2014 Tax Season and Mortgage Debt Forgiveness for Short Sales and Foreclosures

January 12, 2015 â€“ When housing markets began to tank, back in 2007, congress passed a law called the Mortgage Debt Relief Act (MDRA). The law protected those who lost their homes in a foreclosure or short sale from hefty tax bills on the portions of their mortgages that they were unable to pay.

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From the time the law was passed through 2013, congress extended MDRA every year. But a funny thing happened last year. Congress was unable to agree on an extension. That meant that anyone who had mortgage debt forgiven by their mortgage lender in 2014 would have to pay taxes on the amount forgiven.

That all changed last month. Just before Christmas, congress extended the law to cover all short sales and foreclosures taking place in 2014. Thatâ€™s good news for homeowners who went through one of these procedures last year. To give you an idea of what this means to homeowners, take a look at this example. A homeowner who is in a 25% tax bracket and who went through a short sale in which their lender agreed to forgive $100,000 in mortgage debt would have owed the IRS $25,000 in taxes for 2014 had MDRA not been extended. Thatâ€™s in addition to their regular income taxes. With the extension of the law, no additional taxes will be due.

Last monthâ€™s extension of MDRA only covered 2014. That means that congress will need to extend the law again this year. If they donâ€™t, anyone going through a foreclosure or short sale in 2015 would have to pay taxes on any forgiven amount; as described above.
byJim Malmberg
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