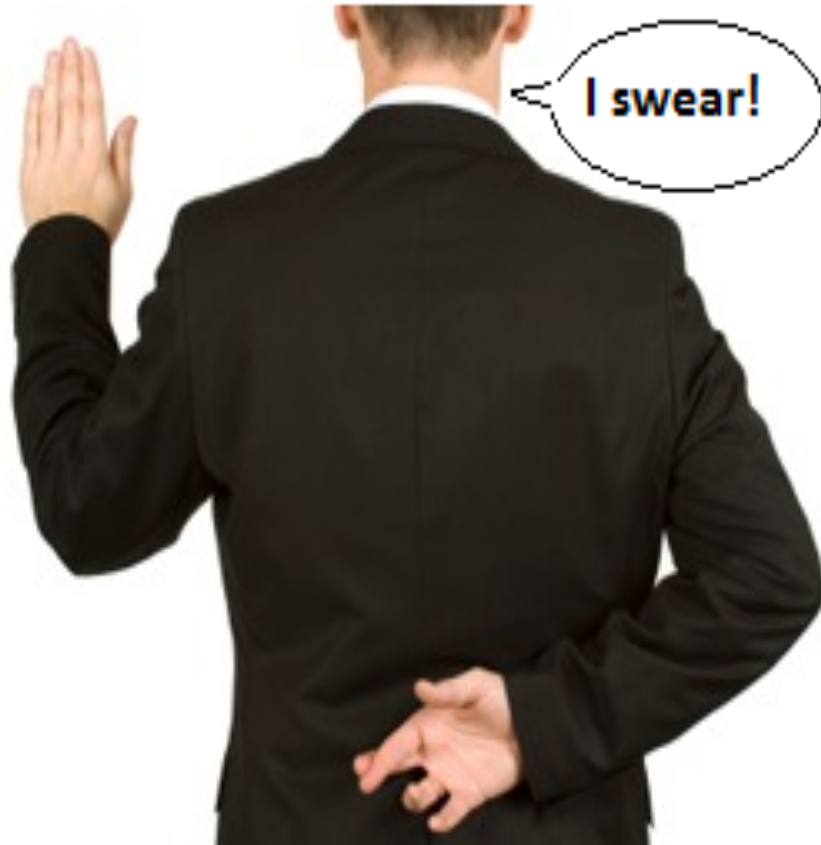


# How Tax Reform Can Destroy the Tax Benefits of Home Ownership by Stealth



Leading tax reform plans promise to leave the mortgage interest deduction largely unchanged



**But this is  
not the case.**

In reality, the tax benefit of the MID would be drastically cut for most taxpayers under these plans



Let's compare 3 actual tax reform plans that have been proposed by major figures in each party



# Dave Camp's Tax Reform Act of 2014



“The [mortgage interest deduction] provision would preserve a substantial tax benefit for homeownership without affecting most taxpayers . . . And for those taxpayers who would continue to itemize, no existing mortgage would be affected by this provision, and 95 percent of future mortgages are also expected to be unaffected.”

Tax Reform Act of 2014 Discussion Draft  
Section-by-Section Summary, p. 19.

# Ron Wyden Tax Reform Plan (2011)



“Wyden-Coats retains many of the most commonly claimed individual tax credits and deductions, **including deductions for mortgage interest** and charitable contributions, credits for children and earned income.”

Summary of The Bipartisan Tax Fairness and Simplification Act of 2011.

# House Republican Tax Reform “Blueprint” (2016)



“The Blueprint will preserve a mortgage interest deduction for homeowners. . . For those taxpayers who continue to itemize deductions, **no existing mortgage will be affected by any changes in the tax code.** Similarly, no changes will affect re-financings of existing mortgages.”

A Better Way: A Pro-Growth Tax Code For All Americans.

# Technically, they are correct!

- The tax reform plans highlighted do not repeal the mortgage interest deduction (MID).
  - In fact, the Wyden plan and the Blueprint do not touch MID at all.
- But in many cases, these plans would not only limit or eliminate the ability to claim the MID, but **would also largely nullify the tax benefits of homeownership.**



# Example – Meet Barbara Buyer



- Barbara is 33, single, and a renter paying \$1,000 per month in Colorado.
- She earns \$65,000/year and buys a condo for \$263,000, making a 5% down payment.
- Her monthly P&I payment would be \$1,193, before the tax benefits.
- Under current law, her 2016 tax benefits of home ownership would be \$3,325 or \$277/month.\*

\*assumes 30-year fixed rate mortgage loan of \$249,850 at 4.0%

# Tax Reform Could **Greatly Limit Tax Advantages** of Buying over Renting

Here are Barbara's tax benefits of homeownership under the three tax reform plans:

<b>Tax Plan</b>	<b>Tax Benefit from Owning a Home</b>
Camp	\$91
Wyden	\$650
Blueprint	\$166
<b>Current Law</b>	<b>\$3,325</b>

# Why Would Tax Benefits of Home Ownership Evaporate Under Tax Reform?



Answer – Because of a **One-Two Punch** of:

1. Big increase in standard deduction,  
  
and
2. Repeal of state & local tax deduction (in case of Camp plan & Blueprint).

