $50,000. Then each 12 months it's 5% more than the previous year. If your modified adjusted gross income on your federal income tax return does not exceed the income limit for the 12-month period in which you sell your residence, you **DO NOT** owe Recapture Tax. If your modified adjusted gross income does exceed the income limit, you **DO** owe Recapture Tax.

How much do I owe?
The amount you owe will be the LESSER of 50% of the gain realized from the sale of your residence OR the product of–

- The income percentage (Consider the amount by which your income exceeds the qualifying limit in the year that you sell. If the amount is $5,000 or more, then your income percentage is 100%. If less than $5,000 then divide the amount by which your income exceeds the limit by $5,000 and round to the nearest whole percentage.)
- The federally subsidized amount (this is .0625 x the highest principal amount of your loan).
- The holding period percentage as shown on the chart below:

Disposition Within # Months of Closing	Holding Period Percentage	Income 1-2 person HH	Income 3 + person HH
1 - 12	20%	$Amt shown for 1-12 months will be	the program limits.
13 - 24	40%	Balance will be	completed on
25 - 36	60%	personalized	form you receive
37 - 48	80%	at closing.	The limits for each
49 - 60	100%	successive 12 mos.	is approx. 5%
61 - 72	80%	higher than the	preceding 12 mos.
73 - 84	60%		
85 - 96	40%		
97 - 108	20%		
109 or More	No Recapture Tax		

FOR MORE INFORMATION
Contact the IRS and request Form 8828 and the instructions for Form 8828 (both available on the **IRS Website:** http://www.irs.gov In the Forms and Publications search box, type “8828" and click). Review the form and instructions now. Consult your tax advisor. In the year that you sell your residence, you are required to complete Form 8828 and submit it with your federal income tax return (even after the full 9 years). The income that will be considered in that year will be your modified adjusted gross income from your federal income tax return.