



Instructions for Form 1098

Section references are to the Internal Revenue Code.

An Item To Note

In addition to these specific instructions, you should also use the **2001 General Instructions for Forms 1099, 1098, 5498, and W-2G**. Those general instructions include information about:

- Backup withholding
- Magnetic media and electronic reporting requirements
- Penalties
- When and where to file
- Taxpayer identification numbers
- Statements to recipients
- Corrected and void returns
- Other general topics

You can get the general instructions from the IRS Web Site at www.irs.gov or by calling 1-800-TAX-FORM (1-800-829-3676).

Specific Instructions for Form 1098

Use **Form 1098**, Mortgage Interest Statement, to report mortgage interest (including points, defined later) of \$600 or more received by you during the year in the course of your trade or business from an individual, including a sole proprietor. Report only interest on a mortgage defined below.

The \$600 threshold applies separately to each mortgage; thus, file a separate Form 1098 for each mortgage. You may, at your option, file Form 1098 to report mortgage interest of less than \$600, but you are subject to the rules in these instructions.

If an overpayment of interest on an adjustable rate mortgage (ARM) or other mortgage was made in a prior year and you refund (or credit) such overpayment, you may have to file Form 1098 to report the refund (or credit) of the overpayment. See **Reimbursement of Overpaid Interest** on page 1098-2.

Exceptions

You need not file Form 1098 for interest received from a corporation, partnership, trust, estate, association, or company (other than a sole proprietor) even if an individual is a coborrower and all the trustees, beneficiaries, partners, members, or shareholders of the payer of record are individuals.

Mortgage Defined

An obligation incurred after 1987 is a mortgage if real property that is located inside or outside the United States secures all or part of the obligation. This applies even though the interest recipient classifies the obligation as other than a mortgage, for example, as a commercial loan.

An obligation incurred after 1984 but before 1988 is a mortgage only if secured primarily by real property.

An obligation in existence on December 31, 1984, is not a mortgage if, at the time the obligation was incurred, the interest recipient reasonably classified the obligation as other than a mortgage, real property loan, real estate loan, or other similar type of obligation. For example, if an obligation incurred in 1983 was secured by real property, but the interest recipient reasonably classified the obligation as a commercial loan because the proceeds were used to finance the borrower's business, the obligation is not considered a mortgage and reporting is not required. However, if over half the obligations in a class established by the interest recipient are primarily secured by real property, it is not reasonable to classify those obligations

as other than mortgages for purposes of this reporting requirement.

Among other things, real property includes a manufactured home or mobile home with a minimum living space of 400 square feet and a minimum width of more than 102 inches of a kind customarily used at a fixed location. See section 25(e)(10).

If property that secures the loan is not real property, you are not required to file Form 1098. However, the borrower may be entitled to a deduction for qualified residence interest, such as may be the case for a boat, which has sleeping space and cooking and toilet facilities, that the borrower uses as a home.

Lines of credit and credit card obligations. Interest (other than points) received on any mortgage that is in the form of a line of credit or credit card obligation is reportable regardless of how you classified the obligation. A borrower incurs a line of credit or credit card obligation when the borrower first has the right to borrow against the line of credit or credit card, whether or not the borrower actually borrows an amount at that time.

Who Must File

File this form if you are engaged in a trade or business and, in the course of such trade or business, you receive from an individual \$600 or more of mortgage interest on any one mortgage during the calendar year. You are not required to file this form if the interest is not received in the course of your trade or business. For example, you hold the mortgage on your former personal residence. The buyer makes mortgage payments to you. You are not required to file Form 1098.

For information about who must file to report points, see **Points** on page 1098-3. For information about who must file to report reimbursements of overpaid interest, see **Reimbursement of Overpaid Interest** on page 1098-2.