# Key Issue – The Standard Deduction



- Standard deduction is like a gift from Uncle Sam – available regardless of actual expenses.
- Taxpayers itemize only if actual expenses exceed standard deduction.
- Only about 1/3 of taxpayers itemize.
- For 2016, standard deduction is \$6,300 for singles and \$12,600 for joint returns.

# What Happens If Standard Deduction Significantly Goes Up?

- Itemized deductions become less relevant and fewer people claim them.
- If one or more of the major itemized deductions is repealed (such as deduction for state and local taxes), effect is compounded.
- The result is a simpler tax system, but one where tax incentives of home ownership could evaporate even while taxes are not necessarily being reduced.

# Barbara Buyer's Itemized Deductions Under Current Law

Deduction	Rents	Buys
Mortgage Interest	\$0	\$9,914
Real Estate Taxes	\$0	\$1,686
Mortgage Insurance Premium	\$0	\$1,999
Other State/Local Taxes	\$3,250	\$3,250
Charitable Contributions	\$2,750	\$2,750
Total	\$6,000	\$19,599
<i>Standard Deduction</i>	<i>\$6,300</i>	<i>\$6,300</i>
Higher of Total or Standard Deduction?	\$6,300	\$19,599
<b>Tax Benefits of Homeownership =</b>	<b>\$3,325</b>	

# Barbara Buyer's Itemized Deductions Under Camp Plan

Deduction	Rents	Buys
Mortgage Interest	\$0	\$9,914
Real Estate Taxes	\$0	\$0
Mortgage Insurance Premium	\$0	\$0
Other State/Local Taxes	\$0	\$0
Charitable Contributions	\$1,450	\$1,450
Total	\$1,450	\$11,364
<i>Standard Deduction</i>	<i>\$11,000</i>	<i>\$11,000</i>
Higher of Total or Standard Deduction?	\$11,000	\$11,364
<b>Tax Benefits of Homeownership =</b>		<b>\$91</b>

Thus, there is very little tax advantage for buying over renting.

# Barbara Buyer's Itemized Deductions Under Wyden Plan

Deduction	Rents	Buys
Mortgage Interest	\$0	\$9,914
Real Estate Taxes	\$0	\$1,686
Mortgage Insurance Premium	\$0	\$0
Other State/Local Taxes	\$3,250	\$3,250
Charitable Contributions	\$2,750	\$2,750
Total	\$6,000	\$17,600
<i>Standard Deduction</i>	<i>\$15,000</i>	<i>\$15,000</i>
Higher of Total or Standard Deduction?	\$15,000	\$17,600
<b>Tax Benefits of Homeownership =</b>	<b>\$650</b>	

**Thus, there is still little tax advantage for buying over renting.**



# Barbara Buyer's Itemized Deductions Under **Blueprint**

Deduction	Rents	Buys
Mortgage Interest	\$0	\$9,914
Real Estate Taxes	\$0	\$0
Mortgage Insurance Premium	\$0	\$0
Other State/Local Taxes	\$0	\$0
Charitable Contributions	\$2,750	\$2,750
Total	\$2,750	\$12,664
<i>Standard Deduction</i>	<i>\$12,000</i>	<i>\$12,000</i>
Higher of Total or Standard Deduction?	\$12,000	\$12,664
<b>Tax Benefits of Homeownership =</b>		
		<b>\$166</b>

**Again, there is even less tax advantage for buying over renting.**

Now that we have seen how tax reform could affect Barbara, let's take a look at some other homeowners to see the effect on them.

# Young Couple with One Child - UT

**Income = \$ 61,000**

**Mortgage = \$ 163,000**

*\*4.5% (2<sup>nd</sup> year)*



Deductions	Amount
MID	\$7,160
Real Estate Taxes	\$1,189
Mortgage Insurance	\$1,304
Other State & Local Taxes	\$2,250
Charitable Contributions	\$6,100
Medical Expense Deduction	\$2,500

Tax Benefits of Homeownership	
Current Law	\$1,185
Camp Plan	\$0
Wyden Plan	\$0
Blueprint	\$0

2016 Tax Liability	
Current Law	\$2,325
Camp Plan	\$2,400
Wyden Plan	\$1,828
Blueprint	\$2,940

# Middle-Aged Family of Four - VA

**Income = \$ 260,000**

**Mortgage = \$ 500,000 \*4% (4<sup>th</sup> year)**

Deductions	Amount
MID	\$18,719
Real Estate Taxes	\$7,848
Mortgage Insurance	\$0
Other State & Local Taxes	\$14,300
Charitable Contributions	\$9,000
Medical Expense Deduction	\$0



