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# Calculating the Tax Savings of Owning Your Own Home

## *The Concept of Rental Equivalency*

Tightening in the tax code leaves mortgages as the only major tax write-off available to the average citizen. This article focuses on whether a purchaser can afford a mortgage loan by comparing the present rental payment of the purchaser with the proposed mortgage payment.

The comparison is made by calculating the rental equivalency of the mortgage payment. The term *Rental Equivalency* refers to the dollar amount of a mortgage payment after determining the effect of favorable tax considerations given homeowners.

Take the example of the renter who is paying \$1,000 each month in rent and has found the perfect home priced at \$160,000:

Rent	Owning	Mortgage Payment (PITI)
\$1,000 per month	\$160,000 Sale Price \$152,000 Mortgage 7.00% for 30 years	\$1,011.26 Principal & Interest (PI) 180.00 Real Estate Taxes (T) 33.00 Homeowners Insurance (I) <u>98.00</u> Mortgage Insurance <b>\$1,322.26 PITI</b>

In this example the mortgage payment is \$322 *higher* than the rental payment of \$1,000 each month. It is natural for you to think,

***“I can afford my rent, but how can I afford an extra \$322 each month?”***



**A few things to note on the above calculations:**

1. There are also state and local tax savings for most borrowers. They were not shown because deductibility of state taxes will mitigate the loss of the standard deduction given to tax payers who do not itemize deductions.
2. There are additional savings for homeowners. The portion of the principal and interest payment which is not interest (\$1,011.26 (PI) - \$866.67 (I) = \$144.59) is principal which goes to pay down the loan. This is equity the homeowner is building up each month- a forced savings plan. In the above example, the *Rental Equivalency* calculated with this additional equity factor would be \$1,029.26 minus \$144.59, or ***\$884.67 – that’s \$115.33 less each month than the \$1,000 a month paid in rent – not to mention the appreciation factor!***

***Yes — owning can actually be cheaper than renting.***

To save you time with these complex calculations, we have created a chart that provides the Rental Equivalency of mortgage payments. The chart assumes that 85% of the typical mortgage payment will be tax deductible. It also assumes the tax bracket of a married couple with no children. The savings for single individuals will be slightly higher. You can use the table to extrapolate to other mortgage payments. For example, the tax savings for a \$950 mortgage payment would be one-half the difference between \$900 and \$1,000.

**Rental Equivalency / Rental Tax Equivalents**

Assuming married, filing jointly, no standard deduction and 85% of PITI is deductible

		Total Mortgage Payments (PITI)					
Monthly Income	\$800	\$900	\$1,000	\$1,200	\$1,500	\$2,000	\$2,500
\$2,000	\$698						
\$3,000	\$696	\$783	\$870	\$1,045			
\$4,000	\$610	\$686	\$762	\$915	\$1,177		
\$5,000	\$610	\$686	\$762	\$914	\$1,143		
\$6,000	\$610	\$686	\$762	\$914	\$1,143	\$1,524	
\$7,000	\$610	\$686	\$762	\$914	\$1,143	\$1,524	\$1,905
\$8,000	\$589	\$663	\$738	\$891	\$1,119	\$1,500	\$1,881
\$9,000	\$589	\$663	\$737	\$884	\$1,105	\$1,473	\$1,851

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