Not in the lending business. If you receive \$600 or more of mortgage interest in the course of your trade or business, you are subject to the requirement to file Form 1098, even if you are not in the business of lending money. For example, if you are a real estate developer and you provide financing to an individual to buy a home in your subdivision, and that home is security for the financing, you are subject to this reporting requirement. However, if you are a physician not engaged in any other business and you lend money to an individual to buy your home, you are not subject to this reporting requirement because you did not receive the interest in the course of your trade or business as a physician.

Governmental unit. A governmental unit (or any subsidiary agency) receiving mortgage interest from an individual of \$600 or more must file this form.

Cooperative housing corporation. A cooperative housing corporation is an interest recipient and must file Form 1098 to report an amount received from its tenant-stockholders that represents the tenant-stockholders' proportionate share of interest described in section 216(a)(2). This rule applies only to tenant-stockholders who are individuals and from whom the cooperative has received at least \$600 of interest during the year. (See the **TIP** under **Box 1** on page 1098-4.)

Collection agents. Generally, if you receive reportable interest payments (other than points) on behalf of someone else and you are the first person to receive the interest, such as a servicing bank collecting payments for a lender, **you** must file this form. Enter your name, address, and taxpayer identification number (TIN) in the recipient entity area. You must file this form even though you do not include the interest received in your income but you merely transfer it to another person. If you wish, you

may enter the name of the person for whom you collected the interest in box 4. The person for whom you collected the interest need not file Form 1098.

However, there is an exception to this rule for any period that **(1)** the first person to receive or collect the interest does not have the information needed to report on Form 1098 and **(2)** the person for whom the interest is received or collected would receive the interest in its trade or business if the interest were paid directly to such person. If **(1)** and **(2)** apply, the person on whose behalf the interest is received or collected is required to report on Form 1098. If interest is received or collected on behalf of another person other than an individual, such person is presumed to receive the interest in a trade or business.

Foreign interest recipient. If you are not a U.S. person, you must file Form 1098 if the interest is received in the United States. A U.S. person is a citizen or resident of the United States, a domestic partnership or corporation, or a nonforeign estate or trust. If the interest is received outside the United States, you must file Form 1098 if **(1)** you are a controlled foreign corporation or **(2)** at least 50% of your gross income from all sources for the 3-year period ending with the close of the tax year preceding the receipt of interest (or for such part of the period as you were in existence) was effectively connected with the conduct of a trade or business in the United States.

Designation agreement. An interest recipient, including a recipient of points, can designate a qualified person to file Form 1098, to provide a statement to the payer of record, and to provide any Rule of 78s notice (see **Rule of 78s Method of Accounting** on page 1098-3).

A **qualified person** is either **(1)** a trade or business in which the interest recipient is under common control as specified in Regulations section 1.414(c)-2 or **(2)** a designee, named by the lender of record or by a qualified person, who either was involved in the original loan transaction or is a subsequent purchaser of the loan.

A **lender of record** is the person who, at the time the loan is made, is named as the lender on the loan documents and whose right to receive payment from the payer of record is secured by the payer of record's principal residence. Even if the lender of record intends to sell or otherwise transfer the loan to a third party after the close of the transaction, such intention does not change who is the lender of record.

The agreement must be in writing, identify the mortgage(s) and calendar years for which the qualified person must report, and be signed by the designator and the designee. A designee may report points on Form 1098 (as having been paid directly by the payer of record) only if the designation agreement contains the designator's representation that it did not lend such amount to the payer of record as part of the overall transaction. The agreement need not be filed with the IRS, but the designator must keep a copy of it for 4 years after the close of the year in which the loan is made.

A designated qualified person is subject to any applicable penalties as if it were the interest recipient. Thus, a designator is relieved from liability for any applicable penalties.

Reimbursement of Overpaid Interest

You are required to report reimbursements of overpaid interest aggregating \$600 or more to a payer of record on Form 1098. You are not required to report reimbursements of overpaid interest aggregating less than \$600 unless you are otherwise required to file Form 1098. That is, if you did not receive at least \$600 of mortgage interest during the year of reimbursement from the person to whom you made the reimbursement, you are not required to file Form 1098 merely to report a reimbursement of less than \$600. However, you may report any reimbursement of overpaid interest that you are not otherwise required to report, but you are subject to the rules in these instructions.

