

Do existing tax incentives increase homeownership?

Probably not. The US homeownership rate is lower than in many other developed countries such as the United Kingdom or Australia, which do not offer tax subsidies for homeownership, and even lower than some other countries with subsidies. Beyond a base level, US subsidies mainly support larger homes and second homes. Additionally, evidence suggests that the subsidies raise housing costs, thus dissipating their effectiveness in helping people buy their own homes.

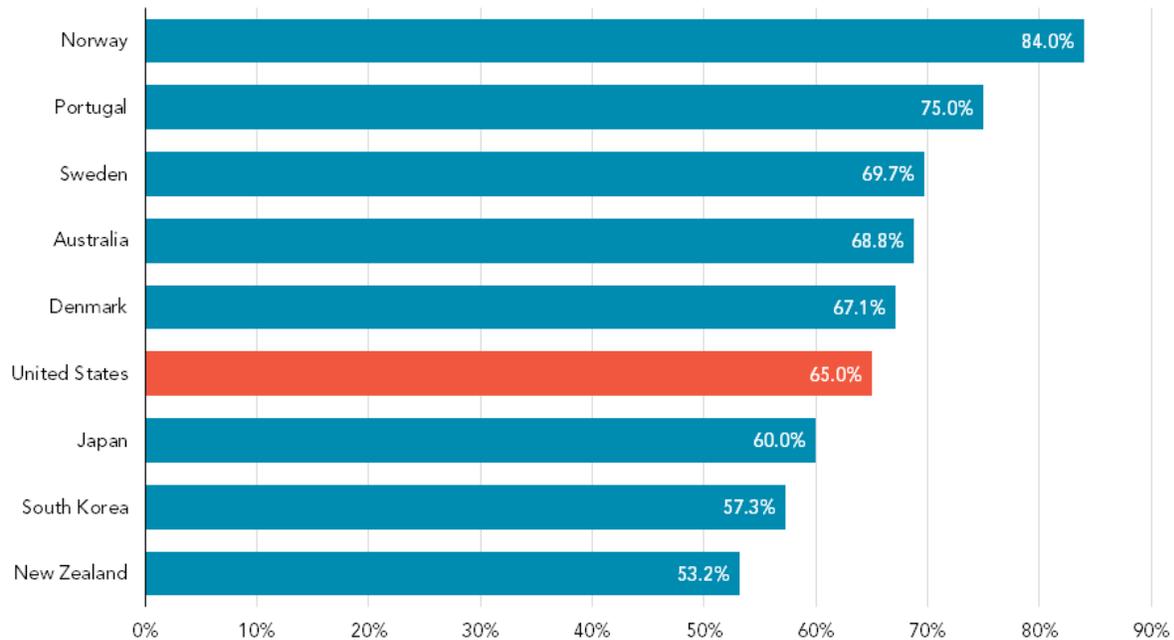
Contrary to popular belief, the mortgage interest deduction was not added to the tax code to encourage home ownership. The deduction existed at the birth of the income tax in 1913—a tax explicitly designed to hit only the richest individuals, a group for whom homeownership rates were not a social concern.

The federal government now provides more than \$120 billion each year in tax benefits to subsidize homeownership, yet our rate of homeownership differs little from that in countries providing no similar subsidies. The bulk of US subsidies go to middle- and upper-income households that likely would own their homes anyway; thus, these subsidies simply facilitate the consumption of more housing. In addition, evidence suggests that the tax subsidies raise housing costs, thus dissipating their effectiveness in helping people buy their own homes.

The US homeownership rate is lower than that in many other developed countries such as the United Kingdom or Australia that have no such subsidies. The rate is even lower than some in countries that have subsidies, such as Sweden and Norway (figure 1). Other factors, including the ease of obtaining a mortgage, home prices, and cultural patterns play significant roles in determining homeownership rates.

FIGURE 1

Homeownership Rates in Select Countries
Share of adults who own their homes



Source: Desilver, 2013.

Because tax deductions are worth more to high-income households, which face the highest tax rates, the deductibility of property taxes and mortgage interest most helps households that would likely own their own homes even without a tax subsidy. Low-income households, which typically are most in need of aid to afford homeownership, get little or no benefit from that deductibility.

Beyond a base level, subsidies mainly support larger homes and second homes. In effect, the federal government encourages middle- and upper-income households to consume more housing than they otherwise would. Limits on the amount of mortgage debt for which taxpayers may deduct interest costs do, however, constrain those subsidies to some degree.

Research suggests that housing subsidies raise housing costs, particularly where land is scarce. By reducing the after-tax cost of housing, the subsidies enable people to pay more than they otherwise would. The resulting increase in demand for housing causes prices to rise, and rise most in markets where supply cannot easily increase to meet that higher demand.

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