NAR Debating the Issue

Tax Reform

Both the House and Senate are considering options to reform the federal tax system using approaches that would broaden the tax base by eliminating undetermined tax deductions, exemptions, and credits, and using at least part of the revenue saved to lower tax rates. While not every tax provision is likely to be eliminated, those benefitting homeownership and real estate investment are particularly vulnerable because they are among the largest "tax expenditures."

Current-law real estate tax provisions are vital to the health of the economy and to homeownership... Tax reform that negatively alters the fundamentals of real estate investment and ownership could halt our current economic recovery.

When meeting with your Member of Congress, they may reference statements that have been made in the media or by others that run counter to NAR's position on this issue. To help you, NAR has highlighted below some of these opposing statements and how you can respond if asked.

Economists tell us that only 25% of tax filers claim the MID. That is a very low utilization rate for the third largest tax expenditure that is estimated to cost the Treasury $379 billion over the next five years.

- The MID is highly utilized among its intended users – homeowners with a mortgage. Among this group, about 75% utilize the MID in any given year.
- About three-quarters of households with a head under age 65 have a mortgage, and about 90% of these claim the MID. Among homeowners age 65 and older, only 25% still have a mortgage, but about 85% of those who do claim the MID.
- NAR estimates that over 70% of homeowners will utilize the MID over their lifetimes, regardless of whether they own or rent in a particular year.

Only about a third of taxpayers are able to itemize, and these are generally in the highest one-third of income levels. This makes it so the MID is greatly skewed in favor of the rich and really does very little for the working poor.

- The data show that the MID is not skewed to the wealthy at all. Of those claiming the MID in 2010, 63% earned less than $100,000 and 91% earned less than $200,000.
- Our income tax system is very progressive. Because of this, it is true that those earning more are able to take more in tax deductions. However, the reason for this is that higher-income earners pay a great deal more of the income tax in the U.S. By definition, those who pay no income tax can get no benefit from a tax deduction.
- A fact that is largely ignored is that anyone who claims the standard deduction is also getting a benefit from the MID, whether they have a mortgage or not. Congress created the standard deduction in 1944 as a simplification tool. It was based on a basket of common deductions, including the MID and the deduction for property taxes. If the standard deduction were not in place, the utilization of the MID would be a great deal higher.

It is unlikely Congress will eliminate the MID, but we can get lower tax rates or reduce the deficit if we simply cap the amount of the deduction or eliminate the deduction for people owning second homes.

- Capping the MID at an arbitrary dollar amount unfairly increases taxes on those living in high cost housing markets. If Congress creates a new cap, won't they just lower it again when they need more revenue? The amount may not affect my market much now, but if it's lowered further it will.
- Most second homes are not mansions on the beach; they are modest lake houses and cabins where people retreat with their families. Often they are in areas where vacation homes drive the local economies and budgets. Eliminating the deduction on second homes would not just hit homeowners, but the communities that depend on second homes.

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- Many Americans at one point are second homeowners whether they know it or not. If a person owns two homes in the same calendar year because they move, they by definition have owned two homes in that tax year. Do we want to create a tax on moving or encourage people to only move at the end of December?

Converting the MID to a tax credit would be more fair because it would deliver the same benefit to all taxpayers, regardless of their income.

- The MID is not biased in favor of high-income taxpayers. Depending on what percentage level a credit were set, converting the deduction to a credit would likely take away the deduction from some homeowners who by no reasonable standard could be called wealthy.
- Unless the credit was refundable, it would not provide the same benefit to everyone. About half of Americans pay no income tax, so a credit would not deliver any benefits to this group. And for those who do pay income tax but who claim the standard deduction, a credit would deliver a double benefit because part of the standard deduction is a proxy for the MID.
- Converting the MID to a credit could have other negative effects on many taxpayers. For example, taxpayers who are currently able to itemize their deductions could find themselves short of the itemization threshold once mortgage interest is taken out of the total. This could have implications on their incentives for making more charitable contributions for the year.

As with the mortgage interest deduction, the lion's share of the real property tax deduction is claimed by higher-income taxpayers.

- Not really. The data show that 75% of the value of property tax deductions in 2012 went to people with cash incomes of less than $200,000. The typical real estate tax deduction beneficiary has an adjusted gross income slightly less than $81,000.
- Taxes paid to state and local governments benefit the general public and are similar in nature to the federal income tax in that they both fund essential government services. Allowing a deduction for these taxes is essential to avoiding double taxation on the same income (or a tax on a tax).

The capital gains exclusion for sale of a home is too generous.

- Congress created the exclusion of gain from the sale of a principal residence to pursue several important public policy goals. First the rule replaced an extremely confusing and burdensome set of rules that required taxpayers to keep extensive records of most major expenditures for their home, often for decades, thus creating a great deal of simplicity for the tax system. Second, the rule encourages saving for retirement through equity in what for most people, is the most significant asset they will own in their lifetime. Finally, the rule encourages a mobile workforce, which is important for economic growth.
- The limits for the exclusion were not indexed for inflation and are already only about half the amount they were when first enacted, on an inflation-adjusted basis.

The current-law tax treatment of like-kind exchanges is a loophole that should be closed in tax reform.

- From almost its beginning, our income tax system has recognized that when an investor in real estate exchanges one property for another of like kind, economically, nothing has changed. Allowing capital to flow more freely among investments is critical to economic growth and job creation.
- Like-kind exchanges are widely used by a broad spectrum of taxpayers ranging from farmers, small businesses, and individuals of modest means to larger firms and successful investors, and they remain a vehicle for economic growth.