The reimbursement must be reported on Form 1098 for the year in which the reimbursement is made. No change should be made to the prior year Form 1098 because of this reimbursement. Report the total reimbursement even if it is for overpayments made in more than 1 year.

To be reportable, the reimbursement must be a refund or credit of mortgage interest received in a prior year that was required to be reported for that prior year by any interest recipient on Form 1098. Only the person who makes the reimbursement is required to report it on Form 1098. For example, if you bought a mortgage on which interest was overpaid in a prior year, you made a reimbursement of the overpaid interest, and the previous mortgage holder was required to report mortgage interest on Form 1098 in the prior year, you must file Form 1098 to report the reimbursement because you are the one making the reimbursement.

Example. In 1999 you received \$5,000 of mortgage interest from the payer/borrower and reported that amount on Form 1098 for 1999. In 2001, you determined that interest due on the mortgage for 1999 was \$4,500, and the payer/borrower had overpaid \$500. You refunded the \$500 overpayment to the payer/borrower in 2001. If you received \$600 or more of interest on the mortgage from the payer/borrower in 2001, you must report the \$500 refund in box 3 of the 2001 Form 1098. No change to the 1999 Form 1098 is required. If, instead of refunding the \$500 overpayment, you credited the payer/borrower's 2001 mortgage interest payments due, \$500 is still shown in box 3, and the interest received from the payer/borrower in 2001 shown in box 1 must include the \$500 credit.

Overpayment and reimbursement in same year. If you reimburse interest in the same year it is overpaid, do not report the overpayment on Form 1098 as interest received during the year or as a reimbursement of overpaid interest. For example, if the borrower paid \$5,000 and you reimbursed \$500 of that amount in 2001, enter \$4,500 in box 1 as interest paid by the borrower. Do not enter the \$500 reimbursement in box 3.

Interest on reimbursement. A financial institution (or its middleman) that pays interest of \$10 or more on the reimbursement must report that interest (under section 6049) on **Form 1099-INT**, Interest Income. Others that pay interest of \$600 or more on the reimbursement must report that interest (under section 6041) on Form 1099-INT. Do not include such interest on Form 1098.

Nonresident Alien Interest Payer

You must file Form 1098 to report interest paid by a nonresident alien only if all or part of the security for the mortgage is real property located in the United States.

Payer of Record

The payer of record is the individual carried on your books and records as the principal borrower. If your books and records do not indicate which borrower is the principal borrower, you must designate one.

If you permit a subsequent purchaser of the property to assume the loan without releasing the first purchaser from personal liability, the subsequent purchaser is the payer of record. Such subsequent purchaser's name, address, and TIN must appear on Form 1098.

Multiple borrowers. Even though there may be more than one borrower on the mortgage, you are required to prepare Form 1098 only for the **payer of record**, and only if such payer of record is an individual, showing the total interest received on the mortgage. Even if an individual is a coborrower, no Form 1098 is required unless the payer of record is also an individual.

Payments by Third Party

Report all interest received on the mortgage as received from the borrower, except as explained under **Seller Payments** on page 1098-3. For example, if the borrower's mother makes payments on the mortgage, the interest received from the mother is reportable on Form 1098 as received from the borrower.

However, do not report mortgage interest received from any governmental unit (or any subsidiary agency). For example, do not report any interest received as housing assistance payments from the Department of Housing and Urban Development (HUD)

on mortgages insured under section 235 of the National Housing Act.

Seller Payments

Do not report in box 1 of Form 1098 any interest paid by a seller on a purchaser's-borrower's mortgage, such as on a "buy-down" mortgage. For example, if a real estate developer deposits an amount in escrow and tells you to draw on that escrow account to pay interest on the borrower's mortgage, do not report in box 1 the interest received from that escrow account. As another example, do not report in box 1 any lump sum paid by a real estate developer to pay interest on a purchaser's-borrower's mortgage. However, if you wish, you may use box 4 to report to the payer of record any interest paid by the seller. See **Points** below for information about reporting seller-paid points in box 2.

Rule of 78s Method of Accounting

If you were permitted by Rev. Proc. 83-40, 1983-1 C.B. 774, or any other revenue procedure, to use the Rule of 78s method to calculate interest earned with respect to a transaction, you may report interest earned under the Rule of 78s method on that transaction as interest received from the borrower in a calendar year. In this case, you must notify borrowers that the Rule of 78s method was used to calculate interest received and that the borrowers may not deduct the amount reported unless the borrowers are also properly using the Rule of 78s method to determine interest deductions. The notification must also state that the Rule of 78s method may be used only in the case of a self-amortizing consumer loan that requires level payments, at regular intervals (at least annually), over a period not in excess of 5 years (with no balloon payment at the end of the loan term), and only when the loan agreement provides for use of the Rule of 78s method to determine interest earned (see Rev. Proc. 83-40 and Rev. Rul. 83-84, 1983-1 C.B. 97). The notice must be furnished to the payer of record on or with the statement of the interest received.



Rev. Proc. 83-40 was obsoleted by Rev. Proc. 97-37, 1997-2 C.B. 455, effective for tax years ending on or after August 18, 1997. However, you may continue to report using the Rule of 78s generally for loans issued before 1999. See section 5.04 of the Appendix in Rev. Proc. 99-49, 1999-52 I.R.B. 725.

Points

You must report certain points paid for the purchase of the payer of record's principal residence on Form 1098. You must report points if the points, plus other interest on the mortgage, are \$600 or more. For example, if a borrower pays points of \$300 and other mortgage interest of \$300, the lender has received \$600 of mortgage interest and must file Form 1098.

Report the total points on Form 1098 for the year of closing regardless of the accounting method you use to report the points as income for Federal income tax purposes.

Who must report points. The lender of record or a qualified person must file Form 1098 to report all points paid by the payer of record in connection with the purchase of the principal residence. If a designation agreement is in effect for a mortgage, only the person designated in the agreement must file Form 1098 to report all points on that mortgage. See **Designation agreement** on page 1098-2.

Amounts received directly or indirectly by a mortgage broker are treated as points to the same extent they would be treated as points if paid to and retained by the lender of record. The lender of record must report those points paid to a mortgage broker.

Reportable points. Report on Form 1098 points that meet all the following conditions:

1. They are clearly **designated on the Uniform Settlement Statement** (Form HUD-1) as points; for example, "loan origination fee" (including amounts for VA and FHA loans), "loan discount," "discount points," or "points."

2. They are **computed as a percentage of the stated principal loan amount.**

3. They are **charged under an established business practice** of charging points in the area where the loan was issued and do not exceed the amount generally charged in that area.

4. They are **paid for the acquisition of the payer of record's principal residence**, and the loan is secured by that residence. You may rely on a signed written statement from the payer of record that states that the proceeds of the loan are for the purchase of the payer of record's principal residence.

5. They are **paid directly by the payer of record.** Points are paid directly if:

- a. The **payer** of record provides funds that were not borrowed from the lender of record for this purpose as part of the overall transaction. The funds may include down payments, escrow deposits, earnest money applied at closing, and other funds actually paid over by the payer of record at or before closing OR

- b. The **seller** pays points on behalf of the payer of record. Points paid by the seller to the interest recipient on behalf of the payer of record are treated as paid to the payer of record and then paid directly by the payer of record to the interest recipient.

Report points paid under 5a and 5b on the payer of record's Form 1098 in box 2.

Exceptions. Do not report on Form 1098 points paid:

1. For loans to improve a principal residence;
2. For loans to purchase or improve a residence that is not the payer of record's principal residence, such as a second home, vacation, investment, or trade or business property even though the borrower may be entitled to amortize points paid for the purchase of a second home, vacation home, etc. and deduct them over the life of the loan;

3. For a home equity or line of credit loan, even if secured by the principal residence;

4. For a refinancing (but see **Construction loans** below), including a loan to refinance a debt owed by the borrower under a land contract, a contract for deed, or similar forms of seller financing;

5. In lieu of items ordinarily stated separately on the Form HUD-1, such as appraisal fees, inspection fees, title fees, attorney fees, and property taxes; and

6. To acquire a principal residence to the extent the points are allocable to an amount of principal in excess of \$1 million.

Construction loans. Points paid on a loan to construct a residence (construction loan) or to refinance a loan incurred to construct a residence are reportable on Form 1098 if they:

1. Are clearly designated on the loan documents as points incurred in connection with the loan, such as loan origination fees, loan discount, discount points, or points;

2. Are computed as a percentage of the stated principal loan amount;

3. Conform to an established business practice of charging points in the area where the loan is issued and do not exceed the amount generally charged in the area;

4. Are paid in connection with a loan incurred by the payer of record to construct (or refinance construction of) a residence that is to be used, when completed, as the principal residence of the payer of record;

5. Are paid directly by the payer of record; and

6. Are not allocable to an amount of principal in excess of \$1 million.

Amounts paid to refinance a loan to construct a residence are not points to the extent they are allocable to debt that exceeds the debt incurred to construct the residence.

Prepaid Interest

Report prepaid interest (other than points) only in the year in which it properly accrues.

Example. Interest received on December 20, 2001, that accrues by December 31 but is not due until January 31, 2002, is reportable on the 2001 Form 1098.

Exception. Interest received during the current year that will properly accrue in full by January 15 of the following year may be considered received in the current year, at your option, and is reportable on Form 1098 for the current year. However, if any part of an interest payment accrues after January 15, then only the amount that properly accrues by December 31 of the current year is reportable on Form 1098 for the current year. For example, if you receive a payment of interest that accrues for the period December 20 through January 20, you cannot report any of the interest that accrues after December 31 for the current year. You must report the interest that accrues after December 31 on Form 1098 for the following year.

Statements to Payers of Record

If you are required to file Form 1098, you must provide a statement to the payer of record. For more information about the requirement to furnish a statement to the payer of record, see part **H** in the **General Instructions for Forms 1099, 1098, 5498, and W-2G**.

Recipient's/Lender's Name and Address Box

Enter the name and address of the filer of Form 1098. Use this same name and address on Form 1096.

Payer's/Borrower's Name and Address Box

Enter the name and address of the person who paid the interest (payer of record).



Be careful to enter the recipient's and payer's information in the proper boxes.

Box 1. Mortgage Interest Received From Payer(s)/Borrower(s)

Enter the **interest** (not including points) received on the mortgage from borrowers during the calendar year. Include

interest on a mortgage, a home equity loan, or a line of credit or credit card loan secured by real property. Do not include government subsidy payments, seller payments, or prepaid interest that does not meet the exception explained under **Prepaid Interest** on page 1098-3. Interest includes prepayment penalties and late charges unless the late charges are for a specific mortgage service.



A cooperative housing corporation that receives any cash part of a patronage dividend from the National Consumer Cooperative Bank must reduce the interest to be reported on each tenant-stockholder's Form 1098 by a proportionate amount of the cash payment in the year the cooperative receives the cash payment. See Rev. Proc. 94-40, 1994-1 C.B. 711.

Box 2. Points Paid on Purchase of Principal Residence

Enter **points** paid on the purchase of the payer of record's principal residence. For an explanation of reportable points, see **Points** on page 1098-3.

Box 3. Refund of Overpaid Interest

Enter the total refund or credit of a prior year(s) overpayment of interest. See **Reimbursement of Overpaid Interest** on page 1098-2.

Box 4. Blank Box

Enter any other item you wish to report to the payer, such as real estate taxes, insurance, or if you are a collection agent, the name of the person for whom you collected the interest. This box is optional and is provided only for your convenience. You do not have to report to the IRS any information provided in this box.