Deduction of Interest by Unit Owners

Question: Can an individual deduct interest on their personal tax return for interest paid by the Association?

The answer is one that addresses a lot of different situations. Below is a summary of the various situations and the related answers:

1. **Cooperatives:** A cooperative housing corporation or other entity actually holds the title to the building. They can obtain a loan of which the collateral is the building. This would be called a mortgage loan if the collateral is the building, similar to a single family dwelling. If the Cooperative secures a mortgage loan the shareholders can take their portion on their personal tax returns as mortgage interest. There is a pass through deduction for this type of entity. The Cooperative should issue a Form 1098 for the mortgage interest to each shareholder.
2. **Condominiums, Townhomes and Homeowner's Associations:** In a condominium or townhome and the homeowners association, the Association does not own the buildings. The unit owners own the buildings and other property in common. When an Association obtains a loan, the loan cannot secure the building with a mortgage lien but must actually obtain a secure position on the future assessments of the Association. The loans that these entities obtain are not considered mortgages and the interest is not considered mortgage interest. **In addition, there is no provision in the IRS code to provide for interest from these entities to pass through to the unit owners.** If the owner is a non-resident investor and paying interest on their special assessment to pay the loan then they probably can deduct the interest they are paying as a business or rental expense. If the unit owner lives in the unit and they are paying interest with the special assessment to pay the loan then the interest is either considered personal interest, (which is not deductible), or investment interest which is deductible up investment income.
3. **Home equity loans:** If the unit owner needs to finance a special assessment and has equity in their unit, (not as prevalent with the real estate market crash), they would normally be better off using their own home equity line of credit or add to their own mortgage. Both of these are deductible within certain limits. If Married and filing jointly the mortgage amount is limited to $1,000,000 and the home equity line is limited to $100,000.

Summary:
The IRS has a publication that goes into all of the rules for deduction of mortgage interest. The Publication is number 936 and the web address is: http://www.irs.gov/pub/irs-pdf/p936.pdf

So to summarize, interest paid by a Cooperative, if it is mortgage interest is deductible. A Condominium, Townhome or Homeowners Association do not have the same treatment and does not pass through to the unit owners. Interest paid on a related special assessment will probably be considered personal interest.

As with all tax matters, your situation may vary from the general assumptions of this explanation and you should consult your personal tax adviser.

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