Tax Benefits of Homeownership	
Current Law	\$7,439
Camp Plan	\$130
Wyden Plan	\$6,953
Blueprint	\$1,228

2016 Tax Liability	
Current Law	\$41,287
Camp Plan	\$45,075
Wyden Plan	\$46,377
Blueprint	\$45,348

# Single Mom with 2 Kids - CA

Income = \$ 135,000

Mortgage = \$ 340,000 \*3.75% (3rd year)

Deductions	Amount
MID	\$12,157
Real Estate Taxes	\$4,081
Mortgage Insurance	\$0
Other State & Local Taxes	\$9,655
Charitable Contributions	\$4,000
Medical Expense Deduction	\$0



Tax Benefits of Homeownership	
Current Law	\$4,059
Camp Plan	\$615
Wyden Plan	\$1,849
Blueprint	\$0

2016 Tax Liability	
Current Law	\$16,537
Camp Plan	\$22,738
Wyden Plan	\$16,614
Blueprint	\$21,198

# Newly-Retired Couple Working Part-Time, Just Downsized – OH

**Income = \$ 95,000**

**Mortgage = \$ 180,000** \*4% (1<sup>st</sup> Year)

Deductions	Amount
MID	\$7,142
Real Estate Taxes	\$5,580
Mortgage Insurance	\$0
Other State & Local Taxes	\$3,250
Charitable Contributions	\$3,800
Medical Expense Deduction	\$1,875



Tax Benefits of Homeownership	
Current Law	\$2,176
Camp Plan	\$0
Wyden Plan	\$0
Blueprint	\$0

2016 Tax Liability	
Current Law	\$8,860
Camp Plan	\$7,300
Wyden Plan	\$8,535
Blueprint	\$8,520

# Widower, Mortgage Paid Off – WI

**Income = \$ 46,000**

**Mortgage = paid off**

Deductions	Amount
MID	\$0
Real Estate Taxes	\$2,940
Mortgage Insurance	\$0
Other State & Local Taxes	\$2,300
Charitable Contributions	\$2,000
Medical Expense Deduction	\$10,950



Tax Benefits of Homeownership	
Current Law	\$441
Camp Plan	\$0
Wyden Plan	\$441
Blueprint	\$0

2016 Tax Liability	
Current Law	3,100
Camp Plan	\$3,500
Wyden Plan	\$3,564
Blueprint	\$4,080

# Summary

<b>Tax Benefits of Owning a Home</b>				
<b>Homeowner</b>	<b>Current Law</b>	<b>Camp Plan</b>	<b>Wyden Plan</b>	<b>Blueprint</b>
Young Single	\$3,325	\$91	\$650	\$166
Couple w/ Child	\$1,185	\$0	\$0	\$0
Family of Four	\$7,439	\$130	\$6,953	\$1,228
Single Mom	\$4,059	\$615	\$1,849	\$0
Retired Couple	\$2,176	\$0	\$0	\$0
Widower	\$441	\$0	\$441	\$0

<b>2016 Tax Liability</b>				
<b>Homeowner</b>	<b>Current Law</b>	<b>Camp Plan</b>	<b>Wyden Plan</b>	<b>Blueprint</b>
Young Single	\$6,109	\$7,762	\$7,088	\$8,190
Couple w/ Child	\$2,325	\$2,400	\$1,828	\$2,940
Family of Four	\$41,287	\$45,075	\$46,377	\$45,348
Single Mom	\$16,537	\$22,738	\$16,614	\$21,198
Retired Couple	\$8,860	\$7,300	\$8,535	\$8,520
Widower	\$3,100	\$3,500	\$3,564	\$4,080



# Main Takeaway

- **Beware** of tax reform that promises to retain the current deduction for mortgage interest.
  - If tax reform offers much larger standard deduction, particularly when combined with repeal of state and local tax deduction, it is likely to gut the tax benefits of homeownership, even if it does not repeal or even modify MID itself.

# The Real Question

- Every taxpayer's situation will be different – some will pay more tax, some will pay less under tax reform. A higher standard deduction will simplify the tax system. But at what cost?
- The three plans outlined largely eliminate the current tax incentives of homeownership, which have been a hallmark of our system for more than a century.
- REALTORS® should ask their MOC's not whether they support the MID, but whether they will stand up to preserve tax incentives for homeownership.

# PwC Study

## Goals of Study:

- Develop model of a tax reform proposal that lowers tax rates, doubles standard deduction & eliminates all itemized deductions except MID & charitable contributions.
  - Estimate impact of tax reform vs. current law by income class, homeowner status & number of households paying more and less tax.
  - Estimate of value of MID and property tax deduction under current law vs. tax reform.
  - Estimate of short-run effect of tax reform on home values and on negative equity.
  - Estimate tax credit equivalent and impact of replacing MID with a credit by income class.