

Homeowner's Monthly



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House Sold - Tax Exempt?

For the most part, homeowners are well aware that they receive a tax break on most or all of the interest they pay. Most homeowners also know that there may be a possible tax break afforded to them by the IRS when the property is sold. There can be some confusion, however, as to how the tax break is applied.

Typically there is a 24-month minimum holding period (as a primary residence) before the tax break can be taken. Another requirement limits the number of times the break can be taken to no more than once in 24 months. But what happens if you sell your primary residence 23 months or even 18 months after first moving in? Many questions like this were unanswered until the IRS released a new batch of regulations in 2002.

So - must you pay tax on the entire gain when you make a "premature" sale? Probably not. Odds are you can avoid any federal tax by claiming a reduced gain exclusion. (However if you're ineligible for this privilege, your entire profit will indeed be taxed.) The IRS rules make it easy to qualify for the reduced gain-exclusion break. If you qualify, it will almost certainly be big enough to shelter the entire gain from making a premature sale. Assuming you're eligible, the reduced exclusion amount equals the full \$250,000 or \$500,000 figure (whichever applies to you) multiplied by a fraction.

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Homeowners Get A Break

If you're a homeowner, you're probably aware of the incredibly generous tax break available when you sell your home. Most taxpayers can lock in a profit of up to \$250,000 (\$500,000 when you file jointly) and owe nothing to the IRS.

This great deal was enacted in 1997 and came with a couple of caveats. It stated that you must have owned and used the property as your primary residence for at least two years out of the five-year period ending on the sale date. The gain-exclusion privilege was also generally unavailable if you excluded an earlier gain within the two-year period ending on the sale date. In other words, it requires a 24-month waiting period before you deleted another home-sale gain from your 1040.

Quote Of The Month

“What a distressing contrast there is between the radiant intelligence of the child and the feeble mentality of the average adult.”
-Sigmund Freud

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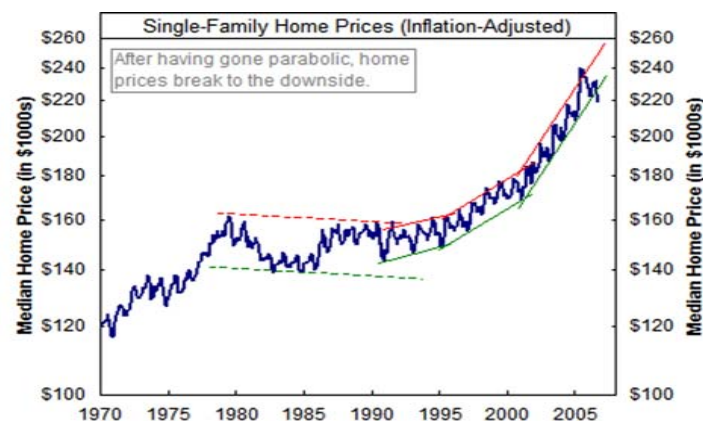
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House Prices Start Downtrend

Recent press reports suggest that the US real estate market is slowing. For some perspective, today's chart illustrates the US median price of a single-family home over the past 36 years. Thanks, in part, to low long-term interest rates, the trend over the past decade has been impressive. Not only did housing prices increase at a rapid rate, the rate at which housing prices increased - increased.



That brings us to this month's chart which illustrates how housing prices have just dropped below their accelerated upward trend. Hot spots like Nevada, Arizona, California, and Florida are now seeing sales figures dropping by over 30% compared to the year before.

Some areas have seen property values stay near their peak values, while other areas have experienced valuation declines of approximately 10%. As housing inventories increase, prices are expected to continue falling. This is not necessarily the "housing bubble" that we tend to read about in the newspapers, but it's certainly affecting the economy. One positive point is that many economists now believe interest rates will decline.

This Month In History...

43 B.C.: Cicero (Marcus Tullius) died. He was a writer, statesman, and was considered ancient Rome's greatest orator.

1066: William the Conqueror was crowned king of England after he had invaded England from France, defeated and killed King Harold at the Battle of Hastings, then marched on London.

1944: During World War II, the Battle of the Bulge began as the Germans launched a big counteroffensive in the Ardennes Forest along a 75-mile front, taking American troops by surprise. There were an estimated 77,000 Allied and 130,000 German casualties.

House Sold - Tax Exempt?, continued from p.1...

