NAR Issue Summary
Federal Tax / Mortgage Interest Deduction

NAR Committee:

Federal Taxation Committee

What is the fundamental issue?

Individuals are permitted to deduct interest paid on mortgage debt of up to $1 million. The deduction is available for interest on mortgages for a principal residence and one additional residence. The $1 million limitation represents the combined allowable debt on two residences. Mortgage interest on up to $100,000 of debt on home equity loans or lines of credit also qualifies for the deduction.

Members of Congress in both Houses and both parties are seriously talking about tax reform that would broaden the base and lower rates. Some House Republican leaders have expressed a goal of reducing the top tax rate for individuals to 25% on a revenue-neutral basis. This means that to "pay for" the lower rates, Congress would need to limit or repeal widely-utilized deductions, which could include the mortgage interest deduction (MID). So far there has been no bipartisan legislation introduced that would reduce or eliminate the MID.

I am a real estate professional. What does this mean for my business?

The mortgage interest deduction is a remarkably effective tool that facilitates homeownership. While only about 30% to 35% of all taxpayers in any given year itemize their deductions, more than 70% of homeowners utilize the deduction over the period they own their home. According to NAR research, eliminating the MID would cause a 12% decline in the value of homes across the nation. In high cost areas, that impact would be greater, while in lower cost areas the effect would be more modest.

NAR Policy:

NAR opposes any changes that would limit or undermine current law. The MID has been in place as long as there has been an Internal Revenue Code. Its value is capitalized into the price of all houses. Decreasing the value of the MID, even for just a limited group, would hurt all homeowners because of the chilling effect any reduction would cause in the market. Moreover, any decline in the value of the most expensive homes compresses the value of all other homes. The major beneficiaries of the MID are not the rich, but young, middle-class families with children who are already carrying more than their fair share of the tax burden. Of all the people who claimed the MID in 2013, 55% earned less than $100,000 and 88% earned less than $200,000.

Opposition Arguments:

Opponents of NAR policy will say that only about a third of taxpayers itemize and thus benefit from the MID, and that the deduction encourages people to buy larger and more expensive homes than what they need. Some will also claim that it primarily benefits high-income Americans.

Legislative/Regulatory Status/Outlook

As part of its budgets for the past several years, the Obama Administration has proposed reducing the value of all itemized deductions (including the MID) for upper income taxpayers. This would be done by limiting the value of itemized deductions to 28% for taxpayers who are in tax brackets higher than 28%. Thus, individuals who are in the 33%, 35%, or the 39.6% tax brackets would find their itemized deductions worth less under this proposal. In other words, an individual in the 35% tax bracket currently gets 35 cents of benefit for every dollar of deduction, where under the Administration proposal, the deduction would be worth only 28 cents per dollar. Individuals with incomes below about $180,000 would generally not be directly affected by this proposal.

Other groups, including the President's Commission on Fiscal Responsibility and Reform, have also proposed different ways to repeal or curtail the MID, including (1) repealing it in favor of lower tax rates, (2) reducing the $1 million cap to $500,000, (3) eliminating the deduction for second homes and (4) converting the deduction to a 12% tax credit.

While NAR has supported and applauds the efforts of the Obama Administration in taking aggressive measures to stabilize both the housing market and the nation’s economy, NAR has vigorously expressed its opposition to the Administration MID proposal, as well as to these other proposals to repeal or cut back on the benefits of the MID. NAR believes these proposals are ill-timed and ill-advised. Each would have an adverse impact on housing values and the pace of economic recovery.

Most members of Congress have also opposed the President’s budget proposal. To date, limits on itemized deductions have not been part of the legislative agenda. In the current deficit environment, many in Congress say that "everything is on the table," but no bipartisan bill has yet been introduced that would eliminate or reduce the MID. However, a tax reform authored by former House Ways & Means Committee Chairman Dave Camp (R-MI) would drastically change the benefit of the MID. Specifically, the proposal would lower the cap on the size of mortgage loans for which the interest is deductible from the current level of $1 million to $500,000 in four steps. But much more significantly, the proposal would also reduce the number of taxpayers eligible to claim the MID from around 33-35% today to an estimated 4-5%. This would occur because the draft plan would eliminate the deduction for state and local taxes and, at the same time, nearly double the size of the standard deduction. The result would be that far fewer homeowners would have itemized deductions in excess of the standard deduction.

The Camp plan was a introduced as a bill, but it did not garner any significant support from even House Republicans. Camp has now retired from the House and the focus of tax reform in 2015 and so far in 2016 has been on business tax reform, and not on the individual side. Thus, the Camp draft as released is no longer an active bill. However, many of the ideas of this plan might be resurrected by other policymakers in future years, including this drastic change to the MID.

Moreover, some of the candidates running for the 2016 Republican nomination for president have released tax reform plans that could be harmful or fatal to the mortgage interest deduction. While these plans are a very long way from enactment, and tax reform affecting the MID is unlikely in 2016, NAR continues to watch this issue very closely.

REALTORS® can expect the MID to be under continuing attack and scrutiny as policymakers continue to explore ideas for tax reform.

Current Legislation/Regulation (bill number or regulation)

None at this time.

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