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Mortgage Deduction Backers Spend Heavily on Politics

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Although he's now bowed out of the 2016 presidential race, retired neurosurgeon Ben Carson left his mark in one respect: In a field that once had 23 major party presidential candidates, he was the only one to openly advocate elimination of the mortgage interest deduction.

Political and tax observers are not surprised. The mortgage interest deduction for homeowners has long been recognized as one of the most untouchable preferences the tax code offers, and it is supported by an influential lobby.

The tax benefit can be traced to the birth of the income tax in 1913 when Congress created a deduction for interest costs, though not necessarily intending it as a way to juice housing construction. But by the late 1940s, it had evolved into a wildly popular preference associated with rapidly expanding homeownership.

According to projections of the Joint Committee on Taxation issued in December 2015 (JCX-141-15), the deduction will cost the federal government $77 billion during fiscal 2016, increasing to $96.4 billion by fiscal 2019. The JCT puts its five-year cost at $419.8 billion -- a big price tag for a deduction with mixed results, many economists argue.

Candidates' Positions

Presidential candidates routinely talk about eliminating "carveouts" and "loopholes" in the tax code but nearly always make an exception for mortgage interest.

This year has been no different, although Democratic candidates Hillary Clinton, the former secretary of state, and Bernie Sanders, the independent senator from Vermont, have proposed limiting the mortgage interest deduction -- and most others as well -- to 28 cents on the dollar. For his part, Republican Sen. Marco Rubio of Florida talks of a "reformed" deduction, limiting it to mortgages of no more than $300,000, down from the current $1 million. And former Republican Gov. Mike Huckabee of Arkansas, when he was still in the race, called for a national sales tax, implying elimination of the income tax and all its associated preferences.

But it was Carson, a Florida resident and formerly of Johns Hopkins Children's Center in Baltimore, who really got attention when he called for getting rid of the deduction during a November 10 debate in Milwaukee.

"Now, I will say that there are a lot of people who say if you get rid of the deductions, you ruin the American dream because, you know, [the] home mortgage deduction," Carson said. "But the fact of the matter is, people had homes before 1913 when we introduced the federal income tax, and later after that started deductions."

When Carson released his formal tax plan January 4, he said, "The overwhelming majority of Americans do not benefit from these itemized deductions."

Whenever there is talk of tampering with the tax break, however, powerful lobbying groups such as the National Association of Realtors and the National Association of Home Builders react quickly -- as former House Ways and Means Committee Chair Dave Camp found out in 2014 when he proposed limiting the eligible amount of mortgage debt to $500,000.

The Realtors' group immediately warned that such a proposal threatened economic harm "to every single American, either directly or indirectly." And the National Association of Home Builders argued that the deduction "supports the aspirations of families at all income levels to become home owners, and Americans overwhelmingly oppose any action by Congress to tamper with" it.

Giving to Candidates

Meanwhile, real estate interests are heavy hitters when it comes to campaign donations to presidential and congressional candidates.

According to figures compiled for Tax Analysts by the Center for Responsive Politics, real estate interests had donated more than $36 million to 2016 presidential candidates as of February 5. The total reflects money given to their official campaign committees and to outside groups, mainly super PACs, that support their candidacies.

The leading recipient has been Sen. Ted **Cruz**, R-Texas, with $16.04 million. Of that total, $15.34 million reflects money that wealthy Texas real estate investors gave to super PACs, which can receive donations of unlimited size. However, while **Cruz** supports continuing the deduction, like Camp he has called for limiting it to mortgages of no more than $500,000.

Former Florida Gov. Jeb Bush, a Republican who quit the presidential race in February, had seen $10.59 million in support from real estate interests, followed by Democratic front-runner Hillary Clinton at $3.28 million, Republican Sen. Marco Rubio of Florida at $1.62 million, and Republican Gov. Chris Christie of New Jersey at $1.16 million. Christie has also suspended his campaign.

Even Carson received $678,234.

Real estate developer Donald Trump, who says he is self-funding his campaign, has gotten $52,998. In 2006 Trump told *The New York Times* that eliminating the deduction would be "a total catastrophe" for the U.S. economy. "It will lead to a major recession, if not a depression," he said.

To all federal candidates, including those running for congressional seats, the real estate sector has so far given $80.42 million in the 2016 elections, according to the Center for Responsive Politics. In 2014 it spent $111.21 million on federal races. And in 2012, another presidential election year, it spent $158.77 million.

Further, the industry spends heavily on lobbying, including close to $80 million in 2015, the center's figures show.

"By far the most active player in the industry is the National Association of Realtors, which spent $7.3 million [on campaign contributions] in the 2012 cycle, slightly favoring Republican candidates and causes over Democratic ones," the center said, adding that the Realtors group makes clear that it wants Congress to "leave unchanged current mortgage interest deduction policies."

Reform Ideas

At Washington think tanks, however, are many who think the deduction is in need of serious surgery, if not elimination. They say the evidence that it fosters homeownership is mixed at best; for one reason, they say, the dollar benefits it provides marginal homeowners is relatively small.

"Phasing out the mortgage interest deduction would make sense as policy, but it will never happen because it's an immensely popular deduction," Len Burman, director of the Urban-Brookings Tax Policy Center, told Tax Analysts.

"The problem with the mortgage interest deduction, as with most other deductions, is that most of the benefit goes to higher-income individuals," added Harry Stein, fiscal analyst with the Center for American Progress Action Fund.

Not only are upper-income individuals more likely to own a home, he said, they are more likely to own an expensive home, increasing the benefits of the deduction for them. Further, Stein said, homes are often priced assuming the deduction, increasing housing costs.

One promising reform idea, he said, is to change it from a deduction to a credit, under which all would claim the same percentage of their mortgage costs. Stein also said the ideas of Clinton and Sanders, to limit the deduction to a certain percentage on the dollar, is worth looking at.

Overall it remains "a huge subsidy," Stein said, adding that it costs the government far more than what's spent on assistance for low-income housing.

Burman offered another idea. "The right answer economically would be to tax net imputed rent (subtracting out interest, property taxes, and depreciation from the gross rental value of the home), but that would be impossible to explain to policymakers or the public," he said.

But economist Curtis Dubay of the Heritage Foundation said the "conventional wisdom" against the mortgage interest deduction is wrong. "Lenders are taxed on their interest income," he said. "In that case, a deduction for the borrower prevents [taxes] from artificially reducing the amount of borrowing and lending in the economy."

He added: "Those that are against the mortgage interest deduction often simultaneously support interest deductions for businesses. But [both deductions] conform to the same principle that if interest income is taxable to lenders, interest expenses should be deductible to borrowers."

But another conservative economist, Chris Edwards of the Cato Institute, said: "The mortgage interest deduction should be eliminated with major tax reform. . . . As with nearly all deductions, exemptions, and credits, the more you get rid of, the lower the rates can be, and the more economic growth you get from both the more neutral base and lower rates."