For example: You and your spouse owned and used a home as your principal residence for 22 months. In this case, the reduced exclusion available to shelter your premature home-sale profit is \$458,333 [$\$500,000 \times (22 \text{ months}/24 \text{ months})$]. Another example: You're unmarried. You sold your previous home 13 months ago and excluded the gain. Now you're about to sell your current home, which has been owned and used as your principal residence for 18 months. (You bought it and occupied it for five months before finally succeeding in selling your previous home.) The reduced exclusion available to shelter gain from prematurely selling your current home is \$135,417 [$\$250,000 \times (13 \text{ months}/24 \text{ months})$].

So when does the reduced exclusion apply? When the premature sale is primarily due to: (1) a change of place of employment; (2) health reasons; or (3) other unforeseen circumstances. The IRS regulations provide favorable rules that you can rely on.

The regulations also allow you to use your valuable gain exclusion to shelter profit from selling vacant land next to your principal residence. You can even sell the parcel with your home and the surrounding vacant land in completely separate transactions. However, the land must be sold within two years before or after you sell the parcel containing your house. Also, the land must be adjacent to that parcel and be used as part of your principal residence.

If you pass these tests, your gain exclusion can be used to offset up to \$250,000 (\$500,000 if you file jointly) of combined profits from selling the parcel containing your house and the adjacent vacant land. Naturally, you will need to discuss your unique situation with a qualified CPA. Additionally, it is important to have the right financing to maximize your total rate of return on the property. For example, if you are expecting to move within the next five years, your mortgage professional (see page 4) is always available to assist in acquiring the appropriate financing.

Winter Solstice Celebration

This month, Christmas is on the minds of many people in the West. In fact, long before Christmas people were celebrating the winter solstice around December 22nd, the shortest day of the year in the Northern Hemisphere. The word "solstice" derives from an ancient Latin word meaning "stop," or "to stand still." According to Webster's New Collegiate Dictionary, it refers to one of two points when the sun is furthest from the celestial equator.



There is significant symbolism about winter solstice holidays. The winter solstice marks a crucial part of the natural cycle. In

a real sense, the sun begins its new journey towards longer days, times of new growth and renewal of the world once again. In a spiritual sense, it is a reminder that in order for a new path to begin, the old one must end and that spring will come again.

Fire and candles are important to many pagan holidays, but especially so for the winter solstice, as the God of most modern pagan traditions is associated with the sun. The winter solstice is a time of feasting and celebration. Often trees are decorated with bright ornaments, a tradition going back to ancient Germanic peoples, who held the oak and the fir tree as sacred. The Yule Log, candles, and mistletoe are all symbols of the winter solstice.

The term Yule stems from the Anglo-Saxon "yula" or "wheel" of the year. In ancient pagan ritual, the Yule Log was lit on the eve of the Winter Solstice and burned for twelve hours. Later, the log was replaced by the Yule tree, but instead of being burned, it was adorned with burning candles.

Pagan holidays have influenced many Christian traditions, including Halloween and Easter. Yule, or the Winter solstice, is considered by many to be the reason Christmas is celebrated in December.

Some of the pagan traditions that have been adopted to celebrate Christmas include burning a Yule log, hanging mistletoe, lighting Advent candles, and decorating trees. All are now part of modern Christmas celebrations.

The selection of December 25th as a Christian holiday was first recorded in scholarly texts dating to 325 A.D., although the actual practice was first decreed in 274 A.D. by the Emperor Aurelian. Since the non-Christians viewed this time as the rebirth of the sun, it made sense for the Church to also mark this period as the celebration of the nativity of Christ. Curiously, the selection of the day appears arbitrary although mankind had long known how to calculate the solstices. One can only guess that, rather than shift the celebration each year, a regularly scheduled event was preferable.



The merry side of Saturnalia (a midwinter Roman festival) was adopted to the observance of Christmas. By 1100 Christmas was the peak celebration of the year for all of Europe. During the 16th century, under the influence of the Reformation, many of the old customs were suppressed and the Church forbade processions, colorful ceremonies, and plays.

In 1647 in England, Parliament passed a law abolishing Christmas altogether. When Charles II came to the throne, many of the customs were revived, but the merrymaking were now more worldly than religious.

Professor Stoxx

PICK OF THE MONTH Pharmaceutical HOLDRS (PPH)

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