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NEWS ANALYSIS

Taking Aim at the Mortgage Tax Break

By DAVID KOCENIEWSKI

Published: November 12, 2010

By proposing to curtail the tax deduction for mortgage interest, the president's deficit commission is sounding an alarm.



Alex Brandon/Associated Press

Erskine Bowles, left, and former Wyoming Sen. Alan Simpson led a deficit commission that proposed ending the mortgage tax break.

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Andrew Harrer/Bloomberg News

Michael Berman, of the Mortgage Bankers Association, said ending the mortgage tax break would hurt consumers.

The home mortgage deduction is one of the most widely used and expensive tax subsidies. More than 35 million Americans claim it, and the federal government estimates it will cost the Treasury \$131 billion in forgone revenue in 2012. Its size, popularity and link to the emotionally charged American notion of homeownership has made it so politically sacrosanct that there are serious doubts whether Congress will even entertain the idea.

But by raising the specter of ending one of the most cherished tax breaks, the commission is trying to jar the public into recognizing the magnitude of the nation's budget deficit and some of the drastic steps that might be needed to close it.

Because the mortgage interest is one of a limited number of tax breaks available to middle-income Americans, the commission's proposal has also rekindled a debate about how much of the pain of deficit reduction should be borne by the middle class.

The proposal, part of a draft by co-chairmen [Alan K. Simpson](#) and [Erskine B. Bowles](#), suggested that the tax code could be streamlined, and income tax rates drastically lowered, by eliminating the \$1.1 trillion in annual tax expenditure entitlements — subsidies and breaks given to targeted businesses and individuals. The commission chairmen also offered the option of capping the deduction at \$500,000 on mortgages, rather than the current limit of \$1 million.

The prospect brought an angry outcry. **House Speaker Nancy Pelosi blasted the commission's suggestions, saying it would force middle-class homeowners to subsidize tax breaks for the wealthy.** Officials in the real estate and mortgage industries warned

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that ending the deduction could cripple an already ailing housing market.

“The mortgage interest deduction is one of the pillars of our national housing policy,” said Michael D. Berman, chairman of the Mortgage Bankers Association. “Limiting its use will have negative repercussions for consumers and home values up and down the housing chain.”

But tax policy experts say that for all its popularity, the value of the deduction in public policy is debatable. It was intended to encourage homeownership, but housing economists point out that countries like Canada and Australia, which do not allow mortgage interest deductions, have homeownership rates similar to those of the United States.

“What the subsidy is doing is driving up prices by encouraging well-off people to take out bigger loans, to buy bigger houses,” said Roberton Williams, a fellow at the Tax Policy Center. “So I think there’s a question about whether that is something the government should be doing with tax money.”

Critics of the subsidy also argue that, despite its broad support, the benefits from the mortgage interest deduction flow disproportionately to the wealthy.

Calvin Johnson, a tax professor at the [University of Texas](#), said that only those in the top third of wage earners even itemized their deductions, meaning that two-thirds of taxpayers weren’t eligible for the break.

“No one can make a serious intellectual argument in favor of the mortgage interest deduction,” he said. “Why should the government subsidize homeowners rather than renters? The only thing it’s good for is middle-class votes.”

In recent years, there have been several proposals to amend the deduction by scaling it back at the upper end. The [Congressional Budget Office](#) in 2008 proposed changes that would limit the savings for wealthier taxpayers, one that would convert the deduction into a 15 percent tax credit and another that would eliminate the deduction on the interest on [home equity loans](#). Because millions of families counted on the deduction when buying their homes, most proposals include provisions to phase in any change over a number of years.

Whether or not a change is included in the deficit commission’s final report, tax policy experts say Congress would probably not consider it except as part of a major overhaul of the tax code.

Even so, economists say that the debate will help clarify the difficult choices the country faces.

The rhetoric of tax-cutting so dominates the political debate in Washington that many elected officials are reluctant to acknowledge that the federal government devotes as about as much money to tax breaks — \$1.1. trillion — as it does to discretionary spending.

“What this proposal does is stress the theme that tax cuts have the same effect as spending,” said Edward C. Kleinbard, a tax professor at the [University of Southern California](#) and former chief of staff of the Congressional Joint Committee on Taxation. “It’s a theme people want to resist, but it is a fact. Giving a tax break without cutting spending is the same as the government writing out checks to people.”

A version of this news analysis appeared in print on November 13, 2010, on page B1 of the New York edition.

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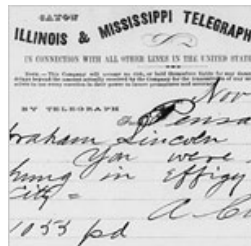


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