AARP Real Possibilities

Carrying Mortgage Debt Into Retirement?

A majority of pre-retirees expect to carry mortgage debt into retirement. If you're among them, it's a good idea to understand what the pros and cons are, and to consider your options. Holding a home mortgage has tax benefits, but they may dry up in retirement. And, of course, you need to figure out if you can swing the mortgage payment on your savings and Social Security benefit. For help figuring that out, use AARP's Retirement Calculator at **www.aarp.org/retirementcalc**.

Here are some issues to think about if you're carrying a mortgage into retirement.

Tax Benefits of a Home Mortgage

A common type of home loan is a 30-year mortgage. With it, your payment generally includes two parts: principal and interest. Your principal payment goes toward the actual loan amount, while the interest payment goes toward the rate your lender charged you to take out the loan. Most of your payment in the early years goes toward interest. But over time, a larger share goes toward your principal.

Mortgage Interest Deduction

Most homeowners benefit from a mortgage interest deduction when tax time rolls around. The amount you pay in mortgage interest is deducted from your gross income, which reduces your federal income tax burden. But remember, the further along you are toward paying off your mortgage, the less interest you're paying. This reduces the benefit of the deduction.

Real Estate Tax Deduction

It's common for mortgage payments to include payments for real estate taxes and insurance. The portion of your payment for these items is held in escrow — a special account from which your mortgage servicer pays these bills. Your state and local real estate taxes are deductible when it comes to filing your federal income taxes.

Tax Drawbacks of Paying on a Mortgage in Retirement

The tax benefits from holding a mortgage can be great, but their value may drop significantly when you retire. First, you may be paying far less interest on your loan, resulting in a far smaller mortgage interest deduction.

Second, it's likely your income in retirement will be less than it was during your working years. Your income taxes will likely be lower, so mortgage interest and real estate tax deductions may have little or no value at tax time.

Also, if you plan to pay your monthly mortgage with money from a 401(k) or IRA, you may end up with a higher tax burden. If your accounts are traditional, meaning you paid no taxes on your contributions, you'll pay taxes on them and your gains when you begin withdrawals. Your income tax rate will likely be lower in retirement than it was during your working years, however.

In addition to pulling money from these accounts for your mortgage payment, you'll be pulling money out to live on. When you combine your income from these accounts with your Social Security benefit, you might tip over a threshold that makes your Social Security benefit taxable.

This happens when your income in retirement, including half of your Social Security benefit, is greater than $25,000 ($32,000 for couples).

What to Do

If you like the idea of holding onto your home and you're in range of paying off your mortgage, it may be worthwhile to stay put. You'll get a welcome drop in monthly expenses when the mortgage payments go away. You'll still have to pay taxes and insurance (and all the upkeep that goes with owning a home), but if you can swing the cost, living mortgage free is a nice place to be. To see how much faster you can pay off your mortgage by making extra payments, check out AARP's Mortgage Payoff Calculator at **www.aarp.org/money**.

If you still have a long way to go before paying off your mortgage, you may continue to benefit from tax deductions. But if your federal income taxes are lower, and the benefit of the deduction isn't great, it may be a good idea to sell.

All these years after the housing bust, real estate sales continue to be soft in parts of the country. If selling isn't an option for you, consider bringing in a renter to help pay the costs of the mortgage and upkeep.

If you do sell, the first $250,000 ($500,000 for married couples) in capital gains is not taxable, as long as you've lived in your home for at least two of the five years before you sell it. The money you make on your home sale could be a boon for your retirement nest egg.

What About a Reverse Mortgage?

If you own your home outright or have largely paid it off, you may be eligible to tap into your home's equity for retirement income while staying there. A reverse mortgage allows you to borrow against your home. You don't have to repay the loan as long as you live there. You must be age 62 or older and live in your home to be eligible.

You can receive payments as a single sum, as a line of credit, as monthly income, or some combination of these. Your payments are based on your home's value, as determined by the lender.

A reverse mortgage is a big financial decision and can be very risky for some people. Learn as much as you can about how one works and what other options you have before making a move. You can start at **www.aarp.org/revmort**.

Take Action!

- ❑ Understand how far your savings and Social Security benefit will go with AARP's Retirement Calculator at **www.aarp.org/retirementcalc**.
- ❑ Take a look at your mortgage paperwork to determine how long into retirement your monthly payments will continue.
- ❑ Figure out if money you will withdraw from pretax retirement plans to pay your mortgage and to live off of, combined with half of your Social Security benefit, will make your benefit taxable.
- ❑ Consider speeding up your payoff. See how extra payments may benefit you with AARP's Mortgage Payoff Calculator at **www.aarp.org/money**.
- ❑ If you're considering a reverse mortgage, proceed with caution. Learn all you can about the ins and outs at **www.aarp.org/revmort**.

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Financial Security
601 E Street NW
Washington, DC 20049

www.aarp